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International Investment Law and the Rule of Law

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International investment treaties constitute one of the principal instruments to enhance the rule of law in investor-state relations. Still, for a long time, they have been little-known and little-used instruments under international law by which states, mostly on a bilateral level, but increasingly often also regionally and in some cases even in multilateral instruments,[2] grant foreign investors from the other contracting state(s) certain rights. It was only during the last decade that international investment law became mainstream in the international law community.[3] This was principally due to the growing dispute settlement practice under investment treaties, which grew

[1] The author was supported in writing this chapter by a European Research Council Starting Grant on 'Transnational Private-Public Arbitration as Global Regulatory Governance: Charting and Codifying the Lex Mercatoria Publica' (LexMercPub, Grant agreement no: 313355).

[2] By June 2013, there were 2,860 bilateral investment treaties and 340 other international investment agreements, such as investment chapters in free trade agreements; see United Nations Conference on Trade and Development (UNCTAD), "International Investment Policymaking in Transition: Challenges and Opportunities of Treaty Renewal", IIA Issues Note No 4 (June 2013) <http://unctad.org/en/PublicationsLibrary/webdiaepcb2013d9_en.pdf> (accessed 9 June 2014) at p 1. Concerning regional investment treaties, the most prominent examples are the North-American Free Trade Agreement (17 December 1992), 32 ILM 289 and 605 (1993) (entered into force 1 January 1994) (NAFTA); the Dominican Republic-Central America-United States Free Trade Agreement (DR-CAFTA) <http://www.ustr.gov/trade-agreements/free-trade-agreements/cafta-dr-dominican-republic-central-america-fta/final-text> (accessed 9 June 2014); and the ASEAN Comprehensive Investment Agreement (26 February 2009) (entered into force 29 March 2012), <http://www.asean.org/images/2012/Economic/AIA/Agreement/ASEAN%20Comprehensive%20Investment%20Agreement%20%28ACIA%29%202012.pdf > (accessed 16 January 2015). See also UNCTAD, *Investment Provisions in Economic Integration Agreements* (2006) <http://www.unctad.org/en/docs/iteiit200510_en.pdf> (accessed 9 June 2014). The most prominent multilateral investment treaty is the Energy Charter Treaty (17 December 1994) 34 ILM 360 (entered into force 16 April 1998).

[3] For a reflection of this development in the literature on investment law, see Stephan W Schill, "W(h)ither Fragmentation? On the Literature and Sociology of International Investment Law" (2011) 22 EJIL 875.

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rapidly, from its first use in the late 1980s in *Asian Agricultural Products v Sri Lanka*[4] to over 560 treaty-based investment disputes in 2013.[5]

Despite their myriad number, investment treaties follow a sufficiently uniform structure, lay down relatively uniform principles for the treatment of foreign investors, and build on a common dispute settlement mechanism, which arguably results in a regime that is largely comparable to a multilateral system.[6] Investment treaties typically grant investors the right not to be expropriated without compensation, to be treated fairly and equitably, to enjoy full protection and security, and to be treated no less favorably than national investors or investors from any third state. In addition, investment treaties typically offer foreign investors access to arbitration against the host state in order to bring claims, usually for damages, for breach of the obligations laid down in the treaty. This allows them to opt out of domestic courts and to bring a claim under international law without the need for the investor's home state to exercise diplomatic protection.[7] This can have a considerable impact on the conduct of all branches of domestic government, including legislation, administration, and the judiciary. International investment law therefore constitutes a special protection regime for foreign investors that combines public law constraints with private-public arbitration as a dispute settlement mechanism.

The growth of investment treaties and investment treaty arbitration has led, within a short space of time, to a lively debate about the benefits, justification, and problems of this special regime for foreign investors. Indeed, this debate has developed into what is often called a "legitimacy crisis" of international investment law.[8] Symptoms of this crisis are the withdrawal of some states from bilateral investment treaties (BITs) and the International Centre for Settlement of Investment Disputes (ICSID);[9] the efforts of many countries to recalibrate their

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[4] *Asian Agricultural Products Ltd. (AAPL) v Republic of Sri Lanka* [1990] ICSID Case No ARB/87/3, final award dated 27 June 1990.

[5] *Cf* UNCTAD, "Recent Developments in Investor-State Dispute Settlement (ISDS)", IIA Issues Note No 1 (2014) (recording 568 treaty-based investment arbitrations at the end of 2013) <http://unctad.org/en/PublicationsLibrary/webdiaepcb2014d3_en.pdf> (accessed 9 June 2014) at p 1.

[6] Stephan W Schill, *The Multilateralization of International Investment Law* (Cambridge University Press, 2009).

[7] Generally on investment treaties see Campbell McLachlan, Laurence Shore and Matthew Weiniger, *International Investment Arbitration – Substantive Principles* (Oxford University Press, 2007); Andrew Newcombe and Luis Paradell, *Law and Practice of Investment Treaties* (Kluwer Law International, 2009); Rudolf Dolzer and Christoph Schreuer, *Principles of International Investment Law* (2nd edn, Oxford University Press, 2012).

[8] See Charles N Brower and Stephan W Schill, "Is Arbitration a Threat or a Boon to the Legitimacy of International Investment Law?" (2009) 9 *Chicago Journal of International Law* 471 at 473 (with further references).

