Page 1378 - 1386 **DOI:** *https://doij.org/10.10000/IJLMH.113141*

INTERNATIONAL JOURNAL OF LAW MANAGEMENT & HUMANITIES

[ISSN 2581-5369]

Volume 5 | Issue 3

2022

The Arbitration Settlement of Investment Disputes between States and Nationals of other States

HARSHIKA MEHTA [1]

ABSTRACT

This paper focuses on the settlement of investment disputes between States. There are numerous ways to handle the legal issues which arise from investment practices. This paper mainly deals with the areas of state-investor dispute settlement from the point of view of the state as well as the investor. How the venues for the dispute settlement are decided and how the disputes are resolved in accordance with Alternative Dispute Resolution (ADR) mechanisms. These third-party resolution procedures help to gain the trust of the investor and also create a space for a fair process of settling these disputes. On the other hand, there are some countries that have been following the old tradition where foreign investors are not allowed to go for the methods of dispute settlement and are only entitled to resolve their disputes through the judiciary system or the national courts of the country. This paper will further discuss the various options that are there when a dispute settlement is considered in international investment agreements. The inclusion of dispute settlement procedures can be omitted in investment agreements, the reference of a dispute settlement approach can be based upon the consent of the disputing parties and can come under the jurisdiction of the courts and tribunals. The choice offered to the disputing parties makes it easier for them to choose an approach whether national or international, in cases that are exceptional, a dispute can be compulsorily referred to as an international mode of dispute settlement.

I. INTRODUCTION

The rise of International Investment Agreements (IIAs) is due to the development of international investments and trade in developed as well as developing nations. This development has created new opportunities for the global economy to grow. The International Investment Agreements regulate various issues which fall under the purview of foreign investments. The provisions of dispute settlement between parties and the host state are given in domestic agreements and also in a number of bilateral investment treaties (BITs).[2] The two

[1] Author is a student, India.

[2] United Nations Conference on Trade and Development (UNCTAD) (forthcoming a). *Dispute Settlement: State-*

 [ISSN 2581-5369]

kinds of disputes are Investor-State and State-to-State disputes. Initially, international law used to resolve disputes between states but due to the privatisation of commercial activities done by corortorate sectors and the individuals has raised a big question of whether the disputes which involve such private commercial activities should be entitled the rights to solve these disputes with the country in which they have internationally invested. According to Customary International law, the disputes of a foreign investor are settled in the tribunals or the courts of the country concerned.[3] The corporations or the individuals have to rely on indirect means for the justification of their rights as they fail to stand the test of an international legal personality.

II. THE NATURE OF THE INVESTMENT DISPUTES

The disputes that involve investments are often settled amicably instead of a full litigation process because the disputing parties have a high difference of opinion. The rights and duties listed in the investment agreement between the disputing parties is often an area where the parties disagree upon the interpretation of these rights and duties. The disputes that arise between the foreign investors and the host state takes them to a point where the parties may accuse each other of allegations that are not relevant to their contract, for instance, the failure to provide treatment according to certain standards or failure to provide protection required by treaty or customary law.[4] The proper mechanism in which the dispute will fit dlepends upon how good the relations are between the parties. The third-party settlement procedures ensures that no disputing party gets away with unreasonable demands. The parties can only derive to an amicable agreement if they wish to continue their relationship in goot terms and these sort of disputes are resolved by the mechanisms of dispute settlement provided for in IIAs. The cases which are not capable of deriving a resolution which is mutual, are not settled by the means of negotiations.

There are many areas where there are questions existing with regards to the mechanisms to resolve the disputes, namely:

1. One of the debatable issues that exists in this context is whether the means of international arbitration should be used to settle a dispute as it may belittle the mechanisms of national dispute-settlement systems.

State. UNCTAD *Series on Issues in International Investment Agreements* (New York and Geneva: United Nations). Forthcoming.

[3] Brownlie, I.. *Principles of Public International Law*, 5th ed. (Oxford: Clarendon Press), 1998.

[4]Sornarajah, M.. *The Settlement of Foreign Investment Disputes* (The Hague: Kluwer), 2000..

