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### Challenges Facing Investment Disputes: Reconsidering Dispute Resolution in International Investment Agreements

Susan Franck

*American University Washington College of Law, sfranck@wcl.american.edu*

Karl P. Sauvant

*Columbia Program on International Investment, Columbia Law School*

Michael Chiswick-Patterson

Rainer Geiger

José E. Alvarez

*See next page for additional authors*

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#### Recommended Citation

Franck, Susan; Sauvant, Karl P.; Chiswick-Patterson, Michael; Geiger, Rainer; Alvarez, José E.; Sornarajah, M.; Juillard, Patrick; Salacuse, Jeswald W.; Sacerdoti, Giorgio; Joubin-Bret, Anna; Díaz, Hugo Perezcano; Tracton, Michael K.; Schreuer, Christoph; Mann, Howard; Yannaca-Small, Katia; Legum, Barton; Paulsson, Jan; Qureshi, Asif H.; Khan, Shandana Gulzar; Brummer, Christopher; and Rapier, Brian J., "Challenges Facing Investment Disputes: Reconsidering Dispute Resolution in International Investment Agreements" (2008). *Contributions to Books*. 309.

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## Authors

Susan Franck, Karl P. Sauvart, Michael Chiswick-Patterson, Rainer Geiger, José E. Alvarez, M. Sornarajah, Patrick Juillard, Jeswald W. Salacuse, Giorgio Sacerdoti, Anna Joubin-Bret, Hugo Perezcano Díaz, Michael K. Tracton, Christoph Schreuer, Howard Mann, Katia Yannaca-Small, Barton Legum, Jan Paulsson, Asif H. Qureshi, Shandana Gulzar Khan, Christopher Brummer, and Brian J. Rapier

# Appeals Mechanism in International Investment Disputes

**Karl P. Sauvant, Editor**



# Appeals Mechanism in International Investment Disputes

Edited by

**Karl P. Sauvant**

*Columbia Program on International Investment,  
Columbia Law School*

with

**Michael Chiswick-Patterson**

**OXFORD**  
UNIVERSITY PRESS

**OXFORD**

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198 Madison Avenue, New York, New York 10016

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Library of Congress Control Number:

Appeals mechanism in international investment disputes / edited by Karl P. Sauvant.

p. cm.

Includes bibliographical references and index.

ISBN: 978-0-19-534156-0 (alk. paper) 1. Investments, Foreign (International law) 2. Dispute  
resolution (Law) 3. Arbitration and award, International. I. Sauvant, Karl P.

K3830.A64 2008

346.07--dc22

2007050084

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WASHINGTON AND LEE  
UNIVERSITY  
SCHOOL OF LAW  
Sydney Lewis Hall  
Lexington, VA 24450

**Washington & Lee Public  
Legal Studies Research Paper Series #1427590**

**Accepted Paper 2008**  
February 12, 2008

**“Challenges Facing Investment Disputes:  
Reconsidering Dispute Resolution in  
International Investment Agreements”**

**Susan Franck**

**Accepted Paper**

**APPEALS MECHANISMS IN INTERNATIONAL INVESTMENT DISPUTES,  
KARL P. SAUVANT, ED., OXFORD UNIVERSITY PRESS, 20082**

## CHAPTER 9

# Challenges Facing Investment Disputes: Reconsidering Dispute Resolution in International Investment Agreements

*Susan D. Franck\**

Henry Ward Beecher once observed, “[l]aws and institutions are constantly tending to gravitate ... [and] [l]ike clocks, they must be occasionally cleansed and wound up, and set to true time.”<sup>1</sup> Beecher’s comments reflect that, as law, societies and governments evolve, there are inevitably challenging transitional periods that require a re-examination of the foundations upon which a system was founded. Dispute resolution systems are no different. When they undergo fundamental growth, a re-consideration of the system’s efficacy and utility can promote both its integrity and legitimacy to ensure it provides appropriate services to its stakeholders.<sup>2</sup>

International investment law has experienced a particular growth. While the number of bilateral investment treaties (BITs) expanded in the past four decades,<sup>3</sup>

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\* Assistant Professor of Law, University of Nebraska College of Law. Email: sfranck2@unl.edu.

<sup>1</sup> Henry Beecher, *Life Thoughts, Gathered from the Extemporaneous Discourses of Henry Ward Beecher* (Philips, Sampson and Company: 1858), p. 129.

<sup>2</sup> For the purposes of this chapter, the word “stakeholder” is intended to refer to those persons or entities either directly or indirectly affected by investment-related conflicts. Stakeholders most commonly take the form of home countries, host countries, investors and the citizens of host countries.

<sup>3</sup> “Bilateral Investment Treaties in the mid-1990s,” UNCTAD/ITE/IIT/7, Sales No. E.98.II.D.8 (1998) [Hereinafter UNCTAD 1998].

there has also been a more recent growth of disputes arising under these agreements.<sup>4</sup> Unsurprisingly, the escalation in the availability and use of the dispute resolution process has led to a teething period. The boundaries of States' previously untested international law obligations are being sketched; and parties and non-parties have both cheered and jeered the efficacy, efficiency and fairness of the system for resolving investment disputes. Given these developments, the system may have evolved to the point where it would be useful to clean the proverbial clock.

This chapter explores, on a preliminary basis, how “dispute systems design” could aid the dispute resolution process in investment treaties and permit stakeholders to make a more informed choice about their dispute resolution options. In other words, it considers whether the resolution of investment-treaty disputes might be re-designed to minimize the cost of conflict and maximize its beneficial byproducts. It first discusses the role of conflict and the design of dispute resolution systems. Given the potential insights from dispute systems design, it next assesses the unexplored or under-explored utility of dispute resolution options along the dispute resolution continuum. The chapter concludes by suggesting that a systematic greater consideration of dispute systems design is needed in order to diagnose accurately what the system requires and generate a set of principles to guide the design process. The hope of such an endeavor would be to develop an effective, efficient, fair and legitimate process for resolving investment treaty conflict.

## Conflict, Dispute Systems Design and Investment Treaties

### Reconsidering Conflict

In the classic formulation, conflict is like water. It occurs naturally and, although its structure can be transformed, it will continue to exist. Despite its social connotation, conflict is not *per se* good or evil. Rather, it is necessary for institutions to survive, thrive and develop. Nevertheless, extreme circumstances—whether a flood or a drought—can have serious repercussions on effective development.<sup>5</sup>

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<sup>4</sup> “Research Developments in International Investment Agreements,” UNCTAD Research Notes, UNCTAD/WEB/ITE/IIT/2005/1, 30 August 2005 ([http://www.unctad.org/sections/dite\\_dir/docs/webiteit20051\\_en.pdf](http://www.unctad.org/sections/dite_dir/docs/webiteit20051_en.pdf)) [Hereinafter UNCTAD 2005a], pp. 1–3, 13–15; and “Investor-State Disputes Arising from Investment Treaties: A Review,” UNCTAD/ITE/IIT/2005/4, ([http://www.unctad.org/en/docs/iteiit20054\\_en.pdf](http://www.unctad.org/en/docs/iteiit20054_en.pdf)) [Hereinafter UNCTAD 2005b], pp. 4–6.

<sup>5</sup> Cathy Costantino and Christina Sickles Merchant, *Designing Conflict Management Systems: A Guide to Creating Productive and Healthy Organizations* (Jossey-Bass: 1996) [Hereinafter Costantino and Merchant 1996].

This applies with equal force in the context of international investment.<sup>6</sup> Conflict between investors and host country governments can occur when there is dissatisfaction with an interaction, process or result. Conflict can be a positive force, however. For investors, it can create opportunities for commercial innovations, and governments can use it as an occasion to adapt how they legislate and regulate those they govern.

When conflicts do arise, they can often be addressed informally without the threat of legal sanctions—often because of personal relationships, the ability to adapt business models or regulatory discretion that permits parties to address their underlying needs and interests. These informal processes can fail, however, and conflict can crystallize as a formal dispute. At either the formal or informal stage of conflict management, having a properly designed dispute resolution system can constructively draw conflict to the surface, channel its productive forces and avoid potentially more destructive by-products.

### Approaches to Dispute Resolution

There is a robust literature dedicated to designing disputing systems to manage conflict.<sup>7</sup> This systematic approach to dispute resolution has been surprisingly effective in reducing the negative by-products of conflict. Part of using dispute systems design effectively, however, is to understand the different approaches to dispute resolution.

In their pioneering work on dispute systems design, Ury, Brett and Goldberg articulated a systematic way of looking at dispute resolution procedures. It identified three fundamental approaches parties can use to resolve disputes: (1) using *power* (in the form of violence, war, strikes) to impose a solution; (2) relying on *legal rights* to determine the merits of parties' positions; and (3) focusing on parties underlying *interests* to create mutually acceptable

<sup>6</sup> J.G. Merrills, *International Dispute Settlement*, 4th Edition (Cambridge University Press: 2005) [Hereinafter Merrills 2005], p. 1.

<sup>7</sup> Costantino and Merchant, 1996; Allan J. Stitt, *Alternative Dispute Resolution for Organizations: How to Design a System for Effective Conflict Resolution* (Wiley: 1998) [Hereinafter Stitt 1998]; William L. Ury, Jeanne M. Brett and Stephen B. Goldberg, *Getting Disputes Resolved: Designing Systems to Cut the Costs of Conflict* (Jossey-Bass: 1988) [Hereinafter Ury et al. 1988]; see also Susan D. Franck, "Integrating Investment Treaty Conflict and Dispute Systems Design," 92 MINN. L. REV. 161 (2007) ([http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=969252](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=969252)) [Hereinafter Franck 2007].

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solutions that meet parties' needs. Ury et al. expressed a general preference for interest-based dispute resolution as it tends to reduce transaction costs, improve satisfaction with the result and decrease the probability that disputes will recur. Nevertheless, they acknowledged that there are circumstances when resolving disputes on the basis of rights or power may be necessary—or simply desirable—particularly where uncertainty about the boundaries of parties' legal rights inhibits negotiation, or when a fundamental societal value is at stake.<sup>8</sup> Later scholars have suggested that many dispute resolution systems might start with power-based dispute resolution methods, but they eventually move toward a more rights-based methodology and ultimately evolve to interest-based conflict management.<sup>9</sup>

Having articulated these primary approaches to resolving disputes, Ury and his colleagues suggested that institutions create effective conflict management systems by engaging in: (1) diagnosis of the current system, (2) creation of a dispute resolution system according to practical principles,<sup>10</sup> (3) implementation

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<sup>8</sup> Ury et al. 1988, pp. 4–17.

<sup>9</sup> Costantino and Merchant 1996, pp. 49–54.

<sup>10</sup> Originally, Ury et al.'s principles related to: (1) focusing on interests to encourage the use of interest-based dispute resolution, (2) providing loop-backs to make procedures available that allow parties to return to lower-cost dispute resolution methods, (3) providing low-cost interest-based rights and power or rights-based procedures if the interest-based ones fail, (4) building in consultation before and after disputes, (5) arranging the procedures in a low-to-high cost sequence, and (6) providing the motivation, skills and resources necessary to ensure that the procedures are supported (Ury et al. 1988). Others have since developed different, but related, principles.

Costantino and Merchant, for example, use six different guiding principles including: (1) developing guidelines for whether ADR is appropriate, (2) tailoring the ADR process to the particular problem, (3) building-in preventative methods of ADR, (4) making sure that disputants have the necessary knowledge and skill to choose and use ADR, (5) creating ADR systems that are simple and easy to use and resolve the disputes early, at the lowest organizational level, with the least bureaucracy, and (5) allowing disputants to retain maximum control over choice of ADR method and the selection of a neutral. (Costantino and Merchant, 1996).

Shariff has continued this analysis in an international context and suggests analyzing issues of membership, scope, centralization, control and flexibility. He suggests these issues should be considered in conjunction with the following principles, namely that institutions should: (1) strive for inclusiveness by incorporating into their structure all stakeholders likely to be affected by the institution's work, (2) seek broad coverage of many related issues of interest to the institutional membership rather than being limited to a specific or narrow issue area, (3) seek depth of jurisdiction on individual issues areas such that they are empowered to take many kinds of action on issues within their mandate, (4) seek to build central sources of information gathering and dissemination, (5) decentralize and proliferate discussions and conversations among institutional members in multiple forums and forms, (6) vest control over decisions in those most interested and affected by them, and (7) embed opportunities for regular review of principal design decisions in order to integrate learning from experience (Khalil Z. Shariff, "Designing Institutions to Manage Conflict: Principles for the Problem Solving Organization," 8 *HARV. NEGOT. L. REV.* 113 (2003) [Hereinafter Shariff 2003]).

and approval of the new design, and (4) evaluation of the design and diffusion of the procedures to the rest of the institution.<sup>11</sup> Using these tools, Ury and his colleagues transformed distressed dispute systems—where parties resolved small conflicts by immediate resort to power struggles—into healthier systems. Their efforts focused on designing dispute systems that permit interest-based dispute resolution and, should these efforts fail, relied upon rights-based adjudication—and only used power as a last resort. This remodeling of the dispute resolution architecture had significant benefits. Not only was there an improvement in the result, institutional integrity and ongoing relationships, but there were also reduced transaction costs in terms of lost time, money, emotional investments and opportunities.<sup>12</sup>

### Investment Treaties and Dispute Resolution Options

Given its success, Ury's conception of dispute systems design has grown beyond its original use in U.S. domestic law.<sup>13</sup> Commercial entities and government institutions increasingly resort to conflict management to establish a web of dispute settlement methods to meet the particular needs of the parties' and the dispute.<sup>14</sup> Even with its success in these other contexts, there has been surprisingly little literature that considers the utility of dispute resolution design for investment disputes arising from or related to bilateral investment treaties.

There does appear, however, to be a need for a more systematic consideration of dispute resolution options. Commentators question whether the dispute

<sup>11</sup> Costantino and Merchant have a similar approach. They recommend first identifying and involving the appropriate stakeholders and then finding an appropriate dispute systems designer to conduct an organizational assessment. Next, create a design architecture to consider where, when and how to use ADR on the basis of identified principles. After training and educating the stakeholders on the use of the system, the program can then be implemented, evaluated and revised as necessary (Costantino and Merchant 1996).

<sup>12</sup> Ury et al. 1988.

<sup>13</sup> Lisa Bingham, "Mediation at Work: Transforming Workplace Conflict at the United States Postal Service," IBM Center for the Business of Government (2003) [Hereinafter Bingham 2003]; Peter Robinson, Arthur Pearlstein and Bernard Mayer, "DyADS: Encouraging 'Dynamic Adaptive Dispute Systems' in the Organized Workplace," 10 HARV. NEGOT. L. REV. 339 (2005) [Hereinafter Robinson et al. 2005].