[9] ICSID was created by the Convention on the Settlement of Investment Disputes between States and Nationals of Other States, signed 18 March 1965, entered into force 14 October 1966, 575 UNTS 159 (ICSID Convention). For

investment treaty obligations and to reconsider investment treaty arbitration;[10] and by now a more general public debate about the possibly harmful impact of investment treaties on states' right to regulate, *inter alia*, for the protection of the environment, human rights, or other public interests. Critics question the democratic accountability, independence and impartiality of arbitrators, disapprove of the vagueness of treaty standards, condemn the extent to which arbitrators' interpretations of these standards restrict the right of host states to regulate in the public interest, and deprecate the institution of investor-state dispute settlement.[11]

Criticism of international investment law and investment treaty arbitration has also been launched in respect of the rule of law. One of the most vocal critics, Gus Van Harten, says the following:

> Investment treaty arbitration is often promoted as a fair, rules-based system and, in this respect, as something that advances the rule of law. This claim is undermined, however, by procedural and institutional aspects of the system that suggest it will tend to favour claimants and, more specifically, those states and other actors that wield power over appointing authorities or the system as a whole. On the other hand, other states and investors (especially those that bring claims against a powerful state) can expect to be disadvantaged.[12]

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example, Bolivia, Ecuador and Venezuela denounced the ICSID Convention in 2007, 2009 and 2012, respectively; South Africa is currently in the process of terminating several of its BITs, see Robert Hunter, "South Africa Terminates Bilateral Investment Treaties with Germany, Netherlands and Switzerland" (2013) <http://www.rh-arbitration.com/south-africa-terminates-bilateral-investment-treaties-with-germany-netherlands-and-switzerland/> (accessed 9 June 2014). Indonesia too is planning on terminating most of its BITs see Financial Times, "Indonesia to terminate more than 60 bilateral investment treaties" (26 March 2014) <http://www.ft.com/intl/cms/s/0/3755c1b2-b4e2-11e3-af92-00144feabdc0.html#axzz34QKVh5iI> (9 June 2014). See further the Trade Policy Statement of the Australian Gillard Government expressing opposition to the inclusion of investor-state dispute settlement provisions in future trade agreements: Australian Government, Department of Foreign Affairs and Trade, "Gillard Government Trade Policy Statement: Trading Our Way To More Jobs and Prosperity" at p 14 (April 2011), <http://www.acci.asn.au/getattachment/b9d3cfae-fc0c-4c2a-a3df-3f58228daf6d/Gillard-Government-Trade-Policy-Statement.aspx> (accessed 9 June 2014). Criticism is also omnipresent in the current debates on the EU-level about the direction and content of a future EU international investment policy and the future of investment agreements of Member States; see, in particular, the European Parliament Resolution of 6 April 2011 on the future European international investment policy, 2010/2203 (INI).

[10] See José E Alvarez, "Why Are We "Re-calibrating" Our Investment Treaties?" (2010) 4 *World Arbitration & Mediation Review* 143. For various reform proposals that aim at restricting investment treaty arbitration, see UNCTAD, "Reform of Investor-State Dispute Settlement: In Search of a Roadmap", IIA Issues Note No 2 (2013) <http://unctad.org/en/PublicationsLibrary/webdiaepcb2013d4_en.pdf> (accessed 9 June 2014) at pp 4ff.

[11] See, especially, Gus Van Harten, *Investment Treaty Arbitration and Public Law* (Oxford University Press, 2007) at pp 152ff; David Schneiderman, *Constitutionalizing Economic Globalization: Investment Rules and Democracy's Promise* (Cambridge University Press, 2008); Kyla Tienhaara, *The Expropriation of Environmental Governance* (Cambridge University Press, 2009).

[12] Gus Van Harten, "Investment Treaty Arbitration, Procedural Fairness, and the Rule of Law" in Stephan W Schill (ed), *International Investment Law and Comparative Public Law* (Oxford University Press, 2010) at p 627.

Van Harten's recommendation, as that of other critics, is to get rid of the whole system and to replace the dispute settlement mechanism either with domestic courts[13] or with a to-be-established permanent international investment court.[14]

The supporters of investment law, by contrast, for years have done too little to explain the benefits of system. One of the benefits of investment treaties and investment treaty arbitration is arguably their contribution to creating a rule of law framework for investment relations that is based on international law and that domestic regulation of foreign investment is not necessarily able to provide. In particular in countries with a weak domestic rule of law, investment treaties can help create the legal and institutional infrastructure that is necessary for attracting foreign investment into industries and projects that further host state development, as stated, for example, in the Agenda 21 of the UN Conference on Environment and Development.[15] At the same time, the concept of the rule of law is itself a guiding principle for assessing investment treaties and investment treaty arbitration and in informing treaty and dispute settlement practice. It is therefore two sets of questions this chapter will address: first, how investment treaties can help implement the rule of law domestically particularly in developing countries; and secondly, how the concept of the rule of law should inform and help reform the practice of investment law and arbitration.

The Rule of Law through Investment Treaties

Rather then engaging with the criticism of international investment expressed by Gus Van Harten and others in detail, I want to lay out the positive case for understanding international

[13] See York University, Osgoode Hall Law School, "Public Statement on the International Investment Regime" (2010) at para 10, reproduced in (2011) 8(1) *Transnational Dispute Management*.

[14] Gus Van Harten, *Investment Treaty Arbitration and Public Law* (Oxford University Press, 2007) at pp 152ff; David Schneiderman, *Constitutionalizing Economic Globalization: Investment Rules and Democracy's Promise* (Cambridge University Press, 2008), at pp 180ff.

