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## INTRODUCTION TO DISPUTE SETTLEMENT IN INTERNATIONAL TRADE AND FOREIGN DIRECT INVESTMENT

MALCOLM RICHARD WILKEY\*

### I. PREFACE

If anyone is looking for changes and trends in international or domestic arbitration, surely the first item to note is the sheer volume of activity in all areas of arbitration and dispute settlement. In the domestic arena this is seen as the byproduct of several decades of explosive growth in litigation coupled with the traditional government-run justice system's inability to handle the load in anything approaching a timely and cost-efficient manner. In the international sphere, the explosion is viewed as an inevitable result of the increase in trade,<sup>1</sup> to which should be added foreign direct investment and the discrediting and abandonment of such legal doctrines as the Calvo Clause by developing countries eager to leave the Third World and join the First. The First World has more fun—because it can pay for it.

The arbitration explosion has affected two groups—those who needed private dispute settlement and those who provided the requisite services. The established arbitration centers in Paris, London, and New York therefore expanded their capacities, while new dispute settlement organizations in growing centers of international trade, such as Miami and Los Angeles, were established. The service centers were following the clientele—how many multinational corporations established their international or Latin American division headquarters in the Miami area in the last twenty-five years?

Much of the clientele was new, and so were the arbitrators. Until the late 1970s, those frequently engaged as arbitrators were a lordly lot—partners in prestigious New York, Philadelphia, or London law firms, with a sprinkling of top law school professors with a reputation in transnational law or in this newly thriving business of “alternate dispute resolution.” Europe tended to prefer the professorial (“Herr Doktor”)

\* Retired U.S. Circuit Judge and former U.S. Ambassador. Judge Wilkey also served as one of the four U.S. delegates to the GATT Conference in Punta del Este in September 1986, which launched the Uruguay Round. Prior to his years on the D.C. Circuit, Judge Wilkey served as Assistant Attorney General of the United States and as General Counsel of Kennecott Cooper Corporation. He now engages in arbitration.

1. See generally Yves Dezalay & Bryant G. Garth, *Merchants of Law as Moral Entrepreneurs: Constructing International Justice from the Competition for Transnational Business Disputes*, 29 LAW & SOC'Y REV. 27 (1995).

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and high court judge type. Subsequently, a much younger group of practitioners entered the scene; they looked upon arbitration, mediation, and conciliation as their principal legal practice, either as counsel or as judge. This younger group also has narrowed their services to more precisely specialized areas.

The decade of the 1970s witnessed such discouraging events for foreign direct investment as the Allende confiscations<sup>2</sup> in Chile, the oil pricing crisis in the Middle East, and the beginning of the Iranian hostage crisis in 1979. While these events had an adverse effect on foreign direct investment, they encouraged use of forward-looking provisions in investment and trade contracts calling for arbitration if things went wrong.

In spite of—or perhaps because of—the spiralling price of oil, the 1970s and 1980s were marked by a huge increase in large-scale construction contracts in the Middle East. As a corollary effect of this phenomenon, U.S. multinationals increasingly felt a need to incorporate international arbitration clauses in their contracts. Moreover, the Arab world manifested a new willingness to accept these clauses. By the first year of the Reagan administration, the Iranian hostage crisis and the concomitant disruption of Iran's normal investment and trade relations had resulted in the establishment of the American-Iranian Arbitral Tribunal<sup>3</sup> at the Hague. The Tribunal has created the largest body of international arbitral contract law ever assembled, and in so doing it provided work for thousands of transnational lawyers.

The expansion of all private dispute settlement techniques has not slowed nor will it in the foreseeable future. The successful conclusion of the NAFTA, with the prospective inclusion of Chile, is more of an encouragement for foreign direct investment than for trade. Worldwide confidence in the stability of those countries admitted to this "Club" has been enhanced by the sheer fact of membership.

## II. KEY ELEMENTS OF DISPUTE SETTLEMENT MECHANISMS

Nevertheless, foreign direct investment is no doubt the area in which a previously agreed dispute settlement mechanism is most indispensable,

2. The Writer was General Counsel of Kennecott Copper Corporation until March 1970. Kennecott owned 49% of the El Teniente mine. We devised various legal protections for the Kennecott interest—but none that could stop a Marxist regime bent on outright confiscation.

3. The writer was named by President Reagan as one of the first three U.S. members of the Tribunal in April 1981. The plan was that he should take a leave of absence from the U.S. Court of Appeals and serve with the judicial salary only on the Tribunal—as Judge John Parker of the Fourth Circuit had done at Nuremberg—until the procedures of the arbitration had been well established, estimated at one-and-a-half to two years. However, the situation on the D.C. Circuit in 1981 did not permit this.

able, as the law of two or more sovereigns is involved. Even given the most honest intent and the most astute foresight, disputes still occur.

A lawyer's job is to create a workable mechanism that will serve the parties well in a practical manner when tested by ambiguity and/or disagreement. The parties must agree without reservation that the dispute settlement provisions adopted are fair, impartial, and practical. The provisions should also appear so to disinterested outside observers, to discourage any future effort to seek another forum.

Many checklists of essential ingredients constituting effective mechanisms have been drafted. These lists often start with the applicable substantive and procedural law governing the basic contracts. I would stress defining at the outset the composition of the ultimate arbitral panel that is to give the final answer when the dispute settlement mechanism is invoked. Assuming one or more members are named by each party, a party is wise to select the most prestigious and genuinely qualified candidate available. Assuming a party sincerely believes in his case, a highly competent person respected for his demonstrated impartiality and objectivity, who will likely make a logical, dispassionate and persuasive appraisal of the merits of each party's position, is a good bet not only to decide fairly but also to exercise considerable influence on the presiding neutral and on the member or members named by the other party.

The presiding neutral should be truly neutral, not only devoid of the interests and affiliations that would disqualify him in domestic arbitration but also selected from a region and culture different from that of the parties involved. Cultural ties run deep; regional politics, both national and professional, lurk under the surface of ostensibly even-handed diplomatic amenities. One disillusioning experience will be enough to convince anyone of the wisdom of the above advice.

## III. DISPUTE SETTLEMENT MECHANISMS AND THE PRIVATIZATION OF JUSTICE

Dispute settlement mechanisms allied to foreign direct investment illustrate at the international level the same trend toward privatization of justice seen in our domestic society. Private arbitral settlement of civil disputes of the commercial/contract type is highly developed in the United States and other western countries. Surely punishment of violations of public order (ancient breaches of the King's Peace) and all other criminal offenses will remain with the sovereign. But every aspect of civil justice seems susceptible to privatization in one mode or another.

Yet, as privatization of justice increases, does it begin to look, act, and

feel more and more like that expensive, dilatory, technicality-infested system at the government courthouse that we are desperately trying to avoid? The United States is reputed to be the most litigious society in the world, rivaling the medieval English system in its complex maze of procedural devices, where only *homo legalis* thrives. Some observers assert that the mass entry of Anglo-American practitioners into transnational arbitration has "banalized" and "judicialized" the process. "American style practice has taken off. . . . [with] more attention to fact, motions, objections, [and] delays. [Arbitration is] [b]eginning to look more like litigation."<sup>4</sup>

One bane which originally most arbitral rules either prohibited or severely discouraged was that great invention of the U.S. legal system: discovery. Federal and state laws on arbitration differ regarding the amount of discovery permitted, ranging from no or limited discovery to discovery as generous as permitted by state rules in court litigation. I have arbitrated under all three approaches. My belief is that the less discovery is allowed, the better for arbitration. When full state court-style discovery is permitted, the advantages of arbitration over regular judicial procedure in speed and cost seem slowly dissipated. Theoretically the parties could agree, either in advance or after the issues in dispute arise, to limit discovery irrespective of statute. It may be too late once specific disputes arise; one side may see an advantage in dragging out the proceeding just as in court. If pre-judgement interest is not likely to be awarded, and the sum involved is substantial, cold calculation may show the prospective loser that it is cheaper to pay the lawyers to do everything legal to postpone the day of judgement.

#### IV. OVERVIEW OF ARTICLES IN THIS ISSUE

This issue of *Law and Policy in International Business* gives us a rich lode of useful information and analysis to digest, both in the articles on foreign direct investment and dispute settlement and the articles on international trade dispute settlement.

##### A. *International Investment Dispute Settlement Procedures: The Evolving Regime for Foreign Direct Investment*

Thomas Brewer's *International Investment Dispute Settlement Procedures* winds up with a prediction that "there are likely to be new developments in international law as a result of increased interest in the treatment of

investment disputes," a forecast that I think is right on the money. While more contacts may produce more tensions and disputes, yet the creation of well-understood, civilized procedures for dealing with them must be a net plus. As we slowly shrink the areas in which the rule of law does not prevail, the world becomes a safer place—we hope.

Mr. Brewer is not only an expert navigator among the GATT, the WTO, the OECD, and the NAFTA, he also introduces us to TRIMs, GATS, TRIPs, DSU, and DSB. He notes that "disputes concerning foreign direct investments, as well as trade, will be subject to the new dispute settlement procedures embodied in the Uruguay agreements. The core . . . is established by the Dispute Settlement Understanding. . . ." The Dispute Settlement Body (DSB), as the highest level of the DSU mechanism, now must act *unanimously* to *reject* a decision reached at the lower two levels. Brewer quotes with seeming approval the assessment of another specialist that "whether dispute settlement works is going to be the litmus test of whether the WTO is seen as a success or failure." Since the breakdown of all dispute settlement could destroy the effectiveness of the WTO, this could well be true.<sup>5</sup>

The author then turns to the hemispheric trade organization under the NAFTA, which may be simply AFTA if Chile is admitted, where thus far investment disputes have taken a remote back seat to those involving trade. The encouraging note is that Mexico's acceptance of the Chapter 11(B) procedures represents an abandonment of the ill-starred Calvo doctrine. "This in itself is a major change in the international legal regime for FDI; to the extent that other Latin American countries follow Mexico's lead on this issue, it will obviously be yet more significant." For the countries desiring to join NAFTA (not all will), "the

5. While writing this essay, I encountered this editorial comment in *The Economist*:

Partly reflecting the pro-market shift in much of the Third World, the Uruguay Round lowered tariffs and other barriers to imports, and brought new areas of trade (notably agriculture) within the GATT's purview. *An institutional reform may be even more important.* From the beginning of 1995, the GATT's successor, the World Trade Organisation (WTO) will offer a far more powerful mechanism for resolving disputes over trade. Its findings on such disputes will be much harder to block than were the old arrangements (which, in effect, allowed the offending party to veto the procedure).

However, it remains to be seen whether governments will comply with these new rulings. . . . If governments do comply, the trading system will have what it has long needed: an arrangement for settling arguments over trade that is not subject to capture by protectionists. If they do not, the WTO may soon be defunct.

4. Dezalay & Garth, *supra* note 1, at 55.

*Battle Lines*, *ECONOMIST*, Dec. 24, 1994, at 13.

extent" will be one hundred percent; one does not join a club on the condition it change its bylaws.

On bilateral investment treaties (BITs), Brewer comments, "[t]he provisions of BITs concerning dispute settlement are widely considered to be among the most important means for prospective host governments to provide investors with an attractive investment climate." Now true, but *why* did it take developing countries so long to appreciate this? Enamored of the Calvo Clause and similar protectionist legal doctrines, many obstinately refused to consider language providing for international settlement that has long been accepted throughout the Western world. I am aware of one sequence of events in which the country desired a BIT but would not accept certain language in two clauses standard in the treaties that the United States was then negotiating. A year after the first exploratory contacts had ceased, the other government informed the United States that it could accept the language previously rejected only to be told that the United States was no longer making treaties on that basis. A year or two elapsed and the other government let it be known it would negotiate on the basis of the *new* U.S. treaty language, only to be informed that the U.S. standard BIT now contained different language. After a change in administrations, the other country finally negotiated and signed a BIT with the U.S. Why did this progressive country remain behind the curve of economic legal development? There are still obstacles of this type to be overcome.

Brewer rightfully praises the International Center for the Settlement of Investment Disputes (ICSID). The influence of first Broches and then Shihata in creating and fostering the ICSID has been enormous, much greater than its numerical caseload would indicate. Quoting another author, Brewer notes, "[r]ather, the criterion is whether ICSID contributes to an international ethos in which investment disputes are resolved as matters of principle and objectively, not [on the basis of] politics and influence."

Brewer also speculates as to "which multilateral institution(s) would be the most appropriate location(s) for further steps in the reform process" of FDI and related dispute settlement. From his excellent discussion we gather that they each have slightly different roles to play, and that each has a contribution to make. After listing a nine-point agenda for reform efforts, the author then suggests the possibility "to establish as soon as possible an inter-agency 'Working Group on International Direct Investment'" from the WTO, the OECD, the UNCTAD, the IMF, and the World Bank. Part of the group's mission would be to "explore the possibility of creating a comprehensive new organization

for FDI in the longer term." My reaction is, why do we need to amalgamate everything? Why not let these existing organizations, blessed with the agility and innovative capacity that their size confers compared to a monolithic structure, go ahead and "do their thing"? Each is probably at least partially in competition with one or more other agencies. Let experimentation sobered by competition prevail for many years. There will be refinements, and a healthy result will be reached through natural selection.

#### B. *Toward a General Agreement on the Regulation of Foreign Direct Investment*

Michael Geist's survey of national FDI codes has resulted in a useful piece, *Toward A General Agreement on the Regulation of Foreign Direct Investment*. Like Brewer, Geist sees the opportunity for a greater and therefore useful uniformity in FDI. Geist, however, treats a more limited sphere: the host government administration, the mechanics and time involved for approval of the FDI, and the equality of legal treatment. He eschews dispute settlement, investment incentives, and industry-specific regulations.

Geist refutes the common theory that even though FDI codes are now commonly recognized and accepted, there is still substantial disagreement on how to regulate FDI. His thesis is "that there has been such significant convergence on this issue, [regulation], both with respect to form . . . and to substance . . . that the basic framework for a General Agreement on the Regulation of Foreign Direct Investment GARFDI" is upon us. He buttresses his thesis by conducting a detailed analysis of the FDI codes of eleven diverse countries. The convergence of their rules and practices is certainly far greater than their apparent differences.

Geist establishes the importance of FDI by noting that it has been growing four times as fast as international trade. Slightly more than fifty percent of all international trade is believed to be between related companies, or "intrafirm" trade, which means there is a correlation between trade and investment. A related, overlooked phenomenon (and advantage to the host country) is the eagerness with which foreign investors lobby their home government for favorable policies toward the host state to protect their investments. We have already seen this pattern under the NAFTA from Mexico and now Chile. Host states are slowly being made to realize that the elimination of aberrant disincentives is a far quicker, and cheaper, way to attract FDI than structuring elaborate incentives. One example of such a measure from the NAFTA

stipulates "that national treatment be accorded to FDI originating from any of the three signatories. . . ."<sup>6</sup>

The extent of agreement found in the eleven countries is impressive and surprising. Geist states the most unexpected finding "is the degree to which the criteria used in the evaluation of FDI are similar . . . . The standardization in a GARFDI of the criteria for rejection would be extremely significant . . . ." Geist's overall findings indicate that

[s]tates such as the United States, the United Kingdom, and Argentina have established legal frameworks that create minimal bureaucratic interference and come closest to an unqualified national treatment principle. A second group of states, which includes Canada, Portugal, Poland, and Japan, have established legal frameworks that, while requiring prior approvals, pose few problems for investors and are only moderately restrictive. Even among the most restrictive states surveyed, including South Korea, Thailand, Mexico, and Nigeria, investment is encouraged, and their legal frameworks bear considerable resemblance to the other, more liberal states.