<sup>14</sup> Francisco Orrego Vicuña, "Arbitration in a New International Alternative Dispute Resolution System," 18(2) News from ICSID (2001) (<http://www.worldbank.org/icsid/news/n-18-2-1.htm>) [Hereinafter Vicuña 2001]; Shariff 2003.



resolution system is in crisis,<sup>15</sup> while UNCTAD suggests concerns “could be addressed by improving the dispute settlement procedures” and ICSID revises its arbitration procedures.<sup>16</sup> Presumably changes might reduce financial exposure (of investors and host countries), improve public perception of how investment disputes are managed and possibly prevent future disputes. Irrespective of whether change is needed or implemented, if the re-evaluation is done in a transparent and co-operative manner, the process of evaluating has the potential to strengthen the credibility and institutional legitimacy of the process of resolving investment disputes.

This section will first consider the historical roots and current dispute resolution systems embossed in investment. It will then consider various dispute resolution options and evaluate their unique costs and benefits. Thereafter, the future of managing investment treaty conflict can be assessed in light of the current structure and other potential options.

#### *a. The Evolution of Investment Dispute Resolution*

Recall how conflict scholars suggest that dispute systems evolved. Costantino and Merchant suggested early systems focus on power dynamics; but as they transform, there is a focus on judicialization and rights-based adjudication; and ultimately systems evolve toward a more interest-based conflict management system.<sup>17</sup> Likewise, Ury et al. observed that systems are often distressed where they resort to the use of force or power as a matter of course to resolve disputes; but when systems focus on rights and interests, they become more effective and efficient.<sup>18</sup> This is not dissimilar from the evolution of the resolution of investment treaty conflict.

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<sup>15</sup> Susan D. Franck, “The Legitimacy Crisis in Investment Treaty Arbitration: Privatizing Public International Law Through Inconsistent Decisions,” 73 *FORDHAM L. REV.* 1521 (2005) [Hereinafter Franck 2005a]; Charles H. Brower, II, “Structure, Legitimacy and NAFTA’s Investment Chapter,” 36 *VAND. J. TRANSNAT’L L.* 37 (2003) [Hereinafter Brower 2003]; Ari Afilalo, “Towards a Common Law of International Investment: How NAFTA Chapter 11 Panels Should Solve Their Legitimacy Crisis,” 17 *GEO. INT’L ENVTL. L. REV.* 51, 88 (2004) [Hereinafter Afilalo 2004].

<sup>16</sup> UNCTAD 2005b, pp. 53–54; ICSID, “Possible Improvements of the Framework for ICSID Arbitration,” (22 October 2004), (<http://www.worldbank.org/icsid/highlights/improve-arb.pdf>) [Hereinafter ICSID 2004]; ICSID “Suggested Changes to the ICSID Rules and Regulations: Working Paper of the ICSID Secretariat,” (12 May 2005) (<http://worldbank.org/icsid/highlights/052405-sgmanual.pdf>) [Hereinafter ICSID 2005]; ICSID CONVENTION RULES AND REGULATIONS, ICSID/15 (April 2006) (<http://worldbank.org/icsid/basicdoc/basicdoc.htm>) [Hereinafter ICSID Basic Documents 2006].

<sup>17</sup> Costantino and Merchant 1996, pp. 49–54.

<sup>18</sup> Ury et al. 1988.

Governments historically relied on the use of force and “gunboat diplomacy” to resolve investment disputes. Given the costs—and the failure of this process to encourage foreign investment—States evolved away from this model. Instead, they shifted to a focus on rights. In an effort to promote foreign investment and instill confidence in the stability of the investment environment, States promulgated treaties that created substantive obligations.<sup>19</sup> These efforts primarily began with so-called “Treaties of Friendship, Commerce and Navigation,” and ultimately developed into more structured investment agreements (such as BITs) or other investment agreements (such as multilateral agreements, for example the North American Free Trade Agreement [NAFTA] and the Energy Charter Treaty [ECT]).<sup>20</sup> The treatification of rights and obligations marked a shift away from power-based dispute resolution and a move toward the development of a rights-based system of neutral adjudication. This sea change affected two main areas of international investment law. First, it offered a new, mutually agreed set of substantive rights to foreign investors for rights, including expropriation, national treatment and fair and equitable treatment.<sup>21</sup> Second, for the first time, States offered foreign investors a dispute resolution system that permitted investors to enforce directly their new substantive rights against a host government.<sup>22</sup>

This second aspect is noteworthy. It meant that investors were not simply granted an illusory promise—they were also granted a forum for redressing violations of their substantive rights. Prior to this development, when government conduct adversely affected their investment, investors were relegated to a series of somewhat unappealing dispute resolution options. These options often left investors to the political mercies of either their own or the host country government in deciding how (if at all) to address an investor’s complaints. Specifically, investors might attempt to negotiate directly with government officials—but they would often be ignored. Likewise, they might lobby government officials in their home jurisdiction to either engage in diplomatic negotiations with the host country government or espouse a claim before the International Court of Justice—and they would often be ignored.

<sup>19</sup> Franck 2005a, pp. 1525–1526; Kenneth J. Vandeveld, *United States Investment Treaties: Policy and Practice* (Kluwer: 1992), pp. 7–22.

<sup>20</sup> M. Sornarajah, *International Law on Foreign Investment* (Cambridge University Press: 1994) [Hereinafter Sornarajah 1994], pp. 231–237; Guillermo A. Alvarez and William W. Park, “The New Face of Investment Arbitration: NAFTA Chapter 11,” 28 *YALE J. INT’L L.* 365 (2003), pp. 366–367.

<sup>21</sup> Giorgio Sacerdoti, “Bilateral Treaties and Multilateral Instruments on Investment Protection,” in *Recueil Des Cours*, vol. 269 (Brill Academic: 1997) [Hereinafter Sacerdoti 1997].

<sup>22</sup> Franck, 2005a, pp. 1541–1545.

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Investors also might consider suing host country governments in their home country courts—but this was often fruitless where host countries had recourse to the defense of sovereign immunity.<sup>23</sup> In other cases, investors might have to address the conflict unilaterally. They might simply absorb the cost of adverse government action by either doing nothing or making a claim under their political risk insurance.<sup>24</sup> In extreme cases, investors might consider resorting to physical violence as a self-help remedy.<sup>25</sup>

The “arbitration addition” was revolutionary. It gave investors direct—and nearly unfettered—access to host country governments, which promised to resolve claims arising under investment treaties through what amounted to a sophisticated choice of forum clause.<sup>26</sup> Although there may be preconditions to arbitration,<sup>27</sup> once the conditions are satisfied, treaties typically give investors the right to make an election amongst pre-determined dispute resolution options to resolve a dispute.<sup>28</sup> Once an investor makes the election, the host country government must resolve the matter under the investor’s preferred methodology. For example, investment treaties permit investors to choose among: (1) litigating disputes before the host country government’s national courts, (2) arbitrating disputes before ICSID or (3) arbitrating disputes before an *ad hoc* tribunal that is bound by the UNCITRAL Arbitration Rules.<sup>29</sup>

Part of this “judicialization” of managing investment treaty conflict may be due in part to an evolution in the use of and expectations about international

<sup>23</sup> Ian Brownlie, *Principles of Public International Law*, 6th Edition (Oxford University Press: 2003), pp. 677–715; Sacerdoti 1997, pp. 412–415.

<sup>24</sup> Jeswald W. Salacuse, “Explanations for the Increased Recourse to Treaty-Based Investment Dispute Settlement: Resolving the Struggle of Life Against Form?” in Karl Sauvant, ed., *Coherence and Consistency in International Investment Law* (Oxford University Press: 2007); Franck 2005a, pp. 620–621.

<sup>25</sup> The BBC has reported on a British-owned gold mining company in Ghana that allegedly engaged in a practice of shooting illegal miners on sight. Angus Stickler, *Ghana’s Ruthless Corporate Gold Rush* (18 July 2006) ([http://news.bbc.co.uk/1/hi/programmes/file\\_on\\_4/5190588.stm](http://news.bbc.co.uk/1/hi/programmes/file_on_4/5190588.stm)). The story does not indicate whether this action was part of the company’s normal commercial operation or was, perhaps, a result of the government’s failure to provide full protection and security.

<sup>26</sup> Susan D. Franck, “The Nature and Enforcement of Investor Rights Under Investment Treaties: Do Investment Treaties Have A Bright Future?” 12 U.C. DAVIS J. INT’L L. & POL’Y 47 (2005) [Hereinafter Franck 2005b].

<sup>27</sup> See *infra* section A(3)(b) for a discussion of the current system of resolving investment disputes, including the use of non-binding dispute resolution and other preconditions to arbitration.

<sup>28</sup> Christopher Schreuer, “Traveling the BIT Route: Of Waiting Periods, Umbrella Clauses and Forks in the Road,” 5 J. WORLD INVEST. AND TRADE 231 (2004) [Hereinafter Schreuer 2004].

<sup>29</sup> This is one area in which investor-State and State-to-State dispute resolution diverge. State-to-State arbitration does not generally permit a government to make an election as to the final dispute resolution method.

arbitration. Historically, arbitration was not a forum where decision-makers were prized for their impartiality; rather, arbitrators' value came in their exercise of expert professional discretion, facility to create unique solutions, ability to recommend settlement terms to parties, capacity to act as an internal partisan during deliberations, or some combination of these factors.<sup>30</sup> Under these conditions, the popularity of international arbitration waxed and waned over time.<sup>31</sup> As it has evolved in an international context, however, arbitration has shifted away from a group of "grand old men" dispensing discretionary wisdom. Instead, in the twentieth century, the process has blossomed. Today, international arbitration technocrats focus on creating a fair and impartial process that results in an award based upon the factual record and independent legal analysis.<sup>32</sup>

Part of this judicialization may account for arbitration's success in the resolution of public and private international disputes. In the private international law context, as international trade has flourished, arbitration has become the primary vehicle for the resolution of international commercial disputes. Its popularity and success can be attributed to a variety of sources including its neutrality, speed, cost, confidentiality, ability to select an expert adjudicator and the ease of enforcement under the New York Convention for the Enforcement of Foreign Arbitral Awards.<sup>33</sup>

In the public international context, arbitration has also found fertile ground. It has caused politicians such as Benjamin Franklin to remark "When will mankind be convinced and agree to settle their difficulties by arbitration?"<sup>34</sup> and motivated William Jennings Bryan to attempt to prevent World War I by promoting treaties to foster the resolution of disputes by arbitration.<sup>35</sup> In the investment context, treaties such as the Jay Treaty (1794)<sup>36</sup> and Treaty of

<sup>30</sup> Yves Dezalay and Bryant G. Garth, *Dealing in Virtue: International Commercial Arbitration and the Construction of Transnational Legal Order* (University of Chicago Press: 1996) [Hereinafter Dezalay and Garth 1996]; Laura J. Cooper, "The Process of Process: The Historical Development of Procedure in Labor Arbitration," in *Arbitration 2005: The Evolving World of Work*, Proceedings of the Fifty-Eighth Annual Meeting, National Academy of Arbitrators, Bureau of National Affairs, vol. 99 (2006).

<sup>31</sup> David J. Bederman, *International Law Frameworks* (Foundation Press: 2001), p. 238.

<sup>32</sup> Dezalay and Garth 1996; Catherine Rogers, "Fit and Function in Legal Ethics: Developing a Code of Conduct for International Arbitration," 23 MICH. J. INT'L L. 347, 353 (2002) [Hereinafter Rogers 2002].

<sup>33</sup> Jan Paulsson, "Dispute Resolution," in Robert Pritchard, ed., *Economic Development, Foreign Investment, and the Law* (Kluwer: 1996), pp. 211–212 [Hereinafter Paulsson 1996].

<sup>34</sup> Brainy Quotes (<http://www.brainyquote.com/quotes/quotes/b/benjaminfr169230.html>).

<sup>35</sup> Michael Kazin, *A Godly Hero: The Life of William Jennings Bryan* (Knopf: 2006).

<sup>36</sup> Treaty of Amity, Commerce, and Navigation, Nov. 19, 1794, U.S.–Gr. Brit., 8 Stat. 116 [hereinafter Jay Treaty].

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Ghent (1814) began using arbitration for resolving investment-related disputes by giving creditors access to an international commission to press their claims. Article VI of the Jay Treaty, for example, provided British creditors with the right to adjudicate claims for compensation; and Article VII granted U.S. creditors similar rights against the British government.<sup>37</sup>

Where tribunals adhered to articulated rules and engaged in reasoned legal analysis, arbitration tended to be successful. Cases such as the *Alabama Claims* case, which involved Britain's responsibilities as a neutral during the U.S. Civil War, marked a watershed in the development of international arbitration. The U.S. and British governments established a five-member tribunal composed of nationals from the U.S., Britain, Italy, Switzerland and Brazil. Following a strict juridical procedure and the parties' agreed *lex specialis*, the tribunal issued a reasoned award against Britain, which was paid.<sup>38</sup> Nevertheless, where early "arbitrations" were not pure applications of the rule of law but a blend of juridical and diplomatic considerations, there were concerns that arbitration was an extension of gunboat diplomacy and/or imperialism.<sup>39</sup>

#### *b. The Status Quo for Resolving Disputes*

At present, treaties are individually negotiated between and among sovereign governments. Without a multilateral agreement on investment, there is no uniform treatment of dispute resolution methods in investment treaties.<sup>40</sup> Although there are exceptions, there does appear to be a general trend, however. In particular, the resolution of investor-State treaty claims occurs primarily through some type of non-binding dispute resolution and/or arbitration. State-to-State dispute resolution exhibits a similar pattern.<sup>41</sup>

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<sup>37</sup> Merrills, however, has suggested that this was not arbitration in its modern conception. Rather, it was "supposed to blend juridical with diplomatic considerations to produce (in effect) a negotiated settlement." (Merrills 2005, p. 92).

<sup>38</sup> *Id.*, pp. 94, 105.

<sup>39</sup> *Id.*, pp. 92–93; Bederman 2001, p. 238; Barton Legum, "The Innovation of Investor-State Arbitration under NAFTA," 43 HARV. INT'L L.J. 531, 534–535 (2002) [Hereinafter Legum 2002].

<sup>40</sup> Scholarship in related to dispute resolution design could benefit from an empirical analysis of the most common dispute resolution systems (and most prominent exceptions) provided in BITs. It is, however, very difficult to analyze these matters. See, e.g., Jason W. Yackee, *Conceptual Difficulties in the Empirical Study of Bilateral Investment Treaties* (May 2006) ([http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=903680](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=903680)). Nevertheless, this chapter relies upon publicly available discussions about the content and scope of dispute resolution provisions.

<sup>41</sup> At present, investment treaties contain a unique combination of both State-to-State dispute resolution and investor-State dispute resolution (Franck 2005b). While this chapter focuses primarily on investor-State

In the investor-State context, BITs generally call for the “amicable resolution” of disputes. Commentators suggest that this provision is intended to refer to the use of non-binding dispute resolution mechanisms such as negotiation, mediation or conciliation to resolve disputes.<sup>42</sup> NAFTA is slightly more precise, requiring that “disputing parties should first attempt to settle a claim through consultation or negotiation.”<sup>43</sup> Nevertheless, while the ambiguity may have been intended to preserve flexibility and the informality of the dispute resolution process, the lack of guidance creates difficulties. The meaning of these obligations is not explained; particularly for legal cultures with different dispute resolution traditions, it fails to articulate mutual expectations about how the parties should begin to attempt to resolve their dispute. Moreover, there are no mandates particularizing what the process should entail and how it should be accomplished. This lack of a clear consent to procedural parameters and the lack of substantive obligations leave the “amiable resolution” methodology with little force. It is unclear what effect these provisions have had on the resolution of investment disputes.

