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INVESTOR-STATE DISPUTE SETTLEMENT: REVIEW OF DEVELOPMENTS IN 2014

Highlights

- Investors continue to use the investor–State dispute settlement (ISDS) mechanism. In 2014, claimants initiated 42 known treaty-based ISDS cases. The total number of known ISDS cases reached 608.
- 40 per cent of new cases were initiated against developed countries (the historical average is 28 per cent). A quarter of all new disputes are intra-EU cases.
- The two types of State conduct most commonly challenged by investors in 2014 were cancellations or alleged violations of contracts and revocations or denials of licences. The sectors where most cases were filed in 2014 are the generation and supply of electric energy (at least eleven cases), followed by oil, gas and mining (ten), construction (five) and financial services (three).
- The Energy Charter Treaty (ECT) surpassed the North American Free Trade Agreement (NAFTA) as the most frequently invoked IIA.
- ISDS tribunals rendered at least 43 decisions in 2014, 34 of which are public. The overall number of concluded cases has reached 356, with 37 per cent decided in favour of the State, 25 per cent in favour of the investor and 28 per cent of cases settled.
- Arbitral decisions adopted in 2014 touch upon a number of important legal issues concerning the scope of treaty coverage, the conditions for bringing ISDS claims, the meaning of substantive treaty protections, the calculation of compensation and others. On a number of issues, tribunals continue to arrive at divergent conclusions.
- The IIA regime is going through a period of reflection, review and revision. Investment dispute settlement is at the heart of this debate, with a number of countries reassessing their positions. There is a strong case for a systematic reform of ISDS.
- UNCTAD's forthcoming *World Investment Report 2015* will present an action menu for investment regime reform.

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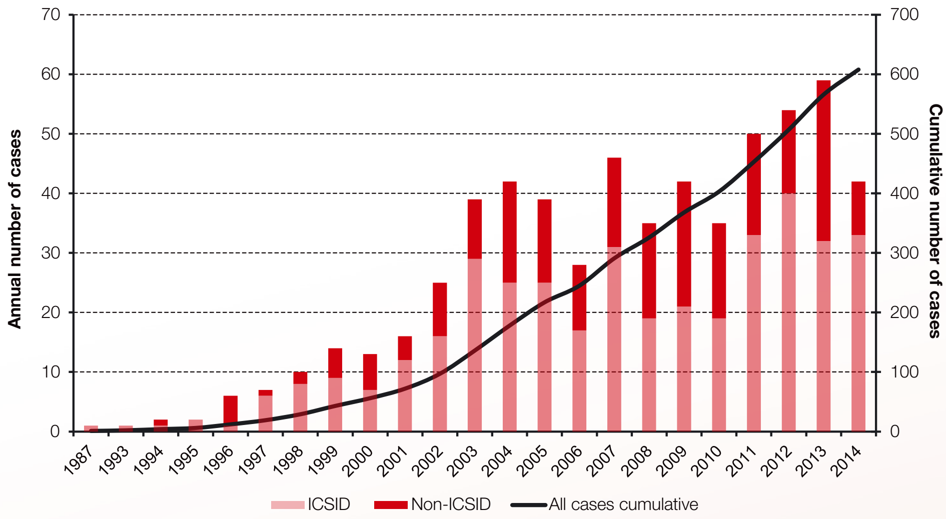
I. Statistical update (as of end 2014)[1]

In 2014, investors initiated 42 known ISDS cases pursuant to international investment agreements (IIAs) (annex 1).[2] This is lower than the record high numbers of new claims in 2013 (59 cases) and 2012 (54 cases) and closer to the annual averages observed in the period between 2003 and 2010.[3] As most IIAs allow for fully confidential arbitration, the actual number of cases is likely to be higher.

Last year's developments brought the overall number of known ISDS claims to 608 (figure 1). Ninety nine governments around the world have been respondents to one or more known ISDS claims (annex 2).

Figure 1. Known ISDS cases, annual and cumulative (1987–2014)



Source: UNCTAD, ISDS database

Respondent States. The relative share of cases against developed countries is on the rise. In 2014, 60 per cent of all cases were brought against developing and transition economies, and the remaining 40 per cent against developed countries. The share of cases against developed countries was 47 per cent in 2013, and 34 per cent in 2012, while the historical average is 28 per cent. In total, 32 countries faced new claims last year. The most frequent respondent in 2014 was Spain (five cases),[4] followed by Costa Rica, the Czech Republic, India, Romania, Ukraine and the Bolivarian Republic of Venezuela (two cases each). Three countries – Italy, Mozambique and Sudan – faced their first (known) ISDS claims in history. The most frequent respondent States are presented in figure 2.

