Dispute Settlement in International Investment Agreements and the Rules of an Indian Model Bilateral Investment Treaty

Andrew Cornford

Coverage and procedures for dispute settlement in international agreements on investment and trade are proving increasingly controversial. The current controversy reflects contentious issues in two ongoing multilateral negotiations, on the TPP (Trans Pacific Partnership) and TTIP (Transatlantic Trade and Investment Partnership). The targets of contention include provisions designed to achieve regulatory convergence among the participants in the negotiations regarding subjects such as environmental regulation and intellectual property rights. Moreover the rules agreed under these agreements will increase the scope for private investors to bring suits against governments for future losses imputed to changes in regulation and other official actions under the procedure known as Investor-State Dispute Settlement (ISDS).

Accords on investment and trade have proliferated in recent years. The coverage of such accords has expanded over the years and now often includes not only domestic regulations which bear on foreign investment - the subject of investment treaties -but also issues traditionally treated as part of cross-border trade.

The first bilateral investment treaty was concluded between the Federal Republic of Germany and Pakistan in 1959. By the end of the 1980s more than 300 such treaties had been signed between advanced and developing economies (Guertin, 1990: 122). By 2006 2,400-2,600 bilateral investment treaties were in place, most of them between advanced and developing countries but several also between developing countries (Lowenfeld, 2008: 554). By 2014 the total had risen to more than 3,200 (UNCTAD, 2013: 2). However, there are indications of dissatisfaction among a number of parties to such treaties, particularly developing countries: this has in some cases led to declarations of intention to modify the treaties' terms or actually to withdraw from them.

Major subjects raised in the controversy over such treaties are worth examining against a model bilateral investment treaty put forward in India which contains provisions clearly designed to avoid common criticisms of such accords. This model treaty is the government's reaction to a recent proliferation of cases in which investors initiated potentially costly arbitral proceedings against India (Krishnan, 2015).The article which follows reviews not only the Indian model treaty but also major provisions of international investment treaties, often with special attention to their historical development.

Investment treaties were a sequel to earlier agreements covering similar issues such Friendship, Commerce and Navigation Treaties. Their development accompanied the absence of consensus concerning the rights of external investors and the appropriate treatment of different parties during a period of proliferating expropriations. Owing to the overlap between foreign investment and domestic regulation, demands for compensation may be triggered not only by partial or complete expropriation but also by the direct and indirect effects on foreign investors of host countries' regulations more generally.

Outline of the Indian model treaty

The classification of subjects in investment treaties varies but the coverage of most treaties is fairly standard. The Indian model treaty is distinguished by the extent to which it emphasises and spells out the obligations of investors. Less emphasis is given to promotion and protection of investment.

Articles 1 and 2 cover definitions, scope and general provisions. The scope is notable for the detailed specification of the investors and investments which are covered by the treaty and of those which are excluded.

Articles 3-7 treat major obligations of the two parties to an investment. Article 3 treats the obligations of the parties under international law and regarding the observance of due process. Article 4 prescribes, subject to certain qualifications, national treatment for investors. Article 5 prescribes rules for deciding whether a measure constitutes expropriation and is thus eligible for claims under this heading. The article explicitly excludes from claims non-discriminatory regulatory actions by a Party that are designed and applied to protect legitimate public welfare objectives such as public health, safety and the environment.

Article 6 covers the conditions under which current and capital cross-border transfers of funds are allowed. Article 7 covers the entry and temporary sojourn of personnel connected to the investment.

Articles 8-13 cover legal obligations of investors and investments as well as those of the investor's home state. Articles 9-13 are fundamental to the operation of the treaty. Article 9 concerns the obligation against corruption. The obligation as to disclosure in Article 10 covers complete information regarding activities, structure, financial situation, performance, relationships with affiliates, ownership, governance, and various other matters. Article 11 contains the obligation to comply with the host state's laws on taxation. Under compliance with the law of the host state (Article 12) are specified laws on wages, employment, labour rights and social security, on the environment and the conservation of natural resources, on human rights, and on consumer protection and fair competition. Under Article 13 investors and investments are to be subject to civil actions for liability in the judicial process of their home state for acts and decisions in the home state where these lead to damage, personal injuries, or loss of life in the host state.

Article 14, the longest of the model treaty, covers settlement of disputes between an investor and a party (in other words the controversial subject of Investor-State Dispute Settlement (ISDS)). Article 14 sets out procedural obligations such as the exhaustion of local remedies which must be met before submission of the dispute to external arbitration, the appointment of the arbitrators for the arbitral tribunal, prevention of conflicts of interest involving the arbitrators, the burden of proof and governing law, counterclaims against the investor and investment, the distribution of the costs of the arbitration, and restrictions on diplomatic exchanges between the parties to the dispute.

Article 15 deals with disputes between the parties over the interpretation and application of the treaty. Articles 16-17 specify the general and security exceptions which can be invoked by the respondent state. Article 18 specifies procedures to be met when general exceptions are invoked.