Irrespective of whether this unparticularized form of dispute resolution is required or simply recommended,<sup>44</sup> there is usually a time limit on how long it must continue. Treaties generally require, for example, that after submitting a notice of dispute investors wait three or six months before filing an official request for arbitration. This suggests the waiting period is primarily intended to provide more of a “cooling off” period to permit parties to gather resources and develop an internal strategy for dispute resolution prior to the commencement of adjudication. By way of example, Schreuer observed that Article 11 of the German model BIT provides “Divergencies [sic] concerning investments ... should as far as possible be settled amicably .... If the divergency cannot be

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arbitration, to complete a thorough analysis of the system, both aspects of the system deserve serious and individual consideration. (United Nations Centre on Transnational Corporations 1988, pp. 66–70; UNCTAD 1998, pp. 92–96; Rudolf Dolzer and Margrete Stevens, *Bilateral Investment Treaties* (Martinus Nijhoff Publishers: 1994) [Hereinafter Dolzer and Stevens 1994], pp. 119–120; “Dispute Settlement: General Topics, Dispute Settlement: Investor-State,” UNCTAD/ITE/IIT/30 (2005). ([http://www.unctad.org/en/docs/iteiit30\\_en.pdf](http://www.unctad.org/en/docs/iteiit30_en.pdf)) [Hereinafter UNCTAD 2003b], pp. 12–14.

<sup>42</sup> Noah Rubins, “Comments to Jack C. Coe, Jr.’s Article on Conciliation,” 21(4) *MEALY’S INT’L ARB. REP.* 21 (2006) [Hereinafter Rubins 2006]; Schreuer 2004.

<sup>43</sup> NAFTA Art. 1118.

<sup>44</sup> Generally, BITs do not require mandatory non-binding dispute resolution, such as conciliation or mediation. Where conciliation is present, it may be offered under established procedures (such as the UNCITRAL, ICSID Conciliation Rules or ICSID Additional Facility Conciliation Rules). Particularly in investor-State disputes, it is typically an option offered either prior to or instead of arbitration (Rubins 2006).

settled within six months of the date when it has been raised by one of the parties in dispute, it shall ... be submitted for arbitration.”<sup>45</sup>

Beyond the question of whether or not BITs provide for non-particularized “amicable settlement” or conciliation, most BITs do provide that arbitration is the final method for resolving treaty-based claims. Given the textual prevalence of arbitration provisions in BITs—and the absence of less systematic reliance on other forms of dispute resolution—it appears that arbitration has historically been the presumed “best” mechanism for resolving investment disputes.<sup>46</sup> There has, unfortunately, been little (if any) systematic or empirical enquiry into whether this assumption is correct—and whether that assumption is equally applicable to investor-State and State-to-State dispute resolution. It is, for example, generally unclear whether drafters of model BITs or individual treaties analyzed the utility of “cooling off” periods, or whether arbitration is the appropriate default dispute resolution mechanism.<sup>47</sup> (See Annex 8, *Novel Features in OECD Countries’ Recent Investment Agreements*.)

### *c. Understanding the Choice for Arbitration*

In explaining the shift toward arbitration and the judicialization of treaty disputes, some suggest the phenomenon occurred because an “increasing number of capital importing countries came to realize that their self-interest was served by agreeing to arbitrate investment disputes.”<sup>48</sup> There has, however, been little explanation or documentation of this phenomenon or why arbitration might also be in the interest of capital exporting countries. Moreover, there has not been a coherent explanation of why other dispute resolution systems were less desirable.

During the initial phase of BIT negotiation during the late 1950s and 1960s, there does not appear to have been a systematic analysis of why arbitration might be preferable to other dispute resolution options—either binding or

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<sup>45</sup> Schreuer 2004, p. 232.

<sup>46</sup> Dolzer and Stevens 1994, pp. 119–122, 129–136.

<sup>47</sup> The Australia–United States Free Trade Agreement, which did provide for State-to-State dispute resolution but failed to provide investors with a direct right to arbitrate disputes, is a notable exception to this general trend (Dodge 2006).

<sup>48</sup> Alvarez and Park 2003, pp. 366–368.

non-binding.<sup>49</sup> Thus, an over-reliance on arbitration is hardly surprising. The “alternative dispute resolution revolution” did not start in the United States until the late 1970s and did not gain significant prominence until the 1980s and 1990s; and the dispute systems design movement was in its infancy during the late 1980s and early 1990s.<sup>50</sup> It has taken even longer for the benefits of alternative dispute resolution and dispute resolution design to find a home across the Atlantic.<sup>51</sup> It is curious, however, that even during the surge of treaty drafting during the 1990s—after these two movements had gained significant ground—there was little (if any) consideration for why arbitration was still the preferred—let alone appropriate—method for resolving disputes.

There are undoubtedly a variety of explanations for this phenomenon. First, as the system of resolving investment treaty claims remained relatively untested during this time, there was little need to re-evaluate the status quo. In other words, changes were unnecessary as there was no visible evidence of dysfunction. Second, as countries continued to draft model BITs and negotiate BITs on that basis, there was likely institutional momentum to stick to the traditionally approved format. Revisions or re-negotiation would require explanations at various levels of government. Expending energy to make changes may not have been worth the effort, particularly where treaties appeared to proffer the promised rewards—namely foreign investment—and the disuse of the arbitration system meant there were minimal costs. Third, practical considerations may have played a role. Although the business community may have started to use interest-based mechanisms to resolve business to business disputes, they may have been unwilling to endorse interest-based dispute resolution models in the investor-State context without evidence of their successful implementation. Similarly, to the extent that non-binding, interest-based dispute resolution mechanisms like mediation and negotiation might exclude the public, non-governmental organizations may not have been interested in advocating for these dispute resolution processes.

Perhaps more importantly, treaty drafters may have used arbitration because it was associated with tried and tested institutions. It was seen as working well

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<sup>49</sup> UNCTAD 1998; Dolzer and Stevens 1994.

<sup>50</sup> Jean R. Sternlight, “ADR is Here: Preliminary Reflections on Where it Fits in a System of Justice,” 3 *NEV. L. J.* 289 (2003) [Hereinafter Sternlight 2003].

<sup>51</sup> David J.A. Cairns, “Mediating International Commercial Disputes: Differences in U.S. and European Approaches,” 60 *OCT. DISP. RESOL. J.* 62 (2005) [Hereinafter Cairns 2005]; Vicuña 2001.



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and had the patina of international legitimacy. Thomas Franck<sup>52</sup> has explained that international institutions can become legitimate by affiliating with the proven institutions of international law's past.<sup>53</sup> The Iran–U.S. Claims Tribunal was able to resolve disputes between foreign investors and host governments using a process that adhered to the rule of law and—with one exception<sup>54</sup>—did not require stakeholders to resort to physical violence to settle complaints.<sup>55</sup> Meanwhile, the ICSID Convention created an institution designed to resolve disputes through arbitration. More importantly, international commercial arbitration was gaining steam with success of the New York Convention and many countries adopting progressive arbitration laws based upon the 1985 UNCITRAL Model Law on International Commercial Arbitration. Arbitration seemed to be working. In contrast to cases resolved at the International Court of Justice,<sup>56</sup> investment disputes were getting resolved efficiently. Sophisticated counsel was available to make effective arguments. Parties were complying with awards, and streamlined enforcement mechanisms were readily available. In these circumstances, it was not unreasonable to desire the continuation of a process that appeared to have some success in achieving practical results.

Beyond the institutional legitimacy, there are practical reasons that arbitration was seen as effective. International commercial arbitration has certain systematic efficiencies in its model that could be grafted onto the investment treaty model. For instance, the neutrality of international arbitration permits the independent and impartial resolution of disputes. It escapes the perception of unfair local advantage or outright partiality of the court system in favor of the host government. In addition, rather than engaging in lengthy litigation before a national or international court, arbitration was presumed to save time, money and other internal resources. Although they outsource authority to resolve the dispute, parties retain a degree of control over the process of resolving

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<sup>52</sup> The author of this essay is unrelated to Professor Franck.

<sup>53</sup> Thomas M. Franck, *The Power of Legitimacy Among Nations* (Oxford University Press: 1990).

<sup>54</sup> Memorandum Re: Challenge to Arbitrators Kashani and Shafeifei by the Government of the United States of America, 7 IRAN U.S.-CL. TRIB. REP. 281, 292 (1986). One Iranian judge was quoted as saying: "If Mangard ever dares to enter the tribunal chamber again, either his corpse or my corpse will leave it rolling down the stairs." *Iranian Judge Threatens A Swede at The Hague*, N.Y. TIMES, Sept. 7, 1984, at A5. Subsequently, the Tribunal's President suspended all tribunal proceedings. *U.S. -Iran Arbitration Suspended at The Hague*, N.Y. TIMES, Sept. 20, 1984, at A9.

<sup>55</sup> Charles N. Brower, *The Iran- United States Claims Tribunal* (Springer: 1998).

<sup>56</sup> See generally F. A. Mann, "Foreign Investment in the International Court of Justice: the ELSI Case," 86 AM. J. INT'L L. 92 (1992); Case Concerning Elettronica Sicula, S.p.A (ELSI), *United States of America v. Italy*, 1989, I.C.J. Reports 4.

the conflict. Not only can they select their decision-makers, but they can also tailor the arbitration process to meet their needs and the peculiarities of a specific investment dispute. There were other unique aspects of arbitration that made it a desirable alternative to litigation before national or international courts. In particular, arbitration was confidential and would permit parties to preserve sensitive commercial data, prevent adverse publicity and preserve ongoing relationships. Arbitration also had a streamlined enforcement mechanism, which made it preferable to having to enforce a judgment through the U.N. Security Council or needing to engage in time-consuming national court litigation to enforce foreign court judgments.<sup>57</sup> Ultimately, investment treaty arbitration has been seen to resolve disputes and, after exhausting contested awards through the normal legal process, parties have generally paid awards.

Nevertheless, one wonders whether a different dispute resolution system would be more efficient, effective and better address concerns of stakeholders. It would, however, be imprudent to presume a different system would be superior to the current framework without a diagnosis of the system, consideration of the dispute design and an assessment of the costs and benefits. The implications are not insignificant. While there have been concerns about transparency, consistency, fairness and regulatory authority, choosing a different system for resolving disputes may ameliorate the problems or perhaps simply lead the issues to manifest themselves in a different fashion. The goal should be to purify the waters of investment-related conflict rather than contaminating the water supply.

The use of dispute systems design to diagnose and assess the current system's dispute resolution needs may be one way to begin this process. Future work can and should consider the specific application of dispute systems design for the resolution of investment treaty conflict. It might, for example, consider how to do a conflict assessment, analyze existing patterns of disputing and consider what are the appropriate principles upon which a system should be based.<sup>58</sup> In connection with this, this chapter turns to a systematic consideration of different options for resolving investment treaty conflict and how they are used (if at all) to manage conflict effectively.

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<sup>57</sup> Recently, however, there has been concern as to the enforceability of investment treaty awards, particularly in the context of the claims against Argentina; see, e.g., Osvaldo J. Marzoti, "Enforcement of Treaty Awards and National Constitutions (the *Argentinean Cases*)," 7 BUS. L. INT'L 226 (2006).

<sup>58</sup> Franck 2007.

## The Range of Options: Appropriate Dispute Resolution and the Dispute Resolution Continuum

It is essential to place the resolution of investment disputes in its wider context. “The settlement of any dispute, not just investment disputes, requires the adoption of the most speedy, informal, amicable and inexpensive method available.”<sup>59</sup> Finding the most “appropriate” mechanism for resolving specific categories of types of investment disputes, however, can be challenging. Nevertheless, there are decided benefits to tailoring a design to the unique needs of the particular system. These benefits might include the promotion of democratic values, minimizing resources exerted on dispute resolution, increasing productivity, increasing satisfaction with outcomes, decreasing the recurrence of disputes and improving public relations.<sup>60</sup> Finding the appropriate dispute resolution is therefore a matter of some importance.

Historically, the term “ADR” has been viewed as “alternative dispute resolution.” There has, unfortunately, been confusion about what that term means. In a domestic context, “alternative dispute resolution” has tended to mean any dispute resolution process that occurs outside national courts; but because of its prevalence in the international context, there has been some debate as to whether arbitration was truly “alternative” dispute resolution.<sup>61</sup> While this is an interesting intellectual debate, it is a distraction from the fundamental need to provide for the appropriate and effective resolution of investment disputes. Therefore, for present purposes, “ADR” is defined as an *appropriate* dispute resolution mechanism. In an effort to facilitate the creation of a dispute resolution system that functions effectively and meets systemic needs for managing conflict, the purpose of this section is to consider the spectrum of mechanisms—whether non-binding, binding or hybrids—that are available to stakeholders for resolving investment disputes.

Beyond the problem of defining ADR, there is also a confusion that persists in many jurisdictions and different cultures as to the meaning of specific ADR alternatives. This lack of a common understanding and mutual expectations

<sup>59</sup> UNCTAD 2003b, p. 11.

<sup>60</sup> Richard C. Reuben, “Democracy and Dispute Resolution: Systems Design and the New Workplace,” 10 HARV. NEGOT. L. REV. 11 (2005) [Hereinafter Reuben 2005]; CPR Institute for Dispute Resolution, *Resource Book For Managing Employment Disputes* (2004); Ury et al. 1998.

<sup>61</sup> Paulsson 1996, p. 210; Vicuña 2001; Ucheora Onwuamaegbu, “The Role of ADR in Investor-State Dispute Settlement: The ICSID Experience,” 2(2) *News from ICSID*, 12 (2005) ([http://www.worldbank.org/icsid/news/news\\_22-2.pdf](http://www.worldbank.org/icsid/news/news_22-2.pdf)) [Hereinafter Onwuamaegbu 2005].

has significant implications.<sup>62</sup> For example, Amy Cohen eloquently explains: “Mediation changes as it travels; its instantiation anywhere is subject to local variation and intervention as it makes contact with state and customary law, politics, and social struggles.”<sup>63</sup> Given different cultural understandings and the potential for mismatched expectations at a sensitive juncture in the dispute resolution process, it is vital to create a common lexicon. Establishing this framework will assist in framing future analysis and debate, foster an appreciation for variations in the approaches and permit stakeholders to make informed choices.

