

# Is State-State Investment Arbitration an Old Option for Latin America?

*International arbitration is a recognized way to resolve economic conflicts. This paper asks if state-state investment arbitration (SSIA) is an option for Latin America. It examines the language of investment treaty provisions, cases and arbitral awards involving states and treaty-making practice in the region. The analysis shows some complementarity between the mechanisms of investor-state arbitration (ISA) and SSIA; sometimes, the latter is the only option. This article concludes that SSIA is neither a backlash nor a more effective mechanism compared to ISA. SSIA constitutes an opportunity for both home and host Latin American states to balance their investment treaty commitments.*

## 1. Introduction

International arbitration is a recognized mechanism to resolve and settle economic conflicts involving foreign investments all over the world. It includes the possibility that an investor brings a claim against its host state, the so-called investor-state arbitration (ISA), based on Bilateral Investment Treaties (BITs) and, more generally, on International Investment Agreements (IIAs). This will ultimately result in arbitral decisions that affect the way that economic and social gains are distributed in global society.

It has been aptly shown that most developing countries have, in a deviation from a fully rational behavior, overestimated the benefits of IIAs, often ignoring their risks (Poulsen 2015, 25–47). As an illustration, the wide scope and reach of some substantive standards in IIAs, such as the fair and equitable treatment, were not previously envisioned. This has led to international liability and damages for acts that states primarily considered to be under their inherent sovereign powers.

The recurrent critiques against ISA (UNCTAD 2015, 120–173) have focused on particular features of the system, like the waiver of the exhaustion of local remedies and the possibility of treaty-shopping based on the nationality of investors.

It is true that each state evaluates the decision to participate in or to exit fully or partially from the current system of IIAs and from arbitral institutions providing for ISA such as the ICSID (International Centre for the Settlement of Investment Disputes). States arguably carry out a net analysis of the benefits, in terms of investments and credibility, and the costs, in terms of constraints in regulatory sovereignty (Aaken 2015, 21). This context prompted a revision on the approaches of some Latin American states.

This paper discusses the possibility of state-state (state-to-state or inter-state) investment arbitration (SSIA) in relation to foreign investments. With the theoretical and practical development of treaty-based investor-state arbitration, the debate around SSIA had been progressively put aside. Any attempt to refer or return to it was considered outdated and a backlash. But the new context justifies a fresh analysis of the mechanism, so that a revival of the conceptual foundations of this “old” kind of dispute settlement should not be dismissed. The paper asks if SSIA is an option for some Latin American states under the current practice of international law.

Recent state-state cases involving Latin America (*Peru v Chile*, *Italy v Cuba and Ecuador v United States*, to be analyzed further) may indicate a resurgence of the practice in the area. They sparked interest and were followed by a new range of academic contributors in this field (Juratowitch 2008; Paparinskis 2009; Muchlinski 2009; Pérez 2012; Potestà 2012; Potestà 2013; Lo 2013; Potestà 2014; Roberts 2014; Trevino 2014; Wong 2014; Bernasconi-Osterwalder 2014; Recanati 2014; Roberts 2014; Paparinskis 2014; Posner and Walter 2015; Sacerdoti and Recanati 2015; Macías 2016). This literature has opened up avenues for further research in the area. One should note the existence of state-state jurisdictional clauses in around 60 BITs between Latin American and Caribbean states and more than 30 other agreements with investment provisions, as

of May 2016. In light of that, this contribution presents a framework to place the debate into the Latin American context.

The paper is divided in three parts. The first part deals with concepts related to state-state arbitration in relation to investment treaty provisions. The second part analyses both old and new Latin American approaches in the field. The third and final part offers the conclusion, which highlights further developments.

## **2. Role of States in Investment Conflicts: Conceptual Foundations**

### **a. SSIA versus ISA**

The introduction of ISA has substituted the recourse to diplomatic protection to a large extent (ICJ case *Ahmadou Sadio Diallo*, para 88; ICSID case *CMS Gas*, para 45). Diplomatic protection has been described as involving the use of diplomatic action or any other means of dispute settlement by a state in response to an injury to its national in face of a wrongful act of another state (Berman 2007, 68).

It is well established that the admissibility of a claim that seeks to determine state responsibility requires the fulfillment of certain criteria. These are the nationality of claims and the exhaustion of local remedies (see art. 44 of the ILC Articles on the Responsibility of States for Internationally Wrongful Acts). One should not forget that, in the absence of an investment treaty with consent to ISA, the recourse to diplomatic protection remains the sole international alternative. Also, diplomatic protection claims, short of SSIA, may take place without any publicity and pass unnoticed, so that they are generally underreported.