Articles 19-23 cover miscellaneous matters: relationship with other treaties, denial of benefits to entities lacking for various reasons the status of bona fide foreign investors and investments, consultations and periodic reviews, amendments, and entry into force. Article 24 specifies the duration of the treaty – ten years unless there is an agreement on renewal - and allows for termination if one party gives the other notice six months in advance of its intention to terminate.

Definition of eligible investors and investments

Investment treaties typically begin with a broad definition of the investors and investments admitted to the host country. Some treaties (such as most of those involving the United States as one of the parties) specify national treatment amongst the conditions for entry, i.e. entry for foreign investors and investments on the same terms as those available for residents, while specifying exceptions from such treatment for certain sectors or activities such as airlines, cabotage, telecommunications and finance. Other treaties provide for entry in accordance with the host party's legislation and regulations. The latter is the approach of the WTO General Agreement on Trade in Services (GATS).

An important feature of investments eligible for admission is the extent (if any) to which it includes different categories of financial instrument. Many bilateral investment treaties include portfolio as well as direct investments under the heading of entry. The coverage of the Indian model treaty is directed at investors rather than financial instruments. Thus "investment" is defined as "an Enterprise in the Host State, constituted, organised and operated in compliance with the Law of the Host State and owned or controlled in good faith by an Investor" (Article 1). The definition of investment continues by specifying "for clarity" that investment does not include various financial assets amongst which are specified "portfolio investments" as well as "any other claims to money that do not involve the kind of interests or operations set out in the definition of Investment in this treaty".

This approach would appear to exclude the liberalisation of capital movements from the obligations of the model treaty. The approach would distinguish the treaty's obligations from those in many other treaties which accommodate such liberalisation. Such exclusion might be justified as being in accord with the recently more accommodating stance of the IMF towards countries' management of capital movements. This stance reflects acknowledgement by the IMF that the management of capital flows can be a reasonable part of policies designed to control the destabilising impact which capital flows can have on countries' macroeconomies (Cornford, 2014: 2-4).

Non-applicability

Bilateral investment treaties generally list some activities or sectors excluded from the coverage of the treaty. These may comprise various activities of the government, taxation, and other national laws and regulations designed to promote or protect the public interest.

The Indian model treaty contains broad provisions under this heading. These include general protection for the governments' legal and regulatory authority (including changes and other reforms): "Nothing in this Treaty shall be interpreted to restrict the rights of either Party to formulate, modify, amend, apply or revoke its Law in good

faith. Each party retains the right to exercise discretion with respect to regulatory, compliance, investigatory matters, including discretion regarding allocation of resources and establishment of penalties" (Article 2.4). Such protection for governmental authority means that in the design and drafting of new laws there is no need for apprehension on the part of the host country that external parties will use bilateral investment treaties as vehicles for nullifying, or restricting the impact of, reforms and regulations (an effect aptly described as "regulatory chill").

The Indian model treaty excludes from applicability government procurement, subsidies and grants, services supplied in the exercise of government authority (services supplied neither on a commercial basis nor in competition with one or more service suppliers), taxation measures, the issuance of compulsory licences granted in relation to intellectual property rights (their revocation, limitation, or creation), and commercial contracts between a Party to the Treaty and an Investment or Investor (Article 2).

The "taking" concept

The early history of the claims of cross-border investors against host states concerns principally cases of partial or total expropriation or nationalisation, often of oil or petroleum interests. Moreover the character of international arbitration of disputes between such parties was strongly influenced by the decisions of an international tribunal in 1981 established to adjudicate claims between United States parties on one side and the government of Iran and Iran state-owned entities on the other. This establishment of this tribunal was part of a settlement, the Algiers Accord, negotiated through the intermediation of the government of Algeria, which also covered the following issues: the release of United States hostages; the return to Iran of a major part of Iranian financial assets in banks in the United States which had been frozen by the American government; the termination of litigation against Iran and Iranian entities in the United States; and the establishment of a fund in a Security Account in the Netherlands from which United States claims against Iran recognised by the tribunal would be satisfied (Lowenfeld, 2008: 542-543).

During a lengthy period, which for minor cases lasted well into the new millennium, the Iran-United States Tribunal adjudicated cases involving not only expropriation but also commercial disputes about payments not made, contracts terminated or not fulfilled, and letters of credit dishonoured or drawn on wrongfully. In cases not involving expropriation or nationalisation the Tribunal generally accepted as part of the basis for its decisions the concept of "taking". This was defined in the 1961 Sohn and Baxter Draft Convention on State Responsibility as follows (Lowenfeld, 2008: 546): "(a) A "taking of property" includes not only an outright taking of property but also any such unreasonable interference, use, enjoyment, or disposal of property as to justify an inference that the owner thereof will not be able to use, enjoy, or dispose of the property within a reasonable period of time after the inception of such interference. (b) A "taking of the use of property" includes not only an outright taking of the property but also any unreasonable interference with the use or enjoyment of the property for a limited period of time".

