

KLUWER LAW INTERNATIONAL

# **Law and Practice of Investment Treaties**

**Standards of Treatment**

By

**Andrew Newcombe**

**Lluís Paradell**



**Wolters Kluwer**

Law & Business

AUSTIN

BOSTON

CHICAGO

NEW YORK

THE NETHERLANDS

*Published by:*

Kluwer Law International  
PO Box 316  
2400 AH Alphen aan den Rijn  
The Netherlands  
Website: [www.kluwerlaw.com](http://www.kluwerlaw.com)

*Sold and distributed in North, Central and South America by:*

Aspen Publishers, Inc.  
7201 McKinney Circle  
Frederick, MD 21704  
United States of America  
Email: [customer.care@aspenpubl.com](mailto:customer.care@aspenpubl.com)

*Sold and distributed in all other countries by:*

Turpin Distribution Services Ltd.  
Stratton Business Park  
Pegasus Drive, Biggleswade  
Bedfordshire SG18 8TQ  
United Kingdom  
Email: [kluwerlaw@turpin-distribution.com](mailto:kluwerlaw@turpin-distribution.com)

*Printed on acid-free paper.*

ISBN 978-90-411-2351-0

© 2009 Kluwer Law International BV, The Netherlands

All rights reserved. No part of this publication may be reproduced, stored in a retrieval system, or transmitted in any form or by any means, electronic, mechanical, photocopying, recording, or otherwise, without written permission from the publisher.

Permission to use this content must be obtained from the copyright owner. Please apply to: Permissions Department, Wolters Kluwer Legal, 76 Ninth Avenue, 7th Floor, New York, NY 10011-5201, United States America. Email: [permissions@kluwerlaw.com](mailto:permissions@kluwerlaw.com).

Printed in Great Britain.

## Authors' Preface

There have been significant developments in investment treaty law and practice over the past twenty years. Since 1990, the date of the first investor-state arbitral award under a modern investment treaty, the growth in the number of investment treaties and treaty disputes has been exponential. This book, drawing on the authors' academic and professional expertise, examines the origins and evolution of investment treaty law and practice, the law applicable to investment treaty disputes, and substantive investment law issues: standards of treatment and exceptions and defences to treaty obligations. Our aim is to provide a systematic, comprehensive and detailed statement of the law, along with applicable principles and policies, and to analyze critically investment treaty jurisprudence in the subject areas covered by the book.

The book is the product of extensive collaboration between the co-authors. Primary research and writing responsibilities were allocated as follows: Chapters 1, 3-8 and 10, Newcombe; and Chapters 2, 9 and 10, Paradell.

Andrew Newcombe  
*Victoria, Canada*

Lluís Paradell  
*Rome*

July 2008

## Acknowledgements

We have benefited greatly from discussions over the past ten years with numerous international law scholars, practitioners and arbitrators, and from their writings and presentations. We thank our colleagues (past and present) at Freshfields Bruckhaus Deringer for their support and contributions to this project. In particular, we thank Jan Paulsson for acting as a mentor to both of us and providing extensive comments on the draft manuscript. We have also received invaluable comments on specific chapters from a number of academics and practitioners: José Alvarez, Andrea Bjorklund, James Crawford, Meg Kinnear, Jürgen Kurtz, Vaughan Lowe, Mark Milford, Martin Paparinskis, Georgios Petrochilos, Michael Reisman, Judge Stephen Schwebel and Todd Weiler. We thank each of them for their time and effort in reviewing draft chapters. The book has been immeasurably improved by their comments. Any errors or omissions remain the sole responsibility of the authors.

Devashish Krishan has been an invaluable resource and has greatly assisted at various stages of the project. We thank him for his significant contributions. We have also benefited from online discussions on the OGEMID e-mail forum. We thank OGEMID participants for sharing their views and insights on investment treaty law.