[15] United Nations Conference on Environment and Development (UNCED), *Agenda 21: Programme of Action for Sustainable Development* UN Doc A/Conf.151/6/Rev.1 (1992) at para 2.23: "Investment is critical to the ability of developing countries to achieve needed economic growth to improve the welfare of their populations and to meet their basic needs in a sustainable manner, all without deteriorating or depleting the resource base that underpins development. Sustainable development requires increased investment, for which domestic and external financial resources are needed. Foreign private investment and the return of flight capital, which depend on a healthy investment climate, are an important source of financial resources." For further references to documents of international conferences and organizations see also Markus W Gehring and Andrew Newcombe, "An Introduction to Sustainable Development in World Investment Law", in Marie-Claire Cordonier Segger, Markus W Gehring and Andrew Newcombe (eds), *Sustainable Development in World Investment Law* (Kluwer Law International 2011) at pp 3, 4-5.

investment law as an instrument for the furtherance of the rule of law. This section of the chapter does so on a conceptual level in discussing how investment treaties and investment treaty arbitration can be understood as an expression of the rule of law. As a definition and benchmark, I want to use a "thick" definition of the rule of law, similar to that developed by Lord Bingham.[16] Given that international investment law is part of international law and hence subjects domestic legal systems to its understanding of the rule of law, but itself also needs to be measured against an international yardstick, the transnational definition contained in the UN Secretary-General's 2012 report, *Delivering Justice: Programme of Action to Strengthen the Rule of Law at the National and International Levels*, seems particularly appropriate in this context. It defines the rule of law:[17]

> as a principle of governance in which all persons, institutions and entities, public and private, including the State itself, are accountable to laws that are publicly promulgated, equally enforced and independently adjudicated, and which are consistent with international human rights norms and standards. It requires, as well, measures to ensure adherence to the principles of supremacy of law, equality before the law, accountability to the law, fairness in the application of the law, separation of powers, participation in decisionmaking, legal certainty, avoidance of arbitrariness and procedural and legal transparency.

The question that arises then is how this definition is reflected in the investment treaty regime. Three aspects, in my view, are worth discussing. These are, first, the question of how the very existence of treaties that provide for special protection to foreign investors can be squared with the concept of the rule of law and the idea of "equality before the law" inherent in it; second, the question to which extent the substantive standards of investment treaties reflect the content of the rule of law as defined above; and finally, how access to investor-state arbitration can be seen as part of the rule of law.

Rule of Law Objectives of Investment Treaties

Turning to the first point, the existence of investment treaties is best considered in relation to the rule of law by looking at the objectives of investment treaties. These are closely related to the functions of the rule of law. According to Jeswald Salacuse, the objectives of investment treaties

[16] Tom Bingham, *The Rule of Law* (Allen Lane, Penguin Press, 2010) at p 8.
[17] *Delivering Justice: Programme of Action to Strengthen the Rule of Law at the National and International Levels, Report of the Secretary General*, UN Doc A/66/749 (2012) at para 2.

can be distinguished into primary, secondary, and long-term objectives.[18] Primary objectives are the protection and promotion of foreign investment; secondary objectives encompass market liberalization and the building of closer economic and political relations among contracting states. Yet, all of this is not an end in itself, but geared towards enhancing, on the long run, the economic welfare of contracting states. Investment protection and promotion, in other words, have the objective to lead to economic growth and, ultimately, human development.

The functions of the rule of law can be seen in parallel to these objectives. The goal to protect foreign investment corresponds to the protection that the rule of law is designed to afford against illegitimate government conduct. The promotion of foreign investment runs parallel to the function of the rule of law in decreasing political risk, that is, the risk resulting from cooperation with a state that has sovereignty over the law regulating the investment and which, in the absence of an investment treaty, exercises complete judicial control over any disputes that might arise between the investor and the host state.[19] And finally, just as investment treaties ultimately aim at contributing to the development of host states, the concept of the rule of law is widely recognized as an important factor for economic growth and development.[20] Richard Posner, for instance, points to the "empirical evidence showing that the rule of law does contribute to a nation's wealth and its rate of economic growth."[21] Similarly, the link between the rule of law and economic development has materialized in the World Bank's legal reform

[18] Jeswald Salacuse, *The Law of Investment Treaties* (Oxford University Press, 2010) at pp 108ff.

[19] On the notion of political risk and dispute settlement through arbitration as a means of risk management, see Noah Rubins and N Stephan Kinsella, *International Investment, Political Risk and Dispute Solution* (Oxford University Press, 2005) at pp 261ff.

[20] Daron Acemoglu, James A Robinson and Simon Johnson, "Institutions as the Fundamental Cause of Long-Run Growth" in Philippe Aghion and Steven N Durlauf (eds), *Handbook of Economic Growth*, Vol 1 A (North Holland, 2005) at pp 385, 389.

[21] Richard A Posner, "Creating a Legal Framework for Economic Development" (1998) 13 *The World Bank Research Observer* 1 at 3. See also Hernando De Soto, *The Other Path* (Harper & Row 1989); James Bradford De Long and Andrei Shleifer, "Princes and Merchants: European City Growth Before the Industrial Revolution" (1993) 36 *Journal of Law and Economics* 671; Timothy Besley, "Property Rights and Investment Incentives: Theory and Evidence from Ghana" (1995) 103 *Journal of Political Economy* 903; William Easterly and Ross Levin, "Africa's Growth Tragedy: Policies and Ethnic Divisions" (1997) 112 *Quarterly Journal of Economics* 1203; William Easterly and Ross Levine, "Tropics, Germs, and Crops: How Endowments Influence Economic Development," (2002) 50 *Journal of Monetary Economics* 3; Stephen Knack and Philip Keefer, "Institutions and Economic Performance: Cross-Country Tests Using Alternative Institutional Measures" (1995) 7 *Economics & Politics* 207; Daron Acemoglu, James A Robinson and Simon Johnson, "The Colonial Origins of Comparative Development: An Empirical Investigation" (2001) 9 *American Economic Review* 1369; Dani Rodrik, Arvind Subramarian and Francesco Trebbi, "Institutions Rule: The Primacy of Institutions over Geography and Integration in Economic Development" (2004) 9 *Journal of Economic Growth* 131.

program[22] and has been reiterated in its good governance agenda, which comprises, as one of the core concepts to help developing countries develop, the rule of law.[23]

The critical point from a rule of perspective, however, remains, how a system for the protection of the specific class of foreign investors can be justified, instead of a system creating rule of law institutions for all investors, both domestic and foreign. The main reason for the limited personal scope of application of investment treaties lies in their pedigree in the international law of aliens which was based on the idea that conduct that interferes with the rights of a foreigner, including her property rights, was a violation of the rights of the foreigner's home state.[24] Yet, notwithstanding the limited protection *ratione personae*, investment treaties are considered to have an impact on domestic investments as well. This is most obvious in case of investment projects that are implemented through joint ventures between a foreign and a domestic investor, where the latter indirectly benefits from the protection afforded to the former.

