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Rethinking ISDS

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RETHINKING ISDS

*George Kahale, III**

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INTRODUCTION

The question of whether investor-state arbitration is broken, which this author posed in a 2012 article,¹ is being increasingly answered with a resounding “yes,” and no longer just by a few countries in Asia, Africa and Latin America, the traditional victims of claims that contracting states under investment treaties never imagined possible when they signed up for investor-state dispute settlement (ISDS) mechanisms.² In

1. George Kahale, III, *Is Investor-State Arbitration Broken?*, 9 TRANSNAT'L DISP. MGMT. 1, 8 (Dec. 2012).

2. For commentary on the care (or lack thereof) taken by states in entering into bilateral investment treaties (BITs), see JONATHAN BONNITCHA, LAUGE N. SKOVGAARD POULSEN & MICHAEL WAIBEL, *THE POLITICAL ECONOMY OF THE INVESTMENT TREATY REGIME* 222 (Oxford Univ. Press, 2017) (“Political symbolism and transnational mimicry were the main drivers of many investment treaties rather than instrumental considerations relating to the legal content and the practical implications of the treaties.”); Alison Ross, *Former Pakistan AG Opens Up About Investment Treaties*, GLOBAL ARB. REV. (Jan. 17, 2011) (reporting on the observations of the former Attorney General of Pakistan about his country’s experience with BITs, admitting that BITs were signed “without any negotiation or consideration of the consequences,” that most of the treaties were signed because a dignitary was visiting a foreign country or vice versa and the two governments “couldn’t think of any other document to sign,” and that a BIT “provides a good photo opportunity”); Department of Trade and Industry, *Bilateral Investment Treaty Policy Framework Review*, in 529 GOV’T GAZETTE 5 (July 7, 2009) (S. Afr.) (“[T]he Executive entered into agreements that were heavily stacked in favour of investors without the necessary safeguards to preserve flexibility in a number of critical policy areas. In reviewing the *travaux préparatoires* of the various BITs entered into at the time, it became apparent that the inexperience of negotiators at that time and the lack of knowledge about investment law in general resulted in agreements that were not in the long term interest of the RSA.”); Lauge N. Skovgaard Poulsen, *Sacrificing Sovereignty by Chance: Investment Treaties, Developing Countries, and Bounded Rationality*, LONDON SCH. ECON. & POL. SCI. 1, 3 (June 2011) (“By overestimating the benefits of BITs and ignoring the risks, developing country governments often saw the treaties as merely ‘tokens of goodwill.’ Many thereby sacrificed their sovereignty more by chance than by design, and it was typically not until they were hit by their first claim, officials realised that the treaties were enforceable in both principle and fact.”).

recent years, India,³ Indonesia,⁴ South Africa,⁵ Bolivia,⁶ Ecuador⁷ and Venezuela⁸ have all taken steps to terminate investment treaties, some more radical than others, but all the result of frustration with treaties that did not fulfill the promise of

3. Alison Ross, *India's Termination of BITs to Begin*, GLOBAL ARB. REV. 155 (Mar. 22, 2017) ("As its self-imposed 31 March deadline for terminating bilateral investment treaties draws near, India has sent notices of termination to 58 countries that are expected to take effect from as early as next month. . . . In relation to its remaining 25 BITs, which have not completed their initial term and therefore cannot be terminated, India has circulated a proposed joint interpretative statement to the counterparty states, seeking to align their interpretation as far as possible with the Model BIT.").

4. Ben Bland & Shawn Donnan, *Indonesia to Terminate More Than 60 Bilateral Investment Treaties*, FIN. TIMES (Mar. 26, 2014).

5. Jackwell Feris, *Challenging the Status Quo — South Africa's Termination of Its Bilateral Trade Agreements*, DLA PIPER INT'L ARB. NEWSL. (Dec. 10, 2014) ("The decision was prompted by a policy review of the actual value of BITs for FDI flow to South Africa and also the risk that certain policy and domestic interventionist measures may be open to attack by foreign investors (including black economic empowerment and procurement policies).").

6. Aldo Orellana López, *Bolivia Denounces Its Bilateral Investment Treaties and Attempts to Put an End to the Power of Corporations to Sue the Country in International Tribunals*, NETWORK JUST. GLOBAL INV. (June 2014), <http://justinvestment.org/wp-content/uploads/2014/07/Bolivia-denounces-its-Bilateral-Investment-Treaties-and-attempts-to-put-an-end-to-the-Power-of-Corporations-to-sue-the-country-in-International-Tribunals.pdf> ("The Bechtel case sparked a growing awareness among Bolivians that finally led to a Constitutional mandate to dismantle the system."); *Bolivia Inicia Retiro del Banco Mundial*, EXPANSIÓN (May 3, 2007).

7. Tom Jones, *Ecuador Set to Terminate BITs*, GLOBAL ARB. REV. (May 4, 2017) ("Ecuador's approach is similar to that of India – which recently announced a termination of its 58 remaining BITs to be replaced with treaties based on a new Indian Model BIT drawn up in 2015 that reflects lessons learned from the state's past experience of investment disputes."); *Ecuador to Pull Out of ICSID*, GLOBAL ARB. REV. (June 15, 2009) ("The country's Congress voted to denounce the World Bank arbitration facility on 12 June, after President Rafael Correa said it signifies 'colonialism, slavery with respect to transnationals, with respect to Washington, with respect to the World Bank and we cannot tolerate this.'").

8. Venezuela terminated its treaty with the Netherlands following the filing of claims by ExxonMobil and ConocoPhillips subsidiaries that incorporated in the Netherlands long after the investments were made in Venezuela. *Venezuela Holdings, B.V. et al. v. Bolivarian Republic of Venezuela*, ICSID Case No. ARB/07/27; *ConocoPhillips Petrozuata B.V., ConocoPhillips Hamaca B.V. and ConocoPhillips Gulf of Paria B.V. v. Bolivarian Republic of Venezuela*, ICSID Case No. ARB/07/30. In 2012, Venezuela withdrew from ICSID. Christopher Toothaker, *Venezuela Leaving World Bank's Arbitration Body*, SAN DIEGO UNION-TRIB. (Jan. 25, 2012).

increased foreign investment and seemed to bring nothing but headache and the risk of catastrophic awards. Now the dissatisfaction with investor-state dispute settlement mechanisms seems to run as deep, if not deeper, in the heart of Europe.⁹

The rise of anti-ISDS sentiment in Europe is hardly surprising, but it is not exclusively attributable to altruism. Rather, it is best described as a long overdue acknowledgment of the failings of a system that was designed to protect U.S. and European enterprises doing business in developing nations but had suddenly turned against the designers. In the last few years, scores of arbitrations under investment treaties have been instituted by investors against Western European countries that used to be and still are the traditional homes of investors bringing claims against countries in Asia, Africa or Latin America. Now the European countries are under fire and, ironically, the fire is coming from investors in Europe, a development that has Europeans up in arms, especially when the investors meet with some success. The moral of the story is that it is one thing to defend and even promote a flawed system when you are the beneficiary, quite another to do so when you are the victim.¹⁰

The European backlash against investor-state arbitration has not yet extended across the Atlantic to the United States, but that is fortuitous. After all, the United States does not like subjecting itself to the jurisdiction of international tribunals in any field, much less *ad hoc* arbitral tribunals sitting in judgment on legislative or other sovereign action in conference centers and hotels around the world. If Congress has misgivings about the United Nations, an international organization at least most Americans have heard of, what can be expected when someday some unknown arbitral tribunal slaps the United States with a

9. See European Commission, Concept Paper: Investment in TTIP and Beyond — the Path for Reform (May 5, 2015), http://trade.ec.europa.eu/doclib/docs/2015/may/tradoc_153408.PDF; European Commission, Trade for All: Towards a More Responsible Trade and Investment Policy (Oct. 2015), http://trade.ec.europa.eu/doclib/docs/2015/october/tradoc_153846.pdf; European Commission, *Recommendation for a Council Decision Authorising the Opening of Negotiations for a Convention Establishing a Multilateral Court for the Settlement of Investment Disputes*, COM (2017) 493 final (Sept. 13, 2017), <https://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:52017PC0493&from=EN>.

10. Not all states are up in arms over ISDS, but the trend is clear. Most acknowledge that the system is in need of reform, and the number of states looking for a complete overhaul or dismantling of the system is on the rise.

multibillion-dollar award because it thinks a foreign claimant's treaty rights have been violated? The reaction is not likely to be pretty.

But for now, ISDS flies largely under the radar in the United States. Unlike in Europe, where ISDS has become a hot topic both in the print media and on television,¹¹ in the United States, there is little public discussion of ISDS outside of the international arbitration community and, with few exceptions, the discussion that takes place there does not reflect a system in decline or in need of a major overhaul. On the contrary, conferences on ISDS tend to be a cross between ISDS rallies and an exploration of means to make it more investor-friendly, with panels of speakers packed with lawyers representing claimants and experts regularly appearing on their behalf.

11. See Envoyé Spécial, *Multinationale Contre Etat: La Loi du Plus Fort* (France 2), YOUTUBE (Nov. 16, 2017), <https://www.youtube.com/watch?v=fLFOeJa8p8w>; Frank Mulder, Eva Schram & Adriana Homolova, *Big Davids, Small Goliaths*, NEW INTERNATIONALIST (June 1, 2016); *The Arbitration Game: Governments Are Souring on Treaties to Protect Foreign Investors*, ECONOMIST (Oct. 11, 2014) ("If you wanted to convince the public that international trade agreements are a way to let multinational companies get rich at the expense of ordinary people, this is what you would do: give foreign firms a special right to apply to a secretive tribunal of highly paid corporate lawyers for compensation whenever a government passes a law to, say, discourage smoking, protect the environment or prevent a nuclear catastrophe. Yet that is precisely what thousands of trade and investment treaties over the past half century have done, through a process known as 'investor-state dispute settlement,' or ISDS."); PIA EBERHARDT & CECILIA OLIVET, PROFITING FROM INJUSTICE: HOW LAW FIRMS, ARBITRATORS AND FINANCIERS ARE FUELLING AN INVESTMENT ARBITRATION BOOM 71 (Helen Burley ed., 2012), available at <https://www.tni.org/files/download/profitfrominjustice.pdf> ("As this report shows, investment lawyers have . . . promoted the use of vague language in treaty clauses which increases the scope for investor-friendly interpretation by arbitrators and the chances of disputes[.] tended to approach investment law from an almost exclusively commercial angle rather than public interest, ignoring or even denouncing arguments based on human rights and sustainable development . . . worked alongside speculative investment funds to provide the finance for corporations to bring more cases, at the expense of states and taxpayers. These actions have not only confirmed the pro-corporate bias of current investment agreements, they have tilted the regime even further in the favour of large multinational corporations. The result is a system driven by commercial interests rather than the delivery of justice."). For a different perspective on the preceding report, see Charles N. Brower & Sadie Blanchard, *What's in a Meme? The Truth about Investor-State Arbitration: Why It Need Not, and Must Not, Be Repossessed by States*, 52 COLUM. J. TRANSNAT'L L. 689 (2014).

Nevertheless, even though there is no public outcry against ISDS in the United States, the U.S. Government has expressed wariness at the potential excesses of arbitral tribunals, as evidenced by the joint interpretation of the fair and equitable treatment (FET) provisions of the North American Free Trade Agreement (NAFTA) issued by the United States and its NAFTA partners, Canada and Mexico,¹² and the evolving U.S. Model BIT,¹³ which reflects concern over the expansive views of tribunals that have taken advantage of amorphous concepts, such as FET, to

12. NAFTA Free Trade Commission, *Notes of Interpretation of Certain Chapter 11 Provisions* (July 31, 2001) (“1. Article 1105(1) prescribes the customary international law minimum standard of treatment of aliens as the minimum standard of treatment to be afforded to investments of investors of another Party. 2. The concepts of ‘fair and equitable treatment’ and ‘full protection and security’ do not require treatment in addition to or beyond that which is required by the customary international law minimum standard of treatment of aliens.”).