"Taking" thus defined covers many different categories of commercial dispute other than outright expropriation or nationalisation. Prior to the Iran-United States Tribunal what could and what could not be subjects of investment disputes eligible for

arbitration or legal settlement had lacked definition. The range and volume of the Tribunal's work has contributed to the evolution of law on international investment and to entrenching the concept that such law applies not only to dispute between states but also between states and other foreign parties.

In the context of the precedents of the work of the Iran-United States Tribunal for subsequent investment disputes it is important to remember that a task of the Tribunal was to decide what constituted a contract eligible for adjudication, since the Tribunal was not adjudicating on the basis of the terms of a pre-existing Treaty or international agreement. As already discussed, the Indian model treaty carefully defines what is covered by Investment.

National Treatment/Fair and Equitable Treatment

National Treatment is designed to assure foreign suppliers of goods or services treatment no less favourable than that accorded to domestic suppliers. National Treatment can cover conditions of entry or market access as well as regulatory treatment to a foreign supplier in a country's market or only the latter. According to the approach of the WTO General Agreement on Services, National Treatment is designed to equalize post-entry conditions of competition for domestic and foreign suppliers. In many bilateral investment treaties, especially those in which the United States is a party, national treatment is an obligation on conditions for entry as well as on post-entry treatment.

However, National Treatment does not guarantee minimum standards of treatment to foreign suppliers even when no discrimination can be shown. Fair and Equitable Treatment is designed to assure that a minimum international standard of behaviour will apply to a foreign supplier. Examples of cases where such a minimum standard has not been applied might be administrative delays which hinder the start of projects or other investments after the receipt of a license or a successful bid by a foreign supplier.

The problem with Fair and Equitable Treatment is that, unlike the case for National Treatment, there is no agreed standard of comparison which will serve as the basis for judging whether it has been met. In 2001 the absence of such a standard led the Free Trade Commission created by the North American Free Trade Agreement (NAFTA) to issue an interpretation of the Minimum Standard of Treatment in Accordance with International Law which includes the following: "The concepts of 'fair and equitable treatment' and 'full protection and security' do not require treatment in addition to or beyond that which is required by the customary international law minimum standard of treatment of aliens", and "A determination that there has been a breach of another provision of the NAFTA, or of a separate international agreement does not establish that there has been a breach of [the Article containing these standards]" (Lowenfeld, 2008: 557-558). This still means that the contents of Fair and Equitable Treatment depends the interpretation of the applicability of customary international law to the case under consideration.

The obligation of National Treatment in the Indian model treaty is post-entry (Article 4). It is also hedged with specified exceptions. These include laws and measures of regional and local government; wide discretion for decisions regarding law enforcement; and the extension of financial assistance by a party in favour of its

investors or investments in pursuit of legitimate public purposes such as the protection of public health, safety and the environment.

There is no reference in the Indian model treaty to Fair and Equitable Treatment as such. However, under Standard of Treatment (Article 3) each party is not to subject Investments of Investors of the other party to measures which constitute the following: (i) denial of justice under customary international law; (ii) unremedied and egregious violations of due process; and (iii) manifestly abusive treatment involving continuous, unjustified and outrageous coercion or harassment. There is also a clause similar to the analogous one in NAFTA's Minimum Standard that determination that there has been a breach of another provision of the treaty does not establish that there has been a breach of the model treaty's Standard of Treatment.

Exceptions

The Indian model treaty contains extensive lists of exceptions designed to provide free scope for government action by the host state as well of subjects off limits for dispute settlement. According the General Exceptions of Article 16: "Nothing in this Treaty precludes the Host State from taking actions or measures of general applicability which it considers necessary to the following": the protection of public morals and the maintenance of public order; ensuring the integrity and stability of the financial system; remedying serious balance-of-payments problems and exchange-rate and external financial difficulties; ensuring public health and safety; protecting and conserving the environment; improving working conditions; securing legal compliance for laws relating to deceptive and fraudulent practices and defaults; protecting personal privacy; and protecting national treasures and monuments. Moreover measures taken by local bodies and authorities are covered by the General Exceptions.

In addition to General Exceptions the Indian model treaty specifies Security Exceptions which cover the disclosure of information considered by a party contrary to its essential security interests or the taking of actions considered necessary for the protection of its essential security interests (Article 17). Measures for the protection of a party's essential security interests are to be imposed on a non-discriminatory basis (Annex 1). The defence of a measure or measures as being justified by Security Exceptions is to be non-justiciable and not open to review by an arbitral tribunal established to settle dispute under the model treaty.

MFN

Most bilateral investment treaties contain most-favoured-nation (MFN) clauses which, as in the case of their analogues for cross-border trade, guarantee treatment to foreign investors covered by the treaty at least equal to that granted to foreign investors from any other country. However, MFN clauses in investment treaties may be subject to specified exclusions of varying degrees of comprehensiveness (Lowenfeld, 2008: 572).