But arguably the indirect impact of investment treaties on domestic investors goes further. As pointed out by Salacuse, a secondary objective of investment treaties is the encouragement of domestic investments. As he argues, "[a]n investment treaty … serves as a 'signaling device' to the domestic private sector that the government's intentions towards private capital, both foreign and domestic, are benign in view of the international commitments it has made in the treaty to protect capital of foreigners."[25] In addition, improved domestic governance and a strengthened rule of law are another secondary objective given that, as soon as governments internalize the disciplines that investment treaties demand in the treatment of foreign investors, domestic investors are likely to benefit through "trickle-down effects". As explained by Salacuse:

> The theory underlying this rationale is that developing country authorities and institutions that have prevented themselves from acting in arbitrary and abusive fashion towards foreign investors by signing a treaty will also be lead to avoid arbitrary and abusive actions towards their own nationals. Over time those

[22] For a critical account, see Lawrence Tshuma, "The Political Economy of the World Bank's Legal Framework for Economic Development" (1999) 8 *Social and Legal Studies* 75.
[23] See World Bank, *Governance and Development* (World Bank 1992) at p 28.
[24] For the classical expression of this idea see *Chorzow Factory Case (Germany v Poland)* (1928) PCIJ Reports (ser A), No 17, 3, 27-28.
[25] Jeswald Salacuse, *The Law of Investment Treaties* (Oxford University Press, 2010) at p 113.

> authorities and institutions may demonstrated improved governance and a heightened respect for the rule of law.[26]

Looking at the primary, secondary, and long-term objectives of investment treaties and comparing them to the function of the rule of law therefore makes a case for understanding investment treaties as an instrument geared towards furthering the rule of law. In this perspective, investment treaties are serving both as substitutes for domestic institutions and the domestic rule of law and as inducements to governments to improve their domestic legal regimes in order to reduce the prospect of future international claims for damages.[27]

Standards of Treatment as Embodiments of the Rule of Law

Turning from the objectives of investment treaties to the substantive standards of protection, how is the rule of law reflected in them? On a general level, the standards of protection contained in investment treaties reflect a liberal, rights-based approach which seeks to limit government action that interferes with protected investments. In terms of their content, these standards correspond, or at least are analogous in some respects, to the rights and principles governing state-market relations found in the domestic legal orders of many countries, mostly at the constitutional level.

The specific guarantees contained in investment treaties aim at implementing structures that are essential for the functioning of a market economy and cover aspects of the rule of law. National and most-favored-nation treatment are designed to bring about equality before the law by ensuring, as a prerequisite for fair competition, a level playing field for the economic activity of foreign and domestic economic actors. The protection against expropriation guarantees respect for property rights as an aspect of the rule of law and an essential prerequisite for market transactions; capital transfer guarantees ensure the free flow of capital in and out of the host state and contribute to the efficient allocation of resources in a global market; and umbrella clauses back up private ordering between foreign investors and the host state by ensuring that contractual and other similar promises vis-à-vis foreign investors benefit from a layer of international law protection in addition to the protections that exist under domestic law. All these standards address problems that businesses face and which concern aspects of the rule of law.

[26] Jeswald Salacuse, *The Law of Investment Treaties* (Oxford University Press, 2010) at p 114.
[27] *Cf* Tom Ginsburg, "International Substitutes for Domestic Institutions: Bilateral Investment Treaties" (2005) 25 Int'l Rev L & Econ 107.

But there is one standard that is even more closely related to the rule of law, that is, the standard of fair and equitable treatment. In fact, as I have argued elsewhere, the way arbitral tribunals have interpreted fair and equitable treatment can be equated with how the rule of law is commonly understood in domestic public law, international law, and in the development efforts of various development organizations as part of the concept of good governance.[28] In close parallel to the definition of the rule of law set out above, and depending upon the context of different cases, arbitral tribunals have variously interpreted the standard of fair and equitable treatment to encompass (1) the requirement of legal security and predictability; (2) the principle of legality; (3) the protection of legitimate expectations; (4) basic due process requirements for administrative and judicial proceedings; (5) protection against arbitrariness and discrimination; (6) legal certainty and transparency; and (7) the concept of proportionality or reasonableness. These concepts reflect elements of the rule of law that one can also find in the administrative and constitutional frameworks of many countries worldwide.

Two examples from arbitral jurisprudence to illustrate the parallels between the rule of law and fair and equitable treatment may suffice for present purposes. The first example is the decision in *Waste Management v Mexico*, an ICSID Additional Facility case under the North American Free Trade Agreement (NAFTA). In its award, the Tribunal understood the fair and equitable treatment to be:

> … infringed by conduct attributable to the State and harmful to the claimant if the conduct is arbitrary, grossly unfair, unjust or idiosyncratic, is discriminatory and exposes the claimant to sectional or racial prejudice, or involves a lack of due process leading to an outcome which offends judicial propriety – as might be the case with a manifest failure of natural justice in judicial proceedings or a complete lack of transparency and candour in an administrative process.[29]

The parallels to the concept of the rule of law as set out above are striking. While not identical, and qualified through adjectives such as "gross" or "manifest", the Tribunal's interpretation of fair and equitable treatment is structurally analogous to elements of the rule of law, such as the prohibition of discrimination and arbitrariness as well as due process and transparency in administrative proceedings.