13. The U.S. Model BIT was amended in 2004 to remove any doubt that FET was never intended to extend beyond the international law minimum standard of treatment. U.S. DEPARTMENT OF STATE, 2004 U.S. MODEL BIT, art. 5 (“2. For greater certainty, paragraph 1 prescribes the customary international law minimum standard of treatment of aliens as the minimum standard of treatment to be afforded to covered investments. 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 that standard, and do not create additional substantive rights.”). In warning against such expansive interpretations of European treaties, the international trade committee of the European Parliament cited the North American experience: “The USA and Canada, which were among the first states to suffer as a result of excessively vague wording in the NAFTA agreement, have adapted their BIT model in order to restrict the breadth of interpretation by the judiciary and ensure better protection of their public intervention domain. The EU should therefore include in all its future agreements a specific clause laying down the right of the EU and [Member States] to regulate. . . . Moreover, standards of protection should be strictly defined, in order to avoid abusive interpretations by international investors. In particular. . . fair and equitable treatment must be defined on the basis of the level of treatment established by international customary law. . . .” European Parliament, Committee on International Trade, *Report on the Future European International Investment Policy (2010/2203(INI))*, at 11–12, Report No. A7-0070/2011 (Mar. 22, 2011), <http://www.europarl.europa.eu/sides/getDoc.do?pubRef=-//EP//NONSGML+REPORT+A7-2011-0070+0+DOC+PDF+V0//EN>. The Canadian Model BIT is to the same effect. Government of Canada, 2004 Canada Model Foreign Investment Promotion and Protection Agreement, art. 5, ¶ 2 (“The concepts of ‘fair and equitable treatment’ and ‘full protection and security’ in paragraph 1 do not require treatment in addition to or beyond that which is required by the customary international law minimum standard of treatment of aliens.”).

extend the scope of investor protection far beyond anything contemplated by contracting states in entering into their treaties.¹⁴ But the key fact is that, despite at least one close call,¹⁵ the United States has not yet experienced a significant setback at the hands of an investor in a treaty claim, and it is hard to get too worked up about excesses of the system when you always win.¹⁶

That does not mean that the United States is immune, although one suspects that it does enjoy certain reputational advantages in ISDS, similar to the impact of star power on a jury. One can easily imagine a day when a massive claim, such as the since-withdrawn 15 billion USD Keystone Pipeline NAFTA claim filed in 2016,¹⁷ will be brought before just the right tribunal to render one of the new-era mega-awards against the United States. That is when the United States, at least if an

14. Andrea Giardina (Rapporteur), *Legal Aspects of Recourse to Arbitration by an Investor Against the Authorities of the Host State under Inter-State Treaties*, INSTITUT DE DROIT INT'L 5–6 (Sept. 13, 2013), http://www.idi-iil.org/app/uploads/2017/06/Question3_Giardina.pdf (“The second fundamental evolution is represented by the fact that starting from the middle of the 2010s, some important capital-exporting States, as the US and Canada, have begun to be respondents in investment arbitration. This has probably been the reason of some changes in the Model BITs adopted by these States, where better consideration is provided for certain public interests of the States.”).

15. See *The Loewen Group, Inc. and Raymond L. Loewen v. United States of America*, ICSID Case No. ARB(AF)/98/3, Award (June 26, 2003); Chris Hamby, *A Homegrown Disaster*, BUZZFEED NEWS (Sept. 1, 2016), <https://www.buzzfeednews.com/article/chrishamby/homegrown-disaster>.

16. The official website of the U.S. Trade Representative proudly proclaims: “Though the U.S. government regularly loses cases in domestic court, we have never once lost an ISDS case and, in a number of instances, panels have awarded the United States attorneys’ fees after the United States successfully defended frivolous or otherwise non-meritorious claims.” *Fact Sheet: Investor-State Dispute Settlement (ISDS)*, OFF. U.S. TRADE REPRESENTATIVE, <https://ustr.gov/about-us/policy-offices/press-office/fact-sheets/2015/march/investor-state-dispute-settlement-isds> (last visited Oct. 17, 2018).

17. *TransCanada Corporation and TransCanada PipeLines Limited v. United States of America*, ICSID Case No. ARB/16/21; Ethan Lou, *TransCanada Formally Seeks NAFTA Damages in Keystone XL Rejection*, REUTERS (June 25, 2016), <https://www.reuters.com/article/us-transcanada-keystone/transcanada-formally-seeks-nafta-damages-in-keystone-xl-rejection-idUSKCN0ZBOR9>. The case was discontinued in March of 2017 after the U.S. Government approved the project. Ethan Lou, *TransCanada Keystone XL Rejection Lawsuit Dropped: Arbitrator*, REUTERS (Mar. 24, 2017), <https://www.reuters.com/article/us-usa-pipeline-keystone-lawsuit/transcanada-keystone-xl-rejection-lawsuit-dropped-arbitrator-idUSKBN16V21G>.

America Firster is still in the White House and the Republicans are still in control of Congress, is likely to join the anti-ISDS fray and pave the way for the dismantling of the system.¹⁸

In the meantime, it cannot be denied that there has been a sea change in the attitude of states toward the system they created in the naïve belief that they were promoting economic development. Years ago, complaints about ISDS fell on deaf ears, even at conferences organized for that purpose. The typical response of states was to brush aside the criticism and defend their treaties as either shining examples of the rule of law or, at worst, necessary evils in the pursuit of the greater good. Today, a conference of state representatives responsible for the defense of investment claims would be largely a forum for venting frustration over self-inflicted wounds and the perceived inability to extricate themselves from long-term treaty commitments.

18. The Trump Administration has given signs that it may want to back away from ISDS in the NAFTA renegotiation. *See, e.g.*, Josh Wingrove & Eric Martin, *U.S. Proposes Gutting Nafta Legal-Dispute Tribunals*, BLOOMBERG (Oct. 14, 2017), <https://www.bloomberg.com/news/articles/2017-10-14/u-s-is-said-to-propose-gutting-nafta-legal-dispute-tribunals> (“For investor-state dispute settlement, presently laid out in Nafta’s Chapter 11, the U.S. wants a system where nations opt in, effectively allowing each country to decide if it will take part. . .”). *See also* Letter from 230 Law and Economics Professors, to President Trump, 230 Law and Economics Professors Urge President Trump to Remove Investor-State Dispute Settlement (ISDS) from NAFTA and Other Pacts (October 25, 2017), *available at* https://www.citizen.org/system/files/case_documents/isds-law-economics-professors-letter-oct-2017_2.pdf. Canada has also expressed deep dissatisfaction with ISDS generally, taking positions similar to the European Union. Robert Howse, *Canada’s NAFTA Renegotiation Objectives-Including Reform of the Investor-State Dispute Settlement Process*, INT’L ECON. L. & POL’Y BLOG (Aug. 14, 2017, 10:40 AM), <http://worldtradelaw.typepad.com/ielpblog/2017/08/canadas-nafta-renegotiation-objectives-including-reform-of-the-investor-state-dispute-settlement-pro.html> (noting that the remarks of Canada’s foreign minister on the renegotiation of NAFTA make it clear that the Comprehensive Economic and Trade Agreement (CETA) is going to be the beginning point of Canada’s negotiating position on most points, but questioning whether the investment court provided for in CETA to replace “discredited traditional investor-state arbitration” may be workable in the NAFTA context given the resistance of the U.S. to the idea of an investment court); Charles-Emmanuel Côté, *An Experienced, Developed Democracy: Canada and Investor-State Arbitration (Paper No. 7)*, in CIGI INVESTOR-STATE ARBITRATION SERIES 1, 27 (July 2016), *available at* https://www.cigionline.org/sites/default/files/isa_paper_series_no.7web.pdf (“A certain ‘de-arbitralization’ and judicialization of [investor-state arbitration] is noticeable in Canadian treaty practice.”).

What explains this sea change? The easy answer is that the number of states that have suffered substantial awards with little or no apparent benefits from the treaties that were supposed to deliver oodles of foreign investment has increased with each passing year; that number never goes down. But this is not just a case of sour grapes. The problem is not that states can and often do lose investment arbitrations; it is that they lose them in a system that lacks credibility.

The list of state gripes about ISDS is long, starting with the fact that they are always the accused, a point that certainly should not have caught them by surprise since that is the object of the system.¹⁹ Some of the gripes can be addressed by tweaking the system. For example, states are generally at a disadvantage from the beginning of a case, when they are often unprepared for the first critical event, the appointment of an arbitrator. There are even occasions where a state is not able to take the bureaucratic steps necessary for the appointment of counsel by the time the tribunal is formed and the first pleading is due, meaning that the state is playing catch-up from the start and running the risk of making strategic mistakes at the outset that invariably affect the course of the entire proceedings.²⁰ These disadvantages, which should not be underestimated, can be somewhat offset by minor adjustments, such as relaxation of the time periods provided by institutional rules for the appointment of arbitrators and the filing of the first pleadings.²¹ They are problems

19. As one professor/arbitrator has pointed out, “to criticize a BIT on the ground that it only gives rights to investors is like criticizing a screwdriver for only being useful for attaching screws.” Vaughan Lowe, *Book Review of “Commentaries on Selected Model Investment Treaties / edited by Chester Brown,”* 30 ICSID REV. — FOREIGN INV. L.J. 275, 276 (2015).

20. The bureaucratic steps often include obtaining the necessary budget to finance the defense of the case, which can be a complicated legal and political process. Many presume that all states have the financial wherewithal to mount forceful defenses, but actual experience does not bear that out. In fact, states are often at a severe disadvantage in defending themselves due to financial constraints, particularly when faced with claims by major private enterprises accustomed to large-scale litigation or third-party funders alleviating the financial burden on claimants.

21. There are important differences among institutional arbitration rules on the timing of appointment of the tribunal. The ICSID Rules of Procedure for Arbitration Proceedings provide a considerably longer period for a state to make its appointment before ICSID will intervene. International Centre for Settlement of Investment Disputes [ICSID], RULES OF PROCEDURE FOR ARBITRATION PROCEEDINGS (2006), available at

with at least partial solutions—not reasons for scrapping the system entirely.

But there are other problems of a far more fundamental nature that cannot be fixed through tweaking. The issue now is no longer whether investor-state arbitration is broken; from the standpoint of states having to defend against the ever-growing number of investor claims, it certainly is. The new question is whether it is so broken that it cannot be fixed without tearing it down and starting over.²²

Let us take another look at some of the more troublesome aspects of ISDS and at why many states are now viewing investment treaties more as weapons of legal destruction than boons for economic development.

I. WHO IS DEVELOPING THIS BODY OF LAW?

The fundamental problems with ISDS are all inter-related, but the analysis starts with the arbitrators who are developing this new body of law. There is no such thing as a perfect judiciary, but most established and respected legal systems make more of an effort than ISDS to approach that goal. ISDS is actually built upon premises that impede rather than promote the objective of a credible legal system. First among those premises is that the interpretation and application of BIT provisions can be

<https://icsid.worldbank.org/en/documents/icsiddocs/icsid%20convention%20english.pdf> [hereinafter ICSID Arbitration Rules]. By contrast, the Rules of Arbitration of the International Chamber of Commerce (ICC) require a respondent, whether it be a state or a private party, to answer the request for arbitration and appoint an arbitrator within thirty days. International Chamber of Commerce, ARBITRATION RULES, art. 5 (2017), available at <https://cdn.iccwbo.org/content/uploads/sites/3/2017/01/ICC-2017-Arbitration-and-2014-Mediation-Rules-english-version.pdf> [hereinafter ICC Rules]. The answer does not have to be very detailed, and extensions are often granted, but they are usually conditioned upon the respondent's appointment of an arbitrator within the thirty-day period, which is simply not practical for a state.