Based on the high degree of similarity across FDI codes, Geist concludes that ". . . a GARFDI may be easier to achieve than is commonly perceived . . . . [T]he existing similarities ensure that most states would need only minor adjustments to their policies in order to comply with the international standard." Geist's objective is limited, but it is important and perhaps achievable in a comparative short term.

One who seems to agree with Geist, but is thinking in much broader terms, is David L. Aaron, U.S. Ambassador to the OECD. In a recent editorial, he opened his article with the statement, "The U.S. believes that it is time to begin negotiating a multilateral investment agreement that would create a comprehensive set of rules liberalizing and safeguarding foreign direct investment. Our recent consultations . . . indicate that there is widespread agreement with this objective."<sup>7</sup> Aaron points out that FDI is growing much faster than foreign trade, yet foreign trade has GATT (WTO) rules while FDI has no multilateral rules. Goods and services from FDI equal \$6 trillion; the same value for trade is \$4 trillion.

The United States is both the largest source and largest recipient of

FDI; surely we have an equivalent stake in a comprehensive multilateral investment agreement (MIA) as a companion energizer and stabilizer to the GATT in the field of trade. Aaron reveals that an OECD proposal would cover three broad areas: first, rules ensuring open national investment regimes; second, strong MIA protection provisions covering repatriation of profits, free transfer of funds, and compensation in the event of expropriation; and third, and most important for our theme here, "a MIA should create a sound dispute settlement mechanism for resolving conflicts not only between governments, but between governments and investors."<sup>8</sup>

Aaron says the U.S. believes the OECD is the proper midwife for an MIA. Furthermore, ". . . the permanent nature of investment requires an OECD-type, rule-based approach backed by strong dispute settlement provisions rather than the adversarial request-and-offer approach typical of trade negotiations."<sup>9</sup>

Ambassador Aaron's column may well herald a deliberate official effort by the United States to achieve a multilateral investment agreement in the near future. How timely and fortunate that this special issue of *Law and Policy in International Business* is devoted to this and related themes.

### C. APEC and Trans-Pacific Dispute Management

Carl Green takes us to another arena in his article, *APEC and Trans-Pacific Dispute Management*. Gone are the comfortable common cultural grounds, particularly in law, which we take for granted in Europe and the Western Hemisphere, diverse as those regions are. This is a partial explanation as to why our most sharply contentious trade disputes recently have been with Japan, China, and Indonesia.

Green's article illustrates that Asians prefer vaguer, more "flexible" arrangements and informal processes. Not an altogether irrational approach. Most successful Western businessmen learn early in their careers that a deal is not worth getting into if it is not profitable for both sides, and that it may not be profitable for either side to enforce rigidly the stern terms of a contract once a situation drastically changes. And in treaty law, "Rebus Sic Stantibus" has long been recognized—and argued about.

But is formal arbitration "workable without established rules against which to judge compliance"? APEC's "Eminent Persons Group" thinks

6. The author cites to North American Free Trade Agreement, art. 1102, Dec. 17, 1992, U.S.-Can.-Mex. (entered into force Jan. 1, 1994), 32 I.L.M. 605, 613 (Dec. 8, 1992) [hereinafter NAFTA].

7. David L. Aaron, *After GATT, U.S. Pushes Direct Investment*, WALL ST. J., Jan. 18, 1995, at A18.

8. *Id.*

9. *Id.*

not, and so recommended a *voluntary* Dispute Mediation Service. Green considers the APEC recommendations inadequate to remedy the problems they address. "The main sources of concern . . . are not so much 'disputes' as they are *highly contentious negotiations*." In other words, there is not yet enough economic (and cultural) consensus and convergence to make feasible compulsory dispute settlements against fixed *agreed standards*. "Since leverage, rather than law, is the key to these disputes or negotiations, the United States will seldom be motivated to bring them before a voluntary mediation service."

My estimate is that, where billion-dollar FDI projects are concerned, something less ethereal than the recommended APEC "Voluntary Conciliation Service," which came out of the Bogor, Indonesia APEC conference, will be required. Obviously, the APEC states are not ready for GATT/WTO- or NAFTA-style dispute resolution panels (discussion hereafter about the article by Castel and Gastle raises the question: are we?). Large scale Western investors will want to "see it all in writing," especially the part providing a mechanism for interpretation and enforcement of the contract before a Western-style international arbitral tribunal.

In apparent agreement with the policy of Confucius, who said, "I try to make the people shun litigation," Green concludes that APEC's effectiveness is threatened, however, by rancorous disputes between Asian countries and the United States, but an APEC Dispute Resolution Mechanism is not the answer. What is needed is much more intensive efforts at policy harmonization on a regional basis.

#### D. *Policy Alternatives for Reform of the Free Trade Agreement of the Americas: Dispute Settlement Mechanisms*

Most of Charles Gastle's *Policy Alternatives for Reform of Dispute Settlement Mechanisms Under the NAFTA* is devoted to changing trade policy to avoid creation of disputes in the first place. A fundamentally sound approach, supported by much detailed analysis.

One significant point, and one that members of the NAFTA should keep in mind in their strenuous efforts to adjust matters among themselves, is that

Canada and the United States may have an interest in developing common policy initiatives as both have similar levels of economic development, regional diversity, and sectoral problems. They both face competition from Europe and Japan, which may have different industrial orientations relating to coopera-

tion and integration between industries and with respect to governmental support.

He quotes Lester Thurow, "the essential difference between the two forms of capitalism is their stress on communitarian versus individualistic values as the route to economic success—the 'I' of the America or the United Kingdom versus 'Das Volk' and 'Japan Inc.'"

Gastle's focus has one dangerous omission—the rest of the American hemisphere: ". . . the trend to regionalism is such that world trade may be carved up into three major blocks—Europe, North America, and Japan/the Pacific Rim." In South America, particularly in the Southern Cone countries of Chile, Argentina, and Uruguay, there has been an ongoing battle for decades between the individualistic philosophy of the Anglo-Saxon world and the statism of the old European order. Thanks to the strong revival of the free market faith in the United States, the Initiative of the Americas of the Bush and Clinton administrations, and the dramatic, undeniable example of what a free market economy can do in Chile with Pinochet and the "Chicago Boys" after 1976, we are about to win that battle. If we do not drop the "North" from the description of the three major trading blocs in our thinking and planning, we will forfeit half the hemisphere to the statist Europeans and Japanese.

One of Gastle's most interesting recurring themes is a comparison between the GATT (WTO) and NAFTA dispute settlement mechanisms. He argues that "[u]nless a significant difference exists between the FTAA and GATT dispute settlement mechanisms, the dispute should be submitted to the GATT, which is superior due to the inclusion of an appellate procedure and the greater pressure that the international community can place upon an FTAA party, and particularly the United States, to implement adverse findings. . . . FTAA mechanisms should only be utilized when there is a specific mechanism that provides a better system of remedies than the GATT."

One of his final conclusions is that the general dispute settlement mechanism of the NAFTA should not be utilized unless there is a substantial advantage over the GATT 1994 Understanding on Dispute Settlement. He suggests one advantage may be in enforcement. To avoid NAFTA tribunals creating differing interpretation of GATT principles, he favors letting GATT panels decide, but they should be empowered to apply any special rules available to NAFTA members. In sum, all dispute settlement among NAFTA members would go through GATT (WTO) tribunals, which would apply substantive and procedural

rules from the NAFTA where necessary. This might produce more consistent interpretations, but it appears to add complexity in an area where we are still trying to devise a system acceptable to the United States and Canada. It would be a hard sell to Congress.

It is clear where the U.S. would take dispute settlement: binding arbitration of some type, especially in investment and financial services disputes. Under Section B of NAFTA Chapter 11, a challenge can be brought pursuant to the ICSID Convention, the Additional Facility Rules of the ICSID, or the UNCITRAL Arbitration Rules. NAFTA Article 1134 gives interim measures of protection but no injunctive relief. A final award is limited to monetary damages—plus interest—or restitution under NAFTA Article 1135 (i). Enforcement can be through the ICSID Convention, the New York Convention, or the Inter-American Convention under NAFTA Article 1136.

Gastle argues persuasively that binding arbitration should be extended throughout the NAFTA, especially to anti-dumping and countervailing duty disputes before they reach the final stages calling for the present unsatisfactory two-tier adjudication by binational panels and extraordinary challenge committees. "There are many disputes that must be determined in accordance with an established set of objective principles or rules (scientific or legal), and these are appropriate for a process of adjudication that is binding upon the parties . . . . Disputes should be subject to a binding panel procedure if they involve a breach of NAFTA or GATT principles determined according to objective criteria, such as legal rules or accepted scientific or economic principles. Such disputes would include safeguard, antidumping and countervailing duty matters . . . determined according to the GATT 1994 Agreements and the complex system of domestic laws and rules that have been established."

Let's think about that a bit. "Objective criteria" are desirable, but they may be hard to establish. "Legal rules" may be clear to judges from one country, but not to judges from another country, as my recent experience in *Softwood Lumber III* attests. "Accepted economic principles" may look different from the point of view of the exporting or importing country. How will the ICSID or UNCITRAL rules deal with the NAFTA or GATT principles versus the "complex system of domestic laws and rules" established in each country? It would be well to take a good number of varied examples of disputes in the anti-dumping and countervailing duty area, run them through a theoretical arbitration procedure under designated rules, and see where we come out.

*E. Should the North American Free Trade Agreement Dispute Settlement Mechanism in Antidumping and Countervailing Duty Cases Be Reformed in the Light of Softwood Lumber III?*

This article, by Jean Castel and Charles Gastle, deals exclusively with trade dispute settlement under the FTA/NAFTA. In fact, it is largely a criticism of my dissent in *Softwood Lumber III*.<sup>10</sup> Four pages are devoted to a discussion of my colleagues' opinions, while twenty-eight pages are devoted to the dissent. One might thus deduce that the impact of the case is derived, in the opinion of the authors, not from the decision itself but from the dissent.

Tempting as it is to reply seriatim to their criticism, the writer cannot, for two reasons: first, by the Code of Conduct for Proceedings under the FTA, a member of an Extraordinary Challenge Committee "shall abstain from any disclosure concerning the proceeding or the panel's deliberations . . . . Except as authorized by law, a member or former member shall not disclose the deliberations of a panel or committee, or any member's view, even after the proceeding has been completed."<sup>11</sup> Second, the criticism is so lengthy that there is no room here for reply, nor would it be worth it to the reader. If a reader has the time and interest to digest the Castel-Gastle article, he may also find the original, dissenting opinion rewarding.

I do not interpret the Code of Conduct to forbid reference to the published opinions themselves; hence, I wish to correct a few misconstructions and errors in the Castel-Gastle article relevant to the future structure of FDI dispute settlement mechanisms.

My first concern is the authors' indiscriminate use of the word "bias." Article 1904 (13) of chapter 19, under which the extraordinary challenge was brought, provides as a ground of such review that "(a) (i) a member of the panel was guilty of gross misconduct, bias, or a serious conflict of interest, or otherwise materially violated the rules of conduct." However loosely the word "bias" may have been thrown around in preliminary discussions between the parties, even in oral arguments, the United States did *not* charge "gross misconduct, bias." As stated in my opinion, "[o]n 6 April 1994 the United States filed a formal Request for an

10. In re Certain Softwood Lumber Products from Canada, No. ECC-94-1904-01USA, U.S.-C.F.T.A. Binat'l Panel Rev., 1994 FTAPD Lexis 11, \*123 (Aug. 3, 1994) [(Wilkey, J., dissenting) hereinafter *Softwood Lumber III*].

11. United States-Canada Free Trade Agreement—Code of Conduct for Proceedings Under Chapters 18 & 19, reprinted in 2 NORTH AMERICAN FREE TRADE AGREEMENTS—TREATY MATERIALS Booklet A.5, at 4 (James R. Holbein & Donald J. Musch eds., Oceana Publications, Inc. 1993)

Extraordinary Challenge Committee. Count One of the allegations of grounds for relief is 'Material breach of the Code of Conduct and Serious Conflict of Interest.' The allegation of material breach of the Code of Conduct applies to both [Panelists], the serious conflict of interest only to Panelist . . ."<sup>12</sup> In spite of their occasional reference to "bias," both Judge Hart<sup>13</sup> and Judge Morgan<sup>14</sup> flatly stated that the United States had not charged "bias" under Article 1904 (13).

Second, the authors' constant linkage of their concept of "bias" with what they term "the role of nationality" creates a totally erroneous impression of the rationale of my opinion. In that part of my opinion dealing with conflicts of interest there is no mention of any peculiarly U.S. or Canadian point of view on these matters. The conflicts were of the type that could have arisen in any U.S. firm. The question was, when the United States finally became aware of them, could the United States require the two panelists to step aside.

My discussion of the divergence between Canadian and U.S. law that produced the decision in this case (characterized by the authors as "nationality") is confined exclusively to the first part of my opinion, dealing with substantive and procedural review of administrative agency action, summarized in three basic points.<sup>15</sup> The authors assert that "there was no argument made relating to the issue of nationality." U.S. counsel probably never dreamed that two judges could write opinions of fifty-four and thirty pages and never once mention the legislative history of the FTA and the NAFTA. The authors refer to "the problem of nationality" and assert that "[Judge Wilkey] is wholly on his own on this issue." Not exactly alone. As is crystal clear in my opinion, my interpretation of the FTA is squarely in accord with the Senate Joint Committee Report (six committees and seventy-five individual Senators) and the House Ways and Means Committee Report (representing the nine committees of the joint referral).

My confidence in the impartiality and high professional skills of Canadian judges was reinforced by my work with my two Canadian colleagues. My confidence in the ability of Canadian or any other foreign judges to divorce themselves from their lifetime experience with their own national law (which on judicial review of administrative agency action and use of legislative history seems diametrically opposed to U.S.

12. *Softwood Lumber III*, 1994 LEXIS FTAPD 11, at \*123, \*223.

13. *Id.* at \*61-62.

14. *Id.*

15. *Id.* at \*124-26.

law) was considerably diminished. Therein lies the danger for the future.

Third, some of the authors' comments were both amazing and amusing to me. They are relevant because they reveal the gulf between at least some Canadians' practices and points of view and the U.S. perspective.

After citing my summary three points (referred to above), the authors find it a problem that "[t]here are a number of instances where Judge Wilkey's dissenting opinion goes far beyond the arguments made before the Committee." Skipping a refutation to the "far beyond" characterization, why is this a "problem"? If a court or single judge has a different insight from that of counsel, is he restrained from expressing it? Indeed, is it not the duty of the judge to bring all his life experience and power of reasoning to bear to decide the case?

The authors also assert that "[t]he concept . . . was never mentioned in argument. At no time did Judge Wilkey put the question to Canadian Counsel, notwithstanding the fact that the Canadian brief squarely addressed the issue." The issue was in the Canadian brief; it was never raised by Canadian Counsel, and Judge Wilkey is at fault for not bringing it up in oral argument? A judge is obligated to dialogue with each counsel on every issue? Or only those issues he later chooses to discuss in an opinion? I confess that I came to oral argument without an opinion previously prepared, and that my view of which concepts and which issues needed to be discussed in an opinion evolved slowly over the next few weeks, as the result of intensive but civilized discourse in person and in writing. This is the way U.S. courts do it, and based on my experience with my Canadian colleagues, despite the authors' criticism, I believe so do Canadian courts.

Finally, the authors argue that "Judge Wilkey did not respond [at oral argument] to Counsel's submission, giving no opportunity for a response to the potential importance of [two congressional committee reports]." The authors state that "[i]t is only Judge Wilkey who boldly pronounces that [the reports] must be given significant weight and does the legal research upon which he attempts to prove his point." Again, the theory that each judge must respond at oral argument to every proposition advanced by counsel is foreign to my experience.