Theoretically, there are a variety of options for resolving investment treated disputes. The classic formulation in dispute resolution circles is that the “forum [should] fit the fuss.”<sup>64</sup> In order to make an informed choice of the appropriate of the design of a dispute resolution system, it is useful to consider the options along the dispute resolution continuum that might be employed individually or in combination to resolve investment-related disputes. Once the spectrum of choices is clear, designing dispute systems is more efficient.<sup>65</sup>

Stressing that “arbitration is only one of many ADR choices,” Costantino and Merchant identify six broad categories of ADR options: preventative, negotiated, facilitative, fact-finding, advisory and imposed ADR.<sup>66</sup> Each category involves varying levels of third-party intervention, with their own distinct costs and benefits; and each category can be implemented at different junctures. In an effort to create a common framework for discussing ADR in the context of investment law, this chapter adopts Costantino and Merchant’s categories for understanding ADR mechanisms.<sup>67</sup> The breadth and generality of the categories promote understanding of the primary nature of the mechanism without being hindered by the particularities of the distinct mechanisms within the categories. Once the fundamental character of the process is defined,

<sup>62</sup> Roger Fisher and William Ury, *Getting to Yes: Negotiating Agreement Without Giving In* (Houghton Mifflin Company: 1981), p. 34.

<sup>63</sup> Amy J. Cohen, “Debating the Globalization of U.S. Mediation: Politics, Power, and Practice in Nepal,” 11 *HARV. NEGOT. L. REV.* 295, 296 (2006).

<sup>64</sup> Frank E.A. Sander and Stephen Goldberg, “Fitting the Forum to the Fuss: A User-Friendly Guide to Selecting an ADR Procedure,” 10 *NEGOT. J.* 49 (1994) [Hereinafter Sander and Goldberg 1994].

<sup>65</sup> Costantino and Merchant 1996; Ury et al. 1988.

<sup>66</sup> Costantino and Merchant 1996, pp. 37–41.

<sup>67</sup> In Ury et al.’s conception of interest, rights and power-based dispute design system, the first five methods are likely to be more interest-based and Imposed ADR is likely to involve rights-based adjudication. Power-based resolution, as previously defined, can take the form of war, violence, strikes, or physical aggression (Ury et al. 1988).

it then identifies primary dispute resolution processes in the category. The description of the various processes is by no means exhaustive. While there will be variations and permutations, articulating the common framework—and beginning to assess the costs and benefits of its elements—is a useful place from which to start.

### Preventative ADR

Preventative ADR mechanisms are designed to preempt disputes. Recognizing that conflict is an inevitable aspect of human interactions, preventative ADR methods do not try to stop conflict from arising; rather they channel potential areas of disagreements into a problem-solving arena in order to avoid the crystallization and escalation of disputes. In the context of investment disputes, this might take various forms, such as negotiated rule making, the use of good offices to engage in peer-review of the dispute or the use of an ombudsperson.<sup>68</sup>

#### *a. The Benefits of Negotiated Rulemaking and Good Offices*

Encouraging host country governments to participate in negotiated rulemaking in domestic administrative law can mitigate potential international law conflicts at the outset rather than waiting until the harmful effects of the regulation are apparent. There is a rich literature considering the value of negotiated rule making in the United States.<sup>69</sup> Undoubtedly, there would be up-front costs related to the process of creating consensus, selecting the right types of areas for negotiated rulemaking and addressing concerns about degree of public participation. Nevertheless, proactively using negotiated rulemaking to prevent disputes could have significant benefits. For instance, it could lead to: the prevention of subsequent disputes, the modeling good government, an improvement in the quality of government regulation, the promotion of democratic values and the enhancement of governmental legitimacy.<sup>70</sup>

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<sup>68</sup> There are also other forms of preventative ADR partnering and joint problem solving. These, however, may work best in a more commercial context.

<sup>69</sup> Cary Conglianese, "Assessing Consensus: The Promise and Performance of Negotiated Rulemaking," 46 DUKE L.J. 1255 (1997) [Hereinafter Conglianese 1997]; Lawrence Susskind and Gerard McMahon, "The Theory and Practice of Negotiated Rulemaking," 3 YALE J. ON REG. 133 (1985) [Hereinafter Susskind and McMahon 1985].

<sup>70</sup> Jody Freeman and Laura I. Langbein, "Regulatory Negotiation and the Legitimacy Benefit," 9 N.Y.U. ENVTL L.J. 60 (2000) [Hereinafter Freeman and Langbein 2000].

Likewise, using “good offices” might have merit. In this instance, a person in a position of authority and prestige could facilitate communications between the parties and provide peer-review to prevent disputes from arising or escalating.<sup>71</sup> Although such preventive diplomacy has achieved mixed results in the public international law context, it remains a potential tool in the toolbox for governments seeking to maximize the utility of the design of their dispute resolution system. UNCTAD has referenced the possibility of using “good offices,” although it has not analyzed the issue systematically.<sup>72</sup> Interestingly, UNCTAD appears to view “good offices” as a step to be taken only after negotiated ADR mechanisms fail; but this should not prevent it from being used as a preventative mechanism to check the escalation of disputes and improve communication *ex ante*.

### *b. Opportunities with Ombuds*

Ombuds might also be used to manage conflict and prevent the escalation of disputes. Ombuds have their roots in China, Egypt and Germanic tribes, but were used most prominently in connection with democratic governance in Sweden, where they provided a bridge between private individuals and the government. More recently, ombuds have been used successfully in the United Kingdom, United States and the European Union, as well as in corporate contexts.<sup>73</sup>

An ombudsperson is an official, appointed either by a public or private institution, whose fundamental function is to remain impartial and receive complaints and questions from a defined constituency about issues within the ombuds’ express jurisdiction. The ombuds’ mandate is to resolve complaints at an early stage. To carry out this method, ombudspersons have many tools. They might direct constituents to other processes or opportunities that may resolve the issues, or, they may raise the problem at an appropriate level within the organization.<sup>74</sup> In its classic definition, the ombudsperson is an “officer appointed by the legislature to handle complaints against administrative and

<sup>71</sup> Linda C. Reif, “Conciliation as a Mechanism for the Resolution of International Economic and Business Disputes,” 14 *FORDHAM INT’L L.J.* 578 (1991) [Hereinafter Reif 1991]; Bederman 2001, p. 236.

<sup>72</sup> UNCTAD 2003b, pp. 11–12.

<sup>73</sup> Harold J. Krent, “Federal Agency Ombuds: The Costs, Benefits and Countenance of Confidentiality,” 52 *ADMIN. L. REV.* 17 (2000) [Hereinafter Krent 2000]; Vicuña 2001; Philip J. Harter, “Ombuds—A Voice for the People,” *DISP. RESOL. MAG.* (Winter 2005), p. 5 [Hereinafter Harter 2005].

<sup>74</sup> Ombuds may also have authority to mediate disputes. By and large, they resolve conflict through a hybrid process of investigation and conciliation in order to prevent the escalation of disputes.

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judicial action,” serving as a watchdog over those actions while exercising independence, expertise, impartiality, accessibility, and powers of persuasion rather than control.<sup>75</sup> While they generally lack the power to make binding decisions, order administrative conduct or reverse administrative action, their capacity to make recommendations and to publicize their findings has an impact. An ombudsperson’s “authority and influence derive from the fact that he is appointed by and reports to one of the principal organs of state, usually either the parliament or the chief executive.”<sup>76</sup> Ultimately, an ombudsperson’s mandate is not to protect the organization’s reputation. Rather, his or her objective is to promote reasoned, fair and ethical conduct in the organization and to take a view based upon integrity, legality and principle.<sup>77</sup>

The use of ombuds has a level of built-in acceptance and confidence in both the governmental and the corporate context. They first have the benefit of history and a legacy of authority. Because ombuds are associated with a practice that has a long, multi-cultural tradition that has been effective in many contexts, this pedigree promotes symbolic validation, which lends the process legitimacy.<sup>78</sup> Ombuds offices have the benefit of equality, where those who are affected by a conflict have a place to give voice to their concerns. Unlike an investor’s unilateral right to bring claims under a treaty, investors, citizens and governmental officials could have theoretical access to the ombuds office for the filing of complaints.<sup>79</sup>

Beyond these more theoretical benefits, there are also practical benefits of using ombudspersons to prevent disputes. For parties with investment-related concerns, an ombuds office offers a clear line of authority for receiving complaints and lowers the cost of raising issues. This has the benefit of permitting smaller investors or parties with smaller conflicts to have their concerns heard and addressed. In essence, it facilitates access to justice and decreases the stigma of announcing and quickly resolving disputes. While theoretically it could increase the number of recorded disputes, presumably this would not mean the number of disputes actually increased but, rather, there would be an increase in reporting problems. Commentators have noted that “submitting an investment dispute to arbitration under a treaty can decrease the chances of

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<sup>75</sup> Shirley A. Wiegand, “A Just and Lasting Peace: Supplanting Mediation with the Ombuds Model,” 12 OHIO ST. J. ON DISP. RESOL. 95, 96 (1996) [Hereinafter Wiegand 1996].

<sup>76</sup> Krent 2000.

<sup>77</sup> Wiegand 1996.

<sup>78</sup> Franck 1990, pp. 91–110.

<sup>79</sup> Wiegand 1996.

amicable resolution of the dispute because settlement of a treaty claim requires approval of additional decision-makers in the government and therefore complicates any resolution.”<sup>80</sup> Ombuds are a natural antidote to this. Rather than letting problems fester and reach the boiling point, an ombudsperson provides an early opportunity to intervene and improve the situation. In other words, there is a formal process that allows parties to address issues informally before ratcheting up the costs and formality of conflict resolution.

As there is often too little information and problems with disbursing the available information at the beginning of a conflict, commentators have suggested that the prospects of early settlement are often “dim”—particularly when multiple agencies are involved.<sup>81</sup> Ombuds, however, could provide an antidote to this problem. Because an ombudsperson is an independent part of the host country government, the office would be in a position to know the agencies, entities or people whose involvement would be needed to resolve matters.

The requirement, for example in an investment treaty, to establish an ombuds office would require governments to determine in advance who would have institutional responsibility for resolving investment-based disputes and with whom ombuds should liaise. Using ombudspersons as an information conduit would create an opportunity to manage conflicts more effectively when they do arise and minimize the information vacuum in order to clear the way for early (or easier) dispute resolution. As “the best chance to resolve a dispute between a foreign investor and a government agency is likely before the investment dispute becomes a dispute under an investment treaty,”<sup>82</sup> ombuds provide a unique opportunity to catch and resolve conflict before a dispute is crystallized. This is a useful alternative to making a formal claim and dedicating institutional resources to win and/or litigate to the end, irrespective of the cost.

An ombuds office could also serve as a conflict barometer. It would alert governments to where they are most likely to encounter difficulties; with that information, they would be in a position to make more informed and rational

<sup>80</sup> Barton Legum, “The Difficulties of Conciliation on Investment Treaty Cases: A Comment on Professor Jack C. Coe’s ‘Towards a Complementary Use of Conciliation in Investor-State Disputes—A Preliminary Sketch,’” 21(4) MEALY’S INT’L ARB. REP. 23 (2006) [Hereinafter Legum 2006]; Jack J. Coe, Jr., “Toward a Complementary Use of Conciliation in Investor-State Disputes—A Preliminary Sketch,” 12 U.S. DAVIS J. INT’L L. AND POL’Y 7 (2005) [Hereinafter Coe 2005].

<sup>81</sup> Legum 2006.

<sup>82</sup> Legum 2006.



legislative and regulatory choices. Moreover, ombuds can enhance the image and legitimacy of government agencies. While it could not make or change policy, the presence of an ombuds office can encourage government officials to support their decisions with sufficient reasoning. In addition, providing the regulated public with a direct form of communication and feedback can promote democratic values and institutional legitimacy.<sup>83</sup>

*c. Challenges with Preventative Dispute Resolution*

The same benefits, however, could create problems for governments, investors and other interested parties. All of these types of Preventative ADR will share common difficulties. Because they are not as frequently used, parties may be hesitant to try them. In the case of negotiated rulemaking or good offices, stakeholders may be unwilling to consider these options until a “mutually hurting stalemate” exists. In other words, until the difficulties with the existing system reach a point that is unbearable for all stakeholders, the system may not be ripe for the use of these options.<sup>84</sup>

Similarly, governments may be unfamiliar with the process of using ombudspersons. Some governments may find it alien and undesirable. Beyond the inertia of continuing with the status quo, governments may be unwilling to expend the resources necessary to create such an office. They may believe, for example, that there are an insufficient number of investment-related conflicts to justify the establishment of an office. Moreover, the creation of an ombuds office would front-load the process of managing disputes by requiring the creation of structures. Should governments fail to see the down-stream, long-term benefits of the creation of an ombuds office, they may decide the cost is not worth the benefit.

There may also be other difficulties. As ombudspersons’ persuasive authority comes from autonomy, expertise, neutrality and status, the office’s effectiveness can be diminished when any of these essential characters are lacking or impaired. Should an ombuds’ affiliation with the government be perceived to compromise independence, people may be less willing to seek his or her assistance.

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<sup>83</sup> Krent 2000.

<sup>84</sup> Andrea Schneider, “The Day After Tomorrow: What Happens Once A Middle East Peace Treaty Is Signed?” 6 NEV. L.J. 401 (2006); I. William Zartman, “Timing and Ripeness,” in Andrea Kupfer Schneider and Christopher Honeyman, eds., *The Negotiator’s Fieldbook: The Desk Reference For The Experienced Negotiator* (ABA Section of Dispute Resolution: 2006).

Ombuds should not be a mouthpiece of the government that institutionalizes the status quo while ignoring the concerns of other stakeholders.<sup>85</sup> In the past, this has been one of the primary obstacles to using ombuds effectively.<sup>86</sup> To ensure proper neutrality and the ability to perform their core functions, any ombuds office would need physical as well as fiscal independence from any one constituency to minimize the appearance of bias.<sup>87</sup>

There may also be challenges related to confidentiality. There are disagreements about whether communications to ombuds are privileged and whether confidentiality is appropriate. Certain stakeholders may assert that the transparency of the ombuds process is critical to promote settlements that are in the public interest. Meanwhile, other stakeholders might suggest confidentiality is fundamental to an effective process. A lack of confidentiality may create difficulties in maintaining the perception of an ombud's neutrality; and it may also inhibit the full and frank disclosure of problems, which might chill the use of the ombuds and frustrate a primary reason for its creation. One can imagine an investor with a long-term regulatory relationship with a government who would be concerned about government reprisals for the reporting of problems.<sup>88</sup>

These possible concerns are not trivial. Consideration should be given to ways to address and neutralize these concerns to strike an appropriate balance. Although the devil would undoubtedly be in the details, the promise of an ombuds office should not be overlooked. The flexibility, distinct capacities and institutional position provides a unique opportunity to constructively resolve conflict. Ultimately, these preventative ADR methods hold the important promise of preventing disputes from crystallizing and allowing parties to allocate their resources effectively.

### Negotiated ADR

Negotiated ADR involves communications between the parties to a conflict; the result of such discussions will be either to create a mutually acceptable resolution or terminate the process, presumably to pursue other ADR methods.

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<sup>85</sup> Wiegand 1996.

<sup>86</sup> *Id.*

<sup>87</sup> If an ombud serves at the whim of a government with little job security, for example, he or she may be tempted to forgo well-deserved criticism of administrative actions.

<sup>88</sup> Krent 2000.