The approach of the Indian model investment treaty is simply to exclude MFN treatment. Such an exclusion enables India to provide differential benefits to foreign investors according to such features of its relations with the investors' home states as the scale of incoming investment from this source.

Expropriation

Expropriation has historically been at the heart of the development of rules on the treatment of international investment. In disputes on the subject before 1945 the so-called Hull Doctrine jostled with the Calvo Doctrine Lowenfeld, 2008: 472-473 and 475-480). The Hull Doctrine was summarised in a statement of the United States Secretary of State (in a letter to the President of Mexico in 1938) as follows:"The Government of the United States readily recognises the right of a sovereign state to expropriate property for public purposes…it has been stated with equal emphasis that the right to expropriate property is coupled with and conditional on the obligation to make adequate, effective and prompt compensation." The Calvo Doctrine drew on the writings of Carlos Calvo, a nineteenth-century Argentine jurist, who maintained that under international law aliens had no rights greater than those of a country's citizens. This could lead to the argument that property owners should be incorporated under the laws of the host country, in the process renouncing all forms of protection on the part of their home country.

During the period from 1945 until the early 1970s there was a wave of expropriations and nationalisation linked to decolonisation, Communist rule in Eastern Europe and elsewhere, and a resurgence of nationalism in Latin America. This was accompanied by debates in the United Nations culminating in 1974 the adoption of a Charter of Economic Rights and Duties of States. Article 2 of the Charter included the following rights: "1. Every State has and shall freely exercise full permanent sovereignty, including possession, use and disposal, over all its wealth, natural resources and economic activities….2. Each State has the right:..(c)To nationalize, expropriate or transfer ownership of foreign property in which case appropriate compensation should be paid by the State adopting such measures, taking into account its relevant laws and regulations and all the circumstances that the State considers pertinent. In any case where the question of compensation gives rise to a controversy, it shall be settled under the domestic law of the nationalizing State and by its tribunals, unless it is freely and naturally agreed by all the States concerned that other peaceful means be sought on the basis of the sovereign equality of States and in accordance with the principle of free choice of means".

On a track parallel to but separate from the debates in the United Nations, the Convention on the Settlement of Investment Disputes between States and Nationals of Other States established International Centre for the Settlement of Investment Disputes (ICSID) within the World Bank. ICSID provides a forum for the settlement of investment disputes between parties from home and host countries which have accepted the Convention.

Private investors are explicitly included amongst the parties eligible to initiate disputes. In 1978 ICSID established the Additional Facility to deal with arbitration and conciliation between host states and investors in cases where the Convention could not be deployed because either the host state or the home state of the investor was not a party to the Convention. Widespread ratification of the Convention, though a gradual process, took in more than 150 countries by the beginning of the new millennium. However recently as part of their re-evaluation of the costs and benefits

of bilateral investment treaties a number of developing countries have announced their intention to withdraw from the Convention.

The concept of expropriation lacks precise definition. It clearly overlaps with "taking" (discussed above). Indeed, it could be argued that in practice expropriation is a subcategory of "taking". Bilateral investment treaties refer to "expropriation or nationalisation", "expropriation direct or indirect", and "expropriation through measures tantamount to expropriation". Some of these terms are clearly designed to include measures constituting creeping expropriation within the treaties' provisions on expropriation (Lowenfeld, 2008: 559).

Central to the concept of "taking" is interference in the business activities of the foreign investor or investment. But this leaves open for interpretation in particular cases the question of whether the interference has been sufficiently serious to qualify as expropriation. In actual cases under NAFTA the argument for expropriation has sometimes been rejected in favour of the lesser failure to accord investor or investment Fair and Equitable Treatment. Importantly in view of the controversy surrounding the TTIP, in legal rulings regulation has not necessarily been associated with a deprivation of ownership rights sufficiently severe to qualify as expropriation (Lowenfeld, 2008: 560-563).

In the Indian model treaty nationalisation and expropriation "for reasons of public purpose" is legitimate but must be accompanied by adequate compensation. The determination of whether a measure or measures should be classified expropriation "requires a case-by-case, fact-based inquiry." The evidence that expropriation has taken place should include the following: "(i) permanent and complete or near complete deprivation of the value of the Investment; and (ii) permanent and complete or near complete deprivation of the Investor's right and management and control over the Investment; and (iii) an appropriation of the Investment by the Host State which results in transfer of the complete or near complete value of the Investment to that party or to an agency or instrumentality of the Party or a third Party" (Article 5.2). "Non-discriminatory actions by a Party that are designed and applied to protect legitimate public welfare objectives such as public health, safety and the environment shall not constitute expropriation" (Article 5.4).

These conditions are stringent and are likely to narrow the range of cases in which the existence of expropriation can be demonstrated. They are consistent with correspondingly stringent rules concerning exceptions (already discussed) and dispute settlement (see below).