To the contrary, the authors' criticism that I did the research myself<sup>16</sup>

16. I was blessed with an extremely competent research assistant with a newly-minted graduate degree in International Law, Miss Marianna Rubino. To her is due much of the credit for unearthing relevant authority not fully developed by counsel.

reflects exactly what I have done during my entire career on the bench<sup>17</sup> and in arbitration. More logically, the authors might have chided U.S. counsel for not making more out of a very strong point. Yet, this would have been unfair, as both the U.S. Trade Representative and the Coalition did cite the congressional reports and could hardly have imagined that judges required to apply U.S. law could have found it possible to completely avoid mentioning the reports. I do plead guilty to doing research myself and finding authority relevant to the issues not cited by counsel.

My conclusion on the Castel-Gastle article is that the mass of criticisms aimed at my dissenting opinion in *Softwood Lumber III* adds up to the identical conclusion to which I regretfully came: that the experience, practice, customs, substantive and procedural law of Canadian judges and practitioners are sufficiently different from those in the U.S. to make it extremely difficult for them to apply U.S. law as the FTA commands. And in a reverse situation the same might be true of U.S. judges and practitioners trying to apply Canadian law.

Finally, on the Castel-Gastle article, after nearly thirty pages devoted in greater part to the dissenting opinion in *Softwood Lumber III*, the recommendations for reform of the NAFTA dispute settlement mechanism and the authors' conclusion seem to recognize the realities that my dissent sought to bring to light. They note that "[i]nconsistency between

17. In my second year on the D.C. Circuit, I was confronted with a case in which I could subscribe to the arguments of neither party. In *Mayers v. Ridley*, 465 F.2d 630 (D.C. Cir. *en banc*, 1972), one side argued that the deed recording law of the District of Columbia permitting (requiring) the recording of deeds including a racial covenant violated various constitutional provisions, the other that the law simply required recording of a title document with no constitutional overtones involved. The idea was never broached in brief or in oral argument, but it occurred to me that there was a simple statutory ground for forbidding the Recorder of Deeds from accepting deeds containing racial covenants. The sole purpose of recording is to "publish," give "notice," to "print"; it has no function in making the conveyance effective between the parties, or so I had been taught in Property I. Those precise acts, to "print," to "publish," to give "notice" of racial covenants in regard to the sale of a dwelling were prohibited by the Fair Housing Act of 1968. So there was a federal statute squarely forbidding the Recorder from publishing, printing, or giving notice of a deed containing a racial covenant. No dubious constitutional theories were needed to stop recording racial covenants in D.C. My colleagues Carl McGowan and Harold Leventhal joined my opinion, no part of which had been briefed or argued. The vote was 6-4, three judges reaching the same result as we on constitutional grounds.

In *Vaughn v. Rosen*, 484 F.2d 820 (D.C. Cir. 1973) the court was confronted with a complete impasse under the Freedom of Information Act. After argument we devised and required a system of indexing, never suggested by the parties, which made the statute work. In *Nixon v. Sirica* (White House Tapes) 487 F.2d 700 (D.C. Cir. *en banc* 1973) all the judges who wrote opinions delved deeply into constitutional sources, going far beyond materials and arguments advanced by very able counsel.

My list of such cases is endless. It's an old American custom.

panel determinations brings the entire process into disrepute . . . . Strengthening the powers of review of the extraordinary challenge committees is one way of addressing this issue." I expressed the fear that the ECCs were being reduced to "judicial eunuchs." Perhaps we can now get back to what the U.S. Congress and I thought ECCs were supposed to do all along.

## V. CONCLUSION

The dispute settlement provisions of the NAFTA and its predecessor, the U.S.-Canada Free Trade Agreement, are an unusual hybrid. Nearly all international agreements to arbitrate, whether made in advance of or after the particular dispute arising, contemplate domestic administrative and judicial action running its course, then putting the ultimate questions left unanswered or unagreed to in the hands of an international panel customarily headed by a neutral person. Not so with the NAFTA dispute settlement mechanism.

The NAFTA formula in effect lops off the two (or three) top tiers of the U.S. administrative-judicial process and substitutes first, a five-person Binational Panel of trade law experts and, second, a three-person Extraordinary Challenge Committee. The members of each are exclusively from the two countries concerned; there is no neutral presiding. These two tiers of review of administrative action replace, in the U.S. system, the Court of International Trade, the U.S. Court of Appeals for the Federal Circuit, and, possibly, by certiorari, the Supreme Court.

What we have done, then, is to introduce a species of international arbitration at a very early stage in the development of the controversy. While the Department of Commerce determination is the product of lengthy hearings and briefings within the Department, it is still the "raw" product of the U.S. administrative system. No U.S. judge, with the detached impartiality given by an appointment for life under Article Three of the Constitution, and with the expertise in the field of trade law acquired during years of experience by the judges of the Federal Circuit and the Court of International Trade, has had a look at the case.

U.S. judicial review of administrative action is a refining process. The court concentrates on agency action tested by due process, correct and consistent interpretation of substantive law applicable to the agency, correct and consistent application of agency regulations, and compatibility of agency regulation with law. Careful review by a court may place agency action in a new light. All this is missing when the ad hoc binational tribunals of the NAFTA take the raw, unjudicially processed agency action of the Commerce Department to review under U.S. law.

While an arbitration process can, by agreement of the parties, be brought in at any stage of the dispute, my experience and observation has been that disputes with an international flavor are better brought to an international tribunal after they have been ripened either by careful negotiation between the parties or by exposure in domestic courts. When we on the five man Bryan-Suarez Commission (U.S.-Chile) took the Letelier-Moffit assassination problem, the issue had been reduced to the amount of damages, which Chile had agreed to pay without any admission of responsibility. Similarly, in a recent commercial arbitration, the parties had, by highly intelligent and careful negotiation, without recourse to any court, reduced the issue to a single figure, the base price to be charged. As the contract had ten years to run, that single sheet of paper with a single figure signed by the three of us carried an award of tens of millions of U.S. dollars.

All this refinement process has been missing in the cases before the ad hoc tribunals created under the dispute settlement mechanism of the U.S.-Canada Free Trade Agreement. This is especially important because under the Canada Agreement and the NAFTA, the law of the country whose administrative action is being challenged applies; so far only U.S. law has been at issue in three ECC cases. Perhaps the ad hoc tribunals would have benefitted by previous judicial review in the United States, and if that had been provided for, the ad hoc tribunals would likely have been differently constituted.

Differently constituted they must now be. The ingenious Chapter 19 binational substitute appellate scheme had three underlying assumptions, or justifications, and they have all three disappeared.

First, the scheme was to be temporary, to last only five years, during which time the two parties would negotiate substantive agreement on AD/CVD rules. Negotiations have failed. There has been no substantive agreement. Yet the arrangement has been tacitly continued.

Second, the arrangement was to apply only to Canada, where the assumed convergence of Anglo-Saxon legal principles would make easy the interpretation and application of the domestic law of one country by judges of another. How well this has worked can be measured by laying the Senate and House Reports on NAFTA side by side with the opinions of the two Canadian judges in *Softwood Lumber III*. In fifty-four and thirty-one pages the legislative history is never mentioned; the interpretation is squarely contrary to that of the Ways and Means Committee of the House and six committees of the Senate (seventy-five senators without a dissenting view). Canadian jurisprudence does not rely on legislative history. Mexico is now in, and Chile likely will be, both civil law countries. The assumed similarity is no longer mentioned.

Lastly, Chapter 19 could be justified in 1987 and 1993 by the fact that there was no readily available alternative. This is no longer true. *The World Trade Organization* with its Dispute Settlement Understanding came into force in January 1995. The WTO provides substantive obligations with regard to AD/CVD. The WTO has a Dispute Settlement Mechanism that provides a two-tier, truly neutral system for adjudicating with finality trade disputes. The three member panel of neutral "qualified persons" and then the three judge panel are not to adjudicate domestic law, but to determine if the action taken violates an international obligation assumed by one of the parties. U.S. courts would thus have the chance to review administrative agency action in customary fashion, before any remaining issues of obligations assumed under the WTO would be turned over to the international WTO tribunals. The United States, Canada, Mexico, and Chile are all signatories to the WTO.

Why continue asking foreign judges to interpret U.S. domestic law under Chapter 19? Or plan to send U.S. judges to Mexico or Chile to tell them what their domestic (civil code) law really means? Looking at the recent past with Canada, can anyone sincerely believe that Chapter 19 will work well with Mexico and Chile? Why not accept for the NAFTA the substantive AD/CVD obligations and the Dispute Settlement Understanding that all four Parties have already accepted in the WTO?

**INTERNATIONAL INVESTMENT DISPUTE  
SETTLEMENT PROCEDURES: THE EVOLVING  
REGIME FOR FOREIGN DIRECT INVESTMENT**

THOMAS L. BREWER\*

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\* Associate Professor, Georgetown School of Business. PhD, University of Michigan. The author is indebted to John Barton, George Coombe, John Garrity, Edward Graham, Stephen Guisinger, Harry Inman, Robert Patterson, Michael Ryan, and Jeffrey Snyder for helpful discussions concerning the focus and scope of the research. Bruce Duncombe, Marie-France Houde, Harry Inman, DeAnne Julius, Robert Ley, Ann Main, Adrian Otten, C. Christopher Parlin, Eney Quinones, and Daniel Wagner made specific suggestions for improving an earlier draft. Many other people were also helpful in various stages of the research: Rolf Alter, John Dealy, Persephone Economou, Richard Eglin, Stephen Gibson, Carl Green, Geoffrey Hamilton, David Hartridge, Dominique Hascher, Johnny Johansson, R. Sergei Kouzmine, H. Roemer McPhee, Hamid Mamdouh, Peter Morrison, Andrew Murphy, Jr., Stanley Nollen, Antonio Parra, Barbara Peitsch, Dennis Quinn, Kathleen Reddy, Frieder Roessler, Alan Rugman, Mary Ryckman, Eugene Salorio, Karl Sauvart, Stephen Schneebaum, David Shark, Andy Shoyer, Kenneth Thomas, B.W. Vigrass, James Waller, Gerald West, William Witherell, Lloyd Wright, and Stephen Young. The research was supported by grants from the Center for International Business Education and Research and the School of Business at Georgetown University, and it was facilitated by joint research on FDI issues with Stephen Young while I was an International Visitor at the University of Strathclyde. Lauren Richards provided excellent research assistance.

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## INTRODUCTION

The Uruguay Round agreements<sup>1</sup> have refocused attention on international institutional arrangements for dispute settlement in international business. Since the new dispute settlement procedures of the World Trade Organization (WTO) encompass investment disputes as well as trade disputes, it is important to examine existing and prospective international institutional arrangements for the settlement of investment disputes. This Article analyzes such procedures within the context of the evolution of the larger regime of international institutional focuses on "direct investments" as opposed to "portfolio investments," and it is therefore concerned with investments involving substantial ownership by a parent firm in one country of an affiliated firm in another country. Direct investments involve international business relationships in which a parent firm has a "lasting interest" and "a significant degree of influence" in the management of an affiliated foreign firm.<sup>2</sup> The term "investment" is thus used throughout this Article specifically to mean foreign direct investment (FDI).

During the past decade, FDI has grown substantially in most regions of the world. In fact, the rate of increase in world-wide FDI flows substantially exceeded the rate of increase in international trade during

1. Final Act Embodying the Results of the Uruguay Round of Multilateral Trade Negotiations, April 15, 1994, reprinted in THE RESULTS OF THE URUGUAY ROUND OF MULTILATERAL TRADE NEGOTIATIONS (GATT Secretariat 1994) [hereinafter RESULTS OF THE URUGUAY ROUND]. Portions of the Final Act also appear in General Agreement on Tariffs and Trade: Multilateral Trade Negotiations Final Act Embodying the Results of the Uruguay Round of Multilateral Trade Negotiations, April 15, 1994, 33 I.L.M. 1125.

2. INTERNATIONAL MONETARY FUND (IMF), BALANCE OF PAYMENTS MANUAL ¶¶408, 415 (1977); OECD, DETAILED BENCHMARK DEFINITION OF FOREIGN DIRECT INVESTMENT ¶¶4-5 (1992). There is a statistical issue raised by the distinction between direct investments and portfolio investments, namely, the percentage of ownership that should be used as a threshold below which investments are treated as portfolio investments and above which they are treated as direct investments. In practice, countries use different thresholds, with 10% being the most common (e.g., the United States) but 25% also being used by some countries (e.g., Germany). Although this inconsistency among countries is disquieting in the abstract, it is of little real consequence since there are relatively few cases of foreign ownership between 10% and 25%.

many of the years since the mid-eighties. Total world FDI flows increased from US\$88 billion in 1986 to US\$234 billion in 1990—an average annual rate of increase, in nominal terms, of twenty-six percent over the period (or eighteen percent in real terms).<sup>3</sup> The increases in outward FDI from Japan and inward FDI into the United States during the latter half of the eighties were particularly conspicuous. While annual inward flows to the United States, as well as total world flows, have been at lower levels since 1991, the proportion channeled to non-OECD countries has increased. FDI in China has increased dramatically, and intra-regional FDI in Southeast Asia has been substantial. In Latin America, the level of annual inward FDI flows has also returned to previous levels after several years of decline during the external debt crisis in the eighties. In selected countries of Central and Eastern Europe and the former Soviet Union, despite current uncertainties that inhibit investment activity, FDI is likely to increase significantly in coming years as well.<sup>4</sup>

These changes in the magnitude and geographic distribution of FDI are likely to result in increases in investment disputes between governments, between firms and governments, and between firms. This is especially true in the countries of Central and Eastern Europe, where much FDI to date has taken the form of rapidly concluded agreements in the midst of revolutionary privatization programs and changing political circumstances. Moreover, the elementary and evolutionary nature of property rights laws, plus the relative inexperience of both host governments and investors with FDI projects in the region, suggest that investment disputes will be relatively common in those countries. In the Pacific Rim region, differences in Asian and Western legal cultures make agreement on dispute resolution procedures unusually difficult; the former emphasizes the importance of flexible procedures and ad

3. DeAnne Julius, *International Direct Investment: Strengthening the Policy Regime*, in MANAGING THE WORLD ECONOMY 269, 276 (1994); U.N. TRANSN'L CORPS. AND MGMT. DIV., WORLD INVESTMENT REPORT 14 (1992).

4. Actual FDI flows to the countries of Central and Eastern Europe and the former Soviet Union have lagged behind expectations, but the number of formal "registrations" of anticipated FDI projects has already become large. According to an estimate of the United Nations Economic Commission for Europe (UNECE), there were 72,334 such registrations totaling US\$ 13.8 billion as of April 1, 1993. This is an unofficial estimate appearing in a preliminary undated table generated by the Trade Division of the UNECE. Most of these projects, however, are quite small, and only a small percentage of them may be implemented. For a list of large projects that have already been implemented, see 14 E.-W. INVESTMENT & JOINT VENTURE NEWS 19-23 (1992); see also OECD, FOREIGN DIRECT INVESTMENT (FDI) IN FOURTEEN CENTRAL AND EASTERN EUROPEAN ECONOMIES IN TRANSITION (1992); Thomas Brewer, *Indicators of Foreign Direct Investment in the Countries of Central and Eastern Europe and the Former Soviet Union*, 3 TRANSN'L CORPS. 115, 126 (1994).

hoc, adaptive resolution of disputes, while the latter emphasizes the establishment of extensive formalized rules that can be applied to individual disputes.