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All negotiations are not the same, however. Even if one agrees to negotiate, parties can use different approaches to negotiation, which creates variations in the negotiation process. Parties tend to adversarial bargaining,<sup>89</sup> interest-based bargaining,<sup>90</sup> or a combination of these approaches<sup>91</sup> during the negotiation process. In adversarial bargaining, parties focus on legal rights, tactical positions, gaming the process, and the use of power to distribute limited resources. Typically, this means a party will make extreme offers, offer few concessions, make threats, and distort information in an effort to be the “winner” in what is typically a win-lose scenario.<sup>92</sup> In the interest-based approach, parties focus on meeting their underlying needs and objectives in order to create joint solutions that fairly address their mutual interests. This approach tends to require parties to separate people from the problem, focus on underlying interests, generating a variety of options before deciding what to do, and making decisions based upon objective criteria.<sup>93</sup>

Irrespective of their theoretical approach, in the context of investment disputes parties might use different types of negotiated ADR. The parties to the dispute may use, for example, either direct or indirect forms of negotiation.

#### *a. The Utility of Indirect Negotiation*

Diplomacy is a form of indirect negotiation. In this process, investors might encourage their home government to engage in private diplomatic discussions with the host country to resolve their underlying complaints about host government behavior. These government-to-government negotiations may increase investors’ leverage. Having their home government to advocate on their behalf brings political clout to the dispute resolution table and emphasizes

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<sup>89</sup> This process has also been referred to in the literature as distributional or positional bargaining (Carrie J. Menkel-Meadow, Lela Porter Love and Andrea Kupfer Schneider, *Mediation: Practice, Policy and Ethics* (2006) [Hereinafter Menkel-Meadow et al. 2006], pp. 39–51).

<sup>90</sup> This process is also referred to as problem-solving, integrative bargaining or principled bargaining; *Id.*

<sup>91</sup> There is a broad literature on negotiation style. See, e.g., G. Richard Shell, *Bargaining for Advantage: Negotiation Strategies for Reasonable People* (Penguin: 1999); Martin A. Rogoff, “The Obligation to Negotiate in International Law: Rules and Realities,” 16 MICH. J. INT’L L. 141 (1994) [Hereinafter Rogoff 1994]; Chris Guthrie, “Panacea or Pandora’s Box?: The Cost of Options in Negotiation,” 88 IOWA L. REV. 601 (2003) [Hereinafter Guthrie 2003]. As a thorough discussion of this important point is beyond the scope of this project, this chapter only provides a cursory overview of the literature.

<sup>92</sup> Russell Korobkin, “A Positive Theory of Legal Negotiation,” 88 GEO. L.J. 1789 (2000) [Hereinafter Korobkin 2000].

<sup>93</sup> Fisher and Ury 1981; Carrie J. Menkel-Meadow, “Toward Another View of Legal Negotiation: The Structure of Problem Solving,” 31 UCLA L. REV. 754 (1984) [Hereinafter Menkel-Meadow 1984].

the importance of the claim. Such an approach may also expand the range of potential solutions by introducing the resources of another party into the dispute resolution process. Nevertheless, there are drawbacks. First, an investor's home government may have little interest in pursuing an investor's claim; and investors will have expended resources for a minimal return. Between 1960 and 1974, for example, the United Nations identified 875 distinct governmental takings of foreign property in 62 countries, but it unclear whether investors' home governments ever pursued these claims.<sup>94</sup> Second, should a government decide to espouse an investor's claim, investors run the risk of having their disputes inextricably intertwined with larger inter-governmental objectives. As a result, little may come from the negotiation. Third, even if negotiations prove successful, investors may find themselves subject to a unsatisfactory resolution over which they had little input or control and which does not address their needs. Fourth, there may be difficulties with enforcement of any diplomatic agreement.

### *b. The Benefits of Direct Negotiation*

An investor also might engage in direct negotiations with a host country government. This option gives more direct control over the process, management and result of the dispute resolution process. It also provides an opportunity to create a solution that is most likely to address the parties' unique needs and interests. Investors and the host country government may find negotiation useful in the case of infrastructure projects, in which protracted dispute resolution may create alienation in a critical on-going relationship; or where there is a desire to minimize the time and cost allocated to resolving small conflicts.

In the context of disputes being resolved primarily by arbitration, there is some anecdotal evidence suggesting that parties have used direct negotiations successfully. ICSID's website suggests that several ICSID cases concluded with settlement agreements. Some of these are BIT claims, such as *AES Summit Generation v. Hungary*; and at least two BIT-based claims, *Lemire v. Ukraine* and *Goetz v. Burundi*, have awards embodying settlement agreements.<sup>95</sup> Interestingly, several of these cases have resulted in settlement after a jurisdictional decision.<sup>96</sup> Meanwhile, counsel for ICSID has also noted that

<sup>94</sup> Jeswald W. Salacuse, "BIT by BIT: The Growth of Bilateral Investment Treaties and Their Impact on Foreign Investment in Developing Countries," 24 INT'L LAW. 655, 659 (1990) [Hereinafter Salacuse 1990].

<sup>95</sup> ICSID List of Pending and Concluded Cases 2006 (<http://www.icsid.org>).

<sup>96</sup> ICSID does not have a publicly available list of investment treaty cases that have resulted in settlement. A cursory analysis of ICSID's website and other publicly available awards, however, indicates that, after a

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there are an “increasing percentage of ICSID [arbitration] cases that are discontinued following settlement.”<sup>97</sup> There have also been negotiated settlements in the context of *ad hoc* arbitration, such as in *Ethyl Corp. v. Canada*, which also settled after a jurisdictional award.<sup>98</sup>

While this anecdotal evidence suggests negotiation has some promise for resolving investment treaty conflict, there are several limitations. First, there is little empirical evidence systematically analyzing the role that direct or indirect negotiation plays in the resolution of investment disputes. It is therefore unclear to what extent this anecdotal information is generalizable to a larger population of investment disputes. Indeed, there may be a sample bias. Those cases settling after the invocation of the ICSID arbitration mechanism may be systematically different than those negotiated settlements arising in different contexts. Likewise, because investment disputes are confidential (either because they are not registered through the ICSID system or have not yet escalated to become public knowledge), there may be fundamental variances between confidential settlements and those cases for which there is public information. Second, although it is clear that some cases are settling, the confidential nature of the settlement means that it is impossible to analyze how the negotiations occur and what factors affect parties’ willingness and ability to settle. Third, because the settlements are confidential, it is difficult to evaluate longitudinally compliance with the settlement, parties’ satisfaction with the substantive result and the recurrence of later investment-related disputes. It would, therefore, be useful to obtain empirical evidence to analyze the potential benefits of negotiation.

#### *c. The Common Challenges for Negotiated ADR*

Despite its strengths, negotiated ADR inevitably has certain pitfalls. As a non-binding and consensual mechanism, there are challenges related to

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decision on jurisdiction, several BIT-based cases have settled, including: (1) *Impregilo S.p.A. v. Islamic Republic of Pakistan*, ICSID Case No. ARB/03/3, (2) *IBM World Trade Corp. v. Republic of Ecuador*, ICSID Case No. ARB/02/10, (3) *Aguas del Tunari S.A. v. Republic of Bolivia*, ICSID Case No. ARB/02/3, and (4) *SGS Société Générale de Surveillance S.A. v. Islamic Republic of Pakistan*, ICSID Case No. ARB/01/13. (ICSID List of Pending and Concluded Cases 2006; ICIS List of Online Decisions 2006; Investment Treaty Arbitration, Chronological Listing of Awards [as of 11 August 2006] [[http://ita.law.uvic.ca/chronological\\_list.htm](http://ita.law.uvic.ca/chronological_list.htm)]).

<sup>97</sup> Onwuamaegbu 2005.

<sup>98</sup> Coe 2005, pp. 29–30; ITA Awards 2006.

securing consent to negotiate, how negotiations occur, the enforceability of the agreement and the public nature of the rights.

Obtaining host country government consent to negotiate may prove challenging. Particularly where governments are not required to negotiate, host country governments might reject or ignore requests for consultation.<sup>99</sup> There may also be difficulties engaging in negotiation where there is intra-government conflict. Governments may find it difficult to use negotiation when: (1) the government is unaware one of its subdivisions, agencies or instrumentalities has engaged in conduct that has led to a dispute, (2) it is unclear what agency is responsible for dispute resolution, (3) a responsible agency does not have authority to settle the dispute, or (4) there may be no governmental resources or funds appropriated to resolve the conflict. Particularly in a novel, complex and inconsistent area like investment treaty law, settling disputes through negotiation can be challenging because of the need for a clear record showing the facts and the law that justify a settlement.<sup>100</sup>

Governments may also actively wish to avoid an investor's approach for negotiation when binding, rights-based adjudication is preferable. Parties may believe adjudication will produce a substantially better result. Parties may also wish to avoid the political fallout for not exhausting all of their legal rights or agreeing to settle a politically sensitive dispute. In some cases it may be more politically expedient to have a third-party impose a decision, rather than having a compromise be seen as a betrayal of national interests.<sup>101</sup> Beyond this, parties may wish to pursue adjudication initially if is likely to create a more favorable opportunities to negotiate a settlement in the future.

The negotiation process itself contains a series of challenges. Because it is non-binding, parties need not pursue negotiation once it starts. Should parties use negotiation to manipulate or delay the proceedings in pursuit of other objectives, this can complicate the dispute resolution process. Negotiation can also be ineffective if the parties' positions are far apart and there are few common interests to create a zone of possible agreement.<sup>102</sup> Particularly for parties using adversarial bargaining, the lack of certainty about the parties' legal rights means parties become entrenched in their reasonable beliefs that

<sup>99</sup> Merrills 2005, pp. 23–24.

<sup>100</sup> Rubins 2006; Legum 2006.

<sup>101</sup> Rubins 2006.

<sup>102</sup> *Id.*

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their case is stronger as a matter of law. This can translate into a belief that compromise is unnecessary, which makes negotiation difficult.

The process can also be complicated by a “stakeholder problem,” where it is unclear who must or should be present at the negotiation table. This can manifest itself in different ways. For example, having inappropriate people involved in negotiations can create difficulties. There may be challenges identifying the right persons who can negotiate effectively on behalf of a government and commit the host country government to a settlement.<sup>103</sup> This can create challenges when a critical branch of government, a key government representative or private entity is absent. Likewise, failure to include other critical stakeholders—such as groups directly affected by the settlement—may create problems. In any of these scenarios, this prevents the forging of a consensus; or, even if an agreement is reached, the negotiated solution may not properly resolve the underlying dispute. The end result is that negotiation that is not handled properly is the breeding ground for future disputes.

Even if negotiations lead to a settlement, there may still be problems with enforcement of settlement agreements. One can only imagine a change in government or corporate leadership that leads a party to abandon the settlement agreement—at which point parties may need again to consider the ADR implications.

Finally there may also be a category of concerns related to the public nature of these rights. Investment treaty rights arise from public international law obligations and tend to implicate public issues.<sup>104</sup> Particularly given the state of the case law in this area, at least one scholar has articulated a concern that such private resolution “is one less reasoned adjudication than might otherwise have been available to contribute” to the development of the jurisprudence.<sup>105</sup> Although written in the context of domestic dispute resolution, the work of Owen Fiss suggests that any loss of the public adjudication of public rights is likely to have an adverse affect on adjudicator’s capacity to redress power imbalances and trivialize the remedial effects of claims designed to redress public wrongs. To the extent that more formal and public adjudication are lost, it runs the risk of imposing profound social costs.<sup>106</sup>

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<sup>103</sup> Onwuamaegbu 2005.

<sup>104</sup> Franck 2005b, pp. 70–77.

<sup>105</sup> Coe 2006, p. 25.

<sup>106</sup> Owen M. Fiss, “Against Settlement,” 93 *YALE L.J.* 1073 (1984) [Hereinafter Fiss 1984].

There is no doubt that these are important considerations in choosing how to resolve disputes, but this does not mean that the benefits of negotiation should be overlooked. The opportunity to create tailor-made resolutions in a cost-effective manner is a fundamental attribute. The goal should be to use dispute systems design to help determine if, when and under what circumstances should cases be negotiated.<sup>107</sup>

### Facilitated ADR

Like its negotiated ADR counterpart, the goal of facilitated ADR is to harmonize parties' expectations, refine claims, clarify the issues, encourage settlement, and thereby decrease transaction costs, improve satisfaction with the result and prevent the recurrence of future disputes. It differs, however, in the process by which these goals are achieved. Facilitated ADR involves a neutral third-party assisting the disputants to reach a satisfactory resolution. This typically involves some form of conciliation or mediation. It might also involve the use of an ombudsperson.

#### *a. Distinguishing Mediation and Conciliation*

In the international context, commentators suggest conciliation and mediation are often used interchangeably.<sup>108</sup> Doubtless, this is because both processes involve a neutral third party assisting the parties to reach a solution of their own accord.<sup>109</sup> Employing the services of a third-party neutral to resolve disputes peacefully is precisely why both mechanisms are a form of facilitated ADR.

<sup>107</sup> Carrie J. Menkel-Meadow, "Whose Dispute Is it Anyway?: A Philosophical and Democratic Defense of Settlement (In Some Cases)," 83 GEO. L.J. 2663 (1995) [Hereinafter Menkel-Meadow 1995].

<sup>108</sup> UNCTAD 2003b, p. 21; Coe 2005; Rubins 2006; Alan Redfern and Martin Hunter, *Law and Practice of International Commercial Arbitration*, 4th Edition (Sweet and Maxwell: 2004). Redfern and Hunter nevertheless suggest at pp. 37–38 that a distinction might be appropriate. They note that a mediator "will listen to an outline of the dispute and then meet each party separately—often 'shuttling' between them—and try to persuade the parties to moderate their respective positions". On the other hand, "a conciliator was seen as someone who went a step further than the mediator, so to speak, in that the conciliator would draw up and propose the terms of an agreement that he or she considered represented a fair settlement."

<sup>109</sup> Onwuamaegbu 2005; Luis Miguel Diaz and Nancy J. Oretskin, "Mediation Furthers the Principles of Transparency and Cooperation to Solve Disputes in the NAFTA Free Trade Area," 30 DENV. J. INT'L L. AND POL'Y 73 (2001) [Hereinafter Diaz and Oretskin 2001].



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Nevertheless, for the purposes of clarity, managing the expectations and creating a common framework for discussion, this chapter draws a distinction between the two concepts. The key difference between mediation and conciliation is the degree and formality of the process.

Mediation is an informal process in which mediators tend to focus on identifying interests, reframing representations and canvassing a range of possible solutions to move the parties toward agreement.<sup>110</sup> There are many forms of mediation, which might involve anything from a mediator serving as information conduit or creating an atmosphere to loosen tension, to engaging in “shuttle diplomacy” to trying to transform the parties’ relationship.<sup>111</sup> Mediation is not about using a series of rules or legal rights to resolve disputes. Rather, it uses a process-based model to bring two parties closer together toward agreement. Although there are variations, most mediation tends to focus on stages of dispute resolution including: (1) agreeing to mediate; (2) understanding the problem by identifying issues and interests; (3) generating options; (4) reaching agreement; and (5) implementing the agreement.<sup>112</sup> What happens in the individual dispute is largely a function of the parties, the nature of the dispute and the orientation and approach of the mediator.