Compensation

The main issues under the heading of compensation concern the period of time before compensation is paid (promptness), the form in which it should be paid (sometimes characterised as effectiveness of compensation), and how much. The third of these issues is the crucial one since performance under the other two depends on settlement of the question of how much.

Under the heading of promptness allowance has to be made for delays due to the resolution of practical problems which have to be dealt with in disputes. Delays are often reflected in interest charges which accrue from the date of the expropriation.

The rules as to the form in which payment is made usually guarantee that the currency of payment should be convertible and not subject to restrictions on transfer. If payment is made in financial instruments the rules guarantee their value (with compensation for discounts from face value, etc.).

Concerning how much compensation should be paid agreement is necessary as to the date of expropriation or other forms of "taking". This is often contentious since the loss of earnings which is to be compensated will be determined by the extent of expropriation or "taking" on this date.

But the most difficult problem associated with how much compensation should be paid is that of valuation of the assets or the "taking". Terminology under this heading is fluid. The concepts denoting compensation go under several names: "market value", "fair market value", "genuine value", and "just compensation", but mostly boil down to one of a limited number of valuation methods.

A useful classification of these methods is that of Robert Herz, former chairman of the United States Financial Accounting Standards Board (FASB) (Herz, 2013: 182-191).This classification consists of three headings: (i) amortised cost, the original cost minus amortisation plus the sum to be received at final settlement; (ii) fair value, the amount for which an asset could be exchanged between knowledgeable parties in an arms-length transaction; (iii) and current value, the present discounted vale of the future net cash flows that an asset is expected to generate.

Each of these valuation methods has advantages and disadvantages.

- Amortised cost is based on contractual features of an asset and thus avoids the misleading volatility and noise which often characterise reported financial results.
- Supporters of fair value stress incorporation by the concept of current market and economic conditions, and not the past costs and prices used to estimate amortised costs. But application of fair vale can be problematic when market prices are not available. In their absence United States accounting rules suggest alternatives such as the prices of similar assets or valuation based on models.
- Current value picks up the phasing in time of inflows and outflows associated with an asset, and also makes possible the incorporation of the effects of changes in interest rates through the discount rates used in estimation. The problem with current value is due to the difficulty of identifying in advance the future inflows and outflows used in the calculation.

Cursory consideration points to the difficulties associated with these valuation methods in investment disputes, especially when one of the parties is a developing country lacking a market for the shares of the investment in question or characterised by economic conditions that complicate estimation of prospective revenues and costs.

In the case of the Iran-United States Tribunal, where identification of the nature and extent of the "taking" was itself often a complex matter, "each case was examined in detail, with accountants and industry experts, in some instances presented by the parties, in others called by the Tribunal itself. The awards rarely accepted the experts'

detailed submissions but reflected also the judgements of the Chamber hearing the case" (Lowenfeld, 2008: 552).

While Bilateral Investment Treaties often specify criteria for compensation in cases of expropriation or measures tantamount to expropriation, corresponding criteria are not included for other violations of treaty terms (such as National Treatment, Fair and Equitable Treatment, or protection and security). In such cases arbitral tribunals have typically borrowed from rulings concerning expropriation (Lowenfeld, 2008: 567). The absence of such criteria makes judgements under such treaties concerning, for example, the impact of regulation more unpredictable or even arbitrary.

Under the Indian model bilateral investment treaty, compensation "shall be adequate and reflect the fair market value of the expropriated Investment, as reduced after application of relevant Mitigating Factors" (Article 5).

The Mitigating Factors specified include the following: (a) current and past use of the Investment; (b) duration and previous profits; (c) compensation and insurance payouts received from other sources; (d) options available for the mitigation of losses and reasonable efforts made towards such mitigation; (e) conduct of the Investor which has contributed to damaging the Investment; (f) relief of obligations due to the expropriation; (g) liabilities owed to the government of the host state; (h) unremedied harm or damage to the environment or to the local community; (i) other relevant considerations regarding the need to balance the public interest and the interests of the Investment.

Moreover "The computation of the fair market value…shall exclude any consequential or exemplary losses or speculative or windfall profits claimed by the Investor, including those relating to moral damages or loss of goodwill" (Article 5). The Mitigating Factors and the exclusion of speculative gains are clearly capable of significantly constraining the amount of compensation. Moreover the rules of the Indian model treaty leaves unsolved the problem mentioned above of which method of valuation should be used, a problem likely to be especially difficult to resolve in the case of takings other than straightforward expropriation.

Financial transfers and entry and sojourn of personnel

Cross-border financial transfers and the access of foreign personnel in connection with operations linked to the investment are subjects which also arise under the heading of international trade in financial services of the WTO General Agreement on Financial services (GATS).