We also thank our editors at Kluwer, beginning with Gwen de Vries and Bas Knipphorst, who originally supported the project, and more recently, Eleanor Taylor who has worked closely with us to bring the book to publication. Thanks also go to Vincent Verschoor and the production team at Kluwer for taking the project from manuscript to book.

Andrew Newcombe expresses his gratitude for the support he has received from the Faculty of Law, University of Victoria, and its faculty members and staff. Dean Andrew Petter and Associate Dean Cheryl Crane supported the project in a multitude of ways over the past five years. Faculty colleagues, Professors Ted McDorman, Benjamin Berger and Gillian Calder, provided invaluable comments

on draft chapters. Professor Jeremy Webber provided wise counsel on academic publishing and much appreciated moral support. Special thanks are due to those in the Law Library – Law Librarian Neil Campbell, Associate Law Librarian Caron Rollins and staff members, including Irene Godfrey, Damaris Simair, Lynne Curry, Carol Shaw, Glenda Lee Jury and Rich McCue – for providing access to a vast array of print and electronic resources consulted while researching for the book. Thanks are also due to Rosemary Garton, who provided secretarial services throughout.

Lluís Paradell wants to thank especially Nigel Blackaby for his support and the extensive exchanges during the preparation of memorials and hearings (and early morning jogging!), which have greatly enriched the book, Lucy Reed for the first opportunity to plead at a hearing and her continued professional guidance, and Robert Volterra for having first introduced him to the subject.

Over the past five years a series of bright and talented University of Victoria law students have assisted with research and editing. Their assistance was invaluable to the success of this project and each of them made a significant contribution. We thank Jennifer Bond, Philippa Estall, Claire Farmer, Anna Johnston, Adam Kay, Sean McGinty, Micah Rankin, Karen Penate and Ania Zbyszewska.

Funding support for Andrew Newcombe's research of this book has come from various sources, including the University of Victoria, Borden Ladner Gervais, LLP, through its Summer Fellowship Program, Miller Thomson LLP, and the Foundation for Legal Research. Their financial support is gratefully acknowledged.

Finally, our greatest thanks are due to our families. We are grateful for their support and encouragement while we have worked on this project over the past five years.

# List of Abbreviations

## GENERAL

ACP	African, Caribbean and Pacific Group of States
ASEAN	Association of South East Asian Nations
BIT	Bilateral Investment Treaty
BLEU	Belgo-Luxembourg Economic Union
CAFTA-DR	Central America-Dominican Republic-United States Free Trade Agreement
DCF	Discounted Cash Flow
DSB	Dispute Settlement Body
EC	European Community
ECJ	European Court of Justice
ECT	Energy Charter Treaty
EU	European Union
FDI	Foreign Direct Investment
FCN	Treaty of Friendship, Commerce and Navigation
FIPA	Foreign Investment and Protection Agreement
FIRA	Foreign Investment Review Act
FTA	Free Trade Agreement
FTC	Free Trade Commission (NAFTA)
GATS	General Agreement on Trade in Services
GATT	General Agreement on Tariffs and Trade
ICC	International Chamber of Commerce
ICCA	International Council for Commercial Arbitration
ICJ	International Court of Justice
ICSID	International Centre for Settlement of Investment Disputes

ICSID Convention	Convention on the Settlement of Investment Disputes between States and Nationals of Other States 1965
IGO	Intergovernmental Organization
IIA	International Investment Agreement
ILA	International Law Association
ILC	International Law Commission
IPPA	Investment Promotion and Protection Agreement
JSEPA	Japan-Singapore Economic Partnership Agreement
LCIA	London Court of International Arbitration
MAI	Draft Multilateral Agreement on Investment
MERCOSUR	Mercado Común del Sur (Common Market of the South)
MFN	Most-Favoured-Nation
NAFTA	North American Free Trade Agreement
OECD	Organisation for Economic Co-operation and Development
PCIJ	Permanent Court of International Justice
SCC	Stockholm Chamber of Commerce
SLA	Softwood Lumber Agreement
SPS Agreement	Agreement on the Application of Sanitary and Phytosanitary Measures
TBT Agreement	Agreement on Technical Barriers to Trade
TRIMS Agreement	Agreement on Trade-Related Investment Measures
TRIPS Agreement	Agreement on Trade-Related Aspects of Intellectual Property Rights
UAE	United Arab Emirates
UN	United Nations
UNCITRAL	United Nations Commission on International Trade Law
UNCTC	United Nations Centre on Transnational Corporations
UNCTAD	United Nations Conference on Trade and Development
UNGA Res	United Nations General Assembly Resolution
UK	United Kingdom
US	United States
USD	United States Dollars
USSR	Union of Soviet Socialist Republics
Vienna Convention	Vienna Convention on the Law of Treaties 1969
WTO	World Trade Organization
WWI	World War I
WWII	World War II