In contrast, given its historical roots in public international law, conciliation tends to provide a more structured process.<sup>113</sup> Rather than relying on general guidelines, it is replete with formal rules related to jurisdictional objections, potential pleadings, the gathering of evidence and issuing written recommendations for settlement.<sup>114</sup> This makes the process more institutionalized, in a manner akin to formal adjudication. Arbitration commentators acknowledge this and describe conciliation as part of a “rules system” where the procedural formalities are articulated in advance—like civil procedure or evidentiary rules—to indicate how the process will operate and on what basis a neutral will make his or her determination.<sup>115</sup> In this sense, the formality of the process makes conciliation look more like non-binding arbitration.<sup>116</sup> Nevertheless, as conciliation is aimed

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<sup>110</sup> Merrills 2005; Reif 1991.

<sup>111</sup> Menkel-Meadow et al. 2006.

<sup>112</sup> Leonard L. Riskin, *Mediation Training Guide* (2004) [Hereinafter Riskin 2004]; Kathleen Severens, *Basic Mediation Training Manual*, 5th Edition (International Institute for Negotiation and Conflict Management: 2005) [Hereinafter Severens 2005]; Diaz and Oretskin 2001, pp. 84–86.

<sup>113</sup> Mary Ellen O’Connell, ed., *International Dispute Settlement* (Ashgate Dartmouth: 2003), p. xvi.

<sup>114</sup> Merrills 2005; Reif 1991.

<sup>115</sup> Rubins 2006.

<sup>116</sup> Onwuamaegbu 2005.

at settlement from the outset, parties may be more likely to reach agreement than they would if participating in a full-scale adversary proceeding.<sup>117</sup>

Irrespective of whether it occurs in the context of mediation or conciliation, third-party neutrals can vary in their orientation and approach.<sup>118</sup> There are a variety of different models of facilitative ADR. The approach of Len Riskin's famous "Grid System" asks neutrals to consider whether: (1) the parties wish to define their dispute broadly or narrowly, and (2) the neutral should adopt either an evaluative or facilitative orientation to problem-solving. In an "evaluative" approach, neutrals may find themselves focusing more on evaluating the relative strengths and weaknesses of the merits of parties' factual and legal contentions in order to push settlement in a particular direction. In contrast, a "facilitative" approach may ask involved parties and the neutral party to focus more on identifying creative "win-win" strategies.<sup>119</sup>

Gary Friedman and Jack Himmelstein have also developed an "understanding-based" model of mediation in which parties resolve their conflicts through understanding their adversary's perspectives, priorities and concerns.<sup>120</sup> Other scholars use transformative mediation as a means of transforming the relationship between disputing parties.<sup>121</sup> Still others may find themselves moving between different styles at different points in the process.<sup>122</sup> Nevertheless, regardless of the approach a particular neutral has, parties generally control selection of the neutral(s) and—as part of the appointment process—may condition appointment on using a particular set of tactics or approach during the facilitative ADR process. Particularly given the multiplicity of definitions available for both mediation and conciliation, setting expectations about what to expect from the neutral and the dispute resolution process is useful.

<sup>117</sup> Lester Nurick and Stephen J. Schnably, *The First ICSID Conciliation: Tesoro Petroleum Corp. v. Trinidad and Tobago*, 1 ICSID REVIEW—FOREIGN INVESTMENT LAW JOURNAL 340, 349 (1986) [Hereinafter Nurick and Schnably 1986].

<sup>118</sup> Diaz and Oretskin 2001, pp. 86–87.

<sup>119</sup> Leonard L. Riskin, "Understanding Mediators' Orientations, Strategies and Techniques: A Guide for the Perplexed," 1 HARV. NEGOT. L. REV. 7 (1996) [Hereinafter Riskin 1996]; Leonard L. Riskin, "Decision-Making in Mediation: The New Old Grid and the New New Grid System," 79 NOTRE DAME L. REV. 1 (2003) [Hereinafter Riskin 2003].

<sup>120</sup> Gary J. Friedman and Jack Himmelstein, "Resolving Conflict Together: The Understanding-Based Approach to Mediation," 4 J. AM. ARB. (2005) [Hereinafter Friedman and Himmelstein 2006].

<sup>121</sup> Robert A. Baruch Bush and Joseph Folger, *The Promise of Mediation: The Transformative Approach to Conflict*, Rev. ed. (Jossey-Bass: 2005).

<sup>122</sup> E. Patrick McDermott and Ruth Obar, "What's Going On In Mediation: An Empirical Analysis of the Influence of a Mediator's Style on Party Satisfaction and Monetary Benefit," 9 HARV. NEGOT. L. REV. 75, 108–109 (2004) [Hereinafter McDermott and Obar 2004].

*b. Using Mediation to Resolve Investment Disputes*

UNCTAD has commented favorably about the creating of mediation as a pre-arbitration means of settling disputes, explaining “mediation may be a more useful means of reaching an amicable settlement than the use of comparatively formal conciliation proceedings.”<sup>123</sup> Nevertheless, at present, ICSID does not provide mediation services. ICSID has expressed interest in establishing a mediation facility to allow parties to resolve disputes on a more informal, voluntary and confidential basis—possibly even with a neutral who does not have subject matter expertise.<sup>124</sup> This approach may serve to facilitate communication, decrease the risk that settlement will cause a party to lose face, and narrow the issues in a dispute in order to achieve cost and time savings.<sup>125</sup> While there have been some suggestions about what the process might entail, the future of ICSID’s efforts to create a mediation facility is uncertain.<sup>126</sup>

Policymakers wanting to provide for mediation would need to address various structural matters such as: (1) should mediation be mandatory, (2) would or could it occur independently or concurrently with an imposed ADR process, or (3) whether it would be institutional or *ad hoc*. There might also be concerns about procedural issues, including the process of selecting mediators, the language and location of the mediation and the rules regarding confidentiality.<sup>127</sup>

*c. Using Conciliation to Resolve Investment Disputes*

ICSID does have a facilitative ADR system for resolving investment disputes. Observing that there is a “particular importance to the availability of facilities for international conciliation,” the ICSID Convention establishes a process for making a request for conciliation, constituting a Conciliation Commission and defining the duties of the conciliators.<sup>128</sup> The Convention requires a Commission “to clarify the issues in dispute between the parties and to endeavor to bring about agreement between them upon mutually acceptable

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<sup>123</sup> UNCTAD 2005b, pp. 53–54.

<sup>124</sup> ICSID 2004, p. 4; Onwuamaegbu 2005.

<sup>125</sup> Onwuamaegbu 2005.

<sup>126</sup> There was a suggestion that mediation should be without prejudice to the rights of parties in other forms of dispute resolution. Similarly, it was suggested that mediation be conducted alongside arbitration proceedings so that a settlement agreement might ultimately be incorporated into an award pursuant to ICSID Arbitration Rules 43(2). *Id.*

<sup>127</sup> Diaz and Oretskin 2001, p. 8.

<sup>128</sup> ICSID 2006, pp. 19–21.

terms [and]... may at any stage of the proceedings and from time to time recommend terms of settlement to the parties". Meanwhile, it obligates the parties to "cooperate in good faith ... [and] give their most serious consideration to [the Commission's] recommendations."<sup>129</sup>

While the ICSID's Conciliation Rules do not articulate how the Commission and the parties should carry out their respective mandates, the Rules suggest the Commission may wish to take a more evaluative approach<sup>130</sup> Rule 22 permits the Commission at any time (either orally or in writing) to "recommend that the parties accept specific terms of settlement or that they refrain ... from specific acts that might aggravate the dispute [and] point out to the parties the arguments in favor of its recommendations." In keeping with the more formal nature of conciliation, the Conciliation Rules also let the Commission request written statements from the parties, rule on its own jurisdiction, rule on requests to disqualify conciliators, hold hearings, and take evidence in the form of documents or witness testimony and issue a report at the closure of the proceedings.<sup>131</sup> Despite these suggested formalities, neither the ICSID Convention nor the Conciliation Rules suggest that conciliators are prohibited from engaging in less formal or facilitative actions; this implicitly suggests conciliators retain discretion to fashion the "forum to the fuss."

The Convention and Conciliation Rules require the Conciliation Commission to prepare a report. If the conciliation was successful, the report notes the issues in dispute and records that the parties have reached agreement. If, on the other hand, it appears to the Commission at any time during the process that there is no likelihood of agreement, the Commission's report must simply note the submission of the dispute to conciliation and record the parties' inability to reach agreement.<sup>132</sup>

In its effort to promote conciliation and provide investment-related dispute resolution services, ICSID also has Additional Facility Conciliation Rules for investor-State disputes where the parties have consented to conciliation. The formal procedures for Additional Facility Conciliation are similar to the conciliation procedures occurring under the ICSID Convention, including

<sup>129</sup> *Id.*, Art. 34(1), p. 21. This is not dissimilar from the UNCITRAL Conciliation Rules that permit the conciliator, at any stage of the proceedings, to make proposals for the settlement of a dispute (Nassib G. Ziadé, "ICSID Conciliation," 13(2) *News from ICSID*, 3 (1996) [Hereinafter Ziadé 1996], p. 6).

<sup>130</sup> Nurick and Schnably 1986, p. 348.

<sup>131</sup> ICSID 2006, pp. 89–97.

<sup>132</sup> ICSID 2006, pp. 21, 97–98; Onwuamaegbu 2005.

requesting written statements from the parties, challenges to jurisdiction and disqualification of conciliators, taking of evidence and issuing a report.<sup>133</sup>

As of 2006, ICSID's website reflects that it has only had five cases registered for conciliation: *SEDITEX Engineering Beratungsgesellschaft für die Textilindustrie m.b.H. v. Madagascar* (ICSID Case No. CONC/82/1); *Tesoro Petroleum Corp. v. Trinidad and Tobago* (ICSID Case No. CONC/83/1); *SEDITEX Engineering Beratungsgesellschaft für die Textilindustrie m.b.H. v. Madagascar* (ICSID Case No. CONC/94/1); *TG World Petroleum Ltd. v. Niger* (ICSID Case No. CONC/03/1); and *Togo Electricité v. Republic of Togo* (ICSID Case No. CONC/05/1).<sup>134</sup> It is not apparent whether all these are all investment treaty cases, as substantive information about these conciliations is not publicly accessible. But to the extent that all ICSID cases involve investment conflict, the available information suggests that conciliation can be effective in fostering settlement. In two cases, *TG World* and the first *SEDITEX* conciliation, the parties reached a settlement soon after the request for conciliation was registered and before a Commission was established. In a third case—in which Lord Wilberforce acted as sole conciliator—*Tesoro* ended with a successful settlement that caused counsel for the host country to write “use of ICSID's conciliation facilities deserves serious consideration in every case.”<sup>135</sup> The second *SEDITEX* case appears not to have been subject to further dispute resolution and was not registered for ICSID arbitration. In only one case, *Togo Electricité*, conciliation efforts appear to have been unsuccessful, and ICSID registered a request for arbitration in the four days after the conciliation proceedings closed.<sup>136</sup>

Although limited in number, these cases suggest that certain types of cases may be well-suited for conciliation. Noting that arbitration may be too adversarial in some cases, counsel from ICSID explains that conciliation can be most effective in “cases in which the parties are engaged in an ongoing long-term project, involving significant amounts in sunk costs, where it is necessary to resolve disputes while the project is continuing. Disputes in oil and gas exploration projects, particularly, come to mind—as do mining and long-term

<sup>133</sup> ICSID, ICSID Additional Facility Rules, ICSID/11 (Apr. 2006) ([http://www.worldbank.org/icsid/facility/AFR\\_English-final.pdf](http://www.worldbank.org/icsid/facility/AFR_English-final.pdf)) [Hereinafter ICSID Additional Facility Rules 2006], pp. 27–42.

<sup>134</sup> ICSID, List of Pending Cases (as of 26 July 2006) (<http://www.worldbank.org/icsid/cases/pending.htm>) and List of Concluded Cases (as of 26 July 2006) (<http://www.worldbank.org/icsid/cases/conclude.htm>) [Hereinafter ICSID Pending and Concluded Cases 2006]; Onwuamaegbu 2005.

<sup>135</sup> Nurick and Schnably 1986, p. 344.

<sup>136</sup> ICSID Pending and Concluded Cases 2006.

infrastructure projects.”<sup>137</sup> Overall, the general anecdotal evidence suggests that conciliation can be used directly (as in *Tesoro*) or indirectly (as in *TG World* and *SEDITEX*) to facilitate settlement.

#### *d. Challenges for Facilitative ADR*

Despite this rosy picture, there are limitations to facilitative dispute resolution. Both mediation and conciliation can only be as effective as the parties wish it to be; and this factor may be governed by the parties’ immediate circumstances and the nature of the dispute.<sup>138</sup> Beyond this, there are difficulties generalizing about the efficacy of mediation and conciliation on the basis of ICSID’s conciliation data. There is a risk that the small and limited set of data from ICSID suffers from sample bias. First, it is not clear whether the cases in which parties opted to conciliate are representative of the broader class of investment disputes, let alone treaty-based investment disputes. If the five cases were atypical, then there would be doubt as to the generalizability of conciliation’s utility in other situations. Second, the data only relate to conciliation at ICSID and do not address mediation or conciliation that occurs on an *ad hoc* basis or through a different institution. Given the unique nature of the ICSID Convention and ICSID Conciliation, it is possible that mediation or conciliation occurring under different auspices may be less (or possibly more) successful. It would be helpful to analyze how investment disputes might be resolved, for example, under the UNCITRAL Conciliation Rules. Third, the success of mediation or conciliation may depend heavily upon the identity of the third-party neutral. Where the parties have greater confidence in the neutral, the recommendations are likely to carry greater weight and positively influence settlement.<sup>139</sup> Likewise, if parties appoint neutrals with an insufficient degree of respect from both parties, they may be less successful.

With only five conciliation cases against 132 arbitration cases registered at ICSID in 2005,<sup>140</sup> the sheer numbers suggest that ICSID Conciliation is a disfavored dispute resolution mechanism. Various factors may have led to this phenomenon. It may be caused by a lack of awareness of its existence. Counsel at ICSID has commented that “the Centre has recently begun to remind

<sup>137</sup> Onwuamaegbu 2005.

<sup>138</sup> Merrills 2005, pp. 41–44, 88–90.

<sup>139</sup> Nurick and Schnably 1986, p. 345.

<sup>140</sup> UNCTAD 2005b, pp. 4–5.

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parties of the existence of the [conciliation] mechanism.”<sup>141</sup> This can cause downstream problems, as parties may be hesitant to use a dispute resolution mechanism viewed as untried and untested.