Host states have been directly challenged by investors and home states have seen their role in arbitration progressively diminished. However, state-state dispute settlement mechanisms still persist in BITs or IIAs, though the recourse to this kind of arbitration has remained rare (Dolzer and Schreuer 2012, 13).

Throughout history, state-state arbitration was occasionally used in disputes related to property; but the Friendship, Commerce and Navigation (FCN) treaties began including jurisdictional clauses more frequently only from the beginning of the 20<sup>th</sup> century (Vandeveldt 2010, 24–25; 504). The first BITs, from 1959 onwards, inherited the clause, which remained even after the introduction of unqualified consent to ISA, starting in 1969 (Dolzer and Schreuer 2012, 7).

According to Douglas, from the inter-state perspective, the BITs contain

international obligations opposable by one contracting State to another, and the *general rules of State responsibility for international wrongs regulate the consequences of any breach thereof*. These obligations can generally be grouped into two categories: (i) adherence to the law of treaties in the interpretation and application of the investment treaty; (ii) the obligation not to frustrate an investor's recourse to international arbitration or the enforcement of any award against the host State. (Douglas 2004, 189 emphasis added)

The analysis of jurisdictional clauses in IIAs providing consent to SSIA is a good starting point. In the current practice, a typical state-state clause in an IIA, this one from the Argentina-Jamaica BIT, reads:

Article 8: Settlement of Disputes between the Contracting Parties

1. Disputes between the Contracting Parties concerning the interpretation or application of this Agreement should, if possible, be settled through the diplomatic channel;
2. If a dispute between the Contracting Parties cannot thus be settled within six months from the beginning of the negotiations, it shall upon the request of either Contracting Party be submitted to an arbitral tribunal.

Some observations are necessary. First of all, it could be claimed that the clauses should be considered dysfunctional remainders of the old FCN treaties. However, if they persisted, the clauses are to be given meaning and purpose; otherwise they “would be rendered almost completely ineffective (an unacceptable result as a matter of treaty interpretation)” (Paparinskis 2009, 296).

Second, one could assume that the main purpose of an IIA is to give direct access to an investor. However, there are parallel purposes of investment agreements, apart from the limited coverage of ISA (Berman 2007, 82). In this regard, there is, in fact, the “possibility of *two different procedures arising from the same claim*: one under ICSID between the investor and the host State, *the other between the two States based on the alleged violations of the investment treaty.*” (Schreuer 2009, 416 emphasis added). Thus, one should conclude that these clauses are not merely subsidiary to ISA, but are in reality complementary to it.

Third, it could be argued that apparently there is a narrower scope in an SSIA clause, which generally refers to the interpretation and/or application of the treaty, in comparison to the investor-state clause, which encompasses *any* dispute concerning an investment (Vandeveldel 2010, 499) (e.g. the United States BIT Model [2012]). However, it should be recognized that the clauses frequently have an all-encompassing broad language, (Roberts 2014, 6–7; 11–12) with expressions such as “any” or “a” dispute, without qualification. Therefore, it is to be accepted that the text, object and purpose (VCLT art. 31[1]) and also the history (VCLT art. 32) of BITs show that state-state arbitration should not be restricted in any way and that its co-existence, without priority, is a fact (Roberts 2014, 5).

Fourth, one could say that ISA is always a more effective mechanism than SSIA. Nevertheless, states, as repeat players in the international arena, have long-term relationship concerns; thus, when systemic interests come into play, the state-state path may be more attractive. It is sometimes the case that the financial burden of bringing a claim would be a barrier for an investor, especially if it is an individual or a small company, so that resorting to its own state may be the most appropriate conduct (Roberts 2014, 14; Berman 2007, 71–72) even in the presence of investor-state provisions. Also, the possibility of settlements might safeguard some interests of the home state (Recanatì 2014, 430; 440).

This is not a contention that SSIA is always a good substitute to ISA in terms of effectiveness to enforce investor's rights or in terms of protection of the sovereign right of host states. From a practical perspective, one could argue that if a treaty only includes the option of SSIA, the politically connected or economically robust companies would probably be the only ones able to convince the states to endorse their claims. The greater risk is for the small and medium enterprises, which are less connected. Since they are the ones who should be benefitting from the investor-state system, a change to SSIA would not be more efficient for them. This could perhaps be addressed by the domestic legal systems of home states. A mechanism regulated by administrative law could allow companies to bring cases to their governments for endorsement in a streamlined manner.