## JOURNALS, REPORTS AND TREATY SERIES

ABAJ	American Bar Association Journal
AULR	American University Law Review
AUILR	American University International Law Review
AIAJ	Asian International Arbitration Journal
AJIL	American Journal of International Law
AJIL Spec Supp	American Journal of International Law Special Supplement
AJCL	American Journal of Comparative Law
AI	Arbitration International
ARIA	American Review of International Arbitration
ASIL Proc	American Society of International Law Proceedings
AYIL	Asian Yearbook of International Law
BCICLR	Boston College International and Comparative Law Review
BLI	Business Law International
BYIL	British Yearbook of International Law
Can-USLJ	Canada-United States Law Journal
CBLJ	Canadian Business Law Journal
CLP	Current Legal Problems
CILJ	Cornell International Law Journal
CJIL	Chicago Journal of International Law
CJICL	Cardozo Journal of International and Comparative Law
CJTL	Columbia Journal of Transnational Law
CLQ	Cornell Law Quarterly
Con TS	Consolidated Treaty Series
CTS	Canadian Treaty Series
CYIL	Canadian Yearbook of International Law
EELR	European Environmental Law Review
EJIL	European Journal of International Law
ELJ	Energy Law Journal
ELR	Environmental Law Reporter
Foreign Aff	Foreign Affairs
Foreign Pol'y	Foreign Policy
FILJ	Fordham International Law Journal
FLR	Fordham Law Review
GYIL	German Yearbook of International Law
GGULR	Golden Gate University Law Review
GBDLJ	Global Business and Development Law Journal
GWJILE	George Washington Journal of International Law and Economics
HICLR	Hastings International and Comparative Law Review

HILJ	Harvard International Law Journal
IALR	International Arbitration Law Review
ICJ Rep	International Court of Justice Reports
ICLQ	International and Comparative Law Quarterly
ICLR	International Community Law Review
ICSID Rep	ICSID Reports
ICSID Rev	ICSID Review - Foreign Investment Law Journal
IFLR	International Financial Law Review
IALR	International Arbitration Law Review
IL	International Lawyer
ILF	International Law Forum
ILM	International Legal Materials
ILR	International Law Reports
ILSA JICL	ILSA Journal of International and Comparative Law
Iran-USCTR	Iran-United States Claims Tribunal Reports
ITBL	International Tax & Business Lawyer
IYBHR	Israel Yearbook on Human Rights
JAIL	Japanese Annual of International Law
JBL	Journal of Business Law
JCE	Journal of Comparative Economics
JDI	Journal de droit international
JENRL	Journal of Energy and Natural Resources Law
JILE	Journal of International Law and Economics
JIA	Journal of International Arbitration
JIEL	Journal of International Economic Law
JPL	Journal of Public Law (now Emory Law Journal)
JWI	Journal of World Investment (now JWIT)
JWIT	Journal of World Investment and Trade
JWT	Journal of World Trade
LCP	Law and Contemporary Problems
LNOJ	League of Nations Official Journal
LN Doc	League of Nations Documents
LNTS	League of Nations Treaty Series
LSI	Law & Social Inquiry
Marq LR	Marquette Law Review
Mich LR	Michigan Law Review
Minn LR	Minnesota Law Review
MJGT	Minnesota Journal of Global Trade
MJIL	Michigan Journal of International Law
NCLR	North Carolina Law Review
NILR	Netherlands International Law Review
NJILB	Northwestern Journal of International Law and Business
NYLJ	New York Law Journal
NYUJIL	New York University Journal of International Law