22. See U.N. Conf. on Trade & Dev. [UNCTAD], *Improving Investment Dispute Settlement: UNCTAD Policy Tools*, in 4 IIA ISSUES NOTE: INT'L INV. AGREEMENTS 6, 10 (2017) (noting concerns about ISDS that have been “well-documented in academic and policy literature,” including lack of legitimacy, transparency and consistency, erroneous decisions, concerns over arbitrators' independence and impartiality, and the high cost of arbitrations, and presenting various options for reforming ISDS, including “abolishing the existing system of *ad hoc* investor-State arbitration and replacing it with other mechanisms for settling investment disputes”) [hereinafter *Improving Investment Dispute Settlement*].

entrusted to arbitrators appointed by the parties or by arbitral institutions.

Most important international arbitrations are conducted by tribunals consisting of three arbitrators, one appointed by each side and the third, acting as president of the tribunal, appointed either by an agreement of the party-appointed arbitrators, sometimes with the participation of the parties themselves, or by the arbitral institution administering the process.²³ The debate as to the wisdom of this practice has heated up in recent years, particularly with respect to the advantages and disadvantages of a party's right to appoint an arbitrator.²⁴ It is often said that participants in international dispute resolution, both investor-state and ordinary commercial arbitration, would be uncomfortable in not having the ability to participate in the formation of the tribunal and reluctant to surrender that right to an international institution. The other side of the argument holds that the practice damages the credibility of the arbitral process due to the perception that party-appointed arbitrators consciously or subconsciously feel an obligation to defend the position of the parties appointing them, even though institutional arbitration rules establish the requirements of independence and impartiality for

23. See, e.g., Convention on the Settlement of Investment Disputes Between States and Nationals of Other States art. 37–40, 56, *opened for signature* Mar. 18, 1965, 17 U.S.T. 1270, T.I.A.S. No. 6090, 575 U.N.T.S. 159 [hereinafter ICSID Convention]; ICSID Arbitration Rules, *supra* note 21, Rules 1–5, 7, 11; United Nations Commission on International Trade Law [UNCITRAL], ARBITRATION RULES, arts. 6–10, 14 (Feb. 2014), *available at* <https://www.uncitral.org/pdf/english/texts/arbitration/arb-rules-2013/UNCITRAL-Arbitration-Rules-2013-e.pdf> [hereinafter UNCITRAL Rules]; ICC Rules, *supra* note 21, arts. 12–13, 15; Arbitration Institute of the Stockholm Chamber of Commerce, ARBITRATION RULES, arts. 17, 21 (Jan. 1, 2017), *available at* https://sccinstitute.com/media/293614/arbitration_rules_eng_17_web.pdf [hereinafter SCC Rules]. *Cf.* London Court of International Arbitration, ARBITRATION RULES, art. 5 (Oct. 1, 2014), *available at* http://www.lcia.org/dispute_resolution_services/lcia-arbitration-rules-2014.aspx (in which the default rule is appointment of the tribunal by the LCIA Court).

24. See Jan Paulsson, *Moral Hazard in International Dispute Resolution*, 25 ICSID REV. 339 (2010); Hans Smit, *The Pernicious Institution of the Party-Appointed Arbitrator*, 33 COLUM. FDI PERSP. (2010); Albert Jan van den Berg, *Dissenting Opinions by Party-Appointed Arbitrators in Investment Arbitration*, in LOOKING TO THE FUTURE: ESSAYS ON INTERNATIONAL LAW IN HONOR OF W. MICHAEL REISMAN 821 (M. Arsanjani et al. eds., Koninklijke Brill 2011); Charles N. Brower & Charles B. Rosenberg, *The Death of the Two-Headed Nightingale: Why the Paulsson-van den Berg Presumption that Party-Appointed Arbitrators are Untrustworthy is Wrongheaded*, 29 ARB. INT'L 7 (2013).

all members of the tribunal, including the party-appointed arbitrators.²⁵ This side places too much faith in the arbitral institutions that would make the appointments, faith that neither investors nor states have.

In commercial arbitration, the practice of party appointments is not as serious an issue. In fact, one can readily understand that the objectives of speed and finality override other considerations in the process of resolving a commercial dispute. Compromise among arbitrators does not have the same adverse consequences in commercial arbitration as it does in investor-state arbitration. The legal issues at stake are rarely of importance beyond the confines of the particular arbitration. Few, if any, of the cases involve the public interest, and the overriding interest of the private parties is often simply to reach a result that both sides can live with and that could have been reached through a vigorous process of negotiation or mediation. Under these circumstances, party participation in the formation of a tribunal has few drawbacks and can even be seen as salutary.

The same is not true in investor-state arbitration, where issues of public international law and national sovereignty are at stake. The implications of a legal decision can and often do reach far beyond the confines of the particular arbitration, and the public interest is directly implicated. It is a mistake to superimpose rules of tribunal formation (or other practices) that may be acceptable in the context of private, commercial arbitration onto investor-state arbitration without undertaking a *de novo* analysis of their suitability to the latter.

If one would be starting a system of investor-state dispute settlement from scratch, it would be natural to give serious consideration to the notion that arbitrators who would be called upon to apply fundamental principles of public international law in the context of claims exceeding the gross domestic product of many countries should pass through a serious vetting system. That is not the case today. Arbitrators are not subject to the same scrutiny, for example, as federal judges in the United States or as members of the International Court of Justice. Although some standouts are superbly qualified to perform their

25. ICSID Convention, *supra* note 23, art. 14; UNCITRAL Rules, *supra* note 23, arts. 11–12; ICC Rules, *supra* note 21, art. 11; SCC Rules, *supra* note 23, art. 18.

tasks and have done so admirably, many others are not, have not, and do not even see that as their primary responsibility.²⁶

Even more troubling is the fact that the method of appointment raises questions as to the ability of any arbitrator, no matter how pure his or her motives may be, to render truly objective legal decisions. A national judge with a lifetime appointment and a heavy caseload received by institutional assignment, rather than party appointment, does not lose sleep over the prospect of losing business as a consequence of rendering the right legal decision. By contrast, an arbitrator whose livelihood depends upon party appointments may think twice before rendering a decision that might be upsetting not only to one of the parties involved, but also to the myriad observers who compile lists of arbitrator candidates for future cases. It should be borne in mind that, unlike commercial arbitration, a large percentage of investor-state awards find their way into the public domain and are studied not only in law schools, but by potential litigants looking for trends and arbitrator candidates for future cases. They also do not escape the notice of third-party funders looking to maximize the chances of financial gain on their speculative investments. It takes a heavy dose of integrity and strong-mindedness, and perhaps a healthy balance sheet, to resist that temptation. No legal system should have to rely upon that to produce competent and unbiased tribunals.

The reality is that with few exceptions, usually state parties before they gain the experience that comes with defending cases in the system they created, litigants do their homework in deciding whom to appoint as arbitrators.²⁷ The further unfortunate

26. There is no consensus in the investment arbitration community as to the role of an arbitrator. Some view an arbitrator's responsibility as limited to the dispensing of justice according to the equities of the particular case; others see a systemic dimension to their role and are more concerned with the impact of their decisions on the development of the law. The former is more in line with traditional concepts of arbitration in a private or commercial context, while the latter is more in line with the concept of ISDS as a legal system. For states, the more flexible approach is the more dangerous one, as flexibility leads to ever-expanding interpretations of the scope of investor protection given the manner in which tribunals are formed and the lack of sufficient legal infrastructure to curb that expansion.

27. The exception of states before they experience the reality of investor-state arbitration dynamics can be seen against the background of the manner in which many states naïvely entered into investment treaties. *See supra* note 2. In the early period of investor-state arbitration, states had a tendency to appoint arbitrators having a certain standing in the international arbitration

reality is that the pool of candidates with a clear track record favoring investors in investor-state arbitration is far wider and deeper than the pool of candidates having sensitivity to the interests of states.

There are numerous reasons for this state of affairs, including the fact that many of the prominent players in investor-state arbitration, both institutions and individuals, are grounded in private commercial arbitration rather than in public international law, but the overarching factor is the method of appointment of tribunals. Investors are not looking to appoint arbitrators with sensitivities for states' concerns or even balanced views; nor are they interested in arbitrators' credentials as public international lawyers. What they are looking for are arbitrators who will give them the best chance of winning, and that means arbitrators well-prepared to defend the positions that are favorable to them (whether due to the arbitrator's conception of the role of a party-appointed arbitrator or to his or her legal philosophy) and, where necessary, to break new ground in the field of investor protection. To complete the picture, all you need to do is remember that there are only so many states in the world defending against investor claims, whereas the number of potential claimants is virtually infinite.

Several statistical studies have been done on whether there exists a bias against states in investor-state arbitration. Some focus on the countries of origin of arbitrators, as if an arbitrator from the United States, Canada or Western Europe would tend to favor expansive views of investor protection and those from Asia, Africa or Latin America would be more sympathetic to states' concerns. That kind of study is of limited utility in analyzing the issue of bias in the system, as there are abundant examples of arbitrators espousing exactly the opposite views as what might be expected from such unwarranted generalizations. While nationality can be a consideration in some cases, checking passports is not what is meant by doing one's homework in the appointment process. The question of whether there is bias in the system cannot be answered by counting the number of arbitrators coming from each country or region in the world.

community, without regard for the actual views they held as reflected in their writings or prior decisions. The result was arbitrator appointments by states that in some cases left reasonably informed observers scratching their heads in disbelief. In more recent years, states have been increasingly doing their homework before making appointments.

Equally unconvincing are statistics showing the percentages of cases won by states, however winning is defined. Those studies, frequently held up as clear refutation of charges of bias in the system, are actually a refutation of nothing. The issue is not whether states can ever win in investor-state arbitration. They can and often do—even a majority of the time by some measures. The question is whether the pool, or some say “club,” of arbitrators includes a disproportionate number of members predisposed to stock investor positions. An affirmative answer to that question cannot be avoided simply by pointing to a percentage of cases won by states. A study showing, for example, that states win as many cases as they lose does not mean that the system is in perfect balance, and one showing that 70 percent of cases are won by states is hardly impressive if most of the cases never should have seen the light of day and if a large percentage of them would not have seen the light of day were it not for the speculation of third-party funders promoting litigation in the hope that two of the three arbitrators on their tribunals have strong pro-investor inclinations.²⁸

The fact is that there is a marked bias in the system against states. This author has previously warned that there was a growing perception of bias, and that the perception of bias was as important as actual bias.²⁹ But actual experience, not statistics, indicates that in this case perception and reality are one and the same.³⁰ That is not to say that all arbitrators have a pro-investor bias. Of course, that is not the case. But it is a fact that

28. See Howard Mann, *ISDS: Who Wins More, Investors or States?*, INV. TREATY NEWS (June 2015) (analyzing UNCTAD statistics on wins and losses and concluding: “The balance in the ISDS system cannot be measured by wins and losses alone. The impacts of the current dominant approach to investment treaties and ISDS go well beyond simply a tally of wins and losses. But with these new numbers, at least it can no longer be said, simplistically, that the system is balanced because states win more than investors—they clearly do not when comparing the proper numbers.”).

