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REPRINTED FROM:
CORPORATE DISPUTES MAGAZINE
JUL-SEP 2020 ISSUE

corporate disputes
JUL-SEP 2020
www.corporatedisputesmagazine.com

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PERSPECTIVES

INVESTMENT TREATY ARBITRATION: TRENDS IN DIFFERENT INDUSTRY SECTORS

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Foreign investments enjoy international legal protection through some 3000 or more bilateral and multilateral investment treaties (BITs and MITs respectively). Investment treaties concluded between two or more states contain reciprocal state-level undertakings for the promotion and protection of foreign investment. A central feature of investment treaties is their dispute resolution mechanisms, which allow protected foreign investors to sue states directly by submitting claims to international arbitration rather than to the national courts. This can be an important protection for an investor making an investment in a country where the national court system may not provide adequate means for resolving a dispute, or in circumstances where that dispute will be against the state itself.

In order to gain treaty protection and submit a dispute to arbitration, a foreign investor will need to demonstrate that certain requirements are met, including as set out below.

A foreign investor must qualify for investment treaty protection. The investor will need to show that the tribunal has jurisdiction under the applicable treaty to decide the dispute. Typically, this requires the investor to demonstrate that it is a national of a state party to the investment treaty that is not the host state. The investor must also have made a qualifying investment in the host state. The term 'investment' is variously defined in investment treaties, but typically covers 'every type of asset' or 'every form of investment', including shares or other forms of participation in local companies, real and contractual property rights, IP rights, bonds and concession contracts. Some tribunals have required a contribution or commitment by the investor, a certain duration, risk and contribution to economic development.

The conduct giving rise to the dispute must be attributable to the state. In order to bring an investment treaty claim against the state, the investor will need to show that the conduct giving rise to the dispute is attributable to the state. This will be clear-cut in circumstances where the relevant conduct is carried out by an arm of the state, for example the judiciary through court decisions, or a ministry through the revocation of a licence. However, difficulties may arise where the contract or the investor's expectations are violated but the counterparty to the contract is not formally a state body (for example an entity that is only part-owned by the state). In those circumstances, it may still be possible to bring a claim if the contractual counterparty is exercising elements of governmental authority or acting on the instructions of, or under the direction or control of, the state in entering into the contract.

Potential investors should consider the availability of investor protections and how to structure their investment so that these criteria will be deemed satisfied should a dispute arise.

Investment treaties commonly include a suite of minimum rights and protections, including the following.

> **"Potential investors should consider the availability of investor protections and how to structure their investment so that these criteria will be deemed satisfied should a dispute arise."**

First, national treatment is a requirement that foreign investors are treated no less favourably than investors who are nationals of the host state.

Second, most favoured nation (MFN) treatment is a powerful provision that requires a state party to provide investors with treatment no less favourable than it provides to investors under its other investment treaties. This provision can be invoked to import both substantive and procedural protections from other investment treaties.

Third, fair and equitable treatment (FET) is an obligation on host states to accord fair and equitable treatment to foreign investments, including guarantees of: (i) protection against a denial of justice;

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(ii) procedural fairness, due process and transparency; (iii) freedom from coercion or harassment; and (iv) protection of the investor's legitimate expectations.

Fourth, expropriation is a prohibition on unlawful expropriation. Expropriation is the taking by a state, for example by nationalisation, of an investment which essentially deprives the investor of the entirety of its interest. It can be lawful if it is for a public purpose and not discriminatory, but only if prompt, adequate and effective compensation is paid to the investor. Otherwise, it will be unlawful, which requires full reparation of all the investor's losses. Unlawful expropriation can be either direct or indirect. Indirect expropriations entail 'unreasonable interferences', the 'prevention of enjoyment' or the 'deprivation of property rights of foreign investors' (so-called 'creeping' expropriation).

Other rights and guarantees include: (i) the right to full protection and security to prevent the physical destruction of property; (ii) the right to repatriate profits to the investor's home state; and (iii) an obligation on the host state to observe contractual undertakings (a so-called 'umbrella clause').