NYUELJ	New York University Environmental Law Journal
NYULQR	New York University Law Quarterly Review
NYULR	New York University Law Review
RDCADI	Recueil des cours de l' Académie de Droit International de La Haye
RIAA	Reports of International Arbitral Awards
RGD	Revue Générale de Droit
RGDIP	Revue Générale de Droit International Public
SJIL	Stanford Journal of International Law
TDM	Transnational Dispute Management
TILJ	Texas International Law Journal
UCDJILP	UC Davis Journal of International Law and Policy
UCDLR	UC Davis Law Review
UPJIEL	University of Pennsylvania Journal of International Economic Law
UTLJ	University of Toronto Law Journal
UKTS	United Kingdom Treaty Series
UNTS	United Nations Treaty Series
UST	United States Treaties
VJIL	Virginia Journal of International Law
VLR	Virginia Law Review
WCR	World Court Reports
WD	World Development
WILJ	Wisconsin International Law Journal
YJIL	Yale Journal of International Law
VJTL	Vanderbilt Journal of Transnational Law
YBCA	Yearbook of Commercial Arbitration
YBILC	Yearbook of the International Law Commission
YBUN	Yearbook of the United Nations
YWBA	Yearbook of World Affairs

#### FREQUENTLY CITED DRAFT CONVENTIONS AND OTHER INSTRUMENTS

1929 Draft Convention	<i>Convention on the Treatment of Foreigners</i>
1929 Harvard Draft	<i>Draft Convention on Responsibility of States for Damage done in their Territory to the Person or Property of Foreigners</i>
1961 Harvard Draft	<i>Draft Convention on the International Responsibility of States for Injuries to Aliens</i>
1967 Draft OECD Convention	<i>Draft Convention on the Protection of Foreign Property</i>

Abs-Shawcross Draft Convention	<i>Draft Convention on Investments Abroad</i>
Charter	<i>Charter of Economic Rights and Duties of States</i>
ICC Code	<i>International Code of Fair Treatment for Foreign Investment</i>
ILA Statute	<i>Draft Statutes of the Arbitral Tribunal for Foreign Investment and the Foreign Investment Court</i>
NIEO Declaration	<i>Declaration on the Establishment of a New International Economic Order</i>

#### NOTE ON REFERENCES TO BILATERAL INVESTMENT TREATIES

For ease of reference, specific bilateral investment treaties in this book are listed by referring to the two treaty parties in alphabetical order, followed by the date the treaty was signed (not the date of ratification). For example, the *Treaty between the United States of America and the Argentine Republic Concerning the Reciprocal Encouragement and Protection of Investment* (signed 14 November 1991, entered into force 20 October 1994) is referred to as Argentina-US (1991).

# Guide to Investment Treaty Resources

## INTERNATIONAL INVESTMENT AGREEMENTS AND INSTRUMENTS

International investment agreements and instruments are available in two print sources:

United Nations Conference on Trade and Development, *International Investment Instruments: A Compendium* (New York: United Nations, 1996) in three volumes.

International Centre for Settlement of Investment Disputes, *Investment Promotion and Protection Treaties*, looseleaf (New York: Oceana Publications, Inc., 1983) in ten volumes.

The United Nations Conference on Trade and Development (UNCTAD) website has two searchable electronic databases – a compilation of bilateral investment treaty texts and a compendium of international investment instruments. In addition, a number of commercially available databases including Kluwer Arbitration and Investment Claims have various treaty materials available online.

## INVESTMENT TREATY AWARDS AND DECISIONS

Investment treaty awards and decisions are reproduced in various print sources including ICSID Reports, ICSID Review-Foreign Investment Law Journal, International Law Reports and International Legal Materials.