On transfers Article 6 of the Indian model bilateral investment treaty specifies rules similar to those of Article XI of the GATS which permit all funds of as investor related to an investment in its territory to be freely transferred. Likewise the treaty permits temporary restrictions on transfers "in the event of serious balance-of-payments difficulties or threat thereof, or in cases where, in exceptional circumstances, movements of capital cause or threaten to cause serious difficulties for macroeconomic management, in particular, monetary and exchange rate policies" (Article 6). Government policy regarding transfers would also be covered by the General Exceptions of Article 16 which include actions and measures "remedying serious balance-of-payments problems, exchange rate difficulties and external financial difficulties or threat thereof".

On the access of foreign persons each of the parties to the treaty shall permit persons of the other party and employees of the investor or investment, subject to domestic law and considerations of reciprocity, to enter and remain in their territory for the purpose of engaging in activities connected to the investment (Article 7). Under the Article 16 of the WTO GATS, limitations on the access of foreign persons employed in connection with the cross-border provision of financial services are to be a subject in the negotiation of specific commitments.

Dispute settlement/ISDS

Dispute settlement is now one of the most contentious of the subjects of bilateral and multilateral trade and investment treaties. This is to a significant extent due to provisions for ISDS.

As of 1945 investment disputes were settled either through national courts or through international tribunals of which the most important was the International Court of Justice. Article 34 of the latter's statute permits only states to be parties before the Court. Thus, if a private investor wanted to bring a suit against a government, the investor would have had to persuade its government to pursue the case on its behalf, thus transforming the case into a dispute between states (Folsom, Gordon and Spanogle, 1991: 1098-1101).

The proliferation of investment disputes during the following 20 years, due partly to decolonisation, communist governments in some states, and more assertive national economic policies in many developing countries, was the inspiration for the establishment of the ICSID (as described above), which accommodated agreements between private parties and States for the purpose of arbitration or adjudication, although as of the 1980s in only about 40 per cent of bilateral investment treaties was the private investor provided with direct access to arbitration, so that in the remainder working through national governments was still required. (Guertin 1990: 125).

The following years witnessed expansion in the number of agreements covering international investment as well as changes affecting the scope and character of such agreements. Bilateral investment treaties remain the most frequent form of such agreements but investment-related provisions are now also included in economic partnership agreements, free-trade agreements, agreements for regional economic integration, and framework agreements for economic cooperation. Such agreements often include more than two countries as parties and cannot thus be classified as bilateral. This has led to the use of the term international investment agreement as the umbrella class.

Expansion in the number of international investment agreements has been accompanied by not only expansion in the number of investment disputes subject to adjudication or arbitration but also by an increase in the number of cases involving ISDS. Under arbitral tribunals (ICSID and others) dispute settlement involves interpretation of applicable agreements which may or may not include the possibility of ISDS. Article 25of the ICSID Convention defines Nationals of Other Contracting States to include foreign corporations and other juridical entities whom the parties have agreed should be treated as eligible for arbitration under the Convention. Recourse to ISDS is now substantial. By the end of 2014, according to the UNCTAD data bank, the number of concluded ISDS cases had reached 356 (UNCTAD, 2015: 8).

Under the ICSID Convention arbitration usually involves three arbitrators, one selected by each of the parties to the dispute (host state and investor) and a presiding arbitrator agreed by the two parties or, if they cannot agree, by the chairman of the ICSID, ex officio the president of the World Bank. This pattern of selection follows that of other international arbitration tribunals.

In view of these procedures and the now substantial history of ICSID and other similar tribunals why has the subject of ISDS recently become so contentious? Partly this is simply a case of the way in which bilateral and multilateral agreements with an extensive and potentially intrusive scope as far as national regulation is concerned provide enterprises but not other groups (such as trade unions and civil-society groups) privileged access to arbitration and adjudication by offshore tribunals, with in many cases no provision for appeal against their decisions.

Moreover the range of subjects covered in international investment agreements has broadened to large parts of domestic regulation of the environment, investment and finance, intellectual property, etc. The consequences can be perverse. Control of cross-border capital movements, for example, are increasingly accepted as a necessary part of the armoury of policy measures for handling systemic financial risk and the management of the balance of payments. Conflicts between IMF recommendations as to the use of such measures could easily conflict with obligations undertaken by a country under an international investment agreement.

Estimating compensation in favour of investors in cases brought by them concerning a country's regulation presents difficult problems. As noted above, such estimates have long been made in cases of this kind. However, established guidelines are lacking with the result that estimates of risk are unpredictable and arbitrary. How, for example, would estimation be approached for compensation of an investor due to the effect on an investment of the imposition of capital controls?

The growth of ISDS in arbitration under bilateral investment treaties has been accompanied by systemic features which raise serious questions about the justice of the decisions reached. These features (as listed in a speech by George Kahale (Kahale, 2014), a senior arbitration lawyer, include the following:

- A "club of international arbitrators" is shaping a new body of international law, though in many cases the members of the club are not well versed in international law. Members of this group are also dependent upon the parties or arbitral institutions for future appointments–a dependence which all too easily compromises their conduct in particular cases.
- Bilateral investment treaties often contain overly expansive provisions concerning Fair and Equitable Treatment and Most-Favoured Nation.
- "Mega cases" based on a cavalier approach to legal principles and worth more than USD 1 billion have been brought against states. Claims have sometimes been of the same order of magnitude as the country's GDP.
- Although there is nothing to stop an arbitrator from applying a personal interpretation of law, their decisions can be characterised by finality in the absence of procedures for appellate review.