Any significant growth in the number of unresolved investment disputes could be highly detrimental to the future of FDI flows throughout the world, and such disputes could also cause strains in diplomatic relations between governments. As a consequence, investment dispute settlement procedures will take on greater importance, and the existing system of institutional arrangements will be under much more detailed and critical scrutiny.<sup>5</sup>

Recent publications reflect the resurgence of interest in strengthening investment dispute procedures in international institutions. Such procedures are central in multilateral approaches to reforming the international regime for FDI; one such approach has been proposed by Bergsten and Graham and another by Julius. In a wide-ranging outline of potential elements in an FDI regime, Bergsten and Graham<sup>6</sup> suggest that any new accord "must . . . provide for an effective means to settle

5. Two rationales for strengthening the international regime for foreign direct investment, including dispute settlement procedures, are analogous to those for the existence of an international trade regime. The first is that international agreements and accompanying institutional arrangements create pressures for an open, liberal world economic system that is conducive to a more efficient allocation of scarce resources than would be obtained in a system dominated by national barriers to international economic transactions. Second, to the extent that an international regime creates a more stable and transparent legal and institutional framework, it facilitates international investment by reducing investors' (and governments') uncertainties about the future policy environment. There is of course a paradox in these twin rationales: the process of creating a new regime in itself creates uncertainty about the policy environment. However, this is an unavoidable short-term cost that must be borne for the sake of the longer-term gains once the new system is in place.

There are two additional general rationales, which are based more on political, legal and philosophical grounds; they also pertain to international agreements concerning investment and trade alike. The first is that processes and institutions that facilitate international cooperation and constrain international conflict are inherently desirable. For, just as efficiency is a widely accepted criterion for evaluating economic processes and outcomes, cooperation is a widely accepted criterion for evaluating political processes and outcomes. The second is that the advancement of the rule of law at the international level is desirable as a way to counter the anarchic tendencies of a decentralized international political system of legally sovereign nation states.

Extensive analyses of the more general topic of international legal and institutional arrangements concerning foreign direct investment (including, in particular, its promotion) are provided by F.I. Shihata, *Promotion of Foreign Direct Investment—A General Account, with Particular Reference to the Role of the World Bank Group*, 6 ICSID REV. 484 (1991); GEORGE SCHWARZENBERGER, *FOREIGN INVESTMENTS AND INTERNATIONAL LAW* (1969); *FOREIGN INVESTMENT IN THE PRESENT AND A NEW INTERNATIONAL ECONOMIC ORDER* (Detlev C. Dicke ed., 1987).

6. C. Fred Bergsten & Edward M. Graham, *Needed: New International Rules for Foreign Direct Investment*, 7 INT'L TRADE J. 15, 29 (1992).

disputes both between governments and between international corporations and governments." Julius similarly considers effective dispute settlement procedures to be crucial to any new multilateral arrangements for FDI, and she has suggested specific reform measures based on current institutional realities and international FDI regimes in previous eras.<sup>7</sup> (Both the Bergsten-Graham and Julius proposals are discussed in detail in Part III below.) There is, therefore, heightened interest in initiatives to strengthen investment dispute settlement procedures and increased activity on the issue in international organizations.

Dispute settlement procedures concerning inter-government, firm-government, and inter-firm disputes are included in the present Article. There has been a degree of institutionalized specialization of function in terms of these three types of disputes, but a comprehensive understanding of the entire international regime for investment dispute settlement requires an examination of the institutionalized procedures for all three types of disputes.

Part I of the Article briefly reviews the widespread changes in attitudes and national policies toward foreign direct investment that have taken place in recent years. International institutional developments are reviewed in Part II. Plausible scenarios for the future evolution of the international regime are developed in Part III, followed by concluding comments.

### I. CHANGING PERSPECTIVES AND POLICIES

Twenty-five years ago, this journal published an important and widely-cited article by Goldberg and Kindleberger titled *Toward a GATT for Investment: A Proposal for Supervision of the International Corporation*.<sup>8</sup> The article argued that new multilateral institutional arrangements were needed for "the problem of the regulation of the international corporation,"<sup>9</sup> and it "called for a forum for the problems related to the international corporation and some procedures which could embrace dispute resolution . . ."<sup>10</sup>

Since that article, numerous scholars and organizations have discussed the possibility of developing new international institutional and

7. Julius, *supra* note 3; see also DEANNE JULIUS, *GLOBAL COMPANIES AND PUBLIC POLICY: THE GROWING CHALLENGE OF FOREIGN DIRECT INVESTMENT* (1990) [hereinafter JULIUS, *GROWING CHALLENGE*].

8. Paul M. Goldberg & Charles P. Kindleberger, *Toward a GATT for Investment: A Proposal for Supervision of the International Corporation*, 2 LAW & POL'Y INT'L BUS. 295 (1970).

9. *Id.* at 322-23.

10. *Id.* at 322.

legal arrangements concerning the foreign direct investments of corporations. Thus, Bergsten envisioned a "truly new economic order" designed to constrain conflicts concerning investment among home governments, host governments, and international firms.<sup>11</sup> The American Society of International Law suggested that an expanded world trade agreement, built on the GATT, should also include provisions concerning FDI.<sup>12</sup> Whitman briefly referred to the possibility of including FDI in a revised GATT system.<sup>13</sup> Vernon called for a comprehensive set of international codes that would place strict limitations on the behavior of home and host governments regarding preferential treatment of international firms.<sup>14</sup> In a presentation of the outlines for a new Production and Trade Organization, Camps included provisions concerning FDI.<sup>15</sup> The Committee for Economic Development also called for new international institutional arrangements that would liberalize national FDI policies.<sup>16</sup>

Dunning anticipated the creation of a new international institutional framework for FDI as follows:

[I]t seems likely that the response to international business from [governments] and international organizations will increasingly parallel that toward trade, and that, in due course, similar mechanisms will be devised to provide an orderly framework for international production and resource transference, as GATT provides for trade in goods.<sup>17</sup>

More generally Barton and Carter<sup>18</sup> have discussed the need for further

institutional development on the part of international economic organizations in order to more successfully meet the challenges posed by a variety of changes in the world economy.

Recently, there have been important developments within several international organizations reflecting such concerns, and there has been a concomitant resurgence of interest in additional reforms of international institutional arrangements. However, the terms of the discussion and reform efforts have shifted in recent years; whereas the emphasis was previously on regulating corporations, the emphasis now is on liberalizing government policies.

There are several reasons for this shift in emphasis. Host government policy-makers who previously focused on regulating FDI are now more concerned with attracting FDI. This attitude adjustment has been illustrated by the tangible liberalization of FDI policies by many host governments, particularly among developing countries.<sup>19</sup> However, at the same time, attitudes in the United States have shifted in the opposite direction. The large increases in FDI into the United States during the latter half of the eighties prompted public and congressional concern about the implications for the competitiveness of U.S.-owned firms and technology transfers. In response, there has been increasing interest in international institutional initiatives that would take advantage of the more liberal attitudes and policies of developing countries while at the same time resisting the opposite shift in the United States. These shifts in perspective simultaneously have presented an opportunity and a need for reform in international institutional arrangements.

In addition, among academic specialists, the shift in emphasis from regulating corporations to liberalizing government policies reflects a change in theoretical thinking about foreign direct investment. In the earlier period, academic thinking reflected an emphasis on the inefficiencies and economic rents associated with the foreign direct investment behavior of firms in oligopolistic industries. In recent years, this focus on the undesirable features and consequences of FDI has been largely supplanted by a different theoretical emphasis, which focuses on the efficiency gains of FDI as a way to circumvent the inefficiencies due to naturally-occurring and government-created market imperfections associated with international trade and licensing.<sup>20</sup> The foreign direct

11. C. Fred Bergsten, *Coming Investment Wars?*, 53 FOREIGN AFF. 135, 152 (1974).

12. PANEL ON INT'L. TRADE POL'Y & INSTITUTIONS, AM SOC'Y OF INT'L LAW, RE-MAKING THE SYSTEM OF WORLD TRADE: A PROPOSAL FOR INSTITUTIONAL REFORM 17-18 (1976).

13. See generally MARINA VON NEUMANN WHITMAN, *SUSTAINING THE INTERNATIONAL ECONOMIC SYSTEM: ISSUES FOR U.S. POLICY* (1977).

14. See generally Raymond Vernon, *The Multinationals: No Strings Attached*, 33 FOREIGN POL'Y 121 (Winter 1978-79).

15. MIRIAM CAMPS, *THE CASE FOR A NEW GLOBAL TRADE ORGANIZATION* (1980); subsequently published as a chapter in MIRIAM CAMPS & CATHERINE GWINN, *COLLECTIVE MANAGEMENT: THE REFORM OF GLOBAL ECONOMIC ORGANIZATIONS* (1981). See also MIRIAM CAMPS & WILLIAM DIEBOLD, JR., *THE NEW MULTILATERALISM: CAN THE WORLD TRADING SYSTEM BE SAVED?* (1983).

16. PROGRAM COMMITTEE, COMMITTEE FOR ECONOMIC DEVELOPMENT, *FOREIGN INVESTMENT IN THE UNITED STATES: WHAT DOES IT SIGNAL?* (1990).

17. JOHN DUNNING, *MULTINATIONALS, TECHNOLOGY AND COMPETITIVENESS* 25 (1988); see also JOHN DUNNING, *MULTINATIONAL ENTERPRISES AND THE GLOBAL ECONOMY* (1992).

18. See generally John H. Barton & Barry E. Carter, *International Law and Institutions for a New Age*, 81 GEO. L.J. 535 (1993).

19. Evidence of this policy shift during the 1980s can be found in THOMAS BREWER, *FOREIGN DIRECT INVESTMENT IN DEVELOPING COUNTRIES* (1992), UNITED NATIONS CENTER FOR TRANSNATIONAL CORPORATIONS, *GOVERNMENT POLICIES AND FOREIGN DIRECT INVESTMENT* (1991), and JACK N. BEHRMAN & ROBERT E. GROSSE, *INTERNATIONAL BUSINESS AND GOVERNMENTS: ISSUES AND INSTITUTIONS* (1990).

20. For a review and reconsideration of these themes in the theoretical literature on FDI, see

investments of corporations, in this theoretical analysis, thus mitigate the inefficiencies created by government policies that inhibit international trade and licensing. The current reform effort consequently emphasizes the liberalization of government FDI policies. However, there is a continuing interest in finding a suitable mix of obligations and rights for both firms and governments to be included in a new international regime.<sup>21</sup>

The existing scholarly literature on investment disputes is inadequate as an analytic base of ideas and information for public policy discussions in this reform effort. The inadequacy of the literature is evident in three bodies of studies. First, the literature on investment disputes has been dominated by both legal and political risk studies concerning expropriation, particularly in developing countries; although such studies are relevant to the policy reform debate, they are inadequate by themselves because of their narrowly focused concern with expropriation.<sup>22</sup> Second, the literature on trade disputes has been preoccupied with the technicalities of the GATT dispute settlement procedures; again, although this literature is relevant, it is limited by its exclusive focus on trade disputes and neglect of investment disputes. Third, although many commentators have recommended the creation of a new international institutional framework for FDI, and although there have recently been more fully developed outlines for such arrangements presented, as noted above, there has not been detailed scholarship focused specifically on investment dispute settlement procedures.

## II. INTERNATIONAL INSTITUTIONAL ARRANGEMENTS

Proposals to create a new international legal and institutional framework for FDI have not been voiced in a political or diplomatic vacuum. In fact, there have been a variety of reform initiatives and tangible institutional developments over a five decade period, beginning in the mid-forties with efforts to create the International Trade Organization (ITO). The ITO would have complemented the International Monetary

generally Thomas Brewer, *Government Policies, Market Imperfections, and Foreign Direct Investment*, 24 J. OF INT'L BUS. STUDIES 101 (1993).

21. Compare, for instance, the concern with finding such a mix in Bergsten & Graham, *supra* note 6, and the emphasis on the policies of governments in Julius, *supra* note 3.

22. Representative items among the legal studies of expropriation and related investment dispute settlement issues can be found in various issues of *ICSID Review: Foreign Investment Law Journal*; representative items among the political risk studies can be found in *POLITICAL RISKS IN INTERNATIONAL BUSINESS: NEW DIRECTIONS FOR RESEARCH, MANAGEMENT, AND PUBLIC POLICY* (Thomas L. Brewer ed., 1985).

Fund (IMF) and the International Bank for Reconstruction and Development (IBRD), established by the Bretton Woods agreement of 1944. Following the Bretton Woods conference, in a subsequent series of conferences in London (1946), Geneva (1947), and Havana (1948), the United States and the United Kingdom initiated efforts to create a new International Trade Organization that would have had much more extensive authority than the GATT.<sup>23</sup> Although the initial proposals to create the ITO did not include any provisions concerning FDI, during the ITO charter negotiations, the issue of FDI was raised at the London conference by developing countries in the context of a proposed chapter on economic development.

After the U.S. Congress failed to ratify membership in the ITO,<sup>24</sup> there was a lull in diplomatic efforts to create a new multilateral institutional framework for FDI. Since the hiatus following the demise of the ITO initiative, however, there have been many developments in a variety of institutional contexts. These developments are discussed below in terms of their basic features and their relevance to investment dispute settlement procedures. We begin with GATT/WTO and the Uruguay Round agreements since they embody significant changes in institutionalized investment dispute settlement procedures.

### A. General Agreement on Tariffs and Trade—World Trade Organization

Until the Uruguay Round, there were only a few instances in which FDI issues were on the GATT agenda.<sup>25</sup> The first time was in the mid-1950s when a "Resolution on International Investment for Economic Development" was adopted. That resolution called upon the contracting parties to provide for "security for existing and future investment, the avoidance of double taxation, and facilities for the transfer of earnings."<sup>26</sup> An investment-related case entered the GATT

23. WILLIAM BROWN, *THE UNITED STATES AND THE RESTORATION OF WORLD TRADE* 152-53 (1950); RICHARD GARDNER, *STERLING-DOLLAR DIPLOMACY: THE ORIGINS AND THE PROSPECTS OF OUR INTERNATIONAL ECONOMIC ORDER* 365-66 (1969); CLAIR WILCOX, *A CHARTER FOR WORLD TRADE* 145-48 (1972); Havana Charter for an International Trade Organization, Mar. 24, 1948, U.N. Doc. E/CONF.2/78, reprinted in U.S. DEP'T OF STATE, PUB. 3206, *HAVANA CHARTER FOR AN INTERNATIONAL TRADE ORGANIZATION AND FINAL ACT AND RELATED DOCUMENTS* (1948).

24. There was concern in Congress that the ITO would have had too much authority, particularly with regard to anti-competitive business practices.

25. The future of FDI issues more generally at the GATT/WTO is analyzed in a broader diplomatic context in Thomas Brewer & Stephen Young, *The Multilateral Agenda for FDI*, 18 J. WORLD COMPETITION 67, 83 (1995).

26. Paul B. Christy III, *Negotiating Investment in the GATT: A Call for Functionalism*, 12 MICH. J. INT'L L. 743, 776 (1991).

dispute settlement procedure only once, in a case, concerning the Canadian Foreign Investment Review Agency, which dealt primarily with import restrictions.<sup>27</sup> An attempt by the United States to place investment issues on the Tokyo Round of GATT negotiations in the 1970s was unsuccessful.

