ENDANGERED ELEMENT OF ICSID ARBITRAL PRACTICE: INVESTMENT TREATY ARBITRATION, FOREIGN DIRECT INVESTMENT AND THE PROMISE OF ECONOMIC DEVELOPMENT IN HOST STATES.

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Abstract

The omission to define the term ‘investment’ in the ICSID Convention is one of the most critical decisions that have led to the inconsistent jurisprudence and the resulting debate associated with the propriety of the ICSID Convention and investment treaty arbitration. The legislative history and the circumstances leading to the birth of the ICSID Convention strongly suggest that its main objective is the protection and promotion of economic development in the host State. Most of the propositions aimed at giving a meaning to the term ‘investment’ in ICSID arbitral practice have focused more on whether the scope of the meaning of ‘investment’ should extend to any plausible ‘economic activity or asset’. The focus of this approach is flawed. It has relegated the element of considerations for ‘contribution to economic development’ of the host State to the back seat of investment treaty arbitration. This article challenges this relegation as ahistoric to the ICSID Convention. The article argues that from the standpoint of the host State, the ICSID Convention is meaningless if the analysis of the relationship between FDI and investment treaty arbitration excludes considerations for economic development in view of the omission in the ICSID Convention. The article hinges this argument on the implication of international development as the main foundation of the ICSID Convention. The article acknowledges the difficulty that may be associated with the determination of an ‘investment’ that contributes to economic development, but contends that relegating the element of ‘contribution to economic development’ to the back seat of investment arbitration is contrary to the main objective of the ICSID Convention in host States.

INTRODUCTION

The jurisdiction of ICSID arbitration is regulated by Article 25(1) of the ICSID Convention. The gateway to ICSID arbitration and practice is more often than not, determined by the meaning that may be ascribed to the term ‘investment’ pursuant to the ICSID Convention and the applicable investment agreement