

Investor-state arbitration and construction disputes

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What is investor-state arbitration?



What is investor-state arbitration?

- Arbitration between a company or individual investor against a state for breach of that state's obligations under international law to protect the investor's investment.
- An investor's right to bring a claim a state arises most commonly out of a bilateral or multilateral investment treaty ("BIT" or "MIT").
- A state is liable to pay an investor compensation for breaching the obligations set out in an applicable treaty.

International Framework

- Washington Convention on the Settlement of Investment Disputes between States and Nationals of Other States, 1965 (“ICSID Convention”).
- Creation by the World Bank of the International Center for the Settlement of Investment Disputes (“ICSID”) which provides arbitration rules for investment disputes.
- There are two main ways in which ICSID administers arbitrations:
 - Pursuant to the ICSID Convention, Regulation and Rules; or
 - Pursuant to the ICSID Additional Facility Rules.

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Investment Treaties



Investment Treaties

- An investor's right to bring a claim a state arises most commonly out of a bilateral or multilateral investment treaty.
- The United Nations Conference on Trade and Development ("UNCTAD") maintains a searchable database of BITs for each country.
- A BIT is a treaty between two states by which each state agrees to afford rights and protections to investors from the other.
- Rights and protections under an investment treaty apply regardless of whether there is a contractual relationship between the state and investor.

Common protections found in investment treaties

- Protection against unlawful expropriation or nationalisation
- Fair and equitable treatment (“FET”)
- Full protection and security (“FPS”)
- National treatment (“NT”)
- Most-favoured nation treatment (“MFN”)
- Umbrella clauses

Considering an investment treaty claim on an international construction project



What kind of investment treaty claims arise in the course of international construction projects?

- Claims under a relevant construction contract with the state where the state has failed to carry out its contractual obligations.
- Claims against the state for legislative changes, including changes to taxation or other industry regulations, which make the performance of a contract significantly more onerous.
- Claims for the expropriation of companies or assets.
- Claims against a state for the conduct of its public authorities if the actions of those authorities have adversely affected works under a relevant contract.
- Denial of justice claims where courts in the host state have, without lawful basis, refused to enforce a valid commercial arbitration award.

What conditions need to be met to commence a treaty claim?

- Is there a relevant BIT or other investment treaty in force between the host and the state in which the contractor is incorporated?
- Does the contractor qualify as an investor under the terms of the relevant treaty?
- Does the works contract qualify as an investment under the terms of the relevant treaty?
- For contractual claims, is the Employer a state or an organ of state?
- Has the Employer, as either a state or an organ of state, breached the obligations contained in the relevant treaty?
- Has that breach resulted in damage and/or loss to the contractor as an investor?

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Establishing Jurisdiction



Is there a relevant investment treaty in force?

- In which country do the works take place?
- In which country is the Contractor incorporated?
- Is there a BIT or other investment treaty in force between the two countries?
- Difficulties with intra-EU BIT claims

- If the claim is to be determined under the ICSID Convention, the parties must satisfy conditions for ICSID jurisdiction set out in Article 25(1) of the ICSID Convention which states:

“The jurisdiction of the Centre shall extend to any legal dispute arising directly out of an investment, between a Contracting State (or any constituent subdivision or agency of a Contracting State designated to the Centre by that State) and a national of another Contracting State, which the parties to the dispute consent in writing to submit to the Centre. When the parties have given their consent, no party may withdraw its consent unilaterally.”

- With reference to Article 25(1), the conditions for ICSID jurisdiction are:
 - There must be a legal dispute (which must be a dispute concerning the existence or scope of a legal right or obligation and not merely a conflict of interests);
 - That arises directly out of an investment;
 - Between a Contracting State and the national of a Contracting State; and
 - There must be written consent from both parties.

Is the Contractor an investor?

- Only an investor, as defined in a treaty, can bring an arbitration claim pursuant to that treaty.
- Investors can be companies incorporated in the investor's home state, or local subsidiaries, depending on the wording of the treaty.
- If the claim is to be determined under the ICSID Convention, the Contractor must also satisfy the ICSID definition of an investor if different from the treaty definition.

Is the construction contract an investment?

- An investment will be defined in the relevant treaty
- Treaty definitions commonly include:
 - tangible and intangible property
 - shares and bonds
 - licenses, IP and other concessions that might be required to construct and operate an infrastructure project

Defining an investor under the ICSID Convention

- Article 25 of the ICSID Convention does not provide a definition of investment.
- ICSID tribunals rely on the *Salini* test (from *Salini Costruttori SpA v. Kingdom of Morocco*) which considers whether the investment meets the following criteria:
 - Does it involves a contribution of money or other assets of economic value?
 - Is it for a certain duration?
 - Does it includes an element of risk?
 - Does it provides a contribution to the host state's development?
- If a project involves the contribution by a contractor of large sums, know-how and personnel over a significant period of time, this can be defined as an investment for the purposes of an investment treaty claim.

Is the Employer a state or an organ of state?