 [ISSN 2581-5369]

2. It has been contested that the international minimum standards should not be applied to treat aliens and their properties as it is not universally accepted[5]

3. Both developed as well as developing countries believe that the international dispute settlement mechanisms are not reliable and this is evident as there were several disagreements over the provisons of the investor-State dispute-settlements and its contents during the Multilateral Agreement on Investment (MAI) negotiations at the Organisation for Economic Co-operation and Development (OECD)[6] and also, the arbitration awards of the recent North American Free Trade Agreement (NAFTA) were criticised politcally, judicially as well as academically.[7]

III. THE REMEDIES OF DIPLOMATIC PROTECTION AGAINST THE DISPUTE-SETTLEMENT MECHANISMS

The diplomatic protection remedies are not fruitful and has many deficiencies and lacunas from an investors' point of view, namely:

1. The rights granted to the investor by the diplomatic protection are held by the home country and it is in the hands of the home country to exercise these rights or not in order to defend the claim of the investor. It is in the hands of the home state to choose what to pursue as the investor's claim can sometimes hinder the international relations of the home state and the host state.

2. The home country, if in any case supporrts and pursues the claim of the investor, is still not bound to transfer the claim to its national investor.[8]

3. It is very difficult to accurately figure out the nationality of a firm if a corporation which is in a dispute has been affiliated with various countries, each having a different legal nationality and with a high percentage of international shareholders also known as the transnational corporations (TNCs) and hence the state's establishment of diplomatic protection becomes impossible.

Moreover, there are some limitations that come into place when this protection is established practically as the process of this protection calls for relatively small claims that can be resolved

[5] Sornarajah, M. (1994). *The International Law on Foreign Investment* (Grotius Publications: Cambridge University Press).
[6] United Nations Conference on Trade and Development (UNCTAD) *Lessons from the MAI. UNCTAD Series on Issues in International Investment Agreements* (New York and Geneva: United Nations), United Nations publication, Sales No. E.99.II.D.26, 1999
[7] De Palma, A. . "*How NAFTA makes the rules*", International Herald Tribune, 13 March, 2001.
[8] Jennings, R., and Watts, A.. *Oppenheim's International Law,* Vol. I (Harlow, Essex: Longman), 1992.

 [ISSN 2581-5369]

through inter-state mechanisms. Sometimes the implications that this process has over the relations of both the countries and also the corporations and the individuals are sometimes much more in comparison to the claim made by the investor. The home and the host countries would not want their relations to be tarnished and also the private investors would not want to have implications on their future economic endeavours and thus the foreign investors go for the option of resolving their disputes by the means of investor-state dispute-settlement mechanisms and not by diplomatic protection.

IV. NATIONAL DISPUTE SETTLEMENT IN THE HOST COUNTRY

Most of the countries try to maintain and preserve the national sovereignty for the activities going on in the territory of a nation by resolving the investor-State disputes in the national courts. The foreign investors do not have the option to go for the option to resolve their disputes by internationalized methods of dispute settlement. Thus, the United Nations Charter on Economic Rights and Duties of States[9], adopted on 12 December 1974, emphasised that each State has the right "to regulate and exercise authority over foreign investment within its national jurisdiction in accordance with its laws and regulations and in conformity with its national objectives and priorities"[10] This not only prohibits international dispute settlement outrightly but also gives a preference for national dispute settlement in the case of investor-State disputes. The national integirty can be preserved by keeping a requirement of including dispute-settlement provisions with local remedies to be exercised before pursuing the international claims. Local remedies are pursued before the pursuance of external arbitration or conciliation in some cases and time limits are placed on the local remedies requirement.[11] The negotiators believe that the formulations of the When the disputes are between the investor and the state.

On the other hand, as far as investor-State dispute settlement is concerned, the understanding of many negotiators is that the formulations of the bilateral investment treaties imply that the disputing parties have waived the requirement of pursuing the local remedies first.[12]

[9] United Nations Charter on Economic Rights and Duties of States available at: https://digitallibrary.un.org/record/74222?ln=en

[10] Charter of Economic Rights and Duties of States (UNGA resolution 3281 (XXIX)), 1974

[11] United Nations Conference on Trade and Development (UNCTAD). *Bilateral Investment Treaties in the Mid-1990s* (New York and Geneva: United Nations), United Nations publication, Sales No. E.98.II.D.8; Schreuer, C. (2001). T*he ICSID Convention: A Commentary* (Cambridge: Cambridge University Press). pp. 390-393, 1998

[12] Schreuer, id at pp. 390-396; Peters, P.. "Exhaustion of local remedies: ignored in most bilateral investment treaties", *Netherlands International Law Review*, Vol. XLIV, pp. 233-243, 1997

