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INVESTMENT DISPUTES- DEVELOPING ARBITRATION

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ABSTRACT

In recent times, the International Investment Treaties (IIT) network has improved an immense level of legal security in interactions between foreign investors and their host countries. However, the legal system still in place continues to remain underdeveloped and the remedy available is almost exclusively for rights-based arbitration and claims for financial compensation. Owing to the ever-changing nature of the economic, political, technological environment, and the intricate long-term relationship, it has been noted that this system needs the flexibility needed to regulate the same. In each and every significant rule governing the complicated relationship between investors and the host country, this flexibility is required to include the methods by which these rules have an effect in the event of a conflict. In this paper, we will discuss approaches to resolving investment disputes that respond to the need for flexibility and the constraints that these approaches face.

Keywords - *Investment Disputes, ADR, Alternate Dispute Settlement, Foreign Investors, Approaches to ADR, ADR underdeveloped, ADR Development.*

INTRODUCTION

In the recent decades, the network of international investment treaties (IIT) has refined an unprecedented standard of legal security in the relationships between foreign investors and their host states. However, the legal system that it runs by still remains rudimentary and the remedy that is available is almost exclusively for a rights-based arbitration and claims for financial compensation. Due to the ever-changing nature of the economic, political, technological environment and the complex long-term relations, it is observed that this system lacks the flexibility required to govern the same. This flexibility is required in each and every substantial rule governing the complicated relationship between investors and the host state to be including the methods by which these rules are given effects in cases of conflicts. In this paper, I will be

talking about approaches for resolving investment disputes that are responsive to the need for flexibility and the constraints which these approaches face.[1]

Even as arbitration let's a rights-based binding solution that is even necessary for investment disputes, appears desirable and indeed it has become necessary to look for systems beyond arbitration. Other mechanisms should be made available that provide greater flexibility than just a rights-based binding solution, also reconciling the conflicting objectives and interests. ADR in commercial arbitration is to be used as a useful reference in between foreign investors and host states, and thus it must be adjusted according to it.[2]

In this paper, we will be exploring the techniques that are already in practice: the potential they offer and the constraints that come with it. The paper will talk about ADR in commercial disputes and inter-state disputes. Further investment disputes will be observed as a specific category, certain features will be discussed, case analysis by the way of examples. Followed by an assessment of the scope for change in this area. In the end, we will be finally discussing the initiative that has been taken by the International Bar Association (IBA) in preparing Investor-State Mediation Rules will be examined.[3]

ADR IN COMMERCIAL DISPUTES

ADR is understood as a method of dispute resolution that leads us to a solution adopted voluntarily by the parties and it isn't imposed on them by an arbitrator, a judge, or any other authority. The simplest alternative is the parties themselves reaching a solution without the help of others, this is negotiating. These do not have a third person in between them. Third persons depending on the method adopted are seen as a facilitator, mediator, conciliator, neutral, or, in the case of some specialized manner an adjudicator, dispute board, or expert.[4]

[1] Michael E. Schneider, | 'Investment disputes- moving beyond arbitration'| Diplomatic and Judicial Means of Dispute Settlement|119
[2] Ibid
[3] ibid
[4] UNCTAD, Investor-State Disputes: Prevention and Alternatives to Arbitration (UNCTAD Series, 2010), at xii and 19: Goetz v. Burundi.

Neutral is the best way to describe 3rd parties that assist parties to reach settlement. The role of the neutral party may vary considerably, on one hand, they would find forms of assisted negotiations where the neutral simply assist them in primarily solving the dispute in the most efficient manner while also handling their emotions. On the other hand, we have neutrals that simply adjudicate the matter dispute boards or preliminary decision of the expert in any particular matter pertaining to that particular case, over here we can see that the neutral is trying to find a temporary solution at least until the parties sort themselves out.[5]

There exists a combination system of conciliation or mediation with arbitration. In some dispute resolution system, attempts at conciliation are prescribed before a party may commence judicial proceedings, however, the two phases of the proceedings are conducted in stages and before different persons[6]. In a more advanced form, the two forms of dispute settlement are combined before the same person. Such forms are used in Germany where the Code of Civil procedure expressly requires the judge to seek, at all stages of the court proceedings, to reconcile the parties[7]. Alternatively, these can also be found in Switzerland[8].