The lack of use may also be a function of the ready availability of arbitration in BITs and parties’ preference for binding adjudication. Parties may view such non-binding dispute resolution as little more than a needless and time-consuming exercise, as it can involve as much time as, and comparable expenses to, binding dispute resolution. Particularly, investors that have already experienced “protracted correspondence, negotiation, and perhaps even administrative battles with the State” may believe “the time has come for more forceful steps. Likewise, State parties may be unwilling to participate in a process that will not yield a solution imposed from the outside, for bureaucratic and political reasons.”<sup>142</sup> Nevertheless, in certain cases, the “prospect of a binding award may be necessary to motivate one party or the other to bargain seriously” in conciliation.<sup>143</sup>

Negotiated and facilitated ADR share common difficulties. Like its negotiated counterpart, facilitated ADR experiences challenges in obtaining party consent. Part of the problem may be a lack of an express consent to a facilitative ADR method in a BIT. Even with pre-existing consent, parties may not elect to use it or may choose to use it in a dilatory manner. Muthucumaraswamy Sornarajah has suggested that conciliation can “be frustrated by the adoption of dilatory tactics.”<sup>144</sup> In addition, there can be challenges with including the appropriate stakeholders and securing enforcement. In the public international law context, one need only consider the *Rainbow Warrior* situation, where France failed to abide by the terms of its mediated settlement and a binding dispute resolution was ultimately required.<sup>145</sup>

Facilitative ADR experiences other unique issues. As a neutral is involved in the facilitation process, it is vital to ensure that the neutral is both perceived to be and actually is independent and impartial. Decision-facilitators that lack these qualities may have an adverse impact on the legitimacy of the dispute resolution process. Another concern is that, given recent concerns about transparency, governments may be disinclined to be involved in non-transparent

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<sup>141</sup> Onwuamaegbu 2005.

<sup>142</sup> Rubins 2006.

<sup>143</sup> Nurick and Schnably 1986, p. 349.

<sup>144</sup> Sornarajah 1994, p. 266.

<sup>145</sup> Bederman 2001, pp. 236–237.

dispute resolution mechanisms. Since facilitative ADR usually occurs in private and is often subject to confidentiality obligations, this may run counter toward the trend toward increased governmental openness.<sup>146</sup> However, facilitated ADR mechanisms are different from imposed ADR mechanisms that provide a public function by adjudicating public rights. Facilitative ADR is not rights-based adjudication and the creation of legal norms, as it is primarily concerned with interest-based dispute resolution. Unlike fact-finding or imposed ADR, in which confidentiality inhibits a full and informed discussion of the disputes, confidentiality in facilitated ADR is necessary to promote a forthright and effective discussion about the parties' mutual interests and concerns. Without confidentiality, the system functions inefficiently; it creates discomfort that inhibits the full and frank discussions that can lead to the articulation of party interests and mutually satisfactory resolutions.<sup>147</sup> If parties were concerned that comments would be used against them later, this would inhibit the discussion necessary to create opportunities for a win-win settlement.<sup>148</sup>

Consideration of these concerns is vital. Nevertheless, "the unprecedented number of pending investor-State cases and the rate at which new cases are filed would seem to warrant a renewed dose of 'serious consideration' with a view to more fully institutionalizing" some sort of facilitated ADR regime.<sup>149</sup> Using dispute systems design to diagnose and appropriately adapt the system could integrate the strengths of a facilitative process while minimizing the risks of the challenges.

### Fact-Finding ADR

Rather than a formal adjudication of substantive rights, fact-finding ADR mechanisms involve identifying a neutral expert or special master to engage in basic fact-finding in a dispute. This mechanism is similar to an expert determination where a neutral fact-finder, presumably with subject matter expertise, finally resolves fundamental—yet contested—issues.<sup>150</sup>

<sup>146</sup> Onwuamaegbu 2005.

<sup>147</sup> Article 35 of the ICSID Convention provides for confidentiality in conciliation proceedings. Interestingly, although parties are prevented from relying on views expressed by the other party or Commission reports or recommendations, there are no provisions as to the confidentiality obligations of Conciliators or non-parties affiliated with the process. *See* ICSID 2006, p. 21.

<sup>148</sup> Ziadé 1996, pp. 3–4.

<sup>149</sup> Coe 2005, p. 44.

<sup>150</sup> Merrills 2005, pp. 45–48; O'Connell 2003, pp. 26, 105–119.



*a. The Benefits of Fact-Finding*

Fact-finding has the potential to narrow the matters in dispute and create common ground between the parties. Particularly where there is a discrete issue—such as asset valuation—that can be definitively resolved at an earlier stage, this might lead to a quick resolution of a dispute. Put in more commercial terms, using fact-finding to determine the scope of damages before liability may permit parties to bargain more effectively once the scope of precise liability is defined. Using fact-finding could save time and costs, permit investors to concentrate on their core business and let host countries focus on the more pressing duties of government. Likewise, narrowing the scope of a potential dispute provides an opportunity to decrease the risk of escalating or exacerbating a dispute, which may be important when there is an ongoing relationship. Beyond this, a fact-finding body can construct a historical record that—much like the work of truth and reconciliation commissions—may produce benefits for both the parties and society at large.<sup>151</sup>

Unfortunately, the practical utility of using fact-finding to resolve investment disputes is under-explored. Theoretically, as neither the Convention nor the Rules expressly prohibit such actions, an ICSID Conciliation Commission might be able to engage in fact-finding as part of its mandate for recommending settlement terms. ICSID Conciliation Rule 22(2) implies that fact-finding may be a critical facility as, when it issues recommendations, the Commission “shall point out to the parties the arguments in favor of its recommendations.”<sup>152</sup> Given the confidentiality limitations of ICSID Conciliation, there is little information on how neutral experts or panels resolve disputed factual issues through a conciliation facility.

Luckily, in 1978 ICSID created provisions for Additional Facility Fact-Finding. Aaron Broches, ICSID’s Secretary-General when the Fact Finding Rules were introduced, observed that the processes would provide parties with an impartial assessment of facts to prevent disputes on specific factual issues and the escalation of disputes.<sup>153</sup>

Unlike conciliation and arbitration, ICSID’s Fact-Finding Rules do not require at least one party be an ICSID member. Rather, provided both parties agree,

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<sup>151</sup> Martha Minnow, *Between Vengeance and Forgiveness: Facing History after Genocide and Mass Violence* (Beacon Press: 1998).

<sup>152</sup> ICSID 2006, p. 94.

<sup>153</sup> Onwuamaegbu 2005.

any investor or government can initiate a fact finding proceeding. The Fact-Finding Rules provide that an independent committee—comprised of a sole or uneven number of commissioners—will examine the disputed facts and provide the parties with an impartial assessment.<sup>154</sup> The Rules envisage that there will be oral proceedings, written submissions, evidence and witness testimony. The Fact-Finding proceedings end with a Report that “shall be limited to findings of fact. The Report shall not contain any recommendations to the parties nor shall it have the character of an award,” and the parties will be “entirely free as to the effect to be given to the Report.”<sup>155</sup> Although the parties could agree otherwise, it is, in other words, primarily a form of non-binding dispute resolution.

As originally conceived, Additional Facility Fact-Finding was intended to be “a process for preventing, rather than settling legal disputes as a result of a perceived need for fact-finding proceedings in the ‘pre-dispute’ stage.”<sup>156</sup> Nevertheless, in nearly 30 years, no cases have ever been brought under this Facility.<sup>157</sup> This may be due to many of the same problems facing ICSID Conciliation. People may be unaware of the existence of the Fact-Finding Facility. Moreover, the lack of a critical mass of cases establishing it as a tried and tested method of dispute resolution may inhibit parties from using it. The default, non-binding nature of the fact-finding may also make it inappropriate for some cases.<sup>158</sup>

Although the Fact-Finding Facility has suffered from non-use, fact-finding deserves renewed consideration. There are minimal institutional costs to maintaining the current facility. Reconsidering its structure and finding ways to make it more acceptable to stakeholders might actually increase the utility of the process.

In the public international law context, fact-finding bodies, such as the “inquiry” process at the Permanent Court of Arbitration, have been useful in making an impartial investigation of disputed facts. The *Dogger Bank* incident

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<sup>154</sup> ICSID, ICSID Additional Facility for the Administration of Conciliation, Arbitration and Fact-Finding Proceedings (January 2003) (<http://worldbank.com/icsid/facility-archive/facility-en.htm>) [Hereinafter ICSID Additional Facility for the Administration of Conciliation, Arbitration and Fact-Finding 2003], p. vi.

<sup>155</sup> ICSID Additional Facility Rules 2006, pp. 20–22.

<sup>156</sup> ICSID Additional Facility for the Administration of Conciliation, Arbitration and Fact-Finding 2003, p. vi.

<sup>157</sup> Onwuamaegbu 2005.

<sup>158</sup> One wonders whether ICSID Fact-Finding would be more effective if the Additional Facility rules were amended to provide binding dispute resolution.

is a classic example. In *Dogger Bank*, a Russian fleet on its way through the North Sea fired on English commercial fishing trawlers; one vessel was sunk, the remaining two ships were seriously damaged, and there were two dead and six wounded among the civilian crew. The Russians claimed they were attacked by Japanese torpedo boats mingling with the trawlers; if this were true, it would have justified the Russian action. The parties submitted this disputed factual issue to an International Commission of Inquiry. The inquiry found “there was no torpedo boat either among the trawlers nor on the spot, [and] the fire opened by Admiral Rozhdestvensky was not justifiable.” After this single fact was established, the conflict was resolved and Russia gave the United Kingdom an indemnity of £65,000.<sup>159</sup> Cases such as this suggest that there is hidden utility in this methodology that deserves further exploration.

### *b. The Challenges of Using Fact-Finding to Resolve Investment Conflict*

There are various difficulties associated with using Fact-Finding ADR. *Dogger Bank* is only one of five fact-finding commissions at the Permanent Court of Arbitration, which suggests fact-finding processes may not be suitable for broad types of dispute resolution.<sup>160</sup> Moreover, as investment disputes often involve disputes of fact, law and mixed questions of fact and law, many cases may not be suitable for fact-finding. Pure fact-finding commissions might complicate—rather than streamline—the dispute resolution process. As fact-finding does not generally appear as a dispute resolution option in investment treaties, it may prove difficult to get party consent. After a dispute has arisen, it may be challenging to secure party agreement on the use of fact-finding.

There may be other difficulties. Both the investor and State must be willing to accept that a fact-finding body—possibly in public<sup>161</sup>—may show that their

<sup>159</sup> Merrills 2005, pp. 47–48.

<sup>160</sup> “Dispute Settlement: General Topics—1.3,” UNCTAD, Permanent Court of Arbitration, UNCTAD/EDM/Misc.232/Add.26 (2003) ([http://www.unctad.org/en/docs/edmmisc232add26\\_en.pdf](http://www.unctad.org/en/docs/edmmisc232add26_en.pdf)) [Hereinafter UNCTAD 2003a], p. 12.

<sup>161</sup> The confidentiality of ICSID’s Fact Finding Additional Facility is uncertain. The Commission certainly has confidentiality obligations, which were “aimed at fostering an environment of free and uninhibited negotiations...[where] either party would not be restrained by the fear of prejudicing itself should the conciliation prove fruitless” (Ziadé 1996, p. 4). Article 8 requires commissioners to declare they “shall keep confidential all information coming into my knowledge as a result of my participation in the proceeding as well as contents of any report drawn up by the committee”; and Article 9 provides that that the “sessions of the Committee shall not be public” (ICSID Additional Facility Rules 2006, pp. 19–20). Likewise, Article 4(5) of the Additional Facility Rules requires the Secretary-General to “keep confidential any or all information furnished to him” (*Id.*, p. 12). Nevertheless, the rules are silent as to whether the

version of the facts is wrong. As a practical matter, parties may be unwilling to subject themselves to the scrutiny and potential embarrassment. There is some evidence that States may be particularly sensitive to a risk of loss, particularly when it involves reputational harm.<sup>162</sup> Finally, there may be enforcement difficulties, particularly where parties have not agreed to be bound by the factual determinations. While noteworthy, these concerns should not mean investors and States reject this option out of hand. Rather, parties may wish to consider creating a system that incorporates fact-finding facilities at an appropriate juncture for appropriate disputes.

### Advisory ADR

Advisory ADR might be used to evaluate and “reality-test” the parties’ respective claims so that they can make more informed decisions as to the utility of pursuing formal adjudication. This might involve engaging in some sort of early evaluation by a neutral, a mini-trial or some form of non-binding arbitration.

#### *a. Opportunities for Advisory ADR*

In early neutral evaluation, parties may choose a third party to provide an opinion on a legal issue in dispute. In the U.S. domestic context, early neutral evaluation has been used successfully to resolve claims. One empirical study indicates that 80% of lawyers who were required by a court to go through this process later reported they were satisfied with the process and would voluntarily use early neutral evaluation in the future. The same study also suggested that the key predictor to having a successful early neutral evaluation was the attitude and skills of the neutral evaluator.<sup>163</sup>

A mini-trial typically involves attorneys for each side presenting the major aspects of their case to a tribunal composed of their respective clients as well as a presiding neutral who can then advise about a probable outcome and

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parties have a duty of confidentiality or whether the public is prevented from attending those hearings that are not committee sessions, which are related to the proceeding.

<sup>162</sup> Andrew T. Guzman, “The Cost of Credibility: Explaining Resistance to Interstate Dispute Resolution Mechanisms,” 31 J. LEGAL STUD. 303 (2002).

<sup>163</sup> Joshua D. Rosenberg and H. Jay Folberg, “Alternative Dispute Resolution: An Empirical Analysis,” 46 STAN. L. REV. 1847 (1994) [Hereinafter Rosenberg and Folberg 1994].

work with the clients to facilitate settlement.<sup>164</sup> Corporate entities have used mini-trials successfully to promote the free exchange of information and focus the minds of top management on the strengths and weaknesses of their respective cases. The private nature of this process has the potential to minimize costs and time allocated to dispute resolution, preserve an on-going relationship and avoid potential public embarrassment.

Little work has been done to consider how these procedures might apply in the context of investment disputes. This may be due to the challenges that these forms of dispute resolution are likely to face. Presumably some of the benefits of early neutral evaluation might be captured by formats such as ICSID Conciliation or ICSID Additional Facility Conciliation. Moreover, there is an argument that ICSID Conciliation already essentially is non-binding arbitration. There may be critical benefits to working within an existing institution, such as ICSID. Provided it is not inconsistent with the ICSID Convention, it may be possible to modify the nature of the dispute resolution services—or the parties' expectations in how they will be utilized—in order to capture benefits from other ADR formats.

### *b. Challenges Related to Advisory ADR*

Despite the benefits, there are inevitably potential costs. Mini-trial and non-binding arbitration have challenges similar to those experienced by imposed ADR—namely they arguably have all of the costs and none of the benefits of reaching a binding decision. Moreover, to the extent that these non-binding proceedings have the look and feel of binding dispute resolution but are nevertheless private, there may still be concerns related to the public interest and a lack of transparency. Particularly in the context of a mini-trial, non-governmental organizations may wish to participate in the process; and there may be repercussions for exclusion. One also wonders, however, whether States have the same cost-benefit calculus as investors. Presumably foreign investors are rationale actors motivated by the need for profit and would be willing to settle under the acceptable commercial conditions; nevertheless, this may not always be the case and investors may not be able to use the process effectively. Meanwhile, host country governments—who may be influenced by commercial realities—may be more motivated by political objectives. They may also lack the flexibility to settle on purely commercial terms.