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[28] See Stephan W Schill, "Fair and Equitable Treatment, the Rule of Law, and Comparative Public Law" in Stephan W Schill (ed), *International Investment Law and Comparative Public Law* (Oxford University Press, 2010) at pp 151ff.

[29] *Waste Management, Inc v United Mexican States* [2004] ICSID Case No ARB(AF)/00/3, award dated 30 April 2004, at para 98.

A second example is the ICSID case *Tecmed v Mexico*[30] under the Spanish-Mexican BIT. In applying the fair and equitable treatment standard to the relations between an investor in a hazardous waste landfill and the supervisory agency, the Tribunal focused on the concept of legitimate expectations as part of fair and equitable treatment and held that the latter standard

> … requires … treatment that does not affect the basic expectations that were taken into account by the foreign investor to make the investment. The foreign investor expects the host State to act in a consistent manner, free from ambiguity and totally transparently in its relations with the foreign investor … The foreign investor also expects the host State to act consistently, i.e. without arbitrarily revoking any preexisting decisions or permits issued by the State that were relied upon by the investor to assume its commitments … The investor also expects the State to use the legal instruments that govern the actions of the investor or the investment in conformity with the function usually assigned to such instruments, and not to deprive the investor of its investment without the required compensation.[31]

Once again, and even though the interpretation of the *Tecmed* tribunal of fair and equitable treatment differed from that of the *Waste Management* tribunal, there are clear structural parallels between fair and equitable treatment and how the rule of law is applied to administrative relations at the domestic level to protect legitimate expectations of private actors. Structural analogies are also notable in that the *Tecmed* tribunal considered fair and equitable treatment to prohibit the inconsistent application of domestic law or its non-application, as well as arbitrary conduct of the administration.

Not only can an understanding of fair and equitable treatment as an embodiment of the rule of law be reconstructed from arbitral jurisprudence; it can also be linked to the development-related object and purpose of investment treaties. This is possible when considering the debate about the relationship between the rule of law and development together with the object and purpose of international investment law to contribute to the host country's development by protecting and promoting foreign investment.[32] Indeed, development as the wider context and objective of investment treaties is also articulated in the ICSID Convention. Reflecting the development goals of the World Bank Group, of which ICSID forms part, and the belief that the

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[30] *Técnicas Medioambientales Tecmed SA v the United Mexican States* [2003] ICSID Case No ARB (AF)/00/2, award dated 29 May 2003.
[31] *Técnicas Medioambientales Tecmed SA v the United Mexican States* [2003] ICSID Case No ARB (AF)/00/2, award dated 29 May 2003, at para 154.
[32] See text accompanying nn18-27 above.

creation of facilities for the neutral arbitration and conciliation of disputes between private investors and states could further development,[33] the Preamble of the ICSID Convention explicitly draws a connection between economic development and the protection of foreign investment.[34]

Investment Treaty Arbitration as Judicial Review

Turning finally to dispute settlement, investment treaty arbitration serves as a mechanism to implement the rule of law standards laid down in investment treaties. Furthermore, investment treaty arbitration can be understood as a form of access to justice, as a neutral, independent and impartial dispute settlement mechanism that has the function to control government action. In that respect, investment treaty arbitration assumes the role that is usually fulfilled by courts exercising judicial review at the domestic level. Indeed, this right is often backed by a constitutional right to judicial review of government conduct, which itself is an aspect of the rule of law.[35]

In this context, investment treaty arbitration compensates for a number of limitations that may exist for foreigners concerning access to justice under domestic law. In Germany, to take an example, domestic law, including constitutional law, contains a number of important restrictions for foreigners in this respect. The German Constitution, the "Grundgesetz" (Basic Law), for instance, does not grant fundamental rights to foreign juridical persons. Under Article 19(3) Grundgesetz, foreign corporations cannot rely on fundamental rights granted in the Constitution, and hence have no access to the German Constitutional Court.[36] Similarly, Article 12 Grundgesetz, which contains the freedom of enterprise, a right that, *inter alia*, protects against government interference with business enterprises that fall short of interferences with the right to

[33] On this point see Aron Broches, "The Convention on the Settlement of Investment Disputes between States and Nationals of Other States" (1972) 136(2) *Recueil des Cours* 331 at 343.
[34] ICSID, *ICSID Convention, Regulations and Rules* (International Centre for Settlement of Investment Disputes, April 2006) at p 11.
[35] See, *eg*, the Basic Law for the Federal Republic of Germany, Article 19(4); the Constitution of the Italian Republic, Article 24; the Spanish Constitution, Section 24(1); the Political Constitution of the Republic of Chile, Article 20.
[36] There is an exception for juridical persons from other Member States of the European Union (EU) who can invoke their rights of non-discrimination under EU law to claim equal treatment with German juridical persons. See BVerfGE 129, 78, 97ff (German Constitutional Court, 19 July 2011). In the absence of specific treaty commitments, however, juridical persons from outside the EU will not benefit from fundamental rights protection under German constitutional law.

property, is a fundamental right that is only afforded to German natural and juridical persons, not foreigners.[37]