The Uruguay Round agreements, however, include numerous provisions concerning investment issues as well as dispute settlement procedures. It is useful for present purposes to consider the Uruguay Round results as twenty-two principal instruments (twenty-one Agreements and one Understanding), plus the associated Ministerial Decisions and Declarations.<sup>28</sup> They are listed in this article in Appendix 1, where their provisions concerning both investment issues and dispute settlement procedures are noted. For the specific purpose of describing the provisions concerning investment dispute settlement procedures, five agreements and one understanding are particularly important:

- Agreement Establishing the World Trade Organization (WTO),<sup>29</sup>
- General Agreement on Tariffs and Trade 1994 (GATT 1994),<sup>30</sup>
- Agreement on Trade-Related Investment Measures (TRIMs),<sup>31</sup>
- General Agreement on Trade in Services (GATS),<sup>32</sup>
- Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPs),<sup>33</sup>
- Understanding on Rules and Procedures Governing the Settlement of Disputes (DSU).<sup>34</sup>

27. Rachael McCullough & Robert F. Owen, *Linking Negotiations on Trade and Foreign Direct Investment, in THE MULTINATIONAL CORPORATION IN THE 1980s* 334 (Charles P. Kindleberger & David B. Audretsch eds., 1983).

28. See RESULTS OF THE URUGUAY ROUND, *supra* note 1, at vi-viii.

29. Marrakesh Agreement Establishing the World Trade Organization, April 15, 1994, *reprinted in RESULTS OF THE URUGUAY ROUND, supra* note 1, at 5 [hereinafter WTO Agreement].

30. General Agreement on Tariffs and Trade, *opened for signature* Oct. 30, 1947, 4 B.I.S.D. 1 (1969). The initial GATT text can also be found at 61 Stat. pts. 5-6, and 55 U.N.T.S. 187 (unamended).

31. Agreement on Trade-Related Investment Measures, *reprinted in RESULTS OF THE URUGUAY ROUND, supra* note 1, at 163 [hereinafter TRIMs Agreement].

32. General Agreement on Trade in Services, Dec. 15, 1993, *reprinted in RESULTS OF THE URUGUAY ROUND, supra* note 1, at 325 [hereinafter GATS Agreement].

33. Agreement on Trade-Related Aspects of Intellectual Property Rights, Including Trade in Counterfeit Goods, Dec. 15, 1993, *reprinted in RESULTS OF THE URUGUAY ROUND, supra* note 1, at 365 [hereinafter TRIPs Agreement].

34. Understanding on Rules and Procedures Governing the Settlement of Disputes, Dec. 20, 1991, *reprinted in RESULTS OF THE URUGUAY ROUND, supra* note 1, at 404 [hereinafter Dispute Settlement Understanding].

The WTO Agreement is important for both investment issues and dispute settlement procedures because it establishes the umbrella institutional framework, policy process, and administrative structure for all matters. In particular, the WTO Agreement establishes the following bodies: the Ministerial Conference, which will have overall policy authority; the General Council, which will have authority on a continuing basis in the intervals, of up to two years, between the meetings of the Ministerial Conference; the Council for Trade in Goods, which will administer the Uruguay Round agreements on goods, including the TRIMs Agreement; the Council for Trade in Services, which will administer the GATS Agreement; and the Council for Trade-Related Aspects of Intellectual Property Rights, which will administer the TRIPs Agreement. There will also be a Committee on Trade and Development, a Committee on Balance-of-Payments Restrictions, and a Committee on Budget, Finance, and Administration—all of which could become involved in selected aspects of both investment issues and dispute settlement procedures. Furthermore, the WTO will administer the Dispute Settlement Understanding, and the WTO General Council will act as the Dispute Settlement Body.

Investment issues are brought into the WTO institutional framework through three Agreements: the Agreement on Trade Related Investment Measures, the General Agreement on Trade in Services, and the Agreement on Trade Related Aspects of Intellectual Property Rights.

The TRIMs Agreement, which concerns only trade in goods, provides for notification, transparency, national treatment, and the phased elimination of TRIMs. It also provides an "Illustrative List" of TRIMs that are inconsistent with national treatment (domestic content requirements) or that reflect quantitative trade restrictions (import-export balancing requirements, foreign exchange balancing requirements, and export restrictions). A Committee on TRIMs will be established to facilitate consultation among Members and to monitor the implementation of the TRIMs Agreement. In addition, article 9 of the TRIMs Agreement provides that the Council for Trade in Goods will review the operation of the Agreement within five years. The Council will consider whether the Agreement should be complemented with provisions on investment policy and/or competition policy. This review process could add significantly to the coverage of investment issues by the WTO in the future.

The GATS Agreement is more extensive and complex than the TRIMs Agreement, and only a few key provisions can be highlighted here. The GATS Agreement includes foreign direct investment within

the scope of its application by defining trade in services to include, *inter alia*, "the supply of a service . . . by a service supplier of one Member, through commercial presence in the territory of any other Member."<sup>35</sup> It defines "commercial presence" to mean "any type of business or professional establishment, including through (i) the constitution, acquisition or maintenance of a juridical person, or (ii) the creation or maintenance of a branch or a representative office, within the territory of a Member for the purpose of supplying a service."<sup>36</sup> Thus, FDI is one of the four "modes of supply" of services.<sup>37</sup>

The GATS Agreement includes provisions concerning notification, transparency, most favored nation treatment, national treatment, market access, subsidies, and foreign exchange restrictions on capital account and current account transactions. It also provides for "successive rounds of negotiations, beginning not later than five years from the date of entry into force of the WTO Agreement and periodically thereafter, with a view to achieving a progressively higher level of liberalization."<sup>38</sup> As with the five year review provision in the TRIMs Agreement, noted above, this provision in the GATS could lead to more extensive coverage of investment issues.

The TRIPs Agreement is relatively lengthy and complex. Although it does not include any explicit references to foreign direct investment, the Agreement is important to foreign direct investors because their investment projects typically entail international technology transfers between parent firms and their foreign affiliates; hence, licensing agreements concerning the intellectual property rights of parent firms and their foreign affiliates are widely used. Intellectual property is defined broadly in the TRIPs Agreement to include copyrights, trademarks, industrial designs, patents, and layout designs of integrated circuits.

The TRIMs, GATS, and TRIPs Agreements expand the GATT/WTO framework to include a variety of foreign direct investment issues; accordingly, disputes concerning foreign direct investments, as well as trade, will be subject to the new dispute settlement procedures embodied in the Uruguay agreements. The core of the new, strengthened

35. GATS Agreement, *supra* note 32, art. I(2)(c), at 328.

36. *Id.* art. XXVIII(d), at 349.

37. The other three are defined in article I(2) of the GATS as "the supply of a service: (a) from the territory of one Member into the territory of any other Member; (b) in the territory of one Member to the service consumer of any other Member; . . . (d) by a service supplier of one Member, through presence of natural persons of a Member in the territory of any other Member." *Id.* art. I(2), at 328.

38. *Id.* art. XIX(1), at 343.

dispute settlement mechanism is established by the Dispute Settlement Understanding, which is supplemented by five Ministerial Decisions. These new instruments are in addition to the provisions of GATT 1994, which includes the existing GATT articles XXII and XXIII concerning consultation and dispute settlement procedures.

The Dispute Settlement Understanding lists in Appendix I the Agreements that are covered by the Understanding: the agreements on trade in goods (including TRIMs), the General Agreement on Trade in Services, the Agreement on TRIPs, and sectoral Plurilateral Agreements. In addition, most of those agreements also have provisions indicating that the DSU applies to them.<sup>39</sup>

One of the most important provisions of the Dispute Settlement Understanding—and indeed of the entire package of Uruguay Round results—is the significant change in the procedures for the member governments' consideration of dispute panel recommendations.<sup>40</sup> In structural terms, the General Council, acting as the Dispute Settlement Body (DSB), provides a formal forum where Members can review the results of dispute panels and the dispute Appellate Body. The new procedures have reversed the requirement for a "consensus" (i.e. unanimous agreement) of the Members in the process of approving or rejecting the reports of dispute panels or the dispute Appellate Body. In the past, a unanimous vote of the Members, including the Parties to the dispute, was required to approve dispute panel reports. In the future, however, a unanimous vote of the Members, as the Dispute Settlement Body, will be needed to reject a report from a dispute panel or the dispute Appellate Body. This important change is embodied in articles 16(4) and 17(14) as follows:

Within 60 days after the date of circulation of a panel report to the Members, the report shall be adopted at a DSB meeting

39. The application of the DSU in plurilateral agreements is conditional upon agreement by members of those agreements that the DSU applies. There are also "Special or Additional Rules and Procedures Contained in the Covered Agreements," Dispute Settlement Understanding, *supra* note 34, app. 2, at 430. These are the Agreements concerning Anti-Dumping, Technical Barriers to Trade, Subsidies and Countervailing Measures, Customs Valuation, Sanitary and Phytosanitary Regulations, Textiles, and the GATS. However, only the GATS Agreement pertains specifically to investment (as well as trade). The net effect of this additional list is that there is variability in the applicability of the new dispute settlement procedures across agreements; however, the new consensus procedures of the Dispute Settlement Body, as discussed in the next paragraph, apply without restriction to investment issues.

40. These changes were a central concern of some members of the Congress that led them to impose a condition for their support of the WTO—namely the creation of a panel that would determine if U.S. interests are adversely affected by WTO decisions.

unless a Party to the dispute formally notifies the DSB of its decision to appeal or the DSB decides by consensus not to adopt the report. If a Party has notified its decision to appeal, the report by the panel shall not be considered for adoption by the DSB until after completion of the appeal.<sup>41</sup>

An Appellate Body report shall be adopted by the DSB and unconditionally accepted by the Parties to the dispute unless the DSB decides by consensus not to adopt the Appellate Body report within 30 days following its circulation to the Members.<sup>42</sup>

Therefore, whether or not there is an appeal of a dispute panel report through the Appellate Body, the Dispute Settlement Body can reject a report on a dispute only by a unanimous vote within a prescribed time period.<sup>43</sup> Jackson has assessed this innovation as follows: "It ingeniously establishes a new appellate procedure that will substitute for some of the process of council approval of a panel report . . . [T]he ultimate result [is] that the appellate report will come into force as a matter of international law in virtually every case."<sup>44</sup> These changes are not only an important development for the dispute settlement process in particular but are also an important development for the effectiveness of the WTO as a key institutional manifestation of the international investment (and trade) regime. Thus, for instance, Wolff has asserted that

"whether dispute settlement works is going to be the litmus test of whether the WTO is seen as a success or failure."<sup>45</sup>

There is an additional change in the dispute settlement procedures that is of special importance to FDI, namely the provision for cross-retaliation between agreements; there are limitations, however, to the cross-retaliation opportunities.<sup>46</sup> Retaliation as a result of a dispute settlement decision can occur if a losing party chooses not to modify the policy found to be inconsistent with a WTO obligation and bring it into conformity with the dispute settlement decision of the WTO. Cross-retaliation involves retaliation outside the policy area and agreement of the dispute—for instance, withdrawal of an intellectual property concession in a dispute in which a policy concerning trade in goods is found to be inconsistent with WTO obligations. Investment disputes can be linked to trade disputes through the dispute settlement process in the provision of DSU article 22.3(c) under which a complaining Party in a dispute under one agreement can suspend its concessions under another agreement. Thus, trade disputes under the various trade agreements could spill over into investment-related issues under the TRIMs, GATS, or TRIPs Agreements. This could occur even though the disputes would originate under more traditional trade-related agreements, such as those concerning dumping or countervailing duties.<sup>47</sup> Furthermore, the opposite is also possible—that is, cross-retaliation in the form of the withdrawal of a concession concerning trade in goods could result from an investment dispute raised under the GATS. The new dispute resolution procedures will be reviewed within four years of the entry of the WTO into force.

References to dispute settlement procedures are also contained in the industry-specific Agreement on Textiles and Clothing<sup>48</sup> and in the

41. *Id.* art. 16(4), at 417 (emphasis added). Footnote 7 provides that "If a meeting of the DSB is not scheduled within this period at a time that enables the requirements of paragraphs 1 and 4 of article 16 to be met, a meeting of the DSB shall be held for this purpose" *Id.* at 417 n.7.

42. *Id.* art. 17(14), at 419 (emphasis added). Footnote 8 provides that "If a meeting of the DSB is not scheduled during this period, such a meeting of the DSB shall be held for this purpose." *Id.* at 419 n.8.

43. Appendices to the DSU, plus five Ministerial Decisions, provide additional details about the dispute settlement process, including the composition and procedures of dispute panels, the Appellate Body, and Expert Review Groups. The five Ministerial Decisions are: the Decision on Certain Dispute Settlement Procedures for the General Agreement on Trade in Services, reprinted in RESULTS OF THE URUGUAY ROUND, *supra* note 1, at 457; Decision on the Application and Review of the Understanding on Rules and Procedures Governing the Settlement of Disputes, reprinted in RESULTS OF THE URUGUAY ROUND, *supra* note 1, at 465; Decision on Improvements to the GATT Dispute Settlement Rules and Procedures, GATT Doc. MTN/FA III-10 (1994); Decision on Standard of Review for Dispute Settlement Panels, GATT Doc. MTN/FA III-11(b), (1994); Decision on Dispute Settlement pursuant to the Agreement on Implementation of Article VI of GATT 1994 or Part V of the Agreement on Subsidies and Countervailing Measures 1994, reprinted in RESULTS OF THE URUGUAY ROUND, *supra* note 1, at 453.

44. John H. Jackson, *Managing the Trade System: The World Trade Organization and the Post-Uruguay Round GATT Agenda*, in MANAGING THE WORLD ECONOMY 131, 141 (Peter B. Kenen ed., 1994).

45. Alan W. Wolff, Comment, in MANAGING THE WORLD ECONOMY 152, 154 (Peter B. Kenen ed., 1994).

46. Cross-retaliation is excluded from the government procurement plurilateral agreements. See *Dispute Settlement Understanding*, *supra* note 34, art. 22(5), at 424; *Agreement on Government Procurement*, art. XXII(7), reprinted in RESULTS OF THE URUGUAY ROUND, *supra* note 1, at 438. In addition, retaliation opportunities within the scope of the initially-relevant agreement (e.g. TRIMs, GATS, TRIPs) must be insufficient.

47. For information on the previous GATT procedures, see Christy, *supra* note 26; Guy Ladreit de Lachariere, *The Legal Framework for International Trade*, in TRADE POLICIES FOR A BETTER FUTURE: THE 'LEUTWILER REPORT,' THE NTO/GATT AND THE URUGUAY ROUND 95 (1985); see also PIERRE PESCATORE ET AL., HANDBOOK OF GATT DISPUTE SETTLEMENT (1991).

48. Agreement on Textiles and Clothing, reprinted in RESULTS OF THE URUGUAY ROUND, *supra* note 1, at 85.

Agreement on the Implementation of Article VI<sup>49</sup> concerning anti-dumping. Whereas the Antidumping Agreement provides for dispute settlement through the normal GATT dispute settlement procedure,<sup>50</sup> as strengthened by other Uruguay Round agreements, the Textiles and Clothing Agreement provides for dispute settlement through a special Textile Monitoring Body.<sup>51</sup>

Finally, operation of the Trade Policy Review Mechanism (TPRM), though not a dispute settlement procedure,<sup>52</sup> can affect investment issues by clarifying and reporting members' FDI policies.

### B. Organization for Economic Cooperation and Development

Investment issues have been central to the agenda of the Organization for Economic Cooperation and Development (OECD) since its creation in the early 1960s.<sup>53</sup> During its first year of operation, the OECD member countries adopted two codes to liberalize international capital flows—the Code of Liberalisation of Capital Movements and the Code of Liberalisation of Current Invisible Operations.<sup>54</sup> In addition, in 1976 the OECD members adopted a Declaration on International Investment and Multinational Enterprises, which includes the National Treatment instrument.<sup>55</sup>

To date, however, the OECD has not included strong investment dispute settlement procedures in any of these three instruments.<sup>56</sup>

49. Agreement on Implementation of Article VI of the General Agreement of Tariffs and Trade 1994, reprinted in RESULTS OF THE URUGUAY ROUND, *supra* note 1, at 168 [hereinafter Agreement on Article VI].