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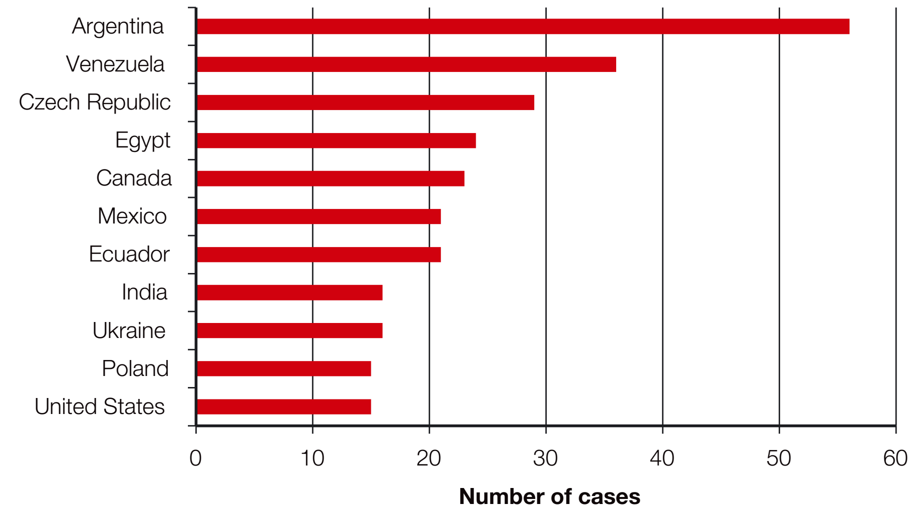
1 Information about 2014 claims has been compiled on the basis of public sources, including specialized reporting services such as *Global Arbitration Review* and *Investment Arbitration Reporter*. We are grateful for additional information received from the ICSID Secretariat and the Energy Charter Treaty Secretariat.

2 This Note does not cover cases that are exclusively based on investment contracts (State contracts) or national investment laws, nor cases where a party has so far only signalled its intention to submit a claim to ISDS, but has not yet commenced the arbitration.

3 Annual and cumulative case numbers are being continuously adjusted as a result of verification and may not exactly match the case numbers reported in the previous years.

4 All five new claims against Spain arise from the same measures that prompted the six claims against the country in 2013. Claimants maintain that the seven per cent tax on the revenues of power generators and a reduction of subsidies for renewable energy producers – introduced by Spain in 2012 to counter the budget deficit – wipe out expected profits from their investments in photovoltaic, solar thermal and wind plants.

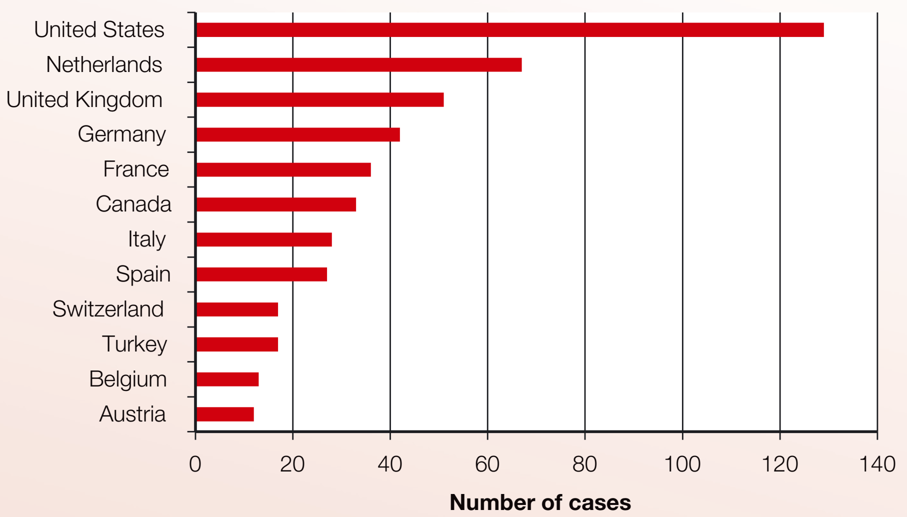
Figure 2. Most frequent respondent States (total as of end of 2014)



Source: UNCTAD, ISDS database

- *Home country of investor.* Of the 42 known new cases, 35 were brought by investors from developed countries and five were brought by investors from developing countries. In two cases the nationality of the claimants is unknown. The most frequent home States in 2014 were the Netherlands (seven cases by Dutch investors), followed by the United Kingdom and the United States (five each), France (four), Canada (three) and Belgium, Cyprus and Spain (two each). This corresponds to the historical trend where developed-country investors – in particular, those from the United States, Canada and several European Union (EU) countries – have been the main users of the system responsible for over 80 per cent of all ISDS claims (figure 3).