Given that the jurisdictional clause had always been available, a legitimate question is: Why has not the mechanism been more frequently used? Several explanations are possible. One may argue that after the rise of investor-state dispute settlement, there has been a misunderstanding as to the real scope or extension of state-state clauses. The most common view was that the clause was limited to deal with the interpretation of the institutional part of the treaties or the general provisions related to entry into force and termination. Second, the possibility of using it as a defense by a host state is something that has only been tried recently. Finally, the requirements of certain aspects of diplomatic protection (nationality, exhaustion of local remedies) are rather burdensome. In this regard, recent treaties cast new light on the clause, by changing the criteria of nationality, regulating exhaustion and establishing the transfer of compensation to private entities.

The recurrent question, however, is whether leaving the decisions to the states means re-politicizing. The question assumes that depoliticization is a useful way to describe the development of investor-state arbitration, which has been challenged (Paparinskis 2011b, 271–282). In fact, to some extent, all disputes involving a state have a political character: they affect important interests in the relations with other states (Lauterpacht 1933, 153–156). In the domestic or international arena, politics will play a role in the decisions to bring a claim, negotiate, settle or fulfill

international obligations. Thus, the proper characterization suggests that one should not consider the return to SSIA as a backlash.

All in all, these clauses are more than present and need to be given meaning and purpose. SSIA can be useful to both host and home states alike, having a much broader scope than diplomatic protection. In addition, it comes generally as complement to ISA.

### **b. State Involvement Beyond Arbitration**

It is to be stressed that the involvement of states in the correct interpretation of their investment treaties can always take place apart from state-state arbitration. Thus, this section briefly describes some institutionalized mechanisms involving states. Alternative dispute settlement between states for the resolution of economic conflicts includes negotiation and consultations, mediation, fact-finding and other mechanisms accepted in international law (UNCTAD 2003, 16–17; 30–33) (UN Charter, art. 33[1]). It is to be recalled that most SSIA clauses come with the requirement of a previous negotiation period or with the classic possibility or obligation of consultations (Vandevelde 2010, 500). In fact, a concept broader than the arbitration itself is encompassed in the expression State-State Dispute Settlement (SSDS) in investments (UNCTAD 2003). Ultimately, there has been an emphasis in dispute prevention, by the enhancement of the role of state–state cooperation for the handling of disputes (UNCTAD 2010, 47–52; 93–98).

Non-party submissions, possible in the North American Free Trade Agreement (NAFTA) and other IIAs, provide for the possibility that the home state brings its views into an investor-state dispute (Alschner 2014, 309–316). This view may or may not coincide with the investors' position. The tribunal will evaluate the contribution presented, but it is, by no means, obliged to do that. The

parties' position may count towards the identification of object and purpose of the treaties and also provide context for interpretation.

Another mechanism is conferring power to interpretative or independent commissions. NAFTA provides that the Free Trade Commission may decide on an interpretation that will be binding on future cases and this was used in relation to the standard of fair and equitable treatment (Roberts 2010, 180–181; 194; 208). Finally, the possibility of *renvoi* of questions of law or facts has been used in relation to technical issues such as financial and tax related aspects of the case (Alschner 2014, 321–324).

Moreover, parties can always agree on subsequent interpretation of their treaties, which would be considered authentic interpretation (VCLT Art. 31 [3] [a]). One should bear in mind that interpretive agreements are likely to come up on issues that have arisen in practice (Ishikawa 2015, 140–141). States have reasons and incentives to delegate or not the interpretation of treaties. Some suggest that there are several intermediate options for outsourcing and retaining certain issues if states are unhappy with ISA (Aaken 2015, 47). In case of dissent in joint administrative commissions or independent agencies, the delegation of the interpretative task to tribunals also ensures credibility of commitments (Aaken 2015, 38).

To some extent, joint interpretive statements are subsequent agreements and may be a helpful way to “control” expansive jurisdictional interpretation of agreements and prevent unintended consequences in investor-state arbitrations. Some policy options have already been proposed such as: (1) obligatory notification of disputes to home states; (2) formal obligation to consult; (3) recourse to joint interpretive statements; and (4) the attribution of a binding character to the interpretative statement (Ishikawa 2015, 146). Another option would be multilateral opt-in statements, that is, unilateral statements by the parties with regard to the interpretation of common provisions of their IIAs (St John and Gertz 2015).