50. "No specific action . . . can be taken except in accordance with the provisions of GATT 1994 . . ." *Id.* art. 18.1, at 193.

51. Agreement on Textiles and Clothing, *supra* note 48, art. 8, at 99-100.

52. Trade Policy Review Mechanism, reprinted in RESULTS OF THE URUGUAY ROUND, *supra* note 1, at 434. See also Jackson, *supra* note 44, at 137.

53. For a more encompassing analysis of FDI issues on the OECD agenda in the past, present, and future, see generally Brewer & Young, *supra* note 25.

54. See, e.g., OECD, OECD INSTRUMENTS FOR PROMOTING THE LIBERALISATION OF FOREIGN DIRECT INVESTMENT (1993); D. GUERTIN & J. KLINE, BUILDING AN INTERNATIONAL INVESTMENT ACCORD (1989); Lars Oxelheim, *Foreign Direct Investment and the Liberalization of Capital Movements, in THE GLOBAL RACE FOR FOREIGN DIRECT INVESTMENT* (Lars Oxelheim ed., 1993).

55. A Draft Convention on the Protection of Foreign Property was completed by the OECD in the mid 1960s, and a related set of principles was accepted by the OECD in 1967. However, the Convention was never formally adopted, and the principles were not made binding on member governments.

56. See Franziska Tschofen, *Multilateral Approaches to the Treatment of Foreign Investment*, in 1 WORLD BANK, LEGAL FRAMEWORK FOR THE TREATMENT OF FOREIGN INVESTMENT 59, 104 (1992).

Christy, for example, notes that:

As compared to the GATT, the dispute settlement mechanism of the [OECD] Codes is weak. The Codes provide no right of retaliation or other means of positive enforcement, but instead seek compliance through a system of notification, examination, and consultation. A committee on Capital Movements and Invisible Transactions (CMIT) is the oversight committee for the Codes and conducts periodic examinations of members' reservations and derogations. For those seeking redress against a member for improperly invoking a derogation or for frustrating or violating its liberalization commitments, there exists only a right to notify the Organization, and in the case of an improper derogation, to have the situation examined by a "special Ministerial Group." The CMIT considers these complaints, but the Codes provide neither "carrot" nor "stick" to ensure compliance.<sup>57</sup>

However, negotiations are currently in progress on a new OECD Multilateral Agreement on Investment (MAI) that would strengthen the provisions of the OECD agreements in several respects and that could include a provision concerning investment dispute settlement procedures in particular.<sup>58</sup> The OECD Secretariat has had a feasibility study under way for several years to determine whether and how a strengthening of the OECD liberalization codes and national treatment instrument might be undertaken.<sup>59</sup> At their June 1993 ministerial meeting, the OECD member governments decided that the feasibility study by the OECD Secretariat should advance to a more detailed analysis of specific problems and alternative solutions in the development of an agreement, and in May 1995 a decision was made by the member governments to enter into more formal negotiations during 1995.<sup>60</sup>

Dispute settlement is one of the specific problem areas now under more detailed analysis by the Secretariat and a working group of member governments, and there is likely to be a provision concerning

57. Christy, *supra* note 26, at 771.

58. William H. Witherell, *Investment, Services, Taxation and Competition*, BUS. ECON., Jan. 1995, at 29. In discussions within the OECD, the MAI was previously known as a "wider investment instrument" (WII) and then as a Multilateral Investment Agreement (MIA).

59. OECD, *supra* note 54, at 13.

60. Witherell, *supra* note 58, at 29.

dispute settlement in any eventual MAI. At this stage of the discussions, however, the nature of such a provision is undecided.<sup>61</sup>

### C. United Nations

In the past, the program on transnational corporations within the United Nations was carried out by the Center on Transnational Corporations (1975–1992) and by the Transnational Corporations and Management Division of the U.N. Department of Economic and Social Development (1992–1993). The Commission on Transnational Corporations negotiated a draft Code of Conduct for Transnational Corporations. The Code, however, remains incomplete, and the negotiations have been discontinued.<sup>62</sup> There were also negotiations within the United Nations Conference on Trade and Development (UNCTAD), particularly to create a Restrictive Business Practices code; however, after many years of activity, beginning in 1976, those negotiations are also moribund.<sup>63</sup>

The principal center of activity on FDI issues within the U.N. system is now the UNCTAD Division on Transnational Corporations and Investment, which serves as the focal point within the United Nations Secretariat for all matters related to transnational corporations. Its Programme on Transnational Corporations (PTC) is continuing the extensive research and publishing program on FDI of its predecessor units. Although its potential as a negotiating forum is unclear, its proximity to the WTO in Geneva may help the WTO to more easily overcome its relative lack of experience and staff expertise on FDI-related issues. The PTC has not conducted studies or negotiations specifically on dispute settlement procedures, but its expertise on a wide range of other FDI issues would enable it to contribute to any discussions or negotiations concerning dispute settlement.

In addition, within the wider United Nations system, the Economic Commission for Europe (ECE) drafted the 1961 European Convention on International Commercial Arbitration, which is still in force and under the administration of the ECE. It is discussed further in section H below.

61. *E.g.*, an OECD agreement on shipbuilding, which is still being negotiated, includes provisions for dispute settlement.

62. Thomas L. Brewer, *International Regulation of Restrictive Business Practices*, 16 J. WORLD TRADE L. 108, 113 (1982).

63. *Id.* at 110.

### D. North American Free Trade Agreement

Dispute settlement procedures associated with the North American Free Trade Agreement (NAFTA) have become highly salient as a result of controversies concerning the side agreements on labor relations and the environment.<sup>64</sup> In addition, the NAFTA accord includes important and path-breaking provisions concerning the settlement of investment disputes. In an important expansion of the dispute resolution procedures in the US-Canada Free Trade Agreement, the NAFTA includes disputes between firms and governments as well as disputes between governments.

The procedures concerning investment disputes are contained in Chapter 11(B), which provides that investors' claims against governments can be submitted to a tribunal of three members—one selected by each of the parties to the dispute and one agreed to by both parties.<sup>65</sup> The tribunals have the authority to award damages based on their decisions. Mexico's acceptance of these new investment dispute settlement procedures for disputes between investors and governments represents a significant departure from its previous adherence to the Calvo doctrine, which asserts that investment disputes can be resolved only in the host country's domestic legal system and not through international legal and institutional arrangements.<sup>66</sup> This in itself is a major change in the international legal regime for FDI; to the extent that other Latin American countries follow Mexico's lead on this issue, it will obviously be yet more significant.

In addition to these provisions concerning investor-government disputes, the NAFTA establishes dispute settlement procedures in Chapter 20 for government-government disputes concerning trade or investment.<sup>67</sup> According to those procedures, the party making a complaint

64. A recent Note in this journal has analyzed the NAFTA dispute settlement procedures in detail, particularly in relation to trade issues. Kristin L. Oelstrom, Note, *The North American Free Trade Agreement and Dispute Settlement Mechanisms*, 25 LAW & POLY INT'L BUS. 783 (1994). The present Article only highlights the investment-related aspects of those procedures as well as the general features that pertain to both trade disputes and investment disputes. See also Gary N. Horlick et al., *Dispute Settlement Mechanism*, in THE CANADA-UNITED STATES FREE TRADE AGREEMENT: THE GLOBAL IMPACT 65 (Jeffrey J. Schott & Murray G. Smith eds., 1988); O. Thomas Johnson, *General Dispute Settlement Under NAFTA*, in THE NORTH AMERICAN FREE TRADE AGREEMENT: ISSUES, OPTIONS, IMPLICATIONS (S. Baker & J. Bialos eds., 1992).

65. Edward M. Graham & Christopher Wilkie, *Multinationals and the Investment Provisions of the NAFTA*, 8 INT'L TRADE J. 9, 19 (1994).

66. GARY C. HUFBAUER & JEFFREY J. SCHOTT, NAFTA: AN ASSESSMENT 81, 82 (1993).

67. Oelstrom, *supra* note 64, at 785.

- (7) the subrogation of compensated investors' claims to their home governments; and
- (8) the settlement of disputes through international arbitration.

The provisions of BITs concerning dispute settlement are widely considered to be among the most important means for prospective host governments to provide investors with an attractive investment climate. Many BITs provide that arbitration will take place through the International Center for the Settlement of Investment Disputes (ICSID), but many also provide for arbitration through other institutions—which are discussed in the next two sections of the Article. BITs vary in their provisions concerning the sequence according to which disputes are subjected to direct negotiations between the parties, host country administrative and judicial procedures, and international arbitration centers.

Disputes between investors and host governments, of course, easily become disputes between host and home governments as well. Consequently, BITs commonly establish procedures for government-government dispute settlement through international arbitration. Time limits are imposed on various stages in both investor-government and government-government dispute settlement procedures. Although BITs include both investor-government and government-government disputes, they are focused mostly on the relationships—and hence potential disputes—between investors and host governments, and the term, "investment dispute" is in fact often used to refer specifically to this category of disputes.<sup>73</sup>

#### G. *International Center for the Settlement of Investment Disputes in the World Bank Group*

Although the World Bank in its original operational form as the International Bank for Reconstruction and Development (IBRD) was not much concerned with FDI, over time FDI has become important through the activities of several organizational components of the larger World Bank Group.<sup>74</sup> The creation of the International Finance Corpo-

73. Istvan Pogany, *Bilateral Investment Treaties: Some Recent Examples*, 2 ICSID REV. FOREIGN INV. L.J. 457, 467 (1987); Scott K. Gudgion, *Arbitration Provisions of U.S. Bilateral Investment Treaties*, in SEYMOUR G. RUBIN & RICHARD W. NELSON, *INTERNATIONAL INVESTMENT DISPUTES: AVOIDANCE AND SETTLEMENT* 41 (1985).

74. Ibrahim F.I. Shihata, *Towards a Greater Depoliticization of Investment Disputes: The Roles of ICSID and MIGA*, 1 ICSID REV. FOREIGN INV. L.J. 1, 13 (1986). The Articles of Agreement of the IBRD specifically include the promotion of private foreign investment as one of its objectives.

ration (IFC) in 1956 provided an organizational mechanism for involvement in FDI through equity participation with private investors and loans to private investors in FDI projects in developing countries. The Foreign Investment Advisory Service (FIAS) was created in 1986 as a part of the IFC to advise developing countries on their policies as hosts to FDI.<sup>75</sup> The Multilateral Investment Guarantee Agency (MIGA) was created in 1988 to provide political risk insurance to foreign direct investors in developing countries. The successful negotiation of the convention establishing MIGA was in fact the culmination of two decades of on-and-off negotiations to create an international investment agency of some type at the World Bank.<sup>76</sup> The Bank's involvement in privatization policies and projects in many countries, in recent years, has also brought its traditional concerns as a development institution into direct contact with FDI issues since foreign investors are often among the investors in privatized firms. The Bank's new guarantee program, which insures private investors in major projects within developing countries against changes in government policies, was created to be more responsive to the role of private investment in the development process.<sup>77</sup>

These diverse FDI-related activities of the World Bank Group assure it an important role in the future development of international institutional arrangements concerning FDI. Here, however, we focus specifically on the activities of the Center for the Settlement of Investment Disputes (ICSID), which was created within the World Bank Group in 1965 to provide a forum for the resolution of disputes between investor firms and host governments.

Although ICSID has been the least conspicuous constituent entity within the World Bank Group, and although it has been used only infrequently in its quarter-century history, it nevertheless represents a central part of the international regime for the settlement of investment disputes.<sup>78</sup> One reason ICSID is important is because most

75. FIAS was subsequently placed under the supervision of a committee of representatives of three components of the World Bank Group: the IFC, the MIGA, and the Bank's Private Sector unit. It has since been re-established as a unit within the IFC.

76. Shihata, *supra* note 74 at 13; Ibrahim F.I. Shihata, *The New Proposal for Establishing a Multilateral Investment Guarantee Agency*, in *POLITICAL RISKS IN INTERNATIONAL BUSINESS* 309, 311 (Thomas L. Brewer ed., 1985).

77. See George Graham, *World Bank Backing for Investors*, *FIN. TIMES* (London), Sept. 13, 1994, at 6. In addition, the Bank's participation in a project as a source of finance reduces the incidence and severity of disputes because governments are reluctant to jeopardize their access to the Bank's funds in the future.

78. Aron Broches, *The Experience of the International Center for Settlement of Investment Disputes*, in

bilateral investment treaties designate it as the prospective arbitration center for disputes, refer to it as an appointing authority, or indicate that its rules would be applicable in ad hoc arbitrations.<sup>79</sup> There are now over 100 contracting parties to ICSID, and this includes many Latin American countries that became signatories in the early 1990s.

Despite the widespread acceptance of ICSID in principle, however, its use in practice has remained limited; only thirty-three cases have been considered by it in nearly thirty years. Because the ICSID arbitration process is rather lengthy and complex, it is used only for disputes involving unusually large claims. However, it has been noted that "the value of ICSID is not to be measured only—or indeed primarily—by its caseload. Rather, the criterion is whether ICSID contributes to an international ethos in which investment disputes are resolved as matters of principle and objectively, not [on the basis of] politics and influence."<sup>80</sup>

#### H. Arbitration Centers

The best known centers for international investment dispute arbitration—other than ICSID—are the International Court of Arbitration of the International Chamber of Commerce (ICC)<sup>81</sup> and the London Court of International Arbitration (LCIA).<sup>82</sup> In addition, there are international arbitration centers in Stockholm, Hong Kong, and other cities,<sup>83</sup> as well as the European Convention on International Commercial Arbitration administered by the U.N. Economic Commission for Europe and the World Intellectual Property Organization (WIPO) in the U.N. system.<sup>84</sup> These arbitration organizations are mainly con-

SEYMOUR G. RUBIN & RICHARD W. NELSON, INTERNATIONAL INVESTMENT DISPUTES: AVOIDANCE AND SETTLEMENT 75 (1985); M. HIRSCH, THE ARBITRATION MECHANISM OF THE INTERNATIONAL CENTER FOR THE SETTLEMENT OF INVESTMENT DISPUTES 38-40 (1993).

79. Jan Paulsson, *ICSID's Achievements and Prospects*, 6 ICSID REV. FOREIGN INV. L.J. 380, 382 (1991).

80. *Id.* at 398.

81. Robert H. Smit, *An Inside View of the ICC Court*, 10 ARB. INT'L 53 (1991); ICC, THE ICC INTERNATIONAL COURT OF ARBITRATION BULLETIN (1994).

82. An Introduction to the London Court of International Arbitration (n.d.).

83. G. Coombe, *International Alternative Dispute Resolution* (n.d.); G. COOMBE, INTERNATIONAL BUSINESS DISPUTE RESOLUTION INVOLVING EAST ASIAN COMPANIES (n.d.); see also Andre Long, *Dispute Resolution in International Trade*, 8 INT'L TRADE J. 367 (1994).

84. United Nations Economic Commission for Europe, Special Meeting of Plenipotentiaries for the Purpose of Negotiating and Signing a European Convention on International Commercial Arbitration, Final Act and European Convention on International Commercial Arbitration, April 21, 1961, 484 U.N.T.S. 349.

cerned with firm-firm disputes, although the ICC sometimes handles firm-government cases as well.