And finally, even if there is access to justice under domestic law, the recourse provided is not necessarily neutral; the forum not necessarily independent from the respondent government; and the recourse provided not necessarily sufficiently efficient. Corrupt or government-dependent courts are only the tip of the iceberg. Even well-developed domestic systems can face problems with their domestic courts. In respect of Germany, for example, the European Court of Human Rights has rendered multiple judgments deciding that the length of domestic court proceedings in Germany was contrary to Article 6(1) of the European Convention on Human Rights which provides for "a fair and public hearing within a reasonable time by an independent and impartial tribunal established by law."[38] What is more, in a pilot proceeding against Germany, the European Court of Human Rights even determined that overly long court proceedings and the inexistence of a remedy under domestic law to address them constituted a "systemic problem".[39]

In all of these instances, investment treaty arbitration can be a means to provide access to justice for foreign investors that may otherwise face problems in domestic courts. Viewing investment arbitration as a mechanism to provide judicial review can also be backed by the rationale of a decision of the European Court of Human Rights that concerned the question of whether Article 6(1) of the European Convention on Human Rights required access to a permanent court in order to bring claims, including against the government. In *Lithgow and others v United Kingdom*, the applicants argued that an "Arbitration Tribunal was not a 'lawful tribunal'" in the sense of Article 6(1) of the Convention "in that it was an extraordinary court, namely a tribunal set up for the purpose of adjudicating a limited number of special issues affecting a limited number of companies".[40] This drew the following response from the Court:

[37] However, non-discrimination provisions under EU law must have the effect of extending that right to foreigners who are EU nationals.
[38] See, amongst others, *Sürmeli v Germany*, ECtHR (Application No 75529/01), decision of 8 June 2006, at para 134; *Kressin v Germany*, ECtHR (Application No 21061/06), decision of 22 December 2009, at para 26; *Spaeth v Germany*, ECtHR (Application No 854/07), decision of 29 September 2011, at para 42.
[39] *Rumpf v Germany*, ECtHR (Application No 46344/06), decision of 2 September 2010, at para 64ff.
[40] *Lithgow and Others v United Kingdom*, ECtHR (Application No 9006/80, Series A102), decision of 8 July 1986, at para 201.

> The Court cannot accept this argument. It notes that the Arbitration Tribunal was 'established by law', a point which the applicants did not dispute. Again, it recalls that the word 'tribunal' in Article 6 para. 1 is not necessarily to be understood as signifying a court of law of the classic kind, integrated within the standard judicial machinery of the country; thus, it may comprise a body set up to determine a limited number of specific issues, provided always that it offers the appropriate guarantees. The Court also notes that, under the statutory instruments governing the matter, the proceedings before the Arbitration Tribunal were similar to those before a court and that due provision was made for appeals.[41]

Even though the decision did not concern recourse to an investment treaty tribunal, its rationale would seem to apply equally in that context. As a consequence, submitting to investor-state arbitration can be considered as a fulfillment of the obligation of the host state to offer a forum for judicial review and therefore provide a dispute settlement infrastructure that is required by the concept of the rule of law.

Taking into consideration all of the above, it is possible to understand investment treaties as a compensatory mechanism for problems that may exists in host states' domestic governance with the domestic rule of law, both as regards substance and procedure. Substantive investment treaty standards reflect rule of law components that are often enshrined in domestic constitutional law, and investment arbitration provides a mechanism through which compliance with these standards can be ensured. Although tribunals cannot repeal measures that are contrary to an investment treaty, or enforce awards ordering specific performance, the preferred remedy under investment treaties, that is damages as a consequence of the host state's international responsibility,[42] arguably creates an incentive for governments to comply with the rule of law standards set out in the treaties.

As additional mechanisms to implement the rule of law standards contained in investment treaties, one could also promote the direct application of investment treaties in domestic courts and by the domestic executive, and consider the introduction of investment treaty impact assessment mechanisms in order to reduce, or even avoid, liability of host states under investment treaties. Finally, it may be worth considering under which conditions investment treaty arbitration can create incentives for domestic court reform. After all, only if domestic

[41] *Lithgow and Others v United Kingdom*, ECtHR (Application No 9006/80, Series A102), decision of 8 July 1986, at para 201.

[42] Notably, awards for damages can be enforced widely, depending on the applicable arbitration rules, either under Art 54(1) of the ICSID Convention or under the Convention on the Recognition and Enforcement of Foreign Arbitral Awards (10 June 1958) 330 UNTS 38 (entered into force 7 June 1959) (the "New York Convention").

courts are as good or better than investment treaty tribunals, are foreign investors likely to consider having recourse to them instead of initiating arbitration. All of this could enhance the rule of law effects of international investment treaties and investment treaty arbitration.

The Rule of Law as a Benchmark for Investment Law

Yet, the rule of law is not only important as an explanation of the structure and content of investment treaties, it is also an important set of standards against which the practice of investment law and in particular investment arbitration has to be measured. Challenges to the rule of law that are caused by investment law itself are manifold. First, investment treaties implement an asymmetric rule of law: they protect foreign investors without expressly having regard to competing rights and interests that are protected under national or international law. How investment treaties interact with human rights, public health, environmental law, labour rights or indigenous rights, and more generally the question of how much space they give to host governments to regulate in the public interest is a concern that must be addressed in order to assess what kind of rule of law investment treaties further.[43]

Secondly, inconsistencies in arbitral awards constitute a problem for legal certainty and predictability and hence for the rule of law.[44] Thirdly, there is an issue of accountability of arbitrators in the way they develop the law, because there are no supervisory mechanisms that are comparable to the ones at the domestic level, namely a supreme or constitutional court at the apex of the court system and a legislature that can act against judicial decisions that it considers undesirable by modifying law to be applied by the courts.[45] Fourthly, the issue of independence and impartiality of arbitrators, the question of an alleged pro-investment bias in their jurisprudence, and what is often called a "double-hat problem", that is, the fact that one and the same person can act as arbitrator in one proceedings and simultaneously as counsel in another