29. George Kahale, III, *A Problem in Investor/State Arbitration*, 6 TRANSNAT’L DISP. MGMT. (Mar. 2009).

30. In some cases, bias manifests itself at a hearing, where a claimant-appointed arbitrator or, occasionally, even the president of a tribunal intervenes for no apparent purpose other than to assist or rescue counsel. Most arbitrators, however, make a conscious effort to refrain from such interventionism. Some even go out of their way to exhibit sensitivity to the positions of both sides. In the end, the important issue remains whether bias exists, an issue that is not resolved exclusively by reference to an arbitrator’s conduct at a hearing.

states have far more difficulty finding acceptable candidates for arbitrator appointments than those involved in the representation of claimants. It is also a fact that when arbitral institutions are called upon to make the all-important selection of the president of the tribunal, the state respondents hope that the selection will be of an arbitrator with some semblance of neutrality and fear that it would be much worse.³¹

This unsatisfactory situation has become downright dangerous with the advent of the megacase. In the early days of ISDS, billion-dollar claims were pie in the sky. These days they are commonplace.³² Does that mean that states are committing more

31. For an example of an academic study of bias, see Gus Van Harten, *Arbitrator Behaviour in Asymmetrical Adjudication: An Empirical Study of Investment Treaty Arbitration*, 50 OSGOODE HALL L.J. 211 (2012) (“The study examines arbitrator behaviour in the unique context of investment treaty arbitration. It employs the method of content analysis to test hypotheses of systemic bias in the resolution of jurisdictional issues in investment treaty law. Unlike earlier studies, the study examines trends in legal interpretation instead of case outcomes and finds statistically significant evidence that arbitrators favour: (1) the position of claimants over respondent states and (2) the position of claimants from major Western capital-exporting states over claimants from other states. There is a range of possible explanations for the results and further inferences are required to connect the observed trends to rationales for systemic bias. The key finding is that the observed trends exist and that they are unlikely to be explained by chance. This gives tentative empirical evidence of cause for concern about the use of arbitration in this context.”). Such studies are worthwhile, but anyone with extensive experience in the defense of investor claims would not need a formal study to draw the above conclusions.

32. The *Yukos* cases against Russia are an extreme example, with staggering claims of around US\$114 billion and awards totaling in excess of \$50 billion USD, by far the largest in the history of arbitration. *Hulley Enterprises Limited (Cyprus) v. The Russian Federation*, UNCITRAL, PCA Case No. AA 226, Final Award (July 18, 2014); *Yukos Universal Limited (Isle of Man) v. The Russian Federation*, UNCITRAL, PCA Case No. AA 227, Final Award (July 18, 2014); *Veteran Petroleum Limited (Cyprus) v. The Russian Federation*, UNCITRAL, PCA Case No. AA 228, Final Award (July 18, 2014). The *Yukos* awards were set aside on jurisdictional grounds by a court in The Hague, a decision now on appeal. *The Russian Federation v. Veteran Petroleum Limited, Yukos Universal Limited and Hulley Enterprises Limited*, Case Nos. C/09/477160 / HA ZA 15-1, C/09/477162 / HA ZA 15-2 and C/09/481619 / HA ZA 15-112, Judgment (The Hague District Court, Chamber for Commercial Affairs 2016). While the *Yukos* awards are unique, there have been many “smaller” claims that reach the billion-dollar level and even a few other billion-dollar awards in recent years. See Matthew Hodgson & Alastair Campbell, *Damages and Costs in Investment Treaty Arbitration Revisited*, GLOBAL ARB. REV. (Dec. 14, 2017).

and more serious treaty violations causing greater and greater damage, or does it mean that investors and their corps of testifying experts have become more adept at manufacturing stratospheric damage claims out of thin air? Whatever the answer, the point is that in this era of the megacase, there is no room for mistakes, whether they be the product of bias or incompetence. It is not enough to say that the system gets it right most of the time. When so much is at stake, even a single mistake can be catastrophic, and if anything is clear about ISDS, it is that serious mistakes are not hard to find.

II. THE STANDARDS FOR ARBITRATOR CHALLENGES

The second premise governing the formation of arbitral tribunals is that the rigid rules of conflicts applicable in established legal systems need not be applied in international arbitration. This means that relationships most judges in a national legal system would consider problematic are hardly given a second thought in international arbitration. Like the issues discussed above, this is not as serious a problem in commercial arbitration as it is in ISDS. When the overriding objective is to arrive at a reasonable commercial resolution of the dispute at hand, rather than the correct application of legal principles in cases involving the public interest, casual relationships and an inclination to defend the appointing party's position are not as troublesome.

Leaders of international arbitration institutions are aware of this concern, but often feel at a loss to address it. There is a general feeling that the rules governing arbitrator activities and relationships should be more relaxed in international arbitration because it is by definition a less formal and more flexible form of dispute settlement than court procedures, and there is a dearth of competent arbitrators to handle investor-state cases, meaning that an application of rigid rules of conflicts would jeopardize the functioning of the entire system. But formal or not, arbitrators are dealing with matters at least as important and often far more important than the routine matters brought before national courts, and it cannot be the case that there is insufficient talent in the world for the formation of truly impartial and independent tribunals. In any event, practical considerations are not an excuse for relaxed standards that tarnish the credibility of the system. If enough suitable and truly independent and impartial arbitrators cannot be found, the answer is to rethink the

entire system—repeal and replace, to borrow an expression from another field—not to defend it.

Strangely, it is often said that the standards for arbitrator challenges in ICSID arbitration, which by definition is investor-state arbitration, are even stricter than in commercial arbitration.³³ That appeared to be softened somewhat in the *Blue Bank* case, in which the Chairman of the ICSID Administrative Council stressed the importance of the appearance of impartiality in the mind of a reasonable third-party observer.³⁴ But those are only words; they cannot be assessed in the abstract. The proof of the pudding is in the actions and attitudes of the arbitrators, who are the first enforcers of the standards, and in the decisions on challenges. Those decisions evince a still high bar for arbitrator challenges, although perhaps not as high as it once was.

It is useful to compare the practice in the U.S. federal judiciary to international arbitration. On paper, the standards for recusal appear similar, but not so in practice. For example, one of this author's former partners who became a federal district judge would recuse himself from any case in which his former colleagues were to appear as counsel. He followed that rule for decades after taking up his position on the bench—a practice that seems completely alien to international arbitration—because of his concern that there might be a perception of partiality due to the former relationship. Another example familiar to the international arbitration community was provided in the *Yukos* enforcement proceeding in Washington, D.C., where the judge recused herself from the case because of the possibility that her

33. Under Article 57 of the ICSID Convention, a proposal for disqualification should be based on a “manifest lack” of the qualities of independence and impartiality required by Article 14 of the ICSID Convention. ICSID Convention, *supra* note 23, arts. 14, 57.

34. *Blue Bank International & Trust (Barbados) Ltd. v. Bolivarian Republic of Venezuela*, ICSID Case No. ARB/12/20, Decision on the Parties' Proposals to Disqualify a Majority of the Tribunal, ¶¶ 59–60 (Nov. 12, 2013) (“Articles 57 and 14(1) of the ICSID Convention do not require proof of actual dependence or bias; rather it is sufficient to establish the appearance of dependence or bias. The applicable legal standard is an ‘objective standard based on a reasonable evaluation of the evidence by a third party.’”) (emphasis in original). See UNCITRAL Rules, *supra* note 23, art. 12, ¶ 1; DAVID D. CARON & LEE M. CAPLAN, *THE UNCITRAL ARBITRATION RULES: A COMMENTARY* 214 (2nd ed., Oxford Univ. Press 2013) (noting that sustaining a challenge “does not necessarily require proof of an arbitrator’s actual lack of impartiality or independence. The appearance of these deficiencies may alone suffice in certain circumstances to disqualify an arbitrator”) (emphasis in original).

contacts with one of the counsel might give rise to an appearance of impropriety, the contacts being that the two had attended the same bar association events and their children had attended the same school.³⁵ Again, that strict approach is unheard of in international arbitration, where far more extensive contacts are routinely dismissed and often not even disclosed.

There are some arbitrators who, as a matter of policy, will withdraw from a case or refuse to accept an appointment at the slightest hint of dissatisfaction of a party with the arbitrator's impartiality or independence. Others do not. Why they do not is a question only they can answer. There are surely some cases in which withdrawal, even if convenient for the arbitrator, would not be in the interests of justice and would be deleterious to the proper functioning of the system. But in others, the nagging question is whether the arbitrator fights a challenge because of a desire to earn the remuneration that comes with the appointment. The busiest members of the "club" can earn substantial sums in arbitrator fees, more than a judge in a national court system and more than the remuneration of any national or international civil servant, including members of the

35. The judge had disclosed the following:

I knew [counsel] professionally only through many years, through many bar activities. We attended a lot of litigation section meetings together, and those did include dinners and receptions and social activities. And then in the late '90s and early 2000s we had two sons who were in the same private school kindergarten and elementary school class through about fourth grade. We are not close personal friends. We have not socialized, gone out to dinner, gone to each other's homes, although I believe I have been to her home, but only in connection with bar-related activities or school activities. She wrote a letter to the White House on my behalf, supporting my nomination to the bench when it was pending.

Transcript of Telephone Status Conference at 3, *Hulley Enterprises Ltd. et al. v. Russian Federation*, No. 1:14-cv-01996-ABJ (D.D.C. Oct. 29, 2015); Alison Ross, "School Mom" Link Spurs Yukos Judge to Step Down, *GLOBAL ARB. REV.* (Nov. 20, 2015); Petitioners' Motion to Recuse or Disqualify the District Judge and Petitioners' Memorandum of Law in Support of Their Motion to Recuse or Disqualify the District Judge, *Hulley Enterprises Ltd. et al. v. Russian Federation*, No. 1:14-cv-01996-ABJ (D.D.C. Nov. 19, 2015). The standard the judge applied in recusing herself was the following: "Any justice, judge, or magistrate judge of the United States shall disqualify himself in any proceeding in which his impartiality might reasonably be questioned." 28 U.S.C. § 455(a) (2018).

International Court of Justice (for their activities on the Court, not as arbitrators).³⁶ Those fees are not earned by resigning from cases, and there is no guarantee that each case an arbitrator gives up will be immediately replaced with a new appointment. There are those who have reached a stage in their careers and earned a reputation for integrity that makes their judgment on such issues beyond reproach, but not all arbitrators fit neatly into that category, and it is unwise to devise a system that assumes that they do.

In ICSID cases, the procedure for deciding arbitrator challenges is seriously flawed. A proposal to disqualify an arbitrator in an ICSID case is to be decided by the other two arbitrators,³⁷ an understandably unwelcome task. It is always unpleasant to pass judgment on a colleague. The natural tendency of an arbitrator in that position would be to avoid controversy and reject the challenge, or at most, pass the buck to ICSID.³⁸ In addition, one again has to ask whether the possibility of reprisals can cloud one's judgment and overshadow what may be serious questions about the challenged arbitrator's independence or impartiality. That concern is heightened when the deciding arbitrators are either members of the club or seeking entry.

There is one subject on which the disqualification rules and practices of national jurisdictions are more liberal than those of international arbitration: issue conflict. Actually, issue conflict is a non-issue in national courts. The fact that it is a topic of discussion in investor-state arbitration is not a compliment to ISDS; it is a function of one of ISDS's principal shortcomings, the sovereignty of individual arbitral tribunals.

In a mature legal system, judges are not free to render decisions on points of law in accordance with their personal views, without regard to binding precedent. They may disregard precedent, but at the risk of their reputations and reversal on appeal.

36. According to the ICJ website, "Each Member of the Court receives an annual salary consisting of a base salary (which, for 2016, amounts to US\$172,978) and post adjustment, with a special supplementary allowance of US\$15,000 for the President. The post adjustment multiplier changes every month and is dependent on the United Nations exchange rate between the United States dollar and the euro." *Members of the Court*, INT'L CT. JUST., <https://www.icj-cij.org/en/members> (last visited Oct. 17, 2018). Busy arbitrators can earn fees many times that amount.