The organizations differ considerably in many respects; thus, it is difficult to generalize about them, and it is beyond the scope of this Article to discuss them in detail individually. However, key dimensions of their variability can be summarized in terms of their geographic emphasis, decision-making structure, rules of procedure, speed, cost, and other features. For instance, some are regionally specialized (e.g., the Asia/Pacific Center for the Resolution of International Business Disputes established by the American Arbitration Association), while others are more global in scope (e.g., the International Chamber of Commerce and the London Court of International Arbitration).

Arbitration offers parties to disputes a less public, less costly, and more rapid "alternative dispute resolution" (ADR) mechanism, as compared to litigation through courts. However, arbitration cases can take years to resolve, and there are variations across arbitration organizations in relative speed and cost. The selection of an arbitration center, the rules of arbitration to be applied, and the site at which arbitration meetings take place are all among the negotiable issues in international contracts between firms, and thus they are idiosyncratic to the particular firms and projects involved.

The larger issues, for the purposes of the present Article, are how these arbitration organizations and rules fit into the entire network of investment dispute settlement procedures and whether they are adequate to the needs of firms and governments. These questions become more pressing as FDI increases in countries with little previous inward FDI and as the number of international joint ventures and strategic alliances between firms from different legal traditions also increases. Such issues are of interest to governments because, in some cases, they are drawn into inter-firm disputes by the parties to the dispute. Thus, there are significant public policy questions about the place of these arbitration centers in the larger international regime for FDI, but those questions require research that extends beyond the scope of this Article.

#### I. Summaries of Principles and Guidelines

The common principles that are manifest in the diverse instruments of the current international regime for investment dispute settlement procedures have been summarized in a World Bank study, which is presented below in Appendix 2. In addition, in an effort to facilitate further progress in the development of the international legal frame-

work concerning FDI, the Joint Development Committee of the World Bank and the International Monetary Fund published "guidelines" concerning investment dispute settlement procedures, and those are presented in Appendix 3.

### III. SCENARIOS FOR THE FUTURE

In the future, the FDI regime reform process will occur at many levels—bilateral and regional as well as global. For dispute settlement procedures in particular, the distinctions among inter-government, firm-government, and inter-firm disputes will remain crucial to an understanding of the institutional reform process. In any case, private arbitration centers will become increasingly important, as the numbers of inter-firm disputes submitted to them will almost inevitably continue to increase. The existence of hundreds of bilateral investment treaties (BITs), plus the continuing negotiation of such agreements, ensures that there will be a significant bilateral element in the FDI regime. Similarly, the provisions for investment dispute settlement procedures in the NAFTA ensures that there will be a regional dimension as well. NAFTA's dispute settlement procedures and other provisions have been suggested as a possible example for the further development of an investment agreement by APEC.<sup>85</sup>

At the multilateral-global level, a key diplomatic issue in future scenarios is the determination of which multilateral institution(s) would be the most appropriate location(s) for further steps in the reform process.<sup>86</sup> The multilateral institutions that have been involved in FDI issues in recent years can continue to play their traditional and complementary roles. These roles will evolve as specific initiatives progress from the analytic phase to the negotiation phase and then to the implementation phase. The OECD, the United Nations' Programme on Transnational Corporations, and the World Bank can continue to do the analytic work that provides the foundation of information and ideas for discussion as issues are more actively addressed by governments. All three have strong traditions of excellence in their analytic work. Moreover, they complement one another in other ways. For instance, because of its membership, the OECD is principally concerned with industrial

85. Edward M. Graham, *Towards an Asia Pacific Investment Code*, 3 TRANSNAT'L CORP. 1, 27 (1994).

86. A scenario involving the OECD and the World Bank Group is developed in D. L. Guerin, *A Program Leading to an International Agreement on Foreign Direct Investment*, in FOREIGN DIRECT INVESTMENT IN THE 1990s (Cynthia Day Wallace ed., 1990).

countries, while the United Nations and the World Bank are more concerned with developing countries.<sup>87</sup>

Although all three of these organizations can play important roles in the *negotiation* phase, the WTO is a more plausible forum, in the long term, for many future negotiations. Because of its experience and its demonstrated ability to accommodate the differing policy orientations of both industrial and developing countries in complex negotiations, the WTO is a more suitable and politically feasible forum than the OECD, the World Bank, or the United Nations for negotiations that include large numbers of both industrial and developing countries.<sup>88</sup> Industrial countries are not likely to find the United Nations acceptable, particularly in light of the lengthy negotiations at the CTC on a Code of Conduct and at UNCTAD on a Restrictive Business Practices Code—both of which were generally considered unwelcome prospects by firms and governments in industrial countries. On the other hand, many developing countries are not likely to find the OECD acceptable; despite Mexico's membership, the general absence of developing countries in the OECD makes it unsuitable as a forum for global negotiations. However, this does not preclude the OECD from negotiating new agreements that are open to signature by non-members. Finally, although the World Bank has been able to accommodate both developing and industrial country orientations and although it conducted negotiations to create MIGA, its basic nature is that of an institution that conducts operational programs, not one that provides a forum for formal global policy negotiations.

In the *implementation* phase of reform initiatives, all four organizations may play roles, as will others. For investment dispute settlement procedures, in particular, ICSID at the World Bank may become more fully developed and active. The WTO's dispute settlement process will also continue to expand into investment related disputes, especially those that have trade-related dimensions. The roles of the OECD and the UNCTAD Division on Transnational Corporations and Investment may be less conspicuous but not necessarily less important. The OECD, for instance, could continue to provide a forum for discussion of subsequent

87. Although the Bank's expertise in macro-economic analysis of FDI issues is limited, it has extensive staff resources and experience in FDI project analysis (especially in IFC and MIGA) and in developing countries' host government policies (especially in IFTAs), as well as in dispute settlement (in ICISID).

88. However, GATT's staff resources on investment issues will have to be substantially strengthened. In the meantime, it can draw upon the expertise of the United Nations Programme on Transnational Corporations, which is now conveniently located in Geneva.

initiatives of its own and for possible adoption in forums with broader memberships.

A new regime, therefore, is likely to continue to exhibit a substantial degree of diversification of functional activities among institutions, and perhaps a degree of overlapping responsibilities as well. For instance, issues concerning government restrictions on fund transfers have been traditionally treated as one kind of "political risk" and are therefore of interest to MIGA in the World Bank Group. In addition, restrictions on foreign exchange transactions have been a concern of the IMF since its inauguration. These issues are on the agendas at the WTO and OECD and are also evident in cases in international arbitration centers.

It is, of course, unclear at this point how vigorously investment-related disputes and other investment-related issues will be pursued within the new WTO framework. Some commentators have been skeptical about the ability of the GATT (and by implication, the WTO) to become an effective international institution on investment issues. For instance, Ostry noted that the GATT Uruguay Round treated only

a limited number of "trade-related" measures, because of opposition to the very notion of the GATT's treating investment at all (investment, the argument goes, is a domestic matter related to growth and development). That this approach will be inadequate to deal with international friction in this area is quite clear from what is happening in the international economy [i.e. the large increases in FDI flows among OECD countries].<sup>89</sup>

The argument that investment is a domestic issue, in other words, is hardly tenable in a world of globalized economic interdependencies, including the diverse forms of intense international interdependencies created by FDI. Ostry also suggests—as part of an OECD "project for analysis and policy proposals"—that if trade policy is included with investment, "it would be important for the OECD analysis to go beyond the Uruguay Round agenda item of trade-related investment measures. What is required is a comparative analysis of foreign direct investment flows and of differences among the Triad in de jure and de facto impediments to access."<sup>90</sup>

Julius considers the advantages and disadvantages of several existing international institutions as an "organizational base for an interna-

89. SYLVIA OSTRY, *GOVERNMENTS AND CORPORATIONS IN A SHRINKING WORLD: TRADE AND INNOVATION POLICIES IN THE UNITED STATES, EUROPE, AND JAPAN* 76 (1990).

90. *Id.* at 87.

tional regime to liberalize FDI."<sup>91</sup> Although the OECD may be attractive because of its experience in efforts to liberalize FDI flows, its limited membership and absence of enforcement mechanisms make it unsuitable in her view. However, these features of the OECD do not necessarily preclude it from addressing FDI issues in parallel with, or in advance of, their consideration within the WTO.<sup>92</sup> As for the World Bank and IMF, since FDI is not a central concern of either and since their potential for sanctions is limited to the developing countries that borrow from them, neither of those institutions is considered suitable; thus, she believes that GATT/WTO, despite its deficiencies, "provides the best model, or starting point, for an international regime to liberalize FDI."<sup>93</sup>

Julius has emphasized the special place of dispute settlement procedures in any investment regime, and she has proposed that firm-government disputes be added to the WTO dispute settlement process. She acknowledges that "[w]hile this may seem a striking departure from the postwar diplomatic tradition of government-to-government relations, there is a precedent in the recent NAFTA."<sup>94</sup>

The most detailed analysis of the possibility of creating a new international institutional framework for FDI has been offered by Bergsten and Graham.<sup>95</sup> They have developed a comprehensive outline of the issues and provisions that a new FDI regime could entail, and dispute settlement procedures are central to their scheme. They explicitly include both rights and obligations for three sets of actors: host governments, home governments, and corporations. The provisions concerning host governments' obligations would concern the right of establishment, national treatment, and state intervention; host governments' rights would concern their regulatory and taxing authority. Home governments would have an obligation to recognize host governments' rights to regulate the activities of corporations, but they would also have the right to tax and regulate the activities of corporations. Corporations would

91. DEANNE JULIUS, *FOREIGN DIRECT INVESTMENT: THE NEGLECTED TWIN OF TRADE* 29 (1991).

92. However, there now appears to be widespread support among OECD members for the inclusion of a dispute settlement mechanism in a multilateral investment agreement.

93. JULIUS, *supra* note 91, at 31. It should be further noted, however, that the World Bank's orientation toward FDI has become more positive in recent years. *See supra* section G.

94. Julius, *supra* note 3, at 283. Her analysis includes an interesting comparative historical assessment of several eras (FDI regimes) and also the results of a small informal survey of chief economists and government affairs directors of multinational firms in Europe, the United States, and Japan. The importance of effective dispute settlement procedures is evident from both the historical and survey evidence.

95. Bergsten & Graham, *supra* note 6.

also have obligations; in particular, they would be obliged to accept the laws of host and home governments as they pertain to the activities of corporate entities within their respective territories, and they would also be obliged to eschew restrictive business practices.

Such a network of rights and obligations would presumably produce occasional disputes between host and home governments, between host governments and corporations, and between home governments and corporations. As to inter-government disputes, Bergsten and Graham note:

No matter how tightly these rights and obligations are constructed, . . . there will emerge cases where it will be not clear under the rule which government has claim to regulate a particular transaction or activity. Thus, an important adjunct to the rule will be a means by which disputes between home and host nation governments over jurisdiction can be settled . . .<sup>96</sup>

For disputes involving corporations, Bergsten and Graham also note the importance of dispute settlement procedures:

[W]ithout a dispute settlement mechanism that was capable of dealing effectively with disputes that might arise between nation states and international corporations, it is difficult to envisage the investment accord as having much meaning or import. Indeed a rule-driven means of settling such disputes lies at the core of the utility of such an accord.<sup>97</sup>

Although disputes between corporations and governments would often be settled within the legal system of the given government, Bergsten and Graham suggest that there would be three kinds of cases "in which the legal system of a nation state could prove unsatisfactory" for dispute settlement:

1. A government believed that an international corporation was pursuing practices in geographic areas that were outside its jurisdiction but were nonetheless detrimental to its interests and in violation of obligations of the firm under the accord.
2. A firm believed that regulations or policies affecting its operation implemented by a government were inconsistent with

the obligations of that government under the accord and where efforts to resolve the matter with agencies of that government did not lead to resolution of the issue of possible inconsistency. If a firm believed that regulations or policies affecting its operations placed upon it by two different governments put it in a situation where following one set of regulations or policies would contravene the second set.<sup>98</sup>

They foresee a two-stage dispute settlement process for addressing these types of disputes between corporations and governments:

1. One of the parties to the dispute appeals to a panel, the sole role of which would be to determine if there were merit to the appeal. 'Merit' here would be decided largely on procedural grounds, e.g., by the following criteria: Had efforts been made to resolve the dispute through consultation between the affected parties or through the established legal procedures of the affected government? Did the dispute involve interpretation of the investment accord, and, in particular, did it appear *prima facie* that a party to the dispute could be in violation of some provision of the accord?
2. If this panel judged that there was merit to the appeal, the substantive issues of the dispute would be heard by a second panel. This panel would be empowered to recommend a solution to the dispute.<sup>99</sup>

It remains to be seen, of course, how the dynamics of economic diplomacy will evolve to determine the fates of these and other proposals.

## CONCLUSION

It has been fifty-one years since the Bretton Woods conference leading to the establishment of the World Bank and the International Monetary Fund, and it has been nearly that long since the creation of the GATT and the United Nations. The substantial increases in the stocks and flows of foreign direct investment, particularly since the mid-eighties, together with the increased interdependencies between investment and trade and between investment and technology flows, have created new pressures on these international economic institutions. The creation of

the WTO and the changes in GATT's dispute settlement procedures in the Uruguay Round agreement, as well as the incorporation of novel dispute settlement procedures in the NAFTA, provide specific legal foci for the further evolution of dispute settlement procedures. In addition, however, there is continuing momentum to reform the international regime for foreign direct investment more generally, and dispute resolution procedures will be central to that process. The central dispute settlement items now on the agenda for international institutional reform efforts include the following:

1. What problems are likely to emerge in the implementation of the new dispute settlement procedures at the WTO, and how should they be remedied? Should those procedures be expanded to include firm-government disputes?
2. Should the OECD's work on a Multilateral Agreement on Investment include provisions concerning dispute settlement procedures? If so, what should the elements be, and how will they relate to the procedures established by other multilateral agreements and bilateral investment treaties?
3. Should the NAFTA's dispute settlement provisions be used as a model for other regional and multilateral arrangements—such as for an APEC investment code?
4. How can the EU resolve questions about its legal and institutional competence to address FDI-related issues, particularly in its external relations?
5. Should the procedures of ICSID be reformed so that it is more frequently used?
6. What should be the role in the larger international regime of the non-governmental arbitration centers? Can they effectively manage the prospective increases in the volume and variety of investment-related disputes?
7. Are there contradictions in the provisions of existing bilateral investment treaties and multilateral agreements, and, if so, how should they be eliminated?
8. In what industries, if any, should there be sector-specific dispute settlement procedures, and how should those be related to other more generalized and encompassing procedures?
9. How can disparate approaches to dispute resolution that are embodied in different legal traditions be accommodated in an institutional reform process?

10. What provisions, if any, concerning inter-firm disputes should there be in international agreements among governments?

In view of the scope of this agenda, it is tempting to suggest new high-profile global negotiations with the objective of creating a single new comprehensive organization concerned with FDI—one that would include dispute settlement procedures as an integral element. However, lengthy, complex, and contentious negotiations to create such an institution could create uncertainties that may deter FDI during a potentially prolonged period of negotiations.

A more modest approach—but one that is probably also more expeditious and effective—is to establish as soon as possible an inter-agency "Working Group on International Direct Investment" of representatives from the following international agencies: IMF, OECD, UNCTAD, World Bank Group, and WTO. This combination of agencies has an impressive array of analytic capabilities and negotiating experiences to draw upon. The Working Group initially can be a relatively small, low profile group focussed on ways the individual components of the existing system can be improved in the short-term, but the Working Group can, at the same time, explore the possibility of creating a comprehensive new organization for FDI in the longer term. Thus, such a working group can identify gaps, contradictions, and other deficiencies in the present regime and analyze alternative solutions to those deficiencies.