Figure 3. Most frequent home States (total as of end 2014)



Source: UNCTAD, ISDS database

- *Intra-EU disputes.* A quarter of all known new disputes (eleven) are intra-EU cases, which is lower than the year before (in 2013, 42 per cent of all new claims were intra-EU). Half of them were brought pursuant to the Energy Charter Treaty (ECT), and the rest on the basis of intra-EU BITs. The year's developments brought the overall number of intra-EU investment arbitrations to 99, i.e. approximately 16 per cent of all cases globally.[5]

[5] When calculating intra-EU disputes, the time factor (when a particular State joined the EU) has been disregarded; all disputes between States *currently* members of the EU are counted as intra-EU disputes.

- *Arbitral forums/rules.* Of the 42 new known disputes, 33 were filed with the International Centre for Settlement of Investment Disputes (ICSID) (of which three cases were under the ICSID Additional Facility Rules), six under the arbitration rules of UNCITRAL,[6] two under the Stockholm Chamber of Commerce (SCC) and one under the International Chamber of Commerce (ICC) arbitration rules. These numbers are roughly in line with overall historical statistics.
- *Applicable investment treaties.* The majority of new cases (30) were brought under BITs. Ten cases were filed pursuant to the provisions of the ECT (twice in conjunction with a BIT), two cases under the Central America-Dominican Republic-United States Free Trade Agreement (CAFTA), one case under the NAFTA and one case under the Canada-Peru FTA. Looking at the full historical statistics, the ECT has now surpassed the NAFTA as the most frequently invoked IIA (60 and 53 cases respectively). Among BITs, the Argentina-United States BIT remains the most frequently used agreement (20 disputes).
- *Economic sectors involved.* About 61 per cent of cases filed in 2014 relate to the services sector. Primary industries account for 28 per cent of new cases while the remaining eleven per cent arose out of investments in manufacturing. Looking at the industries in which investments were made, the most numerous was generation and supply of electric energy (at least eleven cases), followed by oil, gas and mining (ten), construction (five) and financial services (three).
- *Measures challenged.* The two types of State conduct most frequently challenged by investors in 2014 were (i) cancellations or alleged violations of contracts or concessions (at least nine cases); and (ii) revocations or denial of licenses or permits (at least six cases). Other challenged measures include: legislative reforms in the renewable energy sector, alleged discrimination of foreign investors vis-à-vis domestic ones, alleged direct expropriations of investments, alleged failure on the part of the host State to enforce its own legislation, alleged failure to protect investments, as well as measures related to taxation, regulation of exports, bankruptcy proceedings and water tariff regulation. Information about a number of cases is lacking. Some of the new cases concern public policies, including environmental issues, anti-money laundering and taxation.
- *Amounts claimed.* Information regarding the amount sought by investors is scant. For cases where this information has been reported, the amount claimed ranges from USD 8 million[7] to about USD 2.5 billion.[8]

II. ISDS outcomes in 2014

In 2014, ISDS tribunals rendered at least 43 decisions in investor-State disputes, 34 of which are in the public domain (at the time of writing) (annex 3).[9] Of the 34 public decisions, eleven principally addressed jurisdictional issues, with six decisions upholding the tribunal's jurisdiction (at least in part) and five decisions rejecting jurisdiction.[10] Fifteen decisions on the merits were rendered in 2014, with ten accepting – at least in part – the claims of the investors, and five dismissing all of the claims. The remaining

[6] All of the UNCITRAL cases were filed pursuant to IIAs concluded prior to 2014 and, therefore, the new UNCITRAL Transparency Rules do not apply to any of them, unless the disputing parties agree to their application in their specific dispute.
[7] *Anglia Auto Accessories, Ivan Peter Busta and Jan Peter Busta v. Czech Republic* (SCC).
[8] *Cem Uzan v. Republic of Turkey* (SCC).
[9] There may have been other decisions in 2014 whose existence is not known due to the confidentiality of the dispute concerned.
[10] These exclude those decisions that upheld the tribunal's jurisdiction and considered at the same time the merits of the dispute.

eight public decisions were rendered on applications for annulment and on preliminary objections.