37. ICSID Convention, *supra* note 23, art. 58.

38. If the two arbitrators do not agree, the decision is to be made by the Chairman of the Administrative Council. *Id.*

A litigant appearing before a judge who has previously rendered a decision on a key point of law and has been reversed on appeal can take comfort in the knowledge that the judge cannot simply disregard the appellate court's ruling. In other words, the fundamental check on the power of individual judges provided by the infrastructure of a developed legal system renders the concept of issue conflict largely moot.³⁹ In investor-state arbitration, where that check does not exist, issue conflict assumes greater importance in the impartiality analysis.⁴⁰

Issue conflict becomes more relevant with each passing day due to the fact that a relatively high percentage of investor-state cases are decided by a relatively small number of arbitrators. That level of concentration, coupled with the high degree of similarity in treaty provisions, means that the chances of an arbitrator having prejudged a key issue are not insignificant. A

39. The recent cases regarding enforcement proceedings for ICSID awards in U.S. federal courts provide a good example of how a mature legal system functions. One federal district court in New York held that an action on an ICSID award, unlike one to confirm an award under the New York Convention, did not require the normal process of a civil action against a foreign state under the U.S. Foreign Sovereign Immunities Act. *Mobil Cerro Negro Ltd. v. Bolivarian Republic of Venezuela*, 87 F. Supp. 3d 573 (S.D.N.Y. 2015). A federal court in the District of Columbia held exactly the opposite. *See Micula v. Gov't. of Romania*, 104 F. Supp. 3d 42 (D.D.C. 2015). On appeal of the *Mobil* case, the Second Circuit Court of Appeals reversed the district court's decision, settling the law on that issue for future cases in the Second Circuit. *Mobil Cerro Negro Ltd. v. Bolivarian Republic of Venezuela*, 863 F.3d 96 (2d Cir. 2017).

40. International Council for Commercial Arbitration [ICCA], *Report of the ASIL-ICCA Joint Task Force on Issue Conflicts in Investor-State Arbitration: The ICCA Reports No. 3*, ¶¶ 15, 159 (Mar. 17, 2016) ("While the notion of issue conflict is not equivalent to impartiality, it rests on concerns about impartiality. Does an arbitrator approach a significant disputed issue with the ability to decide it based on the parties' arguments in the case, and not on the basis of some inappropriate predisposition or prejudice? This aspect of issue conflict is crucial for confidence in the integrity of investment arbitration and, ultimately, for its legitimacy. . . . [T]he most fundamental question underlying concerns about inappropriate predisposition remains how to distinguish between unobjectionable forms of predisposition and those triggering reasonable concerns about bias. It may indeed be that allowing challenges alleging issue conflict can chill useful publication or professional development, or dry up the supply of arbitrators with necessary knowledge and experience, all to the detriment of the investment arbitration system. However, these values relate to the welfare of the system; they operate in a different sphere from a party's right to have a claim decided by an impartial arbitrator. A party in a specific case rightly cares about having her claim fairly decided by an unbiased arbitrator, not about the system's future welfare.").

statistical analysis is not needed to appreciate that the chances of an issue conflict arising are even greater when the tribunal consists of highly experienced arbitrators with track records on issues, such as whether the concept of FET extends beyond the minimum standard of treatment under customary international law, whether and to what extent the minimum standard of treatment has evolved beyond the *Neer* standard,⁴¹ whether and to what extent a most favored nation (MFN) clause may be used to import standards of treatment from other treaties,⁴² and any number of other critical issues that recur in investor-state cases.

Until relatively recently, the possibility of winning an arbitrator challenge based on prior decisions, writings, or public statements was considered remote at best. In *Urbaser v. Argentina*,⁴³ an arbitrator was challenged for issue conflict based on prior writings, not decisions. The two remaining arbitrators—it was an ICSID case—rejected the challenge, obviously sensitive to the fact that the best-known and most experienced arbitrators are likely to have expressed views on key issues on various occasions and that disqualification for issue conflict would create an unwarranted chilling effect and unduly disfavor experienced arbitrators to the benefit of the inexperienced who have not yet pronounced themselves on anything. Importantly, the deciding arbitrators did not reject outright the concept of issue conflict, but decided against disqualification on the facts presented, including the challenged arbitrator's affirmation of his impartiality and willingness to approach the issue with an open mind.⁴⁴

41. *L.F.H. Neer and Pauline E. Neer v. Mexico*, No. 136 (Mexico–U.S. General Claims Commission 1926), in 21 AM. J. INT'L L. 555, 556 (1927) (holding that in order to violate the standard, the treatment of an alien “should amount to an outrage, to bad faith, to wilful neglect of duty, or to an insufficiency of governmental action so far short of international standards that every reasonable and impartial man would readily recognize its insufficiency”).

42. Simon Batifort & J. Benton Heath, *The New Debate on the Interpretation of MFN Clauses in Investment Treaties: Putting the Brakes on Multilateralization*, 111 AM. J. INT'L L. 873 (2018).

43. *Urbaser S.A. and Consorcio de Aguas Bilbao Bizkaia, Bilbao Biskaia Ur Partzuergoa v. Argentine Republic*, ICSID Case No. ARB/07/26, Decision on Claimant's Proposal to Disqualify Arbitrator (Aug. 12, 2010).

44. *Id.* ¶ 44 (stating the test as whether the opinions expressed “are specific and clear enough that a reasonable and informed third party would find that the arbitrator will rely on such opinions without giving proper consideration to the facts, circumstances, and arguments presented by the Parties in this proceeding”). See also ICSID Secretariat, *Possible Improvements of the Framework for ICSID Arbitration*, ¶ 17 (Oct. 22, 2004) (“With the large number of new

It was a different story in *Devas*.⁴⁵ That case involved the interpretation of the “essential security interests” provision of the India-Mauritius BIT. One of the arbitrators had previously chaired three separate tribunals holding that an essential security interests provision simply mirrors the “state of necessity” defense under customary international law.⁴⁶ A second arbitrator had also sat on two of the three cases. All three awards were the subject of annulment proceedings, two of which found that the limitation of specific treaty provisions on essential security interests to the state of necessity defense under customary international law constituted manifest error.⁴⁷ The state challenged the two arbitrators on the ground of issue conflict. The challenge was decided by the then President of the International Court of Justice, acting in his capacity as appointing authority under the BIT. One of the arbitrators was disqualified, as he had

cases, the disclosure requirements for ICSID arbitrators might usefully be expanded. Under the UNCITRAL Arbitration Rules, an arbitrator is required to disclose to the parties any circumstances likely to give rise to justifiable doubts as to his or her impartiality or independence. The relevant ICSID provisions, ICSID Arbitration Rule 6(2) and Article 13(2) of the Additional Facility Arbitration Rules, could be amended similarly to require the arbitrator to disclose, not only any past or present relationships with the parties, but more generally any circumstances likely to give rise to justifiable doubts as to the arbitrator’s reliability for independent judgment. This might in particular be helpful in addressing perceptions of issue conflicts among arbitrators. The ICSID provisions could also be amended to make it clear that the expanded disclosure requirement would apply throughout the entire proceeding and not just at its commencement.”).

45. *CC/Devas (Mauritius) Ltd., Devas Employees Mauritius Private Limited and Telcom Devas Mauritius Limited v. The Republic of India*, PCA Case No. 2013-09.

46. *CMS Gas Transmission Company v. Argentine Republic*, ICSID Case No. ARB/01/8, Award (May 12, 2005); *Sempra Energy International v. Argentine Republic*, ICSID Case No. ARB/02/16, Award (Sept. 28, 2007); *Enron Creditors Recovery Corp. and Ponderosa Assets, L.P. v. Argentine Republic*, ICSID Case No. ARB/01/3, Award (May 22, 2007); U.N. International Law Commission [ILC], *Draft Articles on Responsibility of States for Internationally Wrongful Acts*, art. 25, [2001] 2 Y.B. INT’L L. COMMISSION 31, U.N. Doc. A/56/83.

47. *CMS Gas Transmission Company v. Argentine Republic*, ICSID Case No. ARB/01/8, Decision of the *Ad Hoc* Committee on the Application for Annulment of the Argentine Republic (Sept. 25, 2007); *Sempra Energy International v. Argentine Republic*, ICSID Case No. ARB/02/16, Decision on the Argentine Republic’s Application for Annulment of the Award (June 29, 2010); *Enron Creditors Recovery Corp. and Ponderosa Assets, L.P. v. Argentine Republic*, ICSID Case No. ARB/01/3, Decision on the Application for Annulment of the Argentine Republic (July 30, 2010).

indicated that he continued to hold and publicly defend his strong views on the proper interpretation of essential security interests provisions. By contrast, the other noted the annulment decisions that came after his prior decisions on the issue, affirming that he maintained an open mind. He was not disqualified.⁴⁸

When asked for their observations on challenges to them based on issue conflict, arbitrators with clear track records of decisions on the issue in question tend to make two points: first, that they have a right to their own opinions—the freedom of speech point; and second, that consistency in the application of legal principles is a virtue, not a ground for disqualification. Both observations have superficial appeal. While an arbitrator, like everyone else, has an absolute right to his or her own opinions, that is not the question; the question is whether he or she can sit in the case at hand having prejudged an issue on which the case turns. Similarly, the argument of consistency in the application of the law misses the point, which is that the arbitrator has already determined how he or she will rule on the issue. Whatever the virtues of consistency may be in other contexts, in the context of a challenge for lack of impartiality, a determination to be consistent is an indication that the requisite impartiality is lacking.

III. THE SOVEREIGNTY OF TRIBUNALS

The foregoing is a prelude to the key issue of the sovereignty of individual tribunals. The problems associated with the formation of tribunals and the standards for arbitrator conduct are severe enough, but combined with the fact that there is no clear and uniform mechanism for review of awards in accordance with a uniform body of law, they lead to a system that is progressively losing credibility among the actors that created it.

It is true that investor-state arbitration has some of the trappings of a legal system. After all, lawyers and tribunals alike are still citing legal principles and decisional authority in their voluminous briefs and decisions. Indeed, unlike in national court systems, briefs in international arbitration are out of control,

48. *CC/Devas (Mauritius) Ltd., Devas Employees Mauritius Private Limited, and Telecom Devas Mauritius Limited v. The Republic of India*, PCA Case No. 2013-09, Decision on the Respondent's Challenge to the Hon. Marc Lalonde as Presiding Arbitrator and Prof. Francisco Orrego Vicuña as Co-Arbitrator (Sept. 30, 2013).

often reaching several hundred pages in length.⁴⁹ Much space is devoted in those hundreds of pages to a discussion of precedents. Yet, notwithstanding the fact that many arbitrators are sensitive to the perception of legal chaos and unfairness created by conflicting decisions and make an effort to ground their decisions in precedent, others staunchly defend the principle of arbitrator sovereignty. Cynics argue that arbitrators ground their decisions in precedents where the precedents conform to their views, and have no hesitation in departing from precedents with which they disagree. Of course, whether an arbitrator is making new law is another issue that becomes cloudier with each passing year, which brings new and sometimes incomprehensible decisions resulting either from arbitrators pushing the envelope on investor protection or from compromises among members of the tribunals.

Compromise is inherent in ISDS. What else can be expected from tribunals where two of the three members are appointed by the parties? The tendency to compromise is not merely a function of an arbitrator's inclination to defend the position of the appointing party. It also results from the fact that the party-appointed arbitrators often come from opposite schools of thought or legal philosophy, a natural consequence of the parties' exercising due diligence in making their appointments. Thus, compromise may result from an arbitrator's perception of his or her role as a quasi-party representative or from the perceived necessity to reconcile two genuinely held, conflicting positions.⁵⁰

49. Compare the normal length of a brief in an investor-state case with a brief in a federal district court in the United States, which ordinarily would not exceed 25 pages without leave of court.