ADR IN INTERNATIONAL RELATIONS BETWEEN STATES

The international practice has developed a variety of approaches to promote such a peaceful settlement. Legal doctrine grouped them into diplomatic methods on the one hand and legal or judicial methods on the other. The latter includes proceedings before what is now the International Court of Justice, arbitration with a growing number of specialised international tribunals.

Diplomatic methods of dispute settlement are corresponding to ADR in commercial disputes. The traditional methods have been complemented by a variety of multilateral mechanisms. The United Nations, through the Security Council, the General Assembly and the Secretary-general play an

[5] ibid
[6] Michael E. SChnieder, "Combining Arbitration and Conciliation – Report at the Seoul Conference Arbitration', (1996) ICCA Congress, No. 8, at 57-99.
[7] The German Code of Civil Procedure (ZPO), Article 278 (1), provides: "Das Gericht soll in jeder Lage des Verfahrens auf eine gutiche Beilegung des Rechtsstreits oder einzelner Streitpunkte bedacht sein."
[8] Reflected in the provisions of 26 cantonal codes of civil procedure and can be now found in Article 124(3) of the new Federal Code of Civil Procedure.

important role in the prevention and settlement of international disputes; similar functions have been developed in the context of various regional or specialised organizations that provide for various forms of diplomatic despite the settlement.[9]

The traditional methods for dealing with investment disputes through diplomatic protection has given rise to resentment by host states. The avoidance of the causes for the resentment was precisely one of the principal objectives for the development of modern methods for the settlement of investment disputes through ICSID and bilateral investment protection treaties, but even this just promotes that resentment.

At this stage, 3 examples of diplomatic means of dispute settlement may be mentioned.

The first concerns an international mediation that has prefaced a mechanism for the resolution of a large number of claims of foreign investors against their host State. Following the Tehran hostage crisis, Algeria mediated the dispute between Iran and the United States, leading to the 1981 Algiers Declaration.[10]

Another type of settlement mechanism provides for compensation of the victims of international conflicts. The mechanism has been created in favour of workers deported during World War II, to distribute funds held on dormant "accounts, or for restoring property rights of the people expelled from their homes. A particularly remarkable institution in this respect was the United Nations Compensation Commission (UNCC) that adjudicated several million claims against Iraq following its invasion and occupancy of Kuwait and Security Council resolutions declaring Iraq's liability in principle.[11]

A very different example concerns international and domestic efforts to settle the civil conflicts in Tajikistan. In a recent article, Michael Forbes Smith describes that many years of efforts to reconcile conflicting factions in and around that country, bringing an end to the civil war after the state had become independent with the end of the Soviet Union. He seeks to compare the UN-

[9] Michael E. Schneider,|'Investment disputes- moving beyond arbitration'| Diplomatic and Judicial Means of Dispute Settlement|119

[10] Algiers Accords, ILM 20 (1981), at 224 et seq.

[11] Security Council Resolution 687 (1991), for this and other relevant texts see Boutros Boutros-Ghali, The UN and the Iraq-kuwait Conflict (1990-1996), Document N 39, 203, 205 (United Nations, 1996); and the UNCC website.

moderated peace process with classic mediation theory, as applied to the resolution of the civil and commercial disputes and to international political and military disputes.

We can perceive from these examples that the number of methods used in international disputes is various. The possibility of resolving different aspects of a complex dispute by different methods and institutions. The last example explains the complexity that is the normal standard here. Even though the investment disputes are not of a dimension as the civil war in Tajikistan, the diversity in the players and their interests, underlying antagonisms a disrupting development can create obstacles of equal difficulty.[12]

INVESTMENT DISPUTES AS A DISTINCT CATEGORY

As we must understand the role of ADR in investment disputes, it is important to understand the specificity of investment disputes while this shares many character tics with commercial and other disputes, there are some characteristics that are specific to investment disputes or that are more prominent there.

It is to be noted that international investment disputes have an ambiguous status that distinguishes them both from inter-State disputes and from purely commercial disputes, domestic or international; they concern a legal and factual situation centered in the host country and which in many respects is linked with its legal system. The term "investment"[13] , despite the differences in its definition it is implied some form of engagement of resources by a foreign entity in the host country.[14]

At the same time, investment disputes as they are considered here, contain elements of "internationalisation", by providing for jurisdiction of a non-national authority, invariably

[12] Michael E. Schneider,|'Investment disputes- moving beyond arbitration'| Diplomatic and Judicial Means of Dispute Settlement|119

[13] "investment" critical to the jurisdiction of institutions in particular ICSID, and its definition has given rise to legal writing.