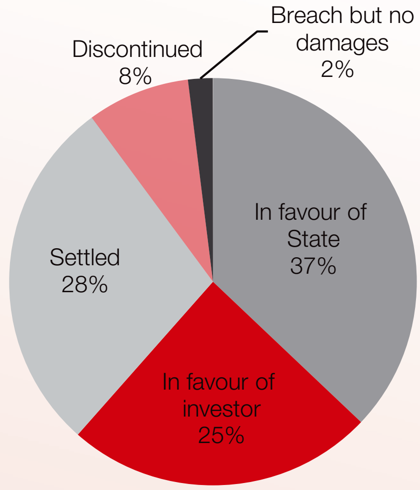
Of the ten decisions finding States liable, six found a violation of the FET provision and seven a violation of the expropriation provision. At least eight decisions rendered in 2014 awarded compensation to the investor, including a combined award of approximately USD 50 billion in three closely related cases, the highest known award by far in the history of investment arbitration.[11]

Five decisions on application for annulment were issued in 2014 by ICSID *ad hoc* committees, all of them rejecting the application for annulment.[12]

Ten cases were reportedly settled in 2014, and another five proceedings discontinued for unknown reasons.

By the end of 2014, the overall number of concluded cases reached 356.[13] Out of these, approximately 37 per cent (132 cases) were decided in favour of the State (all claims dismissed either on jurisdictional grounds or on the merits), and 25 per cent (87 cases) ended in favour of the investor (monetary compensation awarded). Approximately 28 per cent of cases (101) were settled[14] and eight per cent of claims (29) were discontinued for reasons other than settlement (or for unknown reasons). In the remaining two per cent (seven cases) a treaty breach was found but no monetary compensation was awarded to the investor (figure 4).

Figure 4. Results of concluded cases (total as of end 2014)



Source: UNCTAD, ISDS database

[11] The aggregate amount of compensation obtained by the three claimants constituting the majority shareholders of former Yukos Oil Company in the ISDS proceedings against the Russian Federation. See *Hulley Enterprises Limited (Cyprus) v. The Russian Federation*, UNCITRAL, PCA Case No. AA 226, Award, 18 July 2014; *Yukos Universal Limited (Isle of Man) v. The Russian Federation*, UNCITRAL, PCA Case No. AA 227, Award, 18 July 2014; *Veteran Petroleum Limited (Cyprus) v. The Russian Federation*, UNCITRAL, PCA Case No. AA 228, Award, 18 July 2014.

[12] Three out of the five applications for annulment had been filed by the respondent States, and the remaining two by the claimant investors.

[13] As a result of the on-going verification of UNCTAD's ISDS database, a number of proceedings previously thought to be pending or those whose outcome was unknown have been confirmed as concluded.

[14] In settled cases, the specific terms of settlement often remain confidential.

III. 2014 Decisions – An Overview[15]

A. Jurisdictional and admissibility issues

Definition of "investment" for purposes of establishing the scope of application of and jurisdiction under an investment treaty

The tribunal in *Nova Scotia Power v. Venezuela* stated that, in examining whether or not an investment is present, the definition of "investment" in the applicable BIT cannot be considered self-sufficient.[16] In line with recent decisions, such as *Romak*,[17] the *Nova Scotia* tribunal pointed to contribution, duration and risk as "*the triad representing the minimum requirement for an investment*".[18] The *Nova Scotia* tribunal concluded that the claimant's activity was "*essentially […] a sale and purchase of coal, even if it was more complicated in genesis and composition*".[19] Accordingly, the tribunal upheld the respondent's jurisdictional objection that the dispute does not arise out of an "investment".[20]

In an *obiter dictum*, the tribunal in *Nova Scotia* agreed with an approach followed in other recent cases with regard to the question of when intangible assets constitute investment made "in the territory" of a host State.[21] The tribunal explained that the test is "*whether the host State received a benefit*".[22] The *Nova Scotia* tribunal recognized that economic development might indicate a benefit to the host State; however, the tribunal went on to cautioned that the benefit "*does not necessarily have to be economic development, [as this is] a highly subjective element*" that can only be assessed in hindsight.[23] Instead, "*it is the alleged investment at the time of its inception that should be considered, not the impact that the investment has ultimately had.*"[24]