[43] For a critical account see, *eg*, Kyla Tienhaara, *The Expropriation of Environmental Governance* (Cambridge University Press, 2009).
[44] Susan D Franck, "The Legitimacy Crisis in Investment Treaty Arbitration: Privatizing Public International Law Through Inconsistent Decisions" (2005) 73 Fordham L Rev 1521; Stephan W Schill, "W(h)ither Fragmentation? On the Literature and Sociology of International Investment Law" (2011) 22 EJIL 875, at 281ff
[45] For a description of this problem in respect of international courts and tribunals generally, see Armin von Bogdandy and Ingo Venzke, "Beyond Dispute: International Judicial Institutions as Lawmakers" (2011) 12 *German Law Journal* 979.

case, are questions that need to be addressed from the perspective of the rule of law.[46] Finally, transparency and third-party participation are important issues for the rule of law.[47]

All of these issues need to be debated and are currently debated. Yet, the challenges posed for the rule of law in this context should be taken as such: they are challenges that require adaptation of the existing system of international investment law and investor-state dispute resolution, but do not, in my view, militate for abandoning the system of investment law in principle, as some argue. Investment treaties are not *per se* contrary to the rule of law, but can actually further it as argued above. At the same time, and notwithstanding the positive impact investment law can make towards the domestic rule of law, we must use the concept of the rule of law as a yardstick for the investment treaty system itself. After all, only if investment treaties and investor-state arbitration themselves meet the commonly accepted standards embodied in the rule of law will the outcome of arbitral jurisprudence be considered as legitimate. In this sense, the concept of the rule of law can serve as a guidepost in the current debates about the reform of international investment law.

Thus, the concept of the rule of law can be used to demand more transparency and third party participation, a process that is well underway with the coming into effect of the UNCITRAL Rules on Transparency in Treaty-based Investor-State Arbitration on 1 April 2014[48] and the adoption by the General Assembly of the United Nations Convention on Transparency in Treaty-based Investor-State Arbitration on 10 December 2014.[49] Likewise, the concept of the rule of law should also inform debates about the introduction of codes of conduct for arbitrators and counsel, a topic that the EU has introduced, inter alia, in its investment treaty negotiations

[46] On questions of professional ethics in investment arbitration generally, see Catherine Rogers, *Ethics in International Arbitration* (Oxford University Press, 2014).

[47] See Julie Maupin, "Transparency in International Investment Law: The Good, the Bad and the Murky" in Andrea Bianchi and Anne Peters (eds), *Transparency in International Law* (Cambridge University Press, 2013) at p 142; Alessandra Asteriti and Christian J Tams, "Transparency and Representation of the Public Interest in Investment Treaty Arbitration" in Stephan W Schill (ed), *International Investment Law and Comparative Public Law* (Oxford University Press, 2010) at pp 787ff; UNCTAD, *Transparency*, UNCTAD Series on Issues in International Investment Agreements II (2012).

[48] Report of the United Nations Commission on International Trade Law of its Forty-Sixth Session (8-26 July 2013), UN Doc A/68/17 (2013) <www.un.org/en/ga/search/view_doc.asp?symbol=A/68/17> (accessed 13 May 2014) at para 128 and Annex I.

[49] Resolution adopted by the General Assembly on 10 December 2014, UN Doc A/RES/69/116 (2014) <http://www.un.org/ga/search/view_doc.asp?symbol=A/RES/69/116&Lang=E> (accessed 20 January 2015).

with Canada and the United States.[50] The rule of law could also be a guiding principle in discussing strengthened corporate social responsibility in international investment relations in order to emphasize not only the rights of foreign investors, but also their duties. Similarly, the concept of the rule of law can inform governments' efforts to recalibrate investment treaty obligations in order to achieve a better balance between investment protection and competing concerns and to implement a thick rule of law.

In consequence, in order to implement a thick version of the rule of law in treaty-making that has regard to competing rights and the host states' right to regulate, contracting states are: concretizing the substantive standards of treatment in investment treatment, such as the concept of indirect expropriation or fair and equitable treatment;[51] introducing general exceptions in order to allow certain interferences with investor rights for public purposes;[52] clarifying the concept of protected investment;[53] recalibrating access to investor-state arbitration and achieving a better integration of alternative dispute settlement mechanisms;[54] and considering the introduction of control mechanisms for arbitrations, such as appellate mechanisms or joint interpretation commissions that the contracting states can use in order to counter the precedential effect of arbitral decisions the contracting states disapprove of.[55] Finally, governments need to be

[50] See Question 8 of the European Commission's online questionnaire issued in the context of its public consultation on investment protection and investor-to-state dispute settlement in the Transatlantic Trade and Investment Partnership Agreement (TTIP), available via <http://ec.europa.eu/yourvoice/ipm/forms/dispatch?form=ISDS> (accessed 9 June 2014). See also the Agreement Between the Government of Canada and the Government of the People's Republic of China for the Promotion and Reciprocal Protection of Investments (9 September 2012) <http://www.international.gc.ca/trade-agreements-accords-commerciaux/agr-acc/fipa-apie/china-text-chine.aspx?lang=eng> (accessed 17 June 2014), Art 24(2)(c) of which provides that arbitrators must "comply with any additional rules where such rules are agreed to by the Contracting Parties," which would provide an express basis for incorporating ethical rules on arbitrator conduct.

[51] See, for example, Annexes on Expropriation and FET in the 2012 US Model BIT <http://www.ustr.gov/sites/default/files/BIT%20text%20for%20ACIEP%20Meeting.pdf> (accessed 9 June 2014); see further European Commission, "Public consultation on modalities for investment protection and ISDS in TTIP", <http://trade.ec.europa.eu/doclib/docs/2014/march/tradoc_152280.pdf> (accessed 9 June 2014) at Table 3 and Table 4.