The Working Group should be chaired by the OECD because the expertise of the Secretariat, the experience of the government representatives, and the diplomatic momentum on investment issues all suggest that the OECD is the organization now most likely to exhibit effective leadership.<sup>100</sup> The option of transferring the activities of the Working Group to the WTO should be kept open, however, since the Uruguay Round agreements establish schedules for reviews and/or negotiations in four to five years on a variety of issues that are related to FDI. A shift of activity on international economic issues from the OECD to the WTO in the analytic work on trade in services, which began at the OECD in the early seventies and then moved to the GATT for the Uruguay Round negotiations, provides an interesting parallel.<sup>101</sup> Further, the agreement

100. The observation of existing diplomatic momentum on investment issues in the OECD is based on discussions with OECD officials during December 1994.

101. For an analysis of the evolutionary process of framing analytic issues on services trade in the OECD, the eventual negotiation of those issues in GATT, and the role of experts in that process, see William J. Drake & Kalypso Nicolaidis, *Ideas, Interests and Institutionalization: "Trade in Services" and the Uruguay Round*, 46 INT'L ORGANIZATION 37 (1992).

on shipbuilding is a precedent for a "free standing" international agreement that includes non-OECD countries in an agreement negotiated under the auspices of the OECD. Preliminary work on a Multilateral Agreement on Investment at the OECD indicates that there is a consensus that any such agreement should also be a "free standing" agreement open to non-OECD countries. The activities of the proposed inter-agency Working Group on International Direct Investment would complement and inform the development of a free-standing Multilateral Agreement on Investment under the auspices of the OECD. In addition, such an arrangement would facilitate an expansion of the consensus-building process to include non-OECD countries.

Much of the work of the inter-agency Working Group can be done by task forces—each chaired by one of the agencies. For instance, a task force on dispute settlement can be chaired by the World Bank in light of the role of ICSID. The ten items above are suggestive of the scope of the agenda for such a task force.

Such an array of task forces can advance the analytic work on these and other topics associated with FDI while the political and diplomatic issues of FDI regime change are clarified. As part of the process of clarifying political issues, the Working Group will need to decide whether to invite observer groups or create advisory committees. An elaborate network of formal advisory groups might impede the progress of the Working Group. Yet, the political and technical support of such groups will be important to the long-term prospects for success of any major efforts to reform the FDI regime.

In any case, because foreign direct investment has emerged as an important "new issue" on the agenda for international institutional reform and because it is likely to remain a central issue on that agenda for the foreseeable future, there are likely to be new developments in international law as a result of increased interest in the treatment of investment disputes. The continuing development of investment dispute settlement procedures thus presents important opportunities to advance the rule of law in international economic relations.

APPENDIX I  
PROVISIONS IN URUGUAY ROUND AGREEMENTS CONCERNING INVESTMENT  
AND DISPUTE SETTLEMENT PROCEDURES

Agreement	Articles and Other Provisions Concerning:	
	Investment	Dispute Settlement
World Trade Organization	IV <sup>a</sup>	III(3), IV(3)
Trade in Goods, incl. TRIMs	1-9; Annex	VIII
General Agreement on Trade in Services (GATS)	I(2), XXVIII(d)	XXIII <sup>b</sup>
Trade-Related Aspects of Intellectual Property Rights (TRIPs)	none <sup>c</sup>	64
Dispute Settlement Understanding	Appendices 1-2	1-27; Appendices 1-4
GATT 1994	none	VI, XXII, XXIII
Implementation of GATT 1994 article VI (Anti-dumping)	none	17
Implementation of GATT 1994 article VII (Customs Valuation)	none	19
Pre-shipment Inspections	none	8
Rules of Origin	none	8
Import Licensing	none	6
Plurilateral Trade:		
Civil Aircraft	none	none
Dairy	none	none
Government Procurement	none	XXII
Bovine Meat	none	none
Anti-dumping	none	none
Technical Barriers	none	14
Subsidies and Countervailing Duties	none	4,30
Safeguards	none	138
Agriculture	none	19
Sanitary and Phytosanitary Regulations	none	11 35-37
Textiles	none	8

Source: Derived by the author from RESULTS OF THE URUGUAY ROUND, *supra* note 1.

<sup>a</sup> Establishes structure of WTO, including General Council, Council for Trade in Goods, Council for Trade in Services, and Council for Trade-Related Aspects of Intellectual Property Rights—all of which have investment-related responsibilities.

<sup>b</sup> Also, Annex on Financial Services (article 4) and Annex on Air Transportation (article 4).

<sup>c</sup> While the TRIPs agreement does not explicitly refer to investment, it will directly impact a number of investment-related issues.

## APPENDIX 2

## PRINCIPLES AND REPRESENTATIVE PROVISIONS CONCERNING DISPUTE SETTLEMENT, AS SUMMARIZED IN WORLD BANK STUDY

*In Tribunal Awards and Legal Writings*

Recourse to international arbitration is dependent on agreement of the parties. Once the parties have consented to submit their dispute to such arbitration, they should carry out their undertaking and abide by the award. Parties may, however, condition their agreement to resort to international arbitration on the prior exhaustion of local remedies. [152]

*In National Investment Codes*

Disputes between the Government and foreign investors will be settled by local courts. The parties may, however, agree to have recourse instead to international or domestic conciliation or arbitration. [129]

*In Bilateral Investment Treaties*

Any dispute relating to an investment established in the territory of either Contracting State by a national or company of the other Contracting State shall, as far as possible, be settled amicably through consultation between the parties to the dispute. Any such dispute that cannot be so settled within three (six) months from the date of the first written request to enter into such consultation shall, if the investor consents in writing, be submitted to the International Centre for Settlement of Investment Disputes for settlement in accordance with provisions of the Convention on the Settlement of Disputes between States and Nationals of Other States opened for signature in Washington on March 18, 1965. [56]

Any dispute relating to an investment established in the territory of either Contracting State by a national or company of the other Contracting State shall, as far as possible, be settled amicably through consultation by the parties to the dispute. Should the parties fail to arrive at an amicable settlement within three (six) months from the date of the first written request to enter into such consultation, the dispute shall be settled by arbitration in accordance with the [other provisions of the treaty]. [56]

The dispute shall be settled by a Tribunal consisting of three members appointed in the following manner. Within two months of the request for arbitration, each party shall appoint one member of the Tribunal,

and the two members shall, within two months of their appointment, agree on a third who shall act as Chairman of the Tribunal. [56-57]

If within the periods specified [elsewhere in the treaty] the appointments therein mentioned have not been made, either of the parties to the dispute may request the [Secretary-General of the International Centre for Settlement of Investment Disputes/Chairman of the International Court of Arbitration of the International Chamber of Commerce] to make the necessary appointments. [57]

The Tribunal shall reach its decision by a majority of votes. Such decision shall be final and shall be binding on both parties. Each party shall bear the cost of its own member of the Tribunal and of its representation in the arbitration proceedings; the cost of the Chairman and the remaining costs shall, unless the Tribunal decides otherwise, be borne by both parties equally. The Tribunal shall determine its own procedure. [57]

*In Regional and Other Multilateral Agreements*

Investment disputes between States and foreign investors that cannot be amicably settled shall be submitted to the competent courts of the host States. [102]

Parties may agree, however, to submit such disputes to other dispute settlement procedures, either alternatively or subsequently to national review procedures. [102]

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Source: Adapted by the author from THE WORLD BANK GROUP, SURVEY OF EXISTING INSTRUMENTS *passim* [pages are as indicated for each paragraph] (1992).

## APPENDIX 3

## DISPUTE SETTLEMENT PROCEDURES IN "LEGAL FRAMEWORK FOR THE TREATMENT OF FOREIGN INVESTMENT"

*Guideline V*

1. Disputes between private foreign investors and the host State will normally be settled through negotiations between them and failing this, through national courts or through other agreed mechanisms including conciliation and binding independent arbitration.

2. Independent arbitration for the purpose of this Guideline will include any *ad hoc* or institutional arbitration agreed upon in writing by the State and the investor or between the State and the investor's home State where the majority of the arbitrators are not solely appointed by one party to the dispute.

3. In case of agreement on independent arbitration, each State is encouraged to accept the settlement of such disputes through arbitration under the Convention establishing the International Center for Settlement of Investment Disputes (ICSID), if it is a party to the ICSID Convention or through the "ICSID Additional Facility" if it is not a party to the ICSID Convention.

*Report on Guideline V*

[ ] Particularly in the context of arrangements with States, disputes are normally resolved through negotiations and relatively rarely by recourse to contentious procedures. Part 1 of Guideline V further encourages the negotiated resolution of conflicts between foreign investors and their host States. In case negotiations fail, the courts of the host State will normally and unless otherwise provided have jurisdiction over disputes arising out of investments made in the country. In most countries, it is however possible for States and foreign investors to refer their differences to such alternative mechanisms as conciliation or binding arbitration. Recourse to such mechanisms is dependent on agreement between the parties to make use of the mechanism for the dispute in question. In the field of foreign investment, parties frequently do agree to refer their disputes to arbitration in particular. This practice is endorsed by Section 1 of Guideline V.

[ ] One of the advantages of arbitration is that it offers parties great scope to structure as they see fit their dispute settlement procedures. Their decisions on such procedures will be embodied in their agreement to have recourse to arbitration. In this context, States in particular may, as a condition of their agreement to refer disputes with foreign investors

to arbitration, require the investor to resort to local administrative or judicial remedies before initiating such arbitration. This possibility is recognized by such instruments as the Convention establishing the International Centre for Settlement of Investment Disputes (ICSID) and several bilateral investment treaties. It is not however mentioned in the guidelines as it is rarely pursued in practice.

[ ] The arbitration that Guideline V envisages as a possible alternative to adjudication before national courts is impartial or independent arbitration. It is widely acknowledged that in the field of international investment arbitration in particular arbitrators should be, and be seen to be, impartial and independent.<sup>a</sup> At the same time, arbitrators are generally chosen through appointments by the parties to the dispute in question. One of the perceived advantages of arbitration is in fact the opportunity that it thus gives parties to have their dispute decided by judges of their own choosing. In appointing arbitrators, each party may naturally wish to select persons who may be expected to be sympathetic to the point of view of the appointing party. To ensure the necessary impartiality of the tribunal as a whole, arbitral tribunals thus commonly consist of one arbitrator appointed by each side and a presiding arbitrator appointed by agreement of the parties or by a neutral appointing authority designated by the parties. An alternative that avoids the costs to the parties of a three-arbitrator panel is to submit the dispute to a sole arbitrator appointed by both parties or by a third party entrusted by them with the role of making such an appointment. Where however the appointment of a sole arbitrator or of a majority of arbitrators is made by one party only, the independence of the tribunal could easily be put in doubt. Section 2 of Guideline V emphasizes the importance of avoiding such a procedure and excludes a tribunal so constituted from the definition of independent arbitration.

[ ] The independence and impartiality of arbitrators receive particular emphasis in the rules of ICSID, the international conciliation and arbitration forum sponsored by the World Bank and specially designed to handle disputes between States and foreign investors.<sup>b</sup> Provisions for the resolution of such disputes in bilateral investment treaties, national

<sup>a</sup> See, e.g., ALAN REDFERN & MARTIN HUNTER, *LAW AND PRACTICE OF INTERNATIONAL COMMERCIAL ARBITRATION* 213-25 (1991).

<sup>b</sup> See ICSID Convention at arts. 14(1) and 40(2); Ibrahim F. I. Shihata, *The Experience of ICSID in the Selection of Arbitrators, Address Before the Sixth Joint Colloquium*, 6 NEWS FROM ICSID 1, 4 (1989). For general descriptions of ICSID and ICSID arbitration, see, e.g., ARON BROCHES, *ARBITRATION UNDER THE ICSID CONVENTION* (1991); IBRAHIM F.I. SHIHATA, *TOWARDS A GREATER DEPOLITICIZATION OF INVESTMENT DISPUTES: THE ROOTS OF ICSID AND MIGA* (1993); and Paulsson, *supra* note 79, at 380.

investment codes and individual investment agreements frequently refer to the arbitration procedures of ICSID. The widespread acceptability of ICSID procedures, indicated by the large number of countries (120) that have so far signed the ICSID Convention, and by the reference to ICSID arbitration in hundreds of large investment contracts, may be due, in addition to its relatively low cost, to the fact that it is the only form of arbitration where awards are not subject to subsequent judicial review in ICSID member countries. ICSID in fact provides two kinds of independent arbitration procedures: ICSID Convention arbitration procedures, which are available for cases where both the home and the host State of the investor are parties to the ICSID Convention; and arbitration procedures under the so-called ICSID Additional Facility, which are available for cases where either the home or the host State is not a party to the Convention. References to both types of procedures are frequently included in the provisions referred to above of bilateral investment treaties and national investment codes. Part 3 of Guideline V further encourages such use, as appropriate, of procedures provided by the ICSID Convention or Additional Facility.

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Sources: THE INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT/THE WORLD BANK, II GUIDELINES ON THE TREATMENT OF FOREIGN INVESTMENT AND REPORT TO THE DEVELOPMENT COMMITTEE AND GUIDELINES ON THE TREATMENT OF FOREIGN INVESTMENT 30-31, 44 (1992) (footnotes have been modified slightly from the original source to conform with journal style requirements).

## TOWARD A GENERAL AGREEMENT ON THE REGULATION OF FOREIGN DIRECT INVESTMENT

MICHAEL A. GEIST\*

Considering the important developments of the last half-century, the growth of foreign investments and the expansion of the international activities of corporations . . . and considering the way in which the economic interests of states have proliferated, it may at first sight appear surprising that the evolution of law has not gone further and that no generally accepted rules in the matter have crystallised on the international plane.

The International Court of Justice.<sup>1</sup>

### INTRODUCTION

With international trade issues capturing much of the business world's attention, the growth and importance of foreign direct investment (FDI) has gone somewhat unnoticed, despite comments such as those of the *International Court of Justice (ICJ)*.<sup>2</sup> In fact, FDI growth far outpaced trade growth throughout the 1980s, with trade increasing at a compound rate of five percent annually compared to twenty percent annually for FDI.<sup>3</sup> Moreover, as discussed in Part I of this Article, investment is often a key determinant of trade since a large percentage of trade occurs between affiliated companies.<sup>4</sup> Despite its apparent importance, states have thus far been unable, or unwilling, to conclude an international agreement regulating FDI.

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\* Assistant Professor Dalhousie Law School, Halifax, Nova Scotia. LL.M., Cambridge, 1994; LL.B., Osgoode Hall, York University, 1992. This Article is based on a thesis submitted by the author while studying at Cambridge. The author would like to thank Dr. Barry Rider for his supervision; Rene Geist, Guy Harpaz, Jayaprakesh Sen, and Philip Solomon for their helpful comments on earlier drafts; Sam Geist for making Cambridge a reality; and Allison Gelfen for her continued love and support.

1. *Belgium v. Spain*, 1970 I.C.J. Rep. 3, at 47-48 [hereinafter *Barcelona Traction*].

2. Although there is no uniform definition for foreign direct investment, the one advocated by the *International Monetary Fund* has increasingly gained acceptance as the standard definition. The IMF defines foreign direct investment as: "Investment that is made to acquire a lasting interest in an enterprise operating in an economy other than that of an investor, the investor's purpose being to have an effective voice in the management of the enterprise." INTERNATIONAL MONETARY FUND, *BALANCE OF PAYMENTS MANUAL* ¶ 408, at 136 (4th ed. 1977) [hereinafter *BALANCE OF PAYMENTS MANUAL*].

3. DEANNE JULIUS, *GLOBAL COMPANIES AND PUBLIC POLICY* 14 (1990).

4. *Id.* at 74.