50. The perception that unanimity is to be favored in order to enhance the credibility of an award can be a key driver in the decision-making process, but it also is a key driver in producing incomprehensible decisions. One of the grounds for annulment of an ICSID award is that it is not possible "to follow how the tribunal proceeded from Point A. to Point B." *Maritime International Nominees Establishment (MINE) v. Government of Guinea*, ICSID Case No. ARB/84/4, Decision on the Application by Guinea for Partial Annulment of the Arbitral Award, ¶ 5.09 (Dec. 14, 1989); ICSID Convention, *supra* note 23, art. 52. That tends to happen when legal principles are compromised for the sake of maintaining collegiality and achieving unanimity. It has been argued that "annulment committees should not be quick to find contradiction when in fact what is evident from the award is the compromise reached in an international collegiate adjudicative body." *Alapli Elektrik B.V. v. Republic of Turkey*, ICSID Case No. ARB/08/13, Decision on Annulment, ¶ 200 (July 10, 2014). *See also* Gilbert Guillaume, *Failure to State Reasons in ICSID Awards*, in *THE REVIEW*

Either way, the product of the kind of horse-trading it may take to arrive at a decision can make it difficult to follow the reasoning of a decision, which makes it vulnerable to attack and lacking in credibility as a precedent.

It is not the point of this article to catalogue all conflicting decisions in investor-state arbitration. There are many, and they are well-known to members of the international arbitration community. Perhaps the best-known examples are the infamous *CME* and *Lauder* cases, which reached diametrically opposed conclusions within a short period of time in separate arbitrations brought by a corporation and its indirect majority shareholder based on the same facts.⁵¹ The cases are widely considered an embarrassment to ISDS.⁵² More recently, the tribunals in *Mobil v. Venezuela* and *ConocoPhillips v. Venezuela* reached conflicting results in cases arising out of the same nationalization.⁵³

OF INTERNATIONAL ARBITRAL AWARDS 271, 283 (E. Gaillard ed., 2010) (“The same is true where one of the parties alleges that an award is based on contradictory reasons. It is indeed correct to say that truly contradictory reasons cancel each other out and that they are a sign that the award is insufficiently motivated, which in turn should lead to the annulment of the award. However, ‘tribunals must often struggle to balance conflicting considerations and an *ad hoc* Committee should be careful not to discern contradiction when what is actually expressed in a tribunal’s reasons could more truly be said to be but a reflection of such conflicting considerations.”). That kind of justification for incomprehensible awards does not enhance the credibility of ISDS.

51. Ronald S. Lauder v. The Czech Republic, UNCITRAL, Final Award (Sept. 3, 2001); *CME Czech Republic B.V. v. The Czech Republic*, UNCITRAL, Partial Award (Sept. 13, 2001).

52. August Reinisch, *The Proliferation of International Dispute Settlement Mechanisms: The Threat of Fragmentation vs. the Promise of a More Effective System? Some Reflections From the Perspective of Investment Arbitration*, in INTERNATIONAL LAW BETWEEN UNIVERSALISM AND FRAGMENTATION 107, 116 (I. Buffard et al. eds., 2008) (“The ultimate fiasco in investment arbitration occurred in the *Lauder/CME* arbitrations against the Czech Republic.”); August Reinisch, *The Issues Raised by Parallel Proceedings and Possible Solutions*, in THE BACKLASH AGAINST INVESTMENT ARBITRATION 113, 117 (M. Waibel et al. eds., 2010); CAMPBELL MCLACHLAN, LAURENCE SHORE & MATTHEW WEINIGER, INTERNATIONAL INVESTMENT ARBITRATION: SUBSTANTIVE PRINCIPLES ¶ 4.179 (2nd ed., Oxford Univ. Press 2017); Zachary Douglas, THE INTERNATIONAL LAW OF INVESTMENT CLAIMS ¶ 576 (Cambridge Univ. Press 2009); Susan D. Franck, *The Legitimacy Crisis in Investment Treaty Arbitration: Privatizing Public International Law Through Inconsistent Decisions*, 73 FORDHAM L. REV. 1521, 1568 (2005); Chester Brown, *The Relevance of the Doctrine of Abuse of Process in International Adjudication*, 8 TRANSNAT'L DISP. MGMT. 3 (May 2011).

53. *Venezuela Holdings, B.V. et al. v. Bolivarian Republic of Venezuela*, ICSID Case No. ARB/07/27; *ConocoPhillips Petrozuata B.V., ConocoPhillips*

In one case, *Mobil*, the tribunal formed under the BIT between the Netherlands and Venezuela unanimously found that the nationalization was lawful; in the other, a majority of the tribunal, formed under the same treaty, found that Venezuela had breached an obligation to negotiate compensation in good faith.⁵⁴ For present purposes, it is not relevant to delve into the legal analysis of which decision was correct. The material point is that the decisions that were rendered on virtually identical facts are irreconcilable.

The unfortunate reality for states is that on every important issue arising in investor-state arbitration, breaking new ground means expanding the scope of investor protection. This can be seen in the movement to interpret FET clauses as protecting an investor's "legitimate expectations," a concept used by some creative tribunals to fit fact patterns that most treaty negotiators would find standard examples of legitimate state regulation rather than treaty violations.⁵⁵ That is only the most commonly discussed example. Similar remarks can be made about other standard treaty clauses, especially expropriation, full protection and security, MFN and "umbrella" clauses.⁵⁶ What is more

Hamaca B.V. and ConocoPhillips Gulf of Paria B.V. v. Bolivarian Republic of Venezuela, ICSID Case No. ARB/07/30. The author was lead counsel for respondent in both cases.

54. The third arbitrator in the *ConocoPhillips* case, Professor Georges Abi-Saab, resigned for health reasons after rendering two strong dissenting opinions, one on the merits and one on the majority's decision denying an application for reconsideration. *ConocoPhillips Petrozuata B.V., ConocoPhillips Hamaca B.V and ConocoPhillips Gulf of Paria B.V. v. Bolivarian Republic of Venezuela*, ICSID Case No. ARB/07/30, Decision on Respondent's Request for Reconsideration, Dissenting Opinion of Georges Abi-Saab (Mar. 10, 2014); *ConocoPhillips Petrozuata B.V., ConocoPhillips Hamaca B.V and ConocoPhillips Gulf of Paria B.V. v. Bolivarian Republic of Venezuela*, ICSID Case No. ARB/07/30, Decision on Jurisdiction and the Merits, Dissenting Opinion of Georges Abi-Saab (Feb. 19, 2015).

55. As noted earlier, such interpretations by NAFTA tribunals do not coincide with the intentions of any of the three NAFTA states. See NAFTA Free Trade Commission, *supra* note 12.

56. See *Public Statement on the International Investment Regime*, OSGOODE HALL L. SCH. (Aug. 31, 2010), <https://www.osgoode.yorku.ca/public-statement-international-investment-regime-31-august-2010/> ("Awards issued by international arbitrators against states have in numerous cases incorporated overly expansive interpretations of language in investment treaties. . . . This is especially evident in the approach adopted by many arbitration tribunals to investment treaty concepts of corporate nationality, expropriation, most-favoured-nation treatment, non-discrimination, and fair and equitable treatment, all of

difficult to find is a ground-breaking case expanding the scope of sovereign rights and restricting the scope of investor protection in a manner that may credibly be said to be beyond the contemplation of the contracting states in entering into their treaties. Thus, while states hope for decisions that do not depart from their understanding of their own treaties, investors have little fear of a more restrictive view of investor protection and look with optimism at the prospect of an even better outcome with an investor-friendly tribunal, which then is presented as authoritative by other investors in other cases.

The problem is exacerbated by the absence of an effective appellate mechanism for the review of awards. The legal infrastructure of enforcement is designed precisely to prevent appeals, sacrificing the proper dispensing of justice in the interests of finality. For non-ICSID awards, the successful party has available to it conventions, such as the New York Convention, which admits only narrow defenses to recognition and enforcement.⁵⁷ For ICSID awards, the ICSID Convention provides for an annulment procedure, again with narrow grounds for annulment.⁵⁸ Although there have been important decisions granting annulment,⁵⁹ there are also decisions refusing to annul an award that lacked adequate motivation and contained manifest errors of law having a decisive impact on the outcome of the case. The classic example is the *CMS* annulment proceeding following an award against Argentina, where the committee was highly critical of the original award, but refused to annul because of its view of the “narrow and limited mandate conferred by Article 52 of the ICSID Convention.”⁶⁰ Argentina no doubt appreciated the

which have been given unduly pro-investor interpretations at the expense of states, their governments, and those on whose behalf they act.”).

57. Convention on the Recognition and Enforcement of Foreign Arbitral Awards art. 5, June 10, 1958, 21 U.S.T. 2517, 330 U.N.T.S. 3.

58. ICSID Convention, *supra* note 23, art. 52 (improper constitution of the tribunal, manifest excess of powers, corruption on the part of a member of the tribunal, serious departure from a fundamental rule of procedure, or failure to state the reasons on which the award is based).

59. *See, e.g.*, *Venezuela Holdings, B.V. et al. v. Bolivarian Republic of Venezuela*, ICSID Case No. ARB/07/27, Decision on Annulment (Mar. 9, 2017); *Occidental Petroleum Corporation and Occidental Exploration and Production Company v. The Republic of Ecuador*, ICSID Case No. ARB/06/11, Decision on Annulment of the Award (Nov. 2, 2015).

60. *CMS Gas Transmission Company v. Argentine Republic*, ICSID Case No. ARB/01/8, Decision of the *Ad Hoc* Committee on the Application for Annulment of the Argentine Republic, ¶ 158 (Sept. 25, 2007). The annulment

criticism of the award, but presumably would have preferred a simple annulment.

IV. QUANTUM

Pushing the envelope is not a practice limited to the traditional legal questions arising under BITs; it has migrated into the quantum phase of investor-state arbitrations. Quantum is the new battleground in ISDS precisely because it is an area where claimants feel they can put their creativity to best use, given the technical nature of much of the quantum analysis and arbitrators' understandable lack of familiarity with the subject matter.

It should come as no surprise that claimants in any legal system tend to begin their cases with exaggerated claims of compensation, whether it be a personal injury claim of millions of dollars for a coffee spill or a multibillion-dollar expropriation claim. The technique is known as "anchoring."⁶¹ The exaggerated claim is made in the hope that a less exaggerated, but still indefensible amount will seem reasonable by comparison. In a mature legal system with professional judges, there are checks and balances to curb abuse, but in the world of ISDS, the risk of abuse is much higher. That is especially true in cases requiring complex valuations of businesses, often involving natural

committee's criticisms included the following: "[t]he motivation of the Award on this point is inadequate"; "[o]n that point, the Tribunal made a manifest error of law"; "[i]n doing so the Tribunal made another error of law"; "[t]hese two errors made by the Tribunal could have had a decisive impact on the operative part of the Award"; and "[t]hroughout its consideration of the Award, the Committee has identified a series of errors and defects." *Id.* at ¶¶ 125, 130, 132, 135, 158.

61. Lucy Reed, *The 2013 Hong Kong International Arbitration Centre Kaplan Lecture – Arbitral Decision-Making: Art, Science or Sport?*, 30 J. INT'L ARB. 85, 89–90 (2013) ("Arbitrators regularly have to make decisions on the quantum of damages, which is a ripe area for a cognitive bias called 'anchoring.' As Professor Christopher Drahozal of the University of Kansas Law School explains: '[i]n estimating a numerical amount, people tend to start with some initial value – an "anchor" – and then come up with a final estimate by making adjustments to the anchor. If the anchor provides useful information about the underlying value (such as the list price), and if people make reasonable adjustments, this "anchor and adjustment" heuristic can be a useful [decision-making] approach. But anchoring can be problematic if people start with an irrelevant anchor or fail to make adjustments to the initial value.' . . . A lesson for us? Counsel must think carefully about the numbers used in estimating damages in initial requests for arbitration.").

resources, which are typically at issue in investor-state arbitration.⁶²

Years ago, few of the actors in ISDS paid much attention to quantum. That is not surprising considering that the actors are almost exclusively lawyers untrained in economics and business. Many lawyers avoid economic and technical issues like the plague because those issues take them out of their comfort zone. They prefer to concentrate on the legal issues relating to jurisdiction and the merits, happily ceding the technical terrain of quantum to the experts.