- In view of the selection procedures for arbitrators, impartiality is difficult to achieve. As Kahale puts it, "Experienced practitioners are able to predict the outcome of a case purely based on the composition of the tribunal".
- A bias against states and in favour of investors is perceived by many observers. Kahale acknowledges that there are studies showing that states win more than 50 per cent of cases but counters that this figure is "meaningless, if that same figure happens to represent the percentage of cases that never should have seen the light of day or that would never survive a motion to dismiss in a national court".

The approach to ISDS of the Indian model investment treaty is to restrict investors' rights under the treaty regarding recourse to external arbitration. The rights apply only to investors and investments specified in the treaty. Thus the disputes admitted are those dealing with treatment of the investor, expropriation, transfers, and entry and sojourn of the investor's personnel. Excluded from the treaty's scope are portfolio investments (Article 1) Moreover, as already mentioned, cross-border transfers related to investments (such as contributions to capital, profits, interest, royalties, and management fees) must meet conditions as to compliance with a broad range of local laws and regulation (including those concerning labour obligations, and taxation) (Article 6). The control of cross-border capital movements is not only permitted as a response to balance-of-payments difficulties but may also be justified by macroprudential reasons since, as also mentioned above, under Article 6: temporary restrictions on transfer are deployed when movements of capital cause or threaten to cause serious difficulties for macroeconomic management, in particular , monetary and exchange rate policies.

The Indian model treaty's procedures to be pursued in investment disputes include the exhaustion of local remedies and other conditions which must precede submission of a dispute to external arbitration (Article 14). The investor must establish that continued pursuit of domestic relief would be futile because (1) there are no reasonably available legal remedies in the respondent country capable of providing relief regarding the dispute in question or (2) the process for obtaining legal relief provides no reasonable possibility of obtaining such relief in a reasonable period of time. Even after the transmission of the Notice of Dispute to the designated representative of the respondent party the disputing investor and the respondent party are to use their best efforts to resolve the dispute amicably through consultation, negotiation, or continued pursuit of any available domestic remedies or solutions. Non-compliance with any of the conditions set out under these procedures leads to the barring of the investor from taking subsequent steps to pursue external arbitration of the dispute.

Counterclaims against the investor are possible for breaches by the investor of obligations under the treaty regarding corruption, disclosure, taxation, and compliance with the law of the host state. Explicitly mentioned here are laws relating to labour and wages, environmental and conservation law, human rights, and fair competition and consumer protection.

The eventual appointment of three arbitrators is subject to detailed provisions regarding conflicts of interest. Such a conflict will be deemed to exist in the presence of various circumstances including the following:

- the arbitrator is or has been a legal representative of the appointing party or an affiliate of the appointing party in the three years preceding the commencement of the arbitration;
- the arbitrator is a lawyer in the same law firm as the counsel to one of the parties;
- the arbitrator is acting concurrently with the lawyer or law firm of one of the parties in another dispute;
- the arbitrator's law firm is currently rendering or has rendered services to one of the parties or to an affiliate of one of the parties from which the law firm derives a significant financial interest;
- the arbitrator has been comprehensively briefed by the appointing party concerning the merits or procedural aspects of the dispute prior to appointment;
- the arbitrator has publicly advocated a fixed position regarding an issue in the case to be arbitrated.

These conditions should reduce the opportunities for the conflicts of interest and other abuses of the arbitral proceedings in investment disputes which were described earlier.

Under Burden of Proof and Governing Law (Article 14) the treaty is to be interpreted "in the context of the high level of deference that international law accords to States with regard to their development and implementation of domestic policies". More specifically the governing law for the interpretation of the treaty by the arbitral tribunal should be the treaty itself, the general principles of public international law relating to the interpretation of treaties, and- for matters relating to domestic law - the law of the home state of the respondent. The investor must establish a breach of the respondent's obligations under the Scope and General Provisions of the treaty (Article 2 that specifies the subjects to which the treaty applies and subjects excluded from its scope). Moreover he investor must have suffered actual and non-speculative losses as a result of the breach, and the losses must have been foreseeable and directly caused by the breach.

Decisions as to the award of compensation are to be reached by a majority of votes of the arbitral tribunal. Provisions as to the amount of compensation, which are set out under expropriation, were discussed above.

Suggestions as to alternative approaches

The Indian model bilateral investment treaty contains strong stand-alone rules. Other possible ways of confronting perceived shortcomings of investment and trade treaties have also been suggested.

Two such alternatives are contained in proposals of the Global Economic Governance Programme of the Oxford University Blavatnik School of Government. One of these alternatives, which is intended for the TTIP negotiations but could also be deployed in accords between developing and developed countries is an "ISDS Patches Model".