- In relation to contractual claims, the answer to this question is relatively straightforward when the Employer is a national government or ministry of the host state.
- Where the Employer is a publicly owned corporate entity, can it still be defined as an organ of state?
- A host state will be liable for the actions of an entity where:
 - those actions have been taken under the effective control of the state; or
 - where the state has had significant involvement in the commission of the act (*Jan de Nul v Egypt*).

Has the Employer, as host state, breached the obligations set out in an applicable treaty, and has that caused damage?

- Whether the Employer or host state is in breach of its treaty obligations requires an examination of the rights and protections offered by the relevant BIT or other applicable investment treaty:
 - Protection against unlawful expropriation or nationalisation
 - Fair and equitable treatment
 - Full protection and security
 - National treatment
 - Most-favoured nation treatment
- Whether the breach has caused damage is matter of causation assessed on a case by case basis.

Contractual claims as treaty claims

- Difference between contractual claims and treaty claims: domestic law v international public law
- To bring a claim under a treaty for breaches of a contract by a host state Employer, Contractors must either show that:
 - The actions of the host state that led to breaches of the parties' commercial contract also amount to breaches of its treaty obligations; or
 - An umbrella clause exists in the applicable treaty or can be imported via an MFN clause that can be used to elevate contractual claims to treaty claims.
- How is a claim relating to a contract generally dealt with by investment tribunals?

Contractual claims as treaty claims: umbrella clauses

- An umbrella clause is a provision of a treaty under which the host state guarantees that it will perform any obligations assumed in relation to the investor, including obligations assumed under a contract.
- Application of umbrella clauses in this way remains controversial.
- Clear language?
- Inconsistent approaches by tribunals, even where clauses have contained similar wording (*SGS v Philippines and SGS v Pakistan*)
- Broadly two lines of authority:
 - “Expansive” approach: umbrella clauses generally construed as extending to breaches of any obligation of a state in relation to the investment; and
 - “Restrictive” approach: umbrella clauses construed more narrowly.

Investment treaty arbitration: advantages



Advantages of investment treaty arbitration

- Self-contained regime:
 - Awards are final and binding and not subject to review by national courts unlike commercial arbitration awards.
 - Article 54(1), ICSID Convention requires Contracting States to enforce the award on presentation of a certified copy of the award by the Secretary General of ICSID
 - ICSID awards are enforceable in Contracting States in the same way as final judgments of the local courts.
 - ICSID awards are subject to the limited remedies set out in the Convention, including:
 - rectification;
 - interpretation;
 - revision; and
 - annulment.

Advantages of investment treaty arbitration continued...

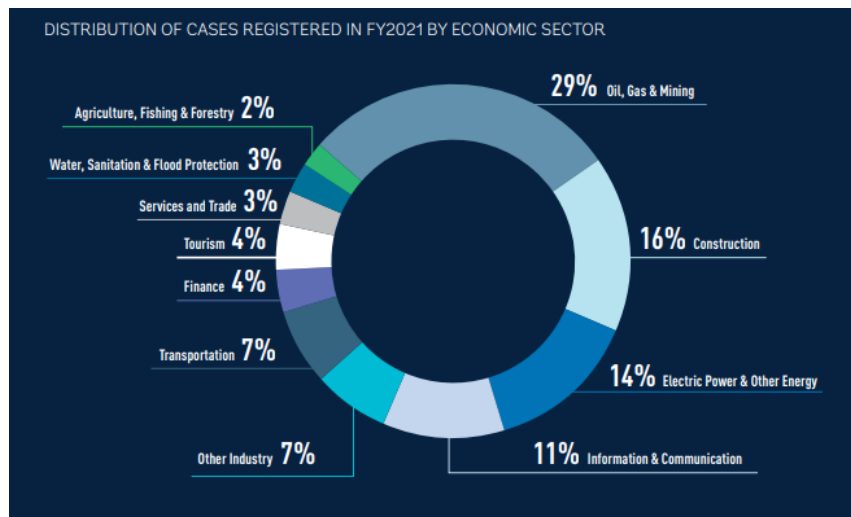
- Procedural law of the place of arbitration has no impact on proceedings;
- Appointment of arbitrators is overseen internally by ICSID; and
- The association with the World Bank may persuade otherwise reticent parties to comply with awards.

Some final thoughts and statistics



ICSID caseload and construction claims

- ICSID's annual caseload has been steadily increasing over the last decade from 172 cases in 2012 to 332 cases in 2021.
- A significant percentage of those cases (16%) relate to the construction sector:



Source: ICSID Annual Report 2021

Thinking about the possibility of investment treaty claims at procurement stage

- Hesitancy by contractors to bring claims because of the potential for jurisdictional issues arising where a contract exists between the parties.
- Contractors can maximise treaty protections at procurement stage by considering the corporate structure of the entity that carries out the works:
 - Incorporated v unincorporated joint venture?
 - Where to incorporate company or JV?
- ICSID statistics show a growth in investment treaty arbitration claims, including a growth in claims relating to the construction sector.

Thank you. Questions?

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