In the corporate world, this ostrich approach places the lawyer at a distinct disadvantage in negotiating the business terms of a transaction. Referring economic and technical issues exclusively to the experts runs the risk of key points falling between the cracks and depriving the lead negotiator of the tools he or she needs to gauge the relative importance of the terms under negotiation. There is no point in drafting a perfect clause on a point of minuscule economic significance, particularly when the focus on that clause distracts attention from the main items affecting value.

Likewise, a lawyer's ignorance of the technical aspects of quantum in a litigation or arbitration can prove costly to the client. In some cases, such as those involving direct expropriation, there is no dispute as to the obligation to compensate. Assuming that no jurisdictional issues exist, the entire case revolves around quantum. That includes some legal issues, such as determination of the appropriate valuation date, but it also involves technical and economic issues with which lawyers and arbitrators feel less comfortable. Failure of lawyers to master those issues, or at least converse intelligently in quantum, results in weak cross-examinations of experts and weak presentations to the tribunal, as well as the even more serious error of focusing

62. The gap between claimants' and respondents' valuations tends to be especially large in natural resource cases, particularly those involving oil. In *Mobil v. Venezuela*, for example, the claim according to the claimants' theory of the case exceeded \$20 billion USD. The respondent's analysis yielded a small fraction of that amount. The tribunal awarded approximately US\$1.6 billion for the two projects at issue, plus interest, or less than 10 percent of the claim. *Venezuela Holdings, B.V. et al. v. Bolivarian Republic of Venezuela*, ICSID Case No. ARB/07/27, Award (Oct. 9, 2014). Subsequently, an annulment panel annulled the bulk of the original award, US\$1.4 billion out of the original US\$1.6 billion. *Venezuela Holdings, B.V. et al. v. Bolivarian Republic of Venezuela*, ICSID Case No. ARB/07/27, Decision on Annulment (Mar. 9, 2017).

on points of relatively low value and leaving high-value points unaddressed; failure of arbitrators to do so runs the risk of making monumental economic mistakes.⁶³ Given the other problems inherent in ISDS, states are too often the ones paying the price for such mistakes.

Other than pure questions of law, the most important quantum issues recurring in investor-state cases concern the application of the discounted cash flow (DCF) methodology to value an interest. The object of the DCF methodology is to ascertain the market value of an interest by estimating the future cash flows it is expected to generate and then applying a discount rate to arrive at the net present value of the interest as of the valuation date. The first step in the analysis is obviously projecting net cash flows for the life of the interest being valued, which requires a projection of each of the inputs into those cash flows—operating costs, capital expenditures, taxes, production, sales and prices—not an easy exercise when the period in question is twenty years or even longer, as in some cases. Actual experience and common sense say that even the best of long-term projections will be wrong, the only question being by how much. Under such circumstances, the battle is over the assumptions concerning each of the inputs into the cash flows, any one of which can have a profound impact on value. The potential for abuse is enormous. Presumably, the committee developing the World Bank Guidelines on the Treatment of Foreign Direct Investment had that in mind when it warned that “particular caution should be observed in applying this method as experience shows that investors tend to greatly exaggerate their claims of compensation for lost future profits.”⁶⁴

One of the principal reasons for the proliferation of billion-dollar damage claims in investor-state cases is the ingenuity of claimants in imbuing surrealistic DCF calculations with the appearance of a sound theoretical foundation. In many cases, this involves breaking new ground by convincing tribunals to apply the DCF methodology even in the absence of a track record of

63. In non-bifurcated cases, the parties and the tribunals often have to explore both the legal and the quantum issues in the same hearing, with only a few hours available for complex technical and economic issues that could easily be the subject of weeks of hearings themselves.

64. World Bank Group [WBG], *Legal Framework for the Treatment of Foreign Investment, Volume II: Report to the Development Committee and Guidelines on the Treatment of Foreign Direct Investment* 26 (1992).

profitability of the business or interest being valued, something that the World Bank Guidelines consider inappropriate.⁶⁵ But arbitrators at least are accustomed to dealing with that kind of DCF issue.⁶⁶ What is more problematic, and what arbitrators tend to be less comfortable with, is the determination of the appropriate discount rate where there is no disagreement on the use of DCF.

A basic calculation illustrates the importance of the discount rate. An undiscounted cash flow of \$20 million USD, generated at the rate of one million per year over a twenty-year period, has a present value of \$4.87 million USD when discounted at an annual rate of 20 percent, but when discounted at the rate of 10 percent, the present value is \$8.51 million USD—almost double. That is a scary thought when what is at stake is a billion dollar-plus claim.

Once again, one need not search far and wide for an example that shows that this is not an academic point. In *Gold Reserve v. Venezuela*,⁶⁷ a popular case with claimants in investor-state arbitration, the tribunal applied a 10.09 percent discount rate in valuing a gold mining interest in Venezuela. The result was an award of approximately \$713 million USD. The key factor in the tribunal's decision on discount rate was its approach to the issue of country risk, the element of discount rate analysis that takes into account the reality that the location of an investment has a direct effect on value.⁶⁸ The *Gold Reserve* tribunal applied a

65. *Id.* at 42.

66. *See, e.g.*, Waguih Elie George Siag and Clorinda Vecchi v. The Arab Republic of Egypt, ICSID Case No. ARB/05/15, Award (June 1, 2009); Metalclad Corporation v. The United Mexican States, ICSID Case No. ARB(AF)/97/1, Award (Aug. 30, 2000); Southern Pacific Properties (Middle East) Limited v. Arab Republic of Egypt, ICSID Case No. ARB/84/3, Award on the Merits (May 20, 1992).

67. *Gold Reserve Inc. v. Bolivarian Republic of Venezuela*, ICSID Case No. ARB(AF)/09/1, Award (Sept. 22, 2014).

68. *Himpurna California Energy Ltd. v. PT (Persero) Perusahaan Listrik Negara, UNCITRAL, Final Award*, (May 4, 1999), in 25 Y.B. COM. ARB. 13 (2000) (discussing “the fundamental issue of country risk, obvious to the least sophisticated businessman,” and stating: “The fact remains that it is riskier to enter into a 30-year venture in Indonesia than in more mature economies. And it is no answer to say that the contract has allocated 99% of the risk to the Indonesian side. After all, there are documents which by their terms allot 100% of the risk to the debtor: bonds. Although they may be denominated in US dollars, although they may stipulate absolute obligations to pay, it still makes a difference whether the issuer is Switzerland or Swaziland.”).

country risk premium of only 4 percent in arriving at its discount rate, accepting the approach of the claimant's economic expert in that case. The same economic expert appeared for the claimants in *Tidewater v. Venezuela*,⁶⁹ making the same basic arguments on country risk, this time unsuccessfully, as the tribunal applied a country risk premium—for the same country—of 14.75 percent, arriving at a discount rate of approximately 26 percent. Had the 26 percent discount rate been applied to value the interest in *Gold Reserve* instead of 10.09 percent, the result would have been a fraction of the 713 million USD awarded, a difference of hundreds of millions of dollars. Once again, the decisions are irreconcilable.

V. THE PATH FORWARD

What can be done? That is not an easy question, to say the least.

There are several impediments to any serious attempt to address the problem of ISDS, starting with the fact that not everyone thinks there is a problem. As mentioned earlier, non-governmental conferences on ISDS tend to resemble rallies for the system. To the extent that reform is on the agenda, the issues tend to be how to speed up the process, how to minimize review of awards, how to expand the substantive protections of investors, and how to persuade tribunals to accept approaches to quantum that make extraordinary damage awards commonplace. There is no point in arguing the demerits of ISDS in that environment.

That is not to say that there is no serious thinking going on about the deficiencies of ISDS. The European Commission deserves much credit for focusing on the weaknesses of the system and pushing for reform.⁷⁰ Thoughtful analyses have been made and proposals advanced by prominent participants in ISDS,⁷¹

69. *Tidewater Investment SRL and Tidewater Caribe, C.A. v. Bolivarian Republic of Venezuela*, ICSID Case No. ARB/10/5, Award (Mar. 13, 2015).

70. *See supra* note 9.

71. *See, e.g.*, Gabrielle Kaufmann-Kohler & Michele Potestà, *Can the Mauritius Convention Serve as a Model for the Reform of Investor-State Arbitration in Connection with the Introduction of a Permanent Investment Tribunal or an Appeal Mechanism?*, GENEVA CENTER INT'L DISP. SETTLEMENT 15 (June 3, 2016); Gabrielle Kaufmann-Kohler & Michele Potestà, *The Composition of a Multilateral Investment Court and of an Appeal Mechanism for Investment Awards*, GENEVA CENTER INT'L DISP. SETTLEMENT (Nov. 15, 2017). Not all members of the arbitration community are on board with the reform movement. *See, e.g.*, Brower & Blanchard, *supra* note 11; Charles N. Brower, Michael

and now we have UNCITRAL, in a radical departure from its past activities, taking up the politically charged question of ISDS with the following broad mandate: “The Working Group would proceed to: (i) first, identify and consider concerns regarding ISDS; (ii) second, consider whether reform was desirable in light of any identified concerns; and (iii) third, if the Working Group were to conclude that reform was desirable, develop any relevant solutions to be recommended to the Commission.”⁷² But it is one thing to consider adjustments to the UNCITRAL Rules falling within the category of tweaking, and quite another to address a subject as controversial as the need to overhaul ISDS. Indeed, much of the recent meeting of delegates in Vienna was spent arguing about who would chair the working group.⁷³ That was a sure sign of deep division between those looking for radical reform and those willing to consider tweaks to the system without altering its basic character.

It may be premature to forecast the failure of these efforts. After all, they are just getting underway, and there are strong forces pushing for reform. But the odds are against success for many reasons, starting with the practical reality that the odds are never in favor of reaching a satisfactory result in a group so large, with interests so disparate.⁷⁴ Some reform—or change labeled as reform—may come, but in all likelihood only after years of negotiation and consensus-building. In the meantime, the existing system, which poses a clear and present danger to states and the public interest, will continue to operate and deteriorate.

Most of the proposals for reform revolve around the incorporation of an appellate mechanism in ISDS or the creation of an

Pulos & Charles B. Rosenberg, *So Is There Anything Really Wrong with International Arbitration As We Know It?*, in CONTEMP. ISSUES INT'L ARB. & MEDIATION: FORDHAM PAPERS 3 (A. W. Rovine ed., Brill 2013).

72. UNCITRAL, Report of Working Group III (Investor-State Dispute Settlement Reform) on the Work of Its Thirty-Fourth Session (Vienna, 27 November–1 December 2017), ¶ 6, U.N. Doc. A/CN.9/930 (Dec. 19, 2017) [hereinafter Report of Working Group III].

73. See Anthea Roberts, *UNCITRAL and ISDS Reform: Not Business as Usual*, EJIL: TALK! (Dec. 11, 2017), <https://www.ejiltalk.org/uncitral-and-isds-reform-not-business-as-usual/>; Alison Ross, *UNCITRAL Celebrates 55th After Tense Talks on ISDS Reform*, GLOBAL ARB. REV. (Dec. 11, 2017).

74. In the past, when states were of one mind with lawyers, arbitrators and investors in promoting ISDS, the chances of reaching consensus on changes were not as slim. Now that states are not seeing their interests as aligned with the other actors in the system, agreement on major change will not come easily.

international investment tribunal. Those proposals do address a number of ISDS deficiencies discussed herein, but the issues requiring consensus before implementation could begin are legion, running the gamut from the formation and composition of the appeals boards or permanent tribunals to the scope of their authority and the impact of their decisions. There is no need to catalogue here those daunting issues, which are well-known to experts in the field. Suffice it to say that each one of them will generate countless hours of debate and countless conflicting opinions that will somehow have to be reconciled, and that is after consensus is reached on the concept of an appellate mechanism or an international investment tribunal, which does not exist today even within the reform community.