The ratione personae jurisdiction under Article 25(2)(b) of the ICSID Convention

In *National Gas v. Egypt*, the tribunal noted that the parties to an IIA can agree to treat companies established in one State as nationals of another State if the latter own or control such companies, which is indeed what the

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15 The Issues Note aims to highlight key findings stemming from all of the (publicly available) decisions that investment treaty tribunals rendered in 2014 (as well as decisions issued in previous years but made public during 2014). However, it is not a comprehensive review; attention is primarily given to capturing those aspects that represent novel developments or otherwise have systemic value. The texts of the relevant arbitral awards can be found at www.italaw.com.

16 *Nova Scotia Power Incorporated v. Bolivian Republic of Venezuela* (ICSID Case No. ARB(AF)/11/1), Award (excerpts), 30 April 2014, para. 77.

17 *Romak S.A. (Switzerland) v. The Republic of Uzbekistan* (UNCITRAL, PCA Case No. AA280), Award, 26 November 2009, para. 207.

18 *Nova Scotia Power Incorporated v. Bolivian Republic of Venezuela* (ICSID Case No. ARB(AF)/11/1), Award (excerpts), 30 April 2014, para. 84.

19 *Ibid.*, para. 113.

20 *Ibid*.

21 See *Abaclat and Others v. Argentine Republic* (ICSID Case No. ARB/07/5) *(formerly Giovanna a Beccara and Others v. Argentine Republic)*, Decision on Jurisdiction and Admissibility, 4 August 2011, para. 374 ("*[T]he relevant question is where the invested funds [were] ultimately made available to the Host State and did they support the latter's economic development.")*; see also *Inmaris Perestroika Sailing Maritime Services GMBH and Others v. Ukraine (ICSID Case No. ARB/08/8), Decision on Jurisdiction, 8 March 2010, para. 124 ("[A]n investment may be made in the territory of a host State without a direct transfer of funds there, particularly if the transaction accrues to the benefit of the State itself.*").

22 *Nova Scotia Power Incorporated v. Bolivarian Republic of Venezuela* (ICSID Case No. ARB(AF)/11/1), Award (excerpts), 30 April 2014, para. 130, citing *Deutsche Bank AG v. Democratic Socialist Republic of Sri Lanka* (ICSID Case No. ARB/09/02), Award, 31 October 2012, para. 295 *("[T]he existence of an investment must be assessed at its inception and not with hindsight.").*

23 *Ibid.*, para. 130.

24 *Ibid.*

parties to the Egypt-United Arab Emirates BIT had agreed.[25] In the case at hand, the tribunal concluded that although National Gas, a company registered in Egypt, was owned by UAE companies, the factual evidence showed unequivocally that it was ultimately controlled by Mr. Reda Ginena, an Egyptian national. The tribunal concluded, therefore, that the "foreign control" requirement in Article 25(2)(b) of the ICSID Convention was not met.[26]

The "futility exception" to the local litigation requirement

Following the approach taken by the tribunal in *Ambiente Ufficio v. Argentina*,[27] the tribunal in *Giovanni Alemanni v. Argentina* confirmed the existence of a "futility exception" to the applicable treaty's requirement to have recourse to local courts for a certain minimum length of time. While it noted that the legal effect of the host State's offer to arbitrate "*can* only *be produced if the investor accepts the offer on the terms specified by the host State*" including the 18-month domestic court requirement),[28] the *Alemanni* tribunal found that that requirement "*shows unambiguously […] that the Contracting States had in view as the intervening step a process that would be potentially effective to settle the issue in dispute*."[29] The *Alemanni* tribunal determined that in the circumstances it was shown that Argentina's judicial system was not "*reasonably capable of providing effective relief*" and therefore the claimants' failure to comply with the BIT's preconditions to arbitration "*does not act as a jurisdictional bar to their commencing ICSID arbitration*".[30]

Jurisdiction over claims brought by dual nationals

In *García Armas v. Venezuela*, the tribunal upheld jurisdiction over a dispute brought against Venezuela by two Spanish nationals who also held Venezuelan nationality.[31] The tribunal based its reasoning on several grounds. First, it pointed out that some Venezuelan IIAs explicitly excluded dual nationals from protection whereas others – including the BIT applicable to the dispute – did not.[32] Second, it noted that the exclusion of dual nationals in Article 25(2) of the ICSID Convention did not apply to the proceedings at hand as they were brought under the UNCITRAL arbitration rules.[33] Finally, it relied on Article 31 of the Vienna Convention