[14] Michael E. Schneider,|'Investment disputes- moving beyond arbitration'| Diplomatic and Judicial Means of Dispute Settlement|119

international arbitration, normally at a seat abroad, and often also the application of a law other than that of the host State.

Traditionally these legal arrangements are often described as State Contracts. The nature of these contracts and of disputes arising under them have been subject to intense academic debates but have also occupied international for an including the United Nations and its specialised agencies.[15]

As part of this development, investment disputes have emerged as a new category in international arbitration. This new category increasingly can be distinguished from commercial arbitration.

Despite their diversity, these international instruments form a legal framework for a large part of international investment; a framework for investments not only in developing countries but as, some recent cases have shown, also in the most advanced industrial countries and this framework provides both substantial legal rules concerning the treatment of foreign investors and the basis for enforcing them in arbitration.

This is how investment disputes have emerged as a new category in international arbitration. It is easily distinguishable from commercial arbitration not only by reference to the parties involved but also by the institutions involved, the professionals work as council and arbitrator acts by the procedural rules. In my observation, more attention must be given to the question of whether arbitration as it is now practiced is the most suitable method of dispute resolution to respond to these challenges and the improvements that can be made by alternative methods.[16]

SPECIFIC FEATURES AND CHALLENGES OF INVESTMENT DISPUTES

- **The Subject Matter of the Dispute**

  Normally these disputes arise because of an alleged breach of contract. Further, these arise as the host government has failed to make contributions that were committed to making the investment project work. Such actions may concern a concession mining rights or for providing

[15] Michael Forbes Smith, "Similarities and Differences Between Commercial Mediation and Political Mediation.
[16] Michael E. Schneider, | 'Investment disputes- moving beyond arbitration'| Diplomatic and Judicial Means of Dispute Settlement|119

certain goods or services to the public, such as operating public transportation, utility supplies, telecommunications, news services, or other trivial things that eventually come to matter in such a dispute. The commitments of the host government often extend to areas of its legislative action, in particular in the field of taxation or any other government-run regulation that affects the investment.[17]

As the breach invoked by the investor doesn't need to be based on a violation of an investment agreement with the calming investor, the scope of such government action is much wider in treaty-based disputes. It may relate to legislative or regulatory actions and their implementation.

These actions of the state actors usually have a diversity of political acts. All the actions of the state are subject to the influence of political actors, legislative, executive and judiciary.

In such cases, disputes may involve interests and considerations quite unrelated to the investment itself because people often have different agendas. It also depends on the size and relative importance of the investment, the measures affecting the investor or the lack of its protection, may be the subject of great public attention and any action taken by the government may cause heated debates in the public arena.[18]

- **The State as a Party in Investment disputes**

We can't forget the fact that for a state there are too many interrelationships involved and too many unpredictable entities. Different organisations are in control of different political entities with different agendas.

From a legal point of view at the international level, and in matters of responsibility the state appears as a single entity. In reality, too many different entities are involved. They may be independent of each other or have different legal personality. They may have different objectives and priorities and may also act in different manners; they would also differ on what acceptable things are. Clarifying all these different entities that have different positions may

[17] ibid
[18] ibid

be a difficult task. Reaching a joint solution is all more difficult if it requires the modifications of previously defended positions, making concessions to the opponent in the dispute.[19]

It is therefore not surprising that observers have highlighted the difficulties "for government officials to engage in a process that may result in a recommended settlement that falls obviously short of the rhetorical positions that they have expounded in parliament and in public"[20]. Or as explained by Michael Reisman

"*…in States in which there are active political oppositions waiting for an opportunity to pounce on the incumbents for having 'betrayed' the national patrimony by settling with an investor, modalities other than transparent third-party decisions can undermine or even bring down governments and destroy personal careers…*"[21]

- **The Position of the Investor**

We have to realise the reality for commercial parties, that is any dispute is treated as a disturbance to their ordinary activity. Not only is its wasteful funding of legal costs but also, any dispute absorbs valuable resources and time that could have been used elsewhere. Also, any dispute with a business partner may render useful cooperation and transaction more difficult if not impossible.