More importantly, one has to question whether the outcome of this reform process, even if “successful,” would be worth the investment of time and effort necessary to achieve it. Assuming that agreement can be reached among all the stakeholders on an appellate mechanism or an international investment tribunal, it cannot simply be presumed that the result would be an improvement over today’s ISDS.⁷⁵ It is entirely possible that the law of unintended consequences would strike yet again and that states would find that they had constructed a new and even more dangerous system on top of the old, like building a new floor on a

75. The term “stakeholders” is used to refer to the broad community involved in ISDS, not just states. That in and of itself is good reason for states to beware of any reform. States were encouraged to send government officials to participate in UNCITRAL’s Working Group III, but private practitioners were still involved. UNCITRAL, Annotated Provisional Agenda, ¶ 10, U.N. Doc. A/CN.9/WG.III/WP.141 (Sept. 15, 2017) (“In line with the UNCITRAL process, Working Group III would, in discharging that mandate, ensure that the deliberations, while benefiting from the widest possible breadth of available expertise from all stakeholders, would be government-led with high-level input from all governments, consensus-based and be fully transparent.”). A definition of “stakeholder” is “one who is involved in or affected by a course of action.” *Stakeholder*, MERRIAM-WEBSTER, <https://www.merriam-webster.com/dictionary/stakeholder> (last visited Oct. 17, 2018). That definition encompasses investors or investor groups and states, but some would say arbitral institutions, arbitrators, lawyers, non-governmental organizations, international organizations, third-party funders and others are included as well. See Pieter H. F. Bekker, *Recalibrating the Investment Treaty Arbitration System Through Non-Compartmentalized Legal Thinking*, 55 HARV. INT’L L.J. ONLINE 1, 3–4 (Dec. 2013). It is fair to say that many of those stakeholders are not looking for the same kind of reform as states that are disillusioned with ISDS, and they are joined by a number of states that are still more interested in preserving ISDS than reforming it.

house with a shaky foundation. If that possibility becomes reality, states will again be clamoring for a do-over within a few years after the “successful” reform sets in. Reformists would therefore be well advised to heed the old warning: “Be careful what you wish for.”

These observations are not meant to discourage discussion of reform. It is always good to shine a light on the problem—the brighter the better—as long as the focus is clear and success is not defined as the achievement of an even more robust ISDS, incorporating and institutionalizing the principal vices that are confounding and threatening states. The concern is that too much effort will be invested in debating and designing mechanisms that will either never come into being or be of dubious value, or even harmful, if they do, the inevitable result of compromise between diametrically opposed views. States need to recognize that the reform movement, with its focus on appellate mechanisms and standing international tribunals to the exclusion of the substantive principles to be applied, is not a panacea for ISDS, and that putting all their eggs in the reform basket may turn out to be a recipe for disaster.⁷⁶

76. See *Improving Investment Dispute Settlement*, *supra* note 22, at 3 (“Reform of investment dispute settlement cannot be viewed in isolation; it needs to be synchronized with reform of the substantive investment protection rules embodied in IIAs. Without a comprehensive package that addresses both the substantive content of IIAs and ISDS, any reform attempt risks achieving only piecemeal change and potentially creating new forms of fragmentation and uncertainty.”). The reform proposals under discussion in UNCITRAL Working Group III make clear that they do not address the substantive body of law that has been developing through the flawed ISDS system. As the December 19, 2017 Report of the recent session of the Working Group in Vienna states: “It was also recalled that ISDS provided a method to enforce the substantive obligations of States. It was noted that critical questions on possible ISDS reform involved the underlying substantive rules. Nonetheless, it was clarified that the mandate given to the Working Group focused on the procedural aspects of dispute settlement rather than on the substantive provisions.” Report of Working Group III, *supra* note 72, ¶ 20. The thinking behind this approach seems to be that experience shows that attempts to reach agreement on substantive issues are doomed to failure. That may be true if the effort is all-encompassing both in terms of the range of issues addressed and the states involved, but it should not be true with respect to individual issues, individual states and individual treaties, where progress would be both useful and feasible. In any event, an inability to restore order on the substance should not be an excuse for designing legal infrastructure that runs the risk of institutionalizing legal principles that have no legitimate foundation.

As noted earlier, the question now is whether ISDS is too broken to be fixed. If so, a conclusion more and more states are reaching, then the focus should be on dismantling the system, not reforming it.⁷⁷ That is not an easy task, as the system is built to last. The thousands of investment treaties that are the backbone of the system are long-term in nature, and even when they are terminated, they have long tails, covering existing investments for years after termination, which is one of the main stumbling blocks to reform of the system.

Nevertheless, at some point states will have to decide whether to take matters into their own hands and at least attempt to undo the system they created. A good start would be to put a freeze on any new investment treaties (or investment chapters in trade agreements). The existing web of treaties is bad enough. Why make matters worse with new treaties? Unless and until the fundamental deficiencies of ISDS can be addressed satisfactorily and a credible system of dispute settlement emerges, investment treaties will continue to be weapons of legal destruction that should be the subject of anti-proliferation policies. To borrow an expression associated with Nancy Reagan, states should “Just Say No” when it comes to new investment treaties. In the exceptional case where a compelling argument can be made for entering into a new treaty, care should be taken to clearly circumscribe the protections offered and avoid language that can easily be distorted. Most importantly, MFN clauses should be avoided, as they can be misused to transform carefully negotiated provisions into unintended, sweeping protections. The expression that best fits MFN clauses is “high risk, low [or no] reward.”

Once the bleeding is stopped, attention should be turned to the small matter of the three thousand-plus existing treaties. There a multipronged approach is in order. First, it would be advisable for states to explore the possibility of reaching agreements with their counterparties on termination, together with an

77. Dismantling ISDS does not mean erasing principles of international responsibility of states. It simply means that investors would not have direct access to international arbitration to assert international law claims. The practice of espousal of claims would remain, and other alternatives, including state-to-state arbitration, could be pursued. At some point, starting with a clean slate based on a well-defined set of legal principles, a new ISDS might emerge, with all the checks and balances of a credible legal system, but it is doubtful that such a system can be built upon the foundation of the current ISDS.

amendment to their treaties' sunset provisions.⁷⁸ Second, where treaties cannot be terminated by mutual agreement, or states feel that there actually are perceptible benefits from particular treaties making them worthy of preservation, consideration should be given to opening discussions with the counterparties to discern the possibility of eliminating or modifying especially troublesome provisions or reaching agreement on interpretations to guide the tribunals applying them.⁷⁹ The NAFTA parties paved the way for that approach with their interpretation of NAFTA's FET provisions.⁸⁰ More recently, other countries have

78. Whether existing treaties can be amended to alter or cut off protections for existing investments is an interesting legal question. Some may argue that investors are third-party beneficiaries whose rights cannot be taken away even if the contracting states purport to do so, but there are stronger arguments in favor of the view that the parties to a treaty may exercise their right to amend the treaty in any way they see fit, either in accordance with the treaty's amendment provisions or under the law of treaties embodied in the Vienna Convention. Vienna Convention on the Law of Treaties arts. 37, 39, May 23, 1969, 1155 U.N.T.S. 331 [hereinafter VCLT] (Article 37: Revocation or Modification of Obligations or Rights of Third States; Article 39: General Rule Regarding the Amendment of Treaties). See Anthea Roberts, *Triangular Treaties: The Extent and Limits of Investment Treaty Rights*, 56 HARV. INT'L L.J. 353 (2015); Tanya Voon, Andrew Mitchell & James Munro, *Parting Ways: The Impact of Mutual Termination of Investment Treaties on Investor Rights*, 29 ICSID REV. 451 (2014).

79. See VCLT, *supra* note 78, art. 31, ¶ 3 (Article 31: General Rule of Interpretation, ¶ 3 states "There shall be taken into account, together with the context: (a) Any subsequent agreement between the parties regarding the interpretation of the treaty or the application of its provisions . . .").

80. NAFTA Free Trade Commission, *supra* note 12. FET is only the most obvious of the issues on which one might expect broad agreement among states. MFN is another, as it should not be too difficult to reach agreement on eliminating the concept or at least clarifying that it should not be used to import standards of treatment from other treaties, much less consents to arbitration. The entire concept of MFN is unsuitable for investment treaties, just as it is unsuitable for any private contract. Aside from substantive legal principles, other important issues that could be tackled individually include the standards to be applied for arbitrator challenges and the role of third-party funders in ISDS. As discussed earlier, the lax standards of conflicts for arbitrators damages the credibility of ISDS, and the proliferation of cases financed by third-party funders has transformed ISDS into a marketplace for a new type of investment that was not the object of protection under investment treaties. Finally, bearing in mind the danger of abuse in connection with quantum in investor-state arbitration, it would be worth addressing some of the recurring quantum issues that have become the object of much creativity in recent years, including discount rate and interest rate.

taken that path.⁸¹ An intermediate step would be to publish unilateral interpretations setting forth the state's understanding of individual provisions of its BITs.⁸² Finally, if agreement cannot be reached on termination, modification or interpretation, states should examine their treaties to determine their expiration dates, renewal provisions, automatic or not, and whether there are any provisions for early termination, with a view toward taking the necessary steps to ensure termination at the earliest opportunity.

On a broader scale, one can envision opening a multilateral convention not just for procedural issues, but to clarify and declare what states think the law is or should be on basic points. Success in this approach is less likely than in the less ambitious approach of addressing substantive issues bilaterally, but each success on the smaller scale is helpful in attaining the objective on the broader scale, particularly if the temptation to strive for consensus on all issues at once is resisted and the focus is placed on the most problematic individual issues, one at a time.

81. Jarrod Hepburn, *Unable to Unilaterally Terminate a 2011 BIT, the Government of India Persuades Counter-Party to Agree Joint Interpretive Note to Clarify BIT's Implications*, INV. ARB. REP. (July 17, 2017); Douglas Thomson, *India's BIT Recast Continues*, GLOBAL ARB. REV. (July 19, 2017). For this purpose, it would be helpful if the treaty itself contained a provision declaring interpretations by the contracting parties to be binding. See U.S. DEPARTMENT OF STATE, 2012 U.S. MODEL BIT, art. 30, ¶ 3 ("A joint decision of the Parties, each acting through its representative designated for purposes of this Article, declaring their interpretation of a provision of this Treaty shall be binding on a tribunal, and any decision or award issued by a tribunal must be consistent with that joint decision."). Even if it does not, such interpretations can be effective. See *Question of Jaworzina (Polish-Czechoslovakian Frontier)*, Advisory Opinion, 1923 P.C.I.J. (ser. B) No. 8, at 37 (Dec. 6, 1923) ("[I]t is an established principle that the right of giving an authoritative interpretation of a legal rule belongs solely to the person or body who has power to modify or suppress it."). UNCITRAL Working Group III or any other large and unwieldy group may not be the ideal forum to achieve agreement on the proper interpretation of basic substantive concepts recurring in investment treaties; one-on-one discussions may be a more fruitful avenue. It is also not a good idea to hold up conclusions on individual issues pending agreement on all issues. Progress on individual issues is of value and can spur progress on others.

82. See Ministry of Finance, Department of Economic Affairs, Investment Division, Office Memorandum: Issuance of Joint Interpretative Statements for Indian Bilateral Investment Treaties, F. No. 26/07/2013-IC (Feb. 8, 2016) (India), available at http://indiainbusiness.nic.in/newdesign/upload/Consolidated_Interpretive-Statement.pdf.

CONCLUSION

In sum, it is high time for states to take action on many fronts. First and foremost, they will have to decide once and for all whether to celebrate the system they created, to reform it, or to consider it an egregious error and tear it down. The first option is no longer in vogue. The second is unlikely to prove fruitful. The third, which may be the most difficult, is increasingly viewed by states as the most appealing, and with good reason.