[25] Article 10(4) of the Egypt-United Arab Emirates BIT provides: *"In case of the existence of a juridical person that has been registered or established in accordance with the law in force in a region [territory] following a Contracting State, and an investor from the other Contracting State owns the majority of the shares of that juridical person before the dispute arises, then such a juridical person shall, for the purposes of the Convention, be treated as an investor of the other Contracting State, in accordance with Article 25(2)(B) of the Convention."*

[26] *National Gas S.A.E. v. Arab Republic of Egypt* (ICSID Case No. ARB/11/17), Award, 3 April 2014, paras. 122-149. This decision is in line with the award in *TSA Spectrum de Argentina S.A. v. Argentine Republic* (ICSID Case No. ARB/05/5), 19 December 2008. For a contrasting approach, see *Rumeli Telekom A.S. and Telsim Mobil Telekomunikasyon Hizmetleri A.S. v. Republic of Kazakhstan* (ICSID Case No. ARB/05/16), Award, 29 July 2008; *The Rompetrol Group N.V. v. Romania* (ICSID Case No. ARB/06/3), Decision on Jurisdiction and Admissibility, 18 April 2008; and *Aguas del Tunari, S.A. v. Republic of Bolivia* (ICSID Case No. ARB/02/3), Decision on Jurisdiction, 21 October 2005.

[27] *Ambiente Ufficio S.p.A. and Others v. Argentine Republic* (ICSID Case No. ARB/08/09), Decision on Jurisdiction and Admissibility, 8 February 2013.

[28] *Giovanni Alemanni v. Argentine Republic, Decision on Jurisdiction and Admissibility, 17 November 2014, para. 305.*

[29] *Ibid.*, para. 311.

[30] *Ibid.*, paras. 316-317.

[31] One claimant was born in Spain and later acquired Venezuelan nationality; the other was born in Venezuela and later acquired Spanish nationality.

[32] *Serafín García Armas and Karina García Gruber v. The Bolivarian Republic of Venezuela* (UNCITRAL), Decision on Jurisdiction, 15 December 2014, para. 180.

[33] *Ibid*., paras. 193-196.

on the Law of Treaties and previous decisions of investment tribunals[34] to conclude that if the treaty did not impose any express limitation on dual nationals, it was "*not possible to devoid of effect the nationality granted freely by a State and accepted as valid by the other*".[35] The tribunal refused to apply the test of "dominant and effective nationality" as it considered it to be part of the law of diplomatic protection and not applicable in the context of investment treaties.[36]

Admission requirement

In *Churchill Mining v. Indonesia*, the tribunal determined that the requirement in Article 2(1) of the Indonesia-UK BIT, which limited the application of the BIT to investments that "*have been granted admission [is] a one-time occurrence, a gateway through [sic] all British investors must pass once*".[37] It thus rejected the respondent's argument that the requirement extends throughout the entire duration of the investment operation. Indonesia had argued that a "*foreign investor violates the admission requirement when engaging in activities that are not covered by the terms of the [original] approval.*"[38] Indonesia alleged that Churchill Mining engaged in actual mining activities, which were not included within the scope of the original approval of mining "services".[39] But the tribunal rejected this argument and agreed with the claimant that the admission requirement embodied in Article 2(1) of the BIT "*applies at the time of entry into the country and not during the entire operation of the project [and] is narrower than a traditional legality requirement in the sense that it only demands admission in accordance with the relevant domestic laws and not general compliance with the host State's legislation*".[40]

Jurisdictional objection based on allegations of fraud, illegal or bad faith conduct related to the investment

In *Minnotte and Lewis v. Poland*, the tribunal noted that, although the Poland-US BIT does not explicitly require the investment to be made in accordance with the host State's law, "*it is now generally accepted that investments made on the basis of fraudulent conduct cannot benefit from BIT protection; and this is a principle that is independent of the effect of any express requirement in a BIT that the investment be made in accordance with the host State's law*".[41] The tribunal however added that it is only the case "*where fraud is so manifest, and so closely connected to facts (such as the making of an investment) which form the basis of a tribunal's jurisdiction as to warrant a dismissal of claims […] for want of jurisdiction.*"[42] The tribunal ultimately dismissed the jurisdictional objection as the circumstances in which the investment at issue was made were "*far from displaying such manifest fraud or other defects*".[43]