These alternative approaches have been resorted to in the Latin American region. For instance, El Salvador submitted its views as non-disputing party submission in a litigation under the Central America-Dominican Republic – United States Free Trade Agreement (CAFTA-DR), involving Costa Rica, as reported in the ICSID case *Spence International Investments* (St John and Gertz 2015, 3). Argentina and Panama agreed subsequently that the most-favored nation clause in their BITs in force does not relate to dispute settlement provisions. Also, a mechanism provided in art. 10.22 (2) of the Additional Protocol of the Pacific Alliance makes all the interpretations issued by the Administrative Commission of the Agreement binding, especially on more sensitive issues such as the interpretation of excluded measures.

The aim here is not to take position on the most desirable policy outcomes, but to attest that all of them leave room for SSIA - for example, when the obligation to consult is frustrated and where the parties, the administrative commissions or technical committees cannot agree on an interpretation. Some believe that, because facts and norms are sometimes difficult to separate from each other, tribunals should be expressly delegated with the final interpretive task (Aaken 2015, 41). That seems to be precisely the role of SSIA and this paper now turns its attention to the specificities of Latin America.

### **3. Latin America and SSIA**

#### **a. The Latin American Challenge**

##### **i. Calvo Doctrine: a reappraisal?**

In the Latin American legal tradition, it is known that the influential Calvo Doctrine, favoring internal courts (Calvo 1896, 137–155 vol 3; for a recent critique Schreuer 2005) was developed in a context of manifest reaction to abuses in diplomatic protection claims supporting an injury to foreigners. Considering the lack of balance between strong European states and the newly formed weak Latin American states, the Calvo doctrine was a clear response against an “imposed”

international rule that foreigners were given more consideration and privileges than nationals (Calvo 1896, 138; 140). The general argument was that the prevailing international rule was unfair, that it went against the principles of equality, independence and solidarity between states and that it violated territorial jurisdiction. European states themselves did not even apply such rule in their relationship with each other. As a result, Calvo proposed that any legal issues arising after a foreigner was established should be solved in the exclusive arena of local courts (Calvo 1896, 140–142).

Criticizing the violence exerted by some European states in South America, Calvo also emphasized the arbitrary and unfair features of diplomatic claims based on damages caused by civil unrest and internal conflict (Calvo 1896, 148–149; 155). The use of force was common especially by Great Britain, in connection with the default of certain portfolio investment (bonds), during the 19<sup>th</sup> century and the beginning of the 20<sup>th</sup> century (Vandeveldt 2010, 29). Several other European states and the United States have resorted to arbitration claims related to investments against Latin American states in the context of domestic riots and revolutions.

On the other hand, Latin America had almost always been persistent objector to the formation of a customary practice regarding the existence of an external standard imposed on an alien, which signified a deviation from municipal law, except arguably for the period in which liberal practices arose later on (Sornarajah 2010, 125). A meaningful endorsement of the Calvo Doctrine was article 9 of the Montevideo Convention on Rights and Duties of States, which prescribed that foreign nationals would not be given further rights than nationals (Vandeveldt 2010, 36). In the international arbitration arena, the Calvo Doctrine was expressed in the form of a clause (Calvo Clause) incorporated into Constitutions, other legislation and in contracts with foreign parties, favoring local courts over arbitration tribunals (Fach Gómez 2011, 195–198).

Drawing on how Latin American states positioned themselves in the negotiation of ICSID Convention, some noticed that they expressed their skepticism against diplomatic protection

(Paparinskis 2009, 283). Peruvians indicated that it was not necessary or convenient to have diplomatic protection either during or after arbitration for the enforcement of the award, the authority of which derived from the Convention; this proposal, however, did not prosper (ICSID 1968, 764; 766–767). Venezuela recalled unpleasant experiences with regard to diplomatic and foreign claims (ICSID 1968, 349). In line with Calvo concepts, Nicaragua and Colombia pointed out that diplomatic protection was restricted to denial of justice, while Ecuador advocated that states were free to include internal legal provisions prohibiting foreigners to ask for diplomatic protection on their behalf (ICSID 1968, 349–350).

It is now settled that the Calvo Clause has limited validity, that is, it solely binds the foreign investor and never its home state: only when an investor actively asks its home state for assistance, would he breach the legislation or a private contract (Shea 1955, 264–268). Since an investor can dispose of a right such as property, it could equally dispose of a connected action to petition its home state (Rezek 1984, XVIII). The state retains the discretion to offer diplomatic protection in the international level, in line with the PCIJ and ICJ decisions. It might also be argued, though, that the Calvo Clause has validity as a regional custom, binding Latin American states (Shea 1955, 279).