However this may not be the same for all investors, for some individual projects may be a part of a larger strategy, in the interest of that strategy or in the interest of good relations with the government in question, a settlement may be more attractive than the payment of damages at the end of several years of a court or arbitration proceedings.[22]

[19] ibid
[20] Stephen Schwebel, "Is Mediation of Foreign Investment Disputes Plausible?", 22(2) (2007) ICSID Review 241.
[21] Michael Reisman, "International Investment and ADR: Married but Best Living Apart" in UNCTAD, Investor-State Disputes Prevention and Alternatives to Arbitration II (2011)
[22] ibid

Investors may also have no other remaining interest in the investment but to recover as much compensation as possible. When considering the possibilities of settlement, one must bear in mind that formal dispute resolution proceedings in arbitration or in the courts may have objectives beyond the specific dispute that they concern. Such proceedings may be pursued by the investor for other reasons, for instance with the objective of obtaining concessions in other areas. It may also be that investors would involve third parties like insurance companies that would be willing to cover the investment amount they have made but require an ongoing claim for compensation to be pursued.

These and other factors play a role on the side of the investor when it comes to determining the disposition towards a settlement and designing procedures intended to bring it about.[23]

- **Past Experiences with ADR in Investment disputes.**

The more general considerations in the preceding section of this chapter can usefully be illustrated by a number of concrete examples from international investment disputes.

- **The International Centre of Settlement of Investment Disputes experience.**

The quasi failure of the ICSID conciliation procedure contrast with another observation: many ICSID cases, like many other disputes, brought to arbitration, settle before an award is rendered. In the experience of ICSID the rate of settlement after the commencement of the arbitration is in the order of 40%. ICSID stats for all cases up to the end of 2011 indicate that 39% of the disputes brought under the Convention and the Additional Facility Rules were "Settled or proceedings otherwise discontinued".[24]

What explains this apparent contradiction – the reluctance of the parties to resort to conciliation and their willingness to settle once the arbitration has commenced? Why the need for commencing the expensive and time-consuming process of arbitration if, in the end, it is not

[23] ibid

[24] The ICSID Caseload Statistics, Issue 1, ICSID publication 2012, at 13.

the arbitration award that resolves the dispute but a voluntary settlement? And if arbitration is necessary to commence the process, what can be done to improve the approach.[25]

- **Difficulties to Settle or Even Negotiate Fairly**

An example of the difficulties faced by a public administration when it must make a decision that implies concessions to the investor is the case of the Republic of Georgia and kardassopoulos and Fuchs. Over here the investors fought for several years but could gain nothing from the government, government officials simply refused to make any sort of settlement, this changed when a new government came in and the investors put a word with the US Secretary of State to gain a favour but even that didn't work out as the claimants were denied any compensation and had to resort to arbitration.[26]

- **Providing justification for a Change in Position**

Judge Schwebel reported on his experience in a case in which he acted as a mediator; both parties "came to the mediation with inflexible demands upon the other. Neither party evidenced a willingness to modify those demands". The Mediation failed shortly after having started. The dispute moved on to arbitration and when the proceedings had advanced and the award became imminent, the party settled. Judge Schwebel had no information about why the sensible solution had not been reached earlier, but he offered as a possible explanation that "the exchange of written pleadings was salutary in demonstrating to the parties that the position of each side had their infirmities".[27]

[25] ibid
[26] Ron Fuchs v. The Republic of Geeorgia, ICSID Case No. ARB/07/15, Award, 3 March 2010, at $$ 443-448.
[27] Schwebel, "Is Mediation of Foreign Investment Disputes Plausible?', at 238.

CONCLUSION: WHAT SHOULD WE DO?

In the circumstances described, one may well reach the conclusion that there is not much that can or should be done: those disputes that can be settled amicably are settled. Since, despite all obstacles, the number of the disputes that are settled, before or during arbitration, seem to be high one may wonder if additional efforts are justified.

Moreover, from the little that is known about those cases where the disputes are settled, it appears that such settlements are brought about indirect negotiations between the parties without the intervention of mediators and other ADR neutrals. However, the number of cases that do proceed through arbitration to the bitter end seems to be higher than those that are settled during the course of the arbitration.

Thus for me to conclude certain points that I personally think would be appropriate for making sure parties settle are, create or strengthening the willingness to settle, improving the methods for reaching a settlement, in particular by enlarging the participants and lastly consider the choice of the persons and institutions assisting in the search for a settlement.[28]

[28] ibid