Online access to current and past investment treaty awards and decisions, along with links to other materials and resources, is available through Professor Andrew Newcombe's Investment Treaty Arbitration website: <<http://ita.law.uvic.ca>>.

## OTHER RESOURCES

A number of specialized websites provide access to current investment treaty decisions, awards and other materials, including links to further resources:

Digest of Investment Treaty Decisions and Awards: <<http://arbitration-icca.org>>

ICSID: <<http://icsid.worldbank.org>>

Investment Arbitration Reporter: <<http://iareporter.com>>

Investment Claims: <<http://investmentclaims.com>>

Investment Treaty Arbitration: <<http://ita.law.uvic.ca>>

Investment Treaty News: <<http://iisd.org/investment/itn>>

Kluwer Arbitration: <<http://kluwerarbitration.com>>

NAFTA Claims: <<http://naftaclaims.com>>

Transnational Dispute Management: <<http://transnational-dispute management.com>>

UNCTAD international investment agreement: <<http://unctad.org>>

# Table of Contents

<b>Authors' Preface</b>	xix
<b>Acknowledgements</b>	xxi
<b>List of Abbreviations</b>	xxiii
<b>Guide to Investment Treaty Resources</b>	xxix
<b>Chapter 1</b>	
<b>Historical Development of Investment Treaty Law</b>	<b>1</b>
Introduction	1
§1.1 A unique treaty framework	1
I Historical Origins of International Investment Law	3
§1.2 Early history	3
§1.3 Diplomatic protection	5
§1.4 Dispute settlement by claims commissions and international arbitration	7
§1.5 Use and abuse of diplomatic protection	8
§1.6 Colonial territories and extraterritorial jurisdiction	10
§1.7 The minimum standard of treatment	11
§1.8 The Calvo Doctrine	13
§1.9 Early jurisprudence on the minimum standard of treatment	14
§1.10 Efforts to codify treatment standards in the 1920s and 1930s	15
§1.11 Convention on the Treatment of Foreigners	16
§1.12 Seventh International Conference of American States	17
§1.13 The Hull Rule	18
II Post-WWII Developments	18
§1.14 Decolonization and nationalizations	18
§1.15 The Havana Charter and the International Trade Organization	19

§1.16	Non-governmental initiatives to create a multilateral legal framework for investment	20
§1.17	Bilateral and regional initiatives	22
§1.18	Increasing resort to international arbitration post-WWII	24
§1.19	New York Convention	25
§1.20	Permanent Sovereignty Over Natural Resources	26
§1.21	International Centre for Settlement of Investment Disputes	27
§1.22	OECD Convention on the Protection of Foreign Property	30
§1.23	Charter of Economic Rights and Duties of States	31
§1.24	Draft UN Code of Conduct on Transnational Corporations	33
§1.25	OECD Declaration on International Investment and Multinational Enterprises	33
§1.26	Lump sum agreements and national claims commissions	34
§1.27	Investment disputes before the International Court of Justice	35
§1.28	Iran-US Claims Tribunal	39
§1.29	Foreign investment insurance	39
III	International Investment Agreements	41
§1.30	The origins of international investment agreements	41
§1.31	The advent of treaty-based investor-state arbitration in BITs	44
§1.32	BITs – the 1970s and 1980s	46
§1.33	BITs – the 1990s	47
§1.34	World Bank Guidelines	49
§1.35	Developments in Latin America	50
§1.36	Developments in Africa, Middle East and Asia	52
§1.37	North American Free Trade Agreement	53
§1.38	Energy Charter Treaty	53
§1.39	World Trade Organization	54
§1.40	Multilateral Agreement on Investment (MAI)	55
§1.41	WTO Working Group on the Relationship between Trade and Investment and the Doha Declaration	55
§1.42	Chinese IIAs	56
§1.43	Indian IIAs	57
IV	Current Status of the Network of IIAs	57
§1.44	The expanding network of IIAs	57
§1.45	The increase in investor-state arbitrations	58
§1.46	IIA jurisprudence	59
§1.47	Renegotiation and new model IIAs	61
§1.48	Investment promotion effects of IIAs	62
§1.49	Critiques of IIAs	63
V	Structure and Scope of Application of IIAs	65
§1.50	The structure of IIAs	65
§1.51	The scope of application – investment	65
§1.52	The scope of application – investors	68
§1.53	Dispute settlement	70