 [ISSN 2581-5369]

V. INTERNATIONAL DISPUTE SETTLEMENT

(A) Ad hoc dispute settlement

Ad hoc arbitration has been used very less as a mechanism for resolving investment disputes. However, the UNCITRAL Arbitration Rules (1976)[13] does not have an institutional system for settling the international disputes, this can be seen as an encouragement of ad hoc international arbitration and adding some value to it for the foreign investors and host States. The main objective is to bring harmony in the rules used in commercial arbitration, providing an optional and generally acceptable system of procedural norms for the conduct of such arbitrations.

(B) Institutional dispute settlement

The section 1 of ICSID convention, regulation and rules, 1966[14] clearly mentions that the institutional dispute settlement is the only system of dispute settlement specifically designed to deal with investor-State disputes. All the procedures related to the institutional dispute settlement mechanisms are listed in the ICSID Convention. The provisions of the convention raises the following points:

1. The parties give consent for an arbitration under the ICSID Convention which makes any other possible remedy unavailable particularly relating to the laws of the state. This makes the institutional arbitration under the ICSID convention an exclusive process which can only take place with the consent of the parties.
2. The state party at dispute gains control over the arbitration process in the degree of sovereignty by putting up the requirement of prior exhaustion of local remedies. In effect, this reverses the rule of customary international law, in that the inapplicability of that rule is presumed in the absence of an express statement by the State party to the dispute.[15]

VI. THE CHOICE OF PROCEDURE AND PROCEDURAL RULES

The following choices are provided to the disputing parties:

1. Choice of dispute-settlement method

2. Procedure for initiating a claim

[13] UNITED NATIONS COMMISSION ON INTERNATIONAL TRADE LAW (UNCITRAL), 1976
[14] International Centre for Settlement of Investment Disputes convention, regulation and rules, s 1, 1966
[15] Schreuer. C.. "Commentary on the ICSID Convention: Article 26", *ICSID Review: Foreign Investment Law Journal, Vol.* 12, pp. 196-197, 1997

 [ISSN 2581-5369]

3. Establishment and composition of the arbitral tribunal
4. Admissibility
5. Applicable law
6. Finality of awards
7. Enforcement of awards
8. Costs

VII. INTERACTION ACROSS ISSUES AND CONCEPTS

The issues that come under the dispute settlement of investment disputes are rudimental to the relationship of a foreign investor and the host country. This means that there is a solid interaction between the investor-State dispute settlement, a wide range of other issues and concepts that arise in investment practice.

Table 1: Interaction across issues and concepts[16]

Concepts in other papers	Investor-State dispute settlement
Admission and establishment[17]	Extensive interaction
Incentives	Moderate interaction
Investment-related trade measures	Moderate interaction
Most-favoured-nation treatment	Moderate interaction
National treatment[18]	Extensive interaction
Fair and equitable treatment[19]	Extensive interaction

[16] United Nations Conference on Trade and Development (UNCTAD) statistics, available at: https://unctad.org/statistics

[17] United Nations Conference on Trade and Development (UNCTAD) *Admission and Establishment. UNCTAD Series on Issues in International Investment Agreements* (New York and Geneva: United Nations), United Nations publication, Sales No. E.99.II.D.10,1999.

[18] United Nations Conference on Trade and Development (UNCTAD) *National Treatment. UNCTAD Series on Issues in International Investment Agreements* (New York and Geneva: United Nations), United Nations publication, Sales No. E.99.II.D.16, 1999.

[19] United Nations Conference on Trade and Development (UNCTAD). *Fair and Equitable Treatment. UNCTAD Series on Issues in International Investment Agreements* (New York and Geneva: United Nations), United Nations

Taxation	Moderate interaction
Transfer pricing[20]	Extensive interaction
Competition	Moderate interaction
Transfer of technology	Moderate interaction
Employment	Moderate interaction
Social responsibility	Moderate interaction
Environment	Moderate interaction
Home country measures	Moderate interaction
Host country operational measures	Moderate interaction
Illicit payments	Moderate interaction
Taking of property[21]	Extensive interaction
State contracts[22]	Extensive interaction
Transparency	Moderate interaction
Transfer of funds	Moderate interaction

publication, Sales No. E.99.II.D.15, 1999.