The other, which is designed specifically for developing countries, involves the use of state of interpretation of investment treaties.

The "ISDS Patches Model" is designed to limit recourse to investment arbitration by ensuring that ISDS is an option only in exceptional cases (Kleinheisterkamp and Poulsen, 2014):

- The first decision on the legality or illegality of acts subject to dispute settlement would be taken by local courts (the "first patch"). This will ensure that investment arbitration is the last rather than the first resort in an investment dispute.
- Under the "second patch" there would be a comprehensive state "filter" of private claims by home and host states. If both agree, the dispute should be settled by domestic judges rather than international arbitrators. The objective here would be to safeguard public policies regarding subjects such as taxation, financial stability, environmental protection, health concerns, and consumer protection.
- The "third patch" would allow parties to issue binding joint and prospective interpretations of the provisions of an investment agreement. This possibility would give states greater control over the arbitral process by steering the development of the law created by the agreements.
- Under the fourth "patch" investors and states would be given the opportunity to appeal the decisions of arbitral tribunals before an independent appellate body analogous to that available at the WTO. This would help to avoid the lack of coherence and occasional contradictions which sometimes characterise the decisions of arbitral tribunals.

The second proposal would involve state interpretation of investment treaties. States would use their full powers to limit and shape the interpretive power of arbitral tribunals regarding investment treaties (Gertz and St John, 2015). This could be done in three ways: (1) through unilateral statements of particular clauses of treaties submitted by a non-disputing as well as a disputing party; (2) joint statements with treaty partners providing agreed clarification and interpretation of clauses for future tribunals; and (3) joint statements by a number of states- not necessarily all parties to the same treaty– on mutually agreed interpretations of provisions common to many investment treaties.

Each of these options is concerned primarily with procedures to be followed in arbitration of investment disputes. The first two "patches" of the "ISDS Patches Model" are drafted in the same spirit as the Indian model bilateral investment treaty. But unlike the model treaty neither proposal includes rules tailored to the particular issues likely to arise in investment disputes.

Recent Indian developments

In response to criticism that the Indian model bilateral investment treaty is too one-sided regarding certain subjects and may excessively deter foreign investment, there have been indications of official reconsideration of key provisions in the form of a review in a recent report of the Law Commission of India (Krishnan, 2015). Particular subjects covered by this review which may lead to modified provisions in a revised

version of the model treaty include the following: (1) extension of the definition of investments covered to include portfolio investments as well as foreign enterprises (Article 1); (2) more flexible rules than the obligatory exhaustion of recourse to local courts with no allowance for re-examination by an arbitral tribunal of legal issues "finally settled by any judicial authority of the host state" or review of the merits of a decision made by such an authority (Article 14); and (3) the substitution of internationally agreed minimum standards to replace the exclusive authority accorded to the government of the host state to decide when it invokes exceptions to justify actions or measures regarding such subjects as public health, the environment, public order and morals, working conditions, and financial stability (Article 16).

The eventual outcome of any modifications is unpredictable since arguments are likely to be put forward against major modifications of the model treaty. Greater openness to portfolio investments can easily become a vehicle for back-door (unwanted) liberalisation of cross-border capital movements. Moreover a difficult balance would need to be achieved in a strengthening of the role of arbitral tribunals in relation to that of local law and courts. Finally minimum international standards may be an inadequate substitute for state policy autonomy regarding exceptions to the treaty.

References

Cornford A (2014), "Macroprudential Regulation: potential implications for cross-border banking", UNCTAD Discussion Paper No.216, April;

Folsom RH, Gordon MW, and Spanogle JA (1991), International Business transactions A Problem-Oriented Coursebook, 2nd edition, St. Paul Minn., West Publishing Company;

Gertz G and St John T (2015), "State interpretations of investment treaties: feasible strategies for developing countries", Blavatnik School of Governance Policy Brief, June;

Guertin DL (1990), "A programme leading to an international agreement on foreign direct investment" in Wallace CD (1990), Foreign Direct Investment in the 1990sA New Climate in the Third World, Dordrecht, etc., Martinus Nijhoff Publishers;

Herz RH (2013), Accounting Changes Chronicles of Convergence, Crisis, and Complexity in Financial Reporting, American Institute of Certified Public Accountants;

Kahale G (2014), Keynote Speech, Eighth Annual Juris Investment Arbitration Conference, Washington, D.C., 28 March;

Kleinheisterhamp J and Poulsen L, (2014),"Investment protection in TTIP: three feasible proposals", Blavatnik School of Governance Policy Brief, December;

Krishnan A (2015), "A bit for the state, a bit for the investor", The Hindu, 8 September;

Lowenfeld AF (2008), International Economic Law, 2nd edition, Oxford, Oxford University Press;

UNCTAD (2013), "Towards a new generation of international investment policies: UNCTAD's fresh approach to multilateral investment policy-making", IIA Issues Note, July.