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<sup>164</sup> Costantino and Merchant 1996, p. 40.

Other factors such as clear authority to settle, the availability of funds, the legal risk and the likelihood of recovery may affect a government's ability to accept the result of early neutral evaluation or a mini-trial. Nevertheless, it is possible that certain disputes might benefit from the availability of this process, and thus this issue is worthy of more systematic consideration.

### Imposed ADR

Imposed ADR is at the most formal end of the dispute resolution continuum. Imposed ADR procedures typically involve an adjudicatory body making a final and binding decision. In this context, adjudicators are typically neutral and may base their decisions upon legal principles.<sup>165</sup> In the international context, the precise format of imposed ADR can vary. The adjudicators might be either arbitrators or judges; and judges may either come from national courts or international judicial bodies. The adjudication process may occur at a mixed claims commission, a claims tribunal akin to the Iran–U.S. Claims Tribunal, a series of independent *ad hoc* arbitral tribunals, or litigation under the auspices of the International Court of Justice (ICJ). It might also take the form of international litigation before a national court. Under each of these approaches, the adjudicators will be bound to follow different set of rules and regulations during the process of resolving the parties' dispute.

#### *a. The Benefits of Imposed ADR*

This chapter has already alluded to a variety of benefits to using an imposed ADR option. The nature of imposed ADR makes its availability critical to promote the final and binding adjudication—and permit bargaining in its proverbial shadow. Many (but not all) imposed ADR methods—particularly arbitration and national court judgments—have the benefit of efficient international enforceability. Imposed ADR has also experienced an increased push toward transparency, which promotes democratic values. Admittedly, imposed ADR varies in its commitment to transparency. The proceedings before the ICJ and the Iran–U.S. Claims Tribunal are typically open to the public. Many—but not all—national courts are transparent. Meanwhile, there is an increasing trend toward transparency in investment treaty arbitration.<sup>166</sup>

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<sup>165</sup> Merrills 2005, pp. 91–92.

<sup>166</sup> Franck 2005a; Franck 2005b.

Specific forms of imposed ADR may have unique benefits. Arbitration and mixed claims commissions have the added benefit of being able to tailor the procedural framework to the issues in the particular dispute. They also offer the benefit of limited opportunities to attack the adjudicator's decision, which further streamlines the dispute resolution procedure. Presumably, such tailoring is likely to create disputes that may be faster and less expensive than their counterparts in national court litigation. Beyond this, there may be utility in being able to "blame any unfavorable result on three foreign arbitrators" and shift responsibility away from the parties.<sup>167</sup>

### *b. The Costs of Imposed ADR*

Nevertheless, not all of these theoretical benefits are realized. Arbitration has particular risks.

#### **i. Lost Time and Money**

Cases can take years to arbitrate and cost more than litigation or other forms of dispute resolution.<sup>168</sup> Anecdotal evidence in the investment context suggests a similar phenomenon, which suggests that—rather than focusing on their core commercial or governmental objectives—parties expend significant resources on dispute resolution. Even investors that have successfully claimed under investment suggest that investment arbitration is simply "too slow, too costly and too indeterminate."<sup>169</sup> Increased fiscal costs for resolving disputes implicate other hidden costs, which may limit parties' access to justice. A smaller corporate investor, particularly with a small dispute, may be unable to pursue arbitration because of the extensive costs—even though the investor is being deprived of investment rights. The situation is more pronounced when a group of small companies are each experiencing distinct deprivations, but have no commercial choice but to absorb the cost of the violation of their legal rights.<sup>170</sup> Likewise, a host country government with limited financial resources may experience a similar phenomenon when it must defend itself on an inadequate budget. Ultimately, the financial cost of imposed ADR may,

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<sup>167</sup> Jeswald Salacuse, *Alternative Methods of Treaty-Based, Investor-State Dispute Resolution* (2006), p. 14 [copy on file with author].

<sup>168</sup> Christian Bühring-Uhle, *Arbitration and Mediation in International Business* (Kluwer: 1996), pp. 140–148.

<sup>169</sup> Coe 2005, p. 9.

<sup>170</sup> Vicuña 2001.

as a practical matter, limit those who have access to the forum. This suggests that the stakeholders may be benefited from a system that provides a broader set of ADR mechanisms.

### ii. Arbitrator Neutrality

There are also concerns that arbitrators are not perceived to be neutral in their adjudication. While there are opportunities to challenge arbitrators who lack impartiality or independence, there are nonetheless continuing reasons for parties' negative perceptions of the fairness and integrity of the dispute resolution process. There may, for example, be difficulties related to an arbitrator's potential "issue conflicts," where the same person serves as arbitrator and counsel in two separate cases with related legal issues and has the capacity to create legal authority as an arbitrator that may be of benefit to a client in his or her role as counsel.<sup>171</sup> Similarly, arbitrators may act as non-neutrals or advocates; there is also the possibility of "toxic" arbitrators who may disrupt or delay proceedings to the advantage of one party.<sup>172</sup>

### iii. Party Control Over Outcome

Although control of the dispute resolution process is also a benefit, this may be illusory. Investment treaties typically present investors with pre-determined options for where and how their disputes can be resolved through arbitration. Although having one option is better than none, one wonders, for example, why countries would want to close the door to their local courthouses or other forms of imposed ADR. For example, although Mexico is willing to entertain NAFTA-based investment litigation, domestic legislation in the United States and Canada appears to prevent foreign investors from bringing NAFTA claims in their respective national courts.<sup>173</sup> Likewise, one wonders whether Argentina would have been happier with an option to create a mixed claims commission to deal with the universe of claims it received as a result of its currency crisis. Beyond a simple choice of forum, requiring arbitration presupposes the use of procedural rules that investors had little opportunity to negotiate; and while

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<sup>171</sup> Judith Levine, "Dealing With Arbitrator 'Issue Conflicts' in International Arbitration," 61 *APR. DISP. RESOL. J.* 60 (2006) [Hereinafter Levine 2006].

<sup>172</sup> James H. Carter, "Improving Life with the Party-Appointed Arbitrator: Clearer Conduct Guidelines for 'Nonneutrals,'" 11 *AM. REV. INT'L ARB.* 295 (2000) [Hereinafter Carter 2000]; Susan D. Franck, "The Role of the International Arbitrator," 12 *ILSA J. INT'L AND COMP. L.* 499 (2006) [Hereinafter Franck 2006].

<sup>173</sup> Franck 2005b.



parties can attempt to agree to variations after the fact, as a practical matter this may prove challenging once a dispute has arisen.

#### **iv. Transposing Benefits into Costs: Confidentiality and Discretion**

In the context of treaty arbitration, some of the benefits of arbitration can become costs. Confidentiality and discretion are two key examples. Confidentiality was historically extolled as a reason to opt for arbitration. Nevertheless, the lack of transparency of the awards and the process of resolving investment disputes has costs. Investment treaties are public documents that articulate public law rights, which are fundamentally different from private commercial rights in at least two ways.

First, treaty disputes have considerable third-party implications that implicate the public interest.<sup>174</sup> Beyond the effect experienced by a foreign investor or its shareholders, investment arbitration affects taxpayers of the host government as well as entities impacted by its legislative and regulatory choices.<sup>175</sup> Excluding those impacted by the resolution of the investment dispute can foster a sense of unfairness and a lack of procedural justice. Particularly for democratic institutions with a tradition of giving the governed a voice in the process of government, this can lead to a backlash with financial and political costs. As a result, it is unsurprising that governments such as those of the United States and Canada have worked to redress this procedural difficulty by making access to awards, pleadings and hearings more open.<sup>176</sup> What is more surprising, however, is the failure of other countries with democratic institutions to follow this lead.

Second, because these awards interpret new international investment rights, keeping treaty claims confidential prevents the efficient and consistent development of a coherent and considered legal doctrine. Unlike commercial law where there is a developed body of law and precedent, investment treaty law is relatively new. As a result, there is a dearth of established legal doctrine. The awards in recent cases that are publicly available have only just begun to sketch the boundaries of legal rights, and the academic literature is still in its formative years. While making awards public arguably increases the cost of arbitration—as tribunals and parties must address them—this overlooks fundamental costs

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<sup>174</sup> OECD, “Transparency and Third Party Participation in Investor-State Dispute Settlement Procedures: Statement by the OECD Investment Committee” (11 June 2005) (<http://www.oecd.org/dataoecd/25/3/34786913.pdf>).

<sup>175</sup> Franck 2005b.

<sup>176</sup> *Id.*

of confidentiality. The availability of analogous cases, legal reasoning or *amicus* submissions can increase the efficiency of a tribunal's determinations and improve the quality of the tribunal's reasoning. In addition, by signaling that like cases will be treated alike, it promotes perceptions of fairness and supports the legitimacy of the process.

Confidentiality also leads to uncertainty for both investors and host governments attempting, respectively, to organize their investments, make governmental policy and determine dispute resolution strategy. Without a sense of how the law will be applied—and access to the awards making those determinations—there can be little justified reliance. While investment arbitration awards are not *de jure* precedent, tribunals and parties treat them as *de facto* authority and rely upon them. Keeping cases confidential deprives tribunals of useful reasoning, prevents tribunals from treating like cases alike and also denies investors and governments a reasonable opportunity to organize their respective affairs in accordance with articulated legal standards.

It seems that governments originally thought that confidentiality was appropriate. Presumably this may have been because they anticipated that there would only be a small number of claims and there was no need to publicize the possibility of government liability; governments may also have been less concerned about inconsistencies in the decisions because, with confidentiality, there would be blissful ignorance of potential inconsistencies. Recent history, however, demonstrates the fallacy of both these propositions. The number of claims has increased; and as arbitrators search for authority to inform their own reasoning when faced with novel legal rights, they have sought out similar awards. Because of the critical nature of the issues raised in investment disputes, awards have found their way into the public domain. As the historical benefit becomes a liability, the future challenge will be how best to manage the need for confidentiality against the desirability of public access.

The use of arbitrators' open-textured discretion to adjudicate cases has also created unexpected costs.<sup>177</sup> In some contexts, parties may need arbitrators to exercise more discretion to issue awards quickly with minimal legal reasoning. This might be desirable in certain circumstances. For example, in labor arbitration there is a preference for final discretionary awards that need not be consistent; this can help prevent labor unrest. Nevertheless, in the context of

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<sup>177</sup> Coe 2005; Michael A. Scodro, "Deterrence and Implied Limits on Arbitral Power," 55 DUKE L.J. 547 (2005).

investment treaty claims, unreasoned and quick awards may be undesirable. It can create confusion. Unexplained decisions create difficulties for parties and arbitrators in understanding the scope of substantive investor protections and what circumstances should constitute liability-creating events. It can also increase litigation risk where tribunals make procedural determinations with an outcome-determinative effect. If, for example, tribunals exercise discretion to shift arbitration costs under the applicable rules—but they do not explain either the legal authority for or their rationale for making a decision—parties may question the fairness and basis of the determination. Likewise, if arbitrators do not shift costs, and still do not explain why, investors and governments are again left in the same precarious situations wondering what factors justify the determination. Perhaps more importantly, investors and host governments involved in future disputes will have minimal information available to them to predict how future tribunals might evaluate costs-related measures, which may not be an insignificant aspect in the case. In *Aguas Del Tunari v. Bolivia*, while the investor claimed at least US\$25,000,000 in damages, the settlement ultimately made Bolivia responsible for US\$1,600,000 in legal fees—well over 5% of the claimed compensation.<sup>178</sup> As parties bargain in the shadow of the law, relying on arbitrator discretion—without information about how rules, standards, practice, and precedence will influence the exercise of that discretion—prevents parties from negotiating effectively. Without reliable and predictable information about the potential costs of the arbitration procedure, there could be an adverse impact on parties' capacity to engage in an accurate and clear cost-benefit calculus.

### *c. Moving Beyond Investment Treaty Arbitration*

Ultimately, investment treaty arbitration may not be everything its creators wished it to be. There are a variety of factors that suggest the theoretical benefits of arbitration may not materialize and purported benefits can transform into costs. This ultimately suggests that it is unwise to focus unduly on arbitration as an all-purpose paradigm.

It does suggest that the time is right to consider proactively how to use other imposed ADR mechanisms—such as a claims commission—to resolve disputes with finality. There have been some suggestions, for instance, that this

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<sup>178</sup> Paul Harris, *Company Drops Demand over Water Contract Canceling*, SAN FRANCISCO CHRONICLE (19 January 2006) p. A-3.

format might address concerns related both to transparency and consistency.<sup>179</sup> Likewise, it suggests that it may be useful to think systematically about the range of ADR mechanisms. As this chapter suggests, other processes—particularly underutilized facilities at ICSID and with ombuds—are promising options. The challenge will be to determine the right blend of party autonomy, efficiency and due process for a wide range of circumstances.

There has been some scholarship that has begun to consider how specific aspects of the ADR continuum, namely mediation and conciliation, might usefully improve the system.<sup>180</sup> Coe has made significant strides in thinking systematically about how and when to use facilitated ADR in connection with imposed ADR. Nevertheless, one wonders whether this conception of the problem is overly narrow. The challenge may be to expand one's conception of conflict management to think more broadly about how to diagnose the difficulties the system is facing, critique the existing process and provide principles to guide the creation of effective and legitimate dispute resolution systems.

## Challenges for the Future

The challenge for the future is how to think seriously about the value of designing comprehensive dispute resolution mechanisms to resolve investment disputes. Being systematic in the approach to conflict management could provide a unique opportunity to capitalize on the efficiency of various processes across the ADR continuum. It also provides an opportunity to increase satisfaction both with the process and the ultimate result, as well as promoting integrity of the dispute resolution system. Nevertheless, there will be challenges as different governments perhaps make different assessments of the utility of engaging in this level of conflict management.

We are at a unique historical juncture in the evolution of resolving investment-related disputes. We have an opportunity not just to ask how to improve the arbitration system by focusing on issues such as transparency, consistency and coherence; rather we can and should consider how to manage conflict related to investment treaties in a systematic manner. Arbitration is no doubt part of that puzzle. But as the review of the dispute resolution continuum suggests, there are other opportunities worthy of ongoing consideration.

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<sup>179</sup> W. Michael Reisman, "Control Mechanisms in International Dispute Resolution," 2 U.S.-MEX. L.J. 129, 136-137 (1994); Franck 2005b, pp. 81-82.

<sup>180</sup> Coe 2006; Rubins 2006; Legum 2005; Onwuamaegbu 2006.

**PART III: PROMOTING CONSISTENCY AND COHERENCE**

The opportunity to decrease costs, increase efficiency and interject procedural fairness in the system should not be discounted. The evaluation of the structure can provide a reasoned explanation for the status quo and give stakeholders affected by the outcome of disputes a chance to participate in the system's creation. Ultimately, such an analysis has the unique benefit of strengthening the legitimacy of the dispute resolution process and giving stakeholders confidence in the system's capacity to protect their rights and produce just results.