[20] United Nations Conference on Trade and Development (UNCTAD). *Transfer Pricing. UNCTAD Series on Issues in International Investment Agreements* (New York and Geneva: United Nations), United Nations publication, Sales No. E.99.II.D.8, 1999.

[21] United Nations Conference on Trade and Development (UNCTAD). *Taking of Property. UNCTAD Series on Issues in International Investment Agreements* (New York and Geneva: United Nations), United Nations publication, Sales No. E.00.II.D.4, 1999.

[22] United Nations Conference on Trade and Development (UNCTAD)(forthcoming b). *State Contracts. UNCTAD Series on Issues in International Investment Agreements* (New York and Geneva: United Nations). Forthcoming.

Dispute settlement: State-State[23]	Extensive interaction
Scope and definition[24]	Extensive interaction

VIII. GUARANTEE OF DISPUTE SETTLEMENT

(A) No reference to investor-State dispute settlement in an agreement

Theoretically, it is possible to not refer to any mode of dispute settlement in an international investment agreement but in practice, it is not possible as the main objective of the IIAs are to ensure a mode of dispute settlement into legally binding terms. This is for the parties to comply with the international legal obligations to settle the dispute in the way which is prescribed in the agreement. Sometimes, when the internal laws of the country are sufficeient to protect the rights and obligations of the host state as well as the foreighn investor, the reference to investor-state dispute settlement prescribed in the IIA are considered to be useless.

(B) Reference to investor-State dispute settlement in an agreement

The following options are given under the reference to investor-state dispute settlement:

- Choice of venue
- Choice of procedure and procedural rules

IX. CONCLUSION

Foreign investments can lead to a lot of disagreements and disputes with various types of parties involved, they all vary in nature and so naturally there is a requirement for advanced mechanisms of dispute-settlements which should not discriminate on the basis of the development of a country who is at dispute. There are mainly two sorts of approached available:

1. National
2. International

Another thing to be kept in mind while closely analysing the implications of the dispute settlement meachanisms is to see whether these mechanisms are providing an efficient way to resolve the disputes. For parties to consent for these third-party dispute-settlement

[23] United Nations Conference on Trade and Development (UNCTAD)(forthcoming a). *Dispute Settlement: State-State. UNCTAD Series on Issues in International Investment Agreements (*New York and Geneva: United Nations). Forthcoming.

[24] United Nations Conference on Trade and Development (UNCTAD). *Scope and Definition. UNCTAD Series on Issues in International Investment Agreements* (New York and Geneva: United Nations), United Nations publication, Sales No. E.99.II.D.9, 1999.

mechanisms, it has to guarantee a long-term stability in investment relations of the disputing parties. Majority of the dispute-settlement clauses are provided in the International Investment Agreements and these clauses are there to resolve cases that are complex and in which the parties cannot come to a mutual agreement easily. There must be a proper conduct to settle the disputes which involve serious investment disputes which must be fair, effective, amicable and in which no party takes undue advantage and be inflexible. The investment disputes arise between the state and a corporation or a private individual carrying out a commercial activity. The dispute-settlement mechanisms must be sensitive to the interests of both the disputing partiesm the disputing parties are not comparable and hence the demands of the private investor can neither be completely legitimate nor be completely disregarded. While drafting the International Investment Agreements there are two types of policy options available, namely:

1. No reference to investor-State dispute settlement in an agreement
2. Reference to investor-State dispute settlement in an agreement

If we go by the latter approach, another two options arise, namely:

1. Choice of venue
2. Choice of procedure and procedural rules

The countries that seek inward Foreign Direct Investments (FDI) have enhanced more as the infrastructure of the dispute-settlement mechanisms are developing. To increase and encourage the trust of the disputing parties in the mechanisms of dispute-settlement, their quality must be enhanced.[25] The countries must try as much as possible that no foreign investor faces a problem in their country, however, if a problem arises, the least However, the most important factor to stress is that investors and the countries in which they operate need to do their utmost to avoid disputes in the first place and, should a dispute arise, use the least hostile approach should be used to resolve the issue. To ensure fair and just settlement, the third party must preserve the choices and claims of both the disputing parties and to recognise their claims and interest. These are the objectives that the International Investment Agreements should pursue.

*****

[25] Asouzu, A.. *International Commercial Arbitration and African States* (Cambridge: Cambridge University Press), 2001.

 [ISSN 2581-5369]