## **ii. Opportunity for Reengagement**

Distancing from ICSID was the option chosen by some Latin American states: Venezuela, Bolivia and Ecuador formally disengaged from the system and many others have had limited participation therein. Latin American states that were never a party of the ICSID Convention include Antigua and Barbuda, Belize (signed, but not ratified), Brazil, Cuba, Dominica, Dominican Republic (signed, but not ratified) and Suriname. At the time of writing, Nicaragua remains a party

to the Convention, despite recent threats by its government to denounce it. One might interpret this is a (re)adoption of the Calvo doctrine, progressively abandoned in the nineties (Fach Gómez 2011).

It should be underlined that there is no single approach to investment law in Latin America so that one cannot assume a hostility of the region towards arbitration (Titi 2014). This paper does not necessarily accept or contest that the current developments represent a (re)adoption of the doctrine, as theoretical argument. The focus here is how SSIA would fit into the arena. Some elements must be considered to evaluate whether the re-appraisal of Calvo's arguments would mean an adoption or a rejection of SSIA as a way to solve disputes.

It could be claimed that the arguments that supported the Calvo doctrine could be used to *support* state-state arbitration in investment cases, in a reaction against ISA. Abandoning consent to investor-state and embracing state-state arbitration would mean, to some extent, one step back to a time when IIAs did not provide ISA and SSIA was the only way to solve disputes by adjudication. In fact, it has been argued that the procedural hurdles of SSIA may arguably result in an outcome more favorable to the host states (Recanatì 2014, 441). The adoption of SSIA could be interpreted as deference to sovereign and regulatory rights, since foreign investors are not given direct access to a route not available to nationals and cannot challenge policies.

However, the non-participation in ICSID means that the states do not feel or have never felt that being a party to the ICSID Convention or using its procedural rules is in accordance with their national interests. It does not mean an exit from ISA, since a state can always act with ICSID Additional Facility, resort to other rules or centers and include consent in contracts. In addition, re-evaluating SSIA could also constitute a recognition of the shortcomings or low effectiveness of ISA in terms of enforcing investor's rights.

One could claim now that the arguments supporting the Calvo doctrine could be used to *oppose* state-state arbitration in investment cases. Only internal courts are competent to deal with investment cases and diplomatic protection would only be possible in case of denial of justice.

Nevertheless, Calvo's main concern seemed to be the attribution to the state of revolutionary conduct (Paparinskis 2011a, 260) and the abuse in the use of force. Calvo himself described state-state arbitration with relation to injuries as an available and growing instrument, used in several occasions by the Latin American states throughout the 19<sup>th</sup> century (Calvo 1896, 432–491).

In the current context, the opt-out from the investment law system can be represented by the termination of all BITs, as in the case of Ecuador and Bolivia, by the selective termination, in the case of Venezuela or by a renegotiation in light of new trends. This means that some substantive standards in the IIAs do not reflect the interests of those states. It seems that the Latin American objections and reactions against diplomatic protection were more related to the content of the obligations, which would base the claims, than with SSIA as a mechanism to solve conflicts.

Thus, one cannot consider that the Calvo doctrine clearly supports or rejects SSIA. The conclusion is that the reference to the Calvo Doctrine does not seem to aid much in this debate, apart from its historical significance.

## **b. New Options and Approaches**

### **i. Cases and Regional Mechanisms**

The region offered the first attempt of coordination between ISA and SSIA proceedings. The ICSID case *Empresa Luchetti v Peru*, referred to *Peru v Chile*, a parallel dispute raised in August 2003. It was for some time the only state-state dispute under a BIT, not considering the *Mexico v. United States* 2001 NAFTA dispute over investments in truck services. The investor's tribunal denied the request for suspension made by the host state (Peru), which had submitted an arbitration against the home state (Chile) regarding the interpretation of the BIT. In the end, however, the investor's tribunal dismissed the claim for lack of jurisdiction.

It is to be stated that a reaction against ISA does not mean disengagement with international investment law. As an illustrative point of the activism of the region, South American states have reached an advanced level of the negotiations towards the constitution of a center for the settlement of disputes, a process initiated in 2008, under the umbrella of UNASUR, institution also open to Latin American states. UNASUR regional initiative came in line with withdrawals from ICSID, as a political reaction against the outcomes of the system (García-Bolívar 2015, 396; 399). This may bring a new arena to decide on or settle disputes involving investors or states of the region and outside it, with mechanisms such as facilitation, mediation and arbitration. In this regard, one might notice the possibility of inclusion of SSIA in the UNASUR Centre (Macías 2016). However, the potential of the UNASUR Centre will only be real if it is progressively given jurisdiction (García-Bolívar 2015, 402) by means of consent in IIAs or contracts, for subsequent disputes.

As another example of the alternatives for states in Latin America, one could reflect on the outcome of litigations such as those related to Argentinian crisis. Several of the cases involved US investors and suffered from a lack of consistency, with impacts on legitimacy (Burke-White 2008). One could wonder if Argentina would still be held liable for breaches of key provisions of its treaties in case of the existence of a binding interpretation from a SSIA tribunal, previous to ISA tribunals. The SSIA tribunal could have reached a completely different conclusion since different parties would be involved in the dispute. Thus, in the context of the Argentina-US BIT, it is worth exploring how both home and host states could have used the state-state arbitration clause, which reads:

Article VI

The Parties agree to consult promptly, on the request of either, to resolve any disputes in connection with the Treaty, or to discuss any matter relating to the interpretation or application of the Treaty.

...

Article VIII

## Conflict Resolution Quarterly (forthcoming) circulation restricted

1. Any dispute between the Parties concerning the interpretation or application of the Treaty which is not resolved through consultations or other diplomatic channels, shall be submitted, upon the request of either Party, to an arbitral tribunal for binding decision in accordance with the applicable rules of international law. In the absence of an agreement by the Parties to the contrary, the arbitration rules of the United Nations Commission on International Trade Law (UNCITRAL), except to the extent modified by the Parties or by the arbitrators, shall govern.

...

First, from the point of view of the home state in the dispute, the United States, there seem to be compelling arguments to believe that it was legally possible they had brought a diplomatic protection claims supporting its investors as a class with the objective of ensuring more consistent results in the litigation (Roberts 2014, 4) provided that the admissibility criteria are fulfilled (nationality of claims and exhaustion of local remedies). This claim would be based on the jurisdiction conferred by art. VIII of the BIT. The United States would only have been barred to include, in its diplomatic protection claim, investors which had already begun ICSID arbitration, due to art. 27 of the ICSID Convention. The decision could have a declaratory nature and base future ISA claims, or less persuasively, could include compensation for the companies subject to the common sense approach of prohibition of double recovery (Paparinskis 2009, 300). Arguably, the consistency would also come to the benefit of Argentina, in litigation terms.

Second, as to an initiative by the host state, in this case, Argentina, one ponders whether it could have ignited a state-state dispute as a defense. The aim would be to obtain an interpretation that it did not breach the provisions of the treaty. In this regard, the *Ecuador v US* case, administered by the Permanent Court of Arbitration – PCA, is illustrative. The silence of the United States with regard to Ecuador’s request for interpretation of an article in the US-Ecuador BIT and the communication that it would not manifest at all on the matter could be interpreted as inaction. This would amount to holding “opposing views”, thereby creating a dispute. [See in the PCA documents, the Expert Opinions of Pellet, McCaffrey and Amerasinghe; for a contrary approach,

see Expert Opinion of Reisman]. The majority of the arbitral tribunal was not convinced and denied jurisdiction. The dissenter, however, reportedly considered that silence represents a dispute.

Since the decision has been discussed and commented on elsewhere (Orecki 2015; Bernasconi-Osterwalder 2014, 11–14; Roberts 2014, 10–16), the focus is on an argument raised by Ecuador, which deserves attention. Considering that most IIAs have provisions on the obligation to consult (art. V in the US-Ecuador BIT), the refusal to do so is a breach of the treaty. It is submitted that an interpretation of the tribunal of the content of provision that was the object of the consultations can be considered proper satisfaction. This is an accepted form of reparation under international law, appropriate to put an end to the violation, as argued by Pellet, Ecuador's legal expert in the case, in its report. This path can be explored, provided that the parties show evidence that the claimant made every effort to consult. In fact, the criteria for using the state-state jurisdictional clause as a defense are not clear. This may explain why it has not been used more extensively. The unsuccessful attempts appear to be due more to the specificities of the cases than to an impossibility of using the clause that way.

Thus, it is convincing to think that Argentina could have initiated consultations with the United States in order to provide a binding interpretation of treaty provisions. In case of disagreement, it could bring a state-state interpretive claim (Cf Roberts 2014, 4). Anyway, it has been reported that Argentina at least envisaged such possibility in order to bring clarity and coherence to divergent interpretation of its cases.

## **ii. SSIA in the New Brazilian Investment Treaty**

In this context, it is worth discussing the dispute settlement mechanism of the new investment treaty model of Brazil. In the region, the model resulted in treaties signed with Mexico, Colombia and Chile (as well as Angola, Mozambique, Malawi) and in current negotiations with Peru among others. Considering the partners chosen, while the model was ignited by the rise of Brazil as the



home state of origin of investments abroad, it seeks to maintain coherence with the traditional policy discourse in Brazil against ISA. Brazilian policy has been aptly described elsewhere (Levy, Borja, and Pucci 2014). Also, there have been some academic and critical analyses of the new model (Titi 2015; Monebhurrin 2016). While not the focus here, the Brazilian model may be criticized for the institution of excessive bureaucracy with the creation of committees and contact points. But attention will be paid to the provisions related to SSIA.

Unlike the other treaties, signed with Angola, Mozambique and Malawi, which refer only to the possibility of future development of SSIA, the IIAs with Mexico, Colombia and Chile contain the consent by the parties to the mechanism.

First of all, it is to be noted that the dispute settlement provisions of the treaties focus primarily on dispute prevention (art. 18 Brazil-Mexico IIA, art. 22 Brazil-Colombia IIA and art 24 of the Brazil-Chile IIA). This seems to be reason why UNCTAD classifies these treaties not as BITs but as other investment agreements. The mechanism is an example of a soft law approach, which has been highlighted in the context of revision of treaty-making practice as an example of an alternative model (UNCTAD 2015, 108; 152).

Second, in the Brazilian model, a traditional system of consultations between the parties is available with regard to the interpretation and application of the treaty. The difference is that, whenever there is an affected investor, it will take part in the proceedings providing information and attending the consultation meetings. A final opinion on the dispute by each of the parties is to be issued at the end of the proceedings.

Third, the result of the consultations will base the SSIA claim. In this regard, the general available remedy within the mandate of the tribunal will be a declaration of the conformity of the measure with the treaty. But this is not equivalent to an order for withdrawal or change of the measure. The claim can also constitute a form of diplomatic protection of the investor. In this regard, it is necessary to provide some context and clarifications.

As seen above, the recourse to diplomatic protection is limited by some requirements. The exhaustion of local remedies is an important principle of international law in that regard but its explicit waiver by treaty is widely recognized. Also, while a waiver is not to be presumed, this is rebuttable, so the possibility of an implicit waiver should not be excluded (Crawford 2006, 49; Sacerdoti and Recanati 2015, 1851). The ILC Draft on Diplomatic Protection with Commentaries – ILCDP – provides, with reference to art. 15 (e), that: “No general rule can be laid down as to when an intention to waive local remedies may be implied. Each case must be determined in the light of the language of the instrument and the circumstances of its adoption”. (paras 12-16, emphasis added).

The *ad hoc* arbitration *Italy v Cuba* is elucidative in this regard (Potestà 2012). It reaffirmed the possibility of a claim based on diplomatic protection with reference to an IIA and its SSIA jurisdictional clause (Recanati 2014, 438–439). It also applied the presumption that the exhaustion of local remedies had not been waived. Moreover, it recognized the right of Italy to apply for a declaratory decision that the rights contained in the BIT were breached or violated with reference to a specific set of facts. In this case, it could be argued that *Italy v Cuba* united a systemic interest with a low monetary damage (Posner and Walter 2015, 392).

With that in mind, in the Brazilian treaties with Mexico, Colombia and Chile, a special system of secondary rules of diplomatic protection is in place from the very moment of the initiation of the dispute prevention mechanism. Bringing an international claim would mean the last stage of the diplomatic protection. Only after the dispute prevention mechanism is exhausted can a party bring a claim in a state-state arbitration. However, nowhere in the agreement is there the need to exhaust local remedies to resort to the dispute prevention mechanism or to SSIA. On the contrary, it is submitted that the language and context of the provisions (eg art. 23 [14] b Brazil-Colombia IIA) constitute sufficient rebuttal of the strong presumption against the waiver of the requirement of exhaustion (for a contrary interpretation, Macías 2016). This departure from

customary rules avoids procedural problems of inter-state disputes (Sacerdoti and Recanati 2015, 1861–1862).