<b>Chapter 2</b>	
<b>Applicable Substantive Law and Interpretation</b>	<b>75</b>
Introduction	75
§2.1 Applicable law and interpretation	75
§2.2 Meaning of applicable substantive law	75
§2.3 Relevance of the applicable law	78
 I	
Choice of Law Clauses	79
§2.4 Express choice of law clauses	79
§2.5 Distinction from other clauses	84
§2.6 Choice of law clauses in arbitration rules	85
 II	
Relevant Sources of Law in IIA Disputes	86
§2.7 Laws relevant to IIA disputes	86
§2.8 Law pleaded and <i>iura novit curia</i>	88
 III	
Role of the IIA	91
§2.9 The IIA as the primary source of law	91
§2.10 The need to supplement the IIA	91
 IV	
Role of Municipal Law	92
§2.11 Existence of the investment as a domestic law issue	92
§2.12 Other matters to which domestic law is relevant	93
§2.13 The <i>renvoi</i> of international law to domestic law	95
§2.14 The relevance of domestic court decisions	95
§2.15 Domestic law questions as jurisdictional issues	95
§2.16 Criticism of the attitude of IIA tribunals towards domestic law	96
§2.17 Limitations to the role of domestic law	97
§2.18 Subsequent changes in the domestic law	98
 V	
Role of International Law	98
§2.19 International law as the law applicable to issues of liability	98
§2.20 IIAs and international law as part of domestic law	100
§2.21 Domestic law applied alongside international law on issues of liability	101
 VI	
Applicable International Law	102
§2.22 Sources of international law in IIA disputes	102
§2.23 Precedents	102
§2.24 Inconsistent decisions	105
§2.25 Human rights	107
 VII	
Interpretation of IIAs	109
§2.26 Treaty interpretation as the process of applying the proper law	109
§2.27 International law rules on treaty interpretation	110
§2.28 Methods of interpretation	111

§2.29	Object and purpose, preambles and pro-investor or pro-state interpretations	113
§2.30	Interpretations and amendments to IIAs by the contracting states	117
§2.31	Interpretation and the adjudicative function under IIAs	119
 <b>Chapter 3</b>		
	<b>Promotion, Admission and Establishment Obligations</b>	<b>121</b>
	Introduction	121
	§3.1 Overview	121
	§3.2 Customary international law obligations	121
	§3.3 IIA obligations	122
I	Treaty Titles and Preambles	122
	§3.4 Treaty practice	122
	§3.5 The use of the treaty title and preamble in interpreting IIA obligations	124
II	Promotion and Encouragement Obligations	126
	§3.6 Promotion and encouragement	126
	§3.7 Favourable conditions	130
III	Admission and Establishment	132
	§3.8 Distinguishing admission and establishment	132
	§3.9 Rationale for freedom of admission and establishment	132
	§3.10 Domestic regulation of foreign investment	133
	§3.11 Treaty models for admission and establishment	134
	§3.12 The post-entry model	134
	§3.13 The pre-entry model	137
	§3.14 WTO General Agreement on Trade in Services (GATS)	140
IV	Other Entry Obligations	142
	§3.15 Entry of personnel	142
	§3.16 Senior management and offices	144
	§3.17 Granting of permits	145
	§3.18 Special formalities for establishment	146
 <b>Chapter 4</b>		
	<b>National Treatment</b>	<b>147</b>
	Introduction	147
	§4.1 Non-discrimination in international economic law	147
	§4.2 A relative standard	148
	§4.3 A treaty-based obligation	149