When a host state interferes with a foreign investment in its territory and a dispute escalates, foreign investors can arbitrate their claims pursuant to the arbitration agreements set out in the relevant treaty, contract or host state legislation, which can negatively impact a state's ability to attract foreign investment. Enforcement of awards against state assets is facilitated by the International Centre for

Settlement of Investment Disputes (ICSID) Convention (and the World Bank) and the New York Convention.

Investment treaty disputes in the banking and finance sector

Historically, investment treaty arbitrations have concerned what might be regarded as 'traditional' investments, such as major infrastructure projects. The general view was that arbitration was incompatible with the needs of banking and finance investors. The tide is turning, however. Investment treaty claims in the banking and finance sector are increasingly commonplace, with over 80 reported investment treaty cases in the sector. Five percent of the cases registered and administered by ICSID in 2019 were brought by banks and financial institutions.

Tribunals have determined that various financings, the operation of bank networks and the issue of sovereign bonds, bank guarantees and derivatives all qualify as protected investments, including promissory notes, even though the funds had not made their way into host state territory, dematerialised government bonds (sovereign debt amounted to an investment under the relevant treaty) and derivative financial products in the form of commodity hedging agreements.

State bailouts and the compulsory administration of banks have also led to a number of investment treaty cases. For example, Future Bank was placed into administration by Bahraini authorities in order to "protect the rights of depositors and policy holders", leading to a claim by the banks under the Bahrain-Iran BIT. State actions arising out of political instability have also led to recent claims by banks and financial institutions, such as an alleged breach of a BIT by Russia because it prevented the claimants from operating their banking business in Crimea. Expropriation claims have also arisen from instances of nationalisation and compulsory acquisition – for example a state's compulsory acquisition of the claimant's interest in certain loan and security agreements.

Investment treaty disputes in the life sciences sector

Investment treaty arbitration has only recently become a popular choice of forum for life sciences and pharmaceutical companies to protect their foreign investments. However, the potential benefit for these companies, which often invest abroad, is significant. BITs can be used to overcome unfair regulatory obstacles and political risks, as evidenced by several recent investment treaty arbitrations. To date, seven disputes brought by pharmaceutical companies have been publicly reported: three claims were brought under NAFTA by Apotex against the US, another NAFTA claim was brought by Eli Lilly against Canada, one claim was brought by Merck against Ecuador, another by Servier against Poland, and one by US and UK individuals against Kazakhstan.

Tribunals have considered the following life sciences and pharma investments to be entitled to protection: a registered trademark and a licence to use that trademark, and drug patents rights. Although there are no investment arbitration awards deciding this issue, the European Court of Human Rights held in *Anheuser-Busch v. Portugal* that applications to register trademarks are property rights and possessions within the meaning of Article 1, Protocol 1 of the European Convention on Human Rights.

In addition, in *Servier v. Poland*, the tribunal concluded that Poland frustrated the investor's legitimate expectations in relation to the cancellation of marketing authorisations. This led to an expropriation of the investment and discrimination against the pharmaceutical company in favour of local competitors. Likewise, in *Merck v. Ecuador,* a tribunal found Ecuador liable for a denial of justice in light of the treatment by its courts of the investor's refusal to sell a pharmaceutical factory to the Ecuadorian company NIFA.

Investment treaty disputes in the telecommunications sector

The telecommunications sector has been transformed over the past decade by privatisation, liberalisation, technological change and growth in demand. These trends have contributed to economic growth and improved sector governance, but they have also produced an increasing number and variety of investment treaty disputes, with a reported 53 investment treaty cases. Five percent of the cases registered and administered by ICSID in 2019 were disputes relating to 'information' and 'communication'.

In the telecommunications sector, the qualifying investment may consist of the rights acquired under a contract to obtain the necessary licences and other permits to establish, own and operate a telecommunications business in a host state territory. Other examples include the acquisition of a direct or indirect shareholding in a telecommunications company, rights under a concession agreement or licence for telecommunications services, issuing loans to a local company engaged in providing a cellular telecommunications network, and contractual rights to construct and operate a mobile phone network. Typical issues encountered include the termination of concessions and licences, the expropriation of assets, changes to the tariff regime, and discriminatory behaviour, for example relating to the renewal of licences. CD

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