[52] See, for example, the Agreement Between the Government of Canada and the Government of the People's Republic of China for the Promotion and Reciprocal Protection of Investments (9 September 2012) <http://www.international.gc.ca/trade-agreements-accords-commerciaux/agr-acc/fipa-apie/china-text-chine.aspx?lang=eng> (accessed 17 June 2014), Art 33.

[53] On the exclusion of sovereign debt from the scope of protected investment, see Peru-Korea Free Trade Agreement (21 March 2011, entered into force 1 August 2011) <http://www.sice.oas.org/TPD/PER_KOR/PER_KOR_Texts_E/09_KPFTA_Investment.pdf> (accessed 9 June 2014), Annex 9d.

[54] See, *eg*, UNCTAD, "Reform of Investor-State Dispute Settlement: In Search of a Roadmap" IIA Issues Note No 2 (2013) <http://unctad.org/en/PublicationsLibrary/webdiaepcb2013d4_en.pdf> (accessed 9 June 2014) at pp 7-8.

[55] See, *eg*, 2012 US Model Bilateral Investment Treaty <http://www.ustr.gov/sites/default/files/BIT%20text%20for%20ACIEP%20Meeting.pdf> (accessed 9 June 2014) at Art 28(10).

reminded of their role as enforcers of obligations that serve interests that compete with investment protection: not only do they have to refrain from illegitimate interference with foreign investment, but they also have a duty to regulate investment efficiently in order to protect competing concerns.

Yet, the rule of law should not only guide governments in treaty-making. It also has to inform arbitrators in how they conduct arbitral proceedings, exercise their procedural powers, and interpret investment treaties. Thus, even though the protection of competing rights and interests is usually not expressly mentioned in investment treaties –unlike in human rights treaties that contain provisions stipulating for which purposes and under which conditions states can interfere with protected rights– investment arbitrators are equipped with sufficient interpretative tools to achieve the idea of a thick rule of law and to ensure sufficient policy space for host states to regulate in the public interest.

Arbitrators can, as I have suggested elsewhere, make more use of comparative law analysis to concretize the interpretation of vague standards of treatment in investment treaties in order to align the application of these standards with commonly accepted legal analysis and outcomes of comparable disputes at the domestic level.[56] One public law concept that can guide the interpretation of investment treaty standards, which is particularly powerful in striking a balance between investment protection and competing rights and interests of host states and their population, is the use of proportionality analysis; notably, such reasoning is an interpretative technique that is increasingly used by arbitrators.[57] Finally, investment tribunals are able to

[56] See Stephan W Schill, "International Investment Law and Comparative Public Law: An Introduction" in Stephan W Schill (ed), *International Investment Law and Comparative Public Law* (Oxford University Press, 2010) at pp 3ff. For examples of such methodology see *Total SA v Argentine Republic* [2010] ICSID Case No ARB/04/1, decision on liability dated 27 December 2010, at para 111; *Toto Costruzioni Generali SpA v Republic of Lebanon* [2012] ICSID Case No ARB/07/12, award dated 7 July 2012, at para 166; *Occidental Petroleum Corporation and Occidental Exploration and Production Company v Republic of Ecuador* [2012] ICSID Case No ARB/06/11, award dated 5 October 2012, at para 402-404; *Gold Reserve Inc v Bolivarian Republic of Venezuela* [2014] ICSID Case No ARB(AF)/09/1, award dated 22 September 2014, at para 576.

[57] See *Tecnicas Medioambientales Tecmed SA v United Mexican States* [2003] ICSID Case No ARB (AF)/00/2, award dated 29 May 2003, at para 122; *Saluka Investments BV v Czech Republic* [2006] UNCITRAL, partial award dated 17 March 2006, at para 306; Benedict Kingsbury and Stephan W Schill, "Public Law Concepts to Balance Investors' Rights with State Regulatory Actions in the Public Interest – The Concept of Proportionality" in Stephan W Schill (ed), *International Investment Law and Comparative Public Law* (Oxford University Press, 2010) at pp 75ff; Alec Stone Sweet, "Investor–State Arbitration: Proportionality's New Frontier" (2010) 4 L Ethics Hum Rights 47; Erlend Leonhardsen, "Looking for Legitimacy: Exploring Proportionality Analysis in Investment Treaty Arbitration" (2011) 1 J Int Disp Settlement 1; Caroline Henckels, "Indirect Expropriation and the Right to Regulate: Revisiting Proportionality Analysis and the Standard of Review in Investor-State Arbitration" (2012) 15 JIEL 223.

safeguard policy space by considering what the appropriate standard of review is of government conduct, in other words the question to which extent certain findings of fact and of law made by the host state prior to taking a measure against a foreign investor can be revisited by an investment tribunal or to which extent deference is appropriate.[58]

Ultimately, the end towards which all of these techniques and approaches should be employed, both in investment treaty-making and investment treaty arbitration, is meeting the goals of the rule of law, as expressed by Joseph Raz: "After all the rule of law is meant to enable the law to promote social good, and should not be lightly used to show that is should not do so. Sacrificing too many social goals on the altar of the rule of law may make the law barren and empty."[59] This should be the guiding vision for the rule of law that investment treaties and investment treaty arbitration help implement for investor-state relations and their contribution to development.

[58] Stephan W Schill, "Deference in Investment Treaty Arbitration: Re-conceptualizing the Standard of Review" (2012) 3(3) J Int Disp Settlement 577.
[59] Joseph Raz, "The Rule of Law and Its Virtues" (1977) 93 LQR 195 at 211.