Fourth, in this system, the remedy of compensation for damages will be available, but only if the parties agree to it afterwards by a specific arbitral agreement, generally when there is already a dispute. This is explicit in Art 19.2 of the Brazil-Mexico IIA, Art 23 (14) a, b, c, d of the Brazil-Colombia IIA; however, an equivalent provision is absent in the Brazil-Chile IIA. The possibility of compensation was present in the Organization for Economic Co-operation and Development (OECD) draft Multilateral Agreement on Investments (MAI), which contained a SSIA clause. According to the abandoned draft, an award in a SSIA claim could include restitution or a pecuniary compensation for any loss or damage (Malanczuk 2001, 144–145). This is a sign that an institutionalized, *lex specialis* system of diplomatic protection was envisaged (see art. 17, ILCDP) and that is acceptable as an opt-out of general international law (Bernasconi-Osterwalder 2014, 9).

When compensation is possible, the Brazilian provision obliges that the parties transfer the amount to the affected investors, according to its own procedures. This is also an innovation in the classic requirements of diplomatic protection, in which this obligation does not take place. Also, this avoids the potentially tense situation whereby a state refuses to transfer the compensation to the investor, which cannot obtain it itself due to the prohibition of double recovery (Roberts 2014, 50).

Finally, there are effective mechanisms to ensure that the constitution of the state-state tribunal is not impaired by inaction of the parties. Moreover, there are possible references to the UNASUR Center of Dispute Settlement, if it allows for SSIA in the future (see art. 19.4, Brazil-Mexico IIA, art 23(1), Brazil-Colombia IIA and Annex 1 art. 2(1), Brazil-Chile IIA). This would mean the replacement of the provisions on the constitution of arbitral tribunals. Moreover, the decision will be mandatory to the parties (art. 19.8, Brazil-Mexico IIA, art 23(12), Brazil-Colombia IIA and Annex 1 art. 7(4), Brazil-Chile IIA). However, there are no additional

mechanisms to ensure compliance. In Latin America, an interesting solution was adopted by art. 17.20 and 17.22 of the Protocol of the Pacific Alliance. There, in case of non-enforcement of a state-state investment dispute award, the affected party can ignite a centralized system of suspension of benefits. This is a viable mechanism in agreements that include both trade and investment.

In policy terms, it is suggested that it would have been wiser to allow for a broader mandate in relation to the SSIA, including the claim of compensation, irrespective of the future consent of the other party. There is a strong incentive for the respondent party not to agree on conferring this power to the tribunal afterwards, so that the provision may remain ineffective. On the other hand, the Brazil-Mexico and the Brazil-Colombia IIAs are two of the few investment treaties to address the issue of compensation in a state-state context, which goes beyond the traditional mandate of SSIA tribunal of interpretation and application.

To conclude, the SSIA provisions in the Brazilian treaty with Mexico and Colombia provide not only for the possibility of declaratory awards but also for a special system of diplomatic protection. The absence of ISA provisions puts much pressure on internal domestic legal systems, with some room for the consultations and the SSIA to solve all pending issues, which is currently unrealistic. Only time will reveal the reliability and effectiveness of the mechanism.

#### **4. Conclusions**

Based on the analysis, the conclusion is that state-state investment arbitration is neither a backlash nor a more effective mechanism compared to investor-state arbitration. It does not necessarily represent a re-politicization of the disputes, considering that it has always been available. It may, though, suffer from lack of effectiveness when home states choose not to bring cases forward and when local remedies are not exhausted, absent a waiver. However, SSIA constitutes an additional opportunity for both home and host states to provide balance to investment

treaty commitments and fine-tune their investment policies.

In several situations, SSIA would be the only possible mechanism, especially due to limitations in the consent to ISA or due to the nature of the obligation to be enforced, such as access rights. In others, SSIA will be complementary to ISA, adding important inputs to the interpretation process, making different remedies available or enabling different litigation strategies for home and host states. This context helps states to better calibrate their investment policies.

While one takes note of the historical clashes in Latin America, it is not assumed there is a general discredit as to investor-state arbitration. This is because several Latin-American states support as well as condemn the current regime, which has given way to new substantive and procedural treaty-making initiatives. These developments have translated into alternative settlement mechanisms, into different IIA models or into more soft law approaches, not necessarily more effective compared to classic ISA. However, SSIA may serve to remediate some of the shortcomings of international arbitration and to re-engage those which have opted out or remained at the margins of the legal development in the area. The extent to which the options developed here may be adopted depends on the degree of concern with the system expressed by each Latin American state.

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### **Bio**

Murilo Lubambo is a doctoral candidate and fellow at the Faculty of Laws of University College London. He has been an exchange scholar at Yale University as visiting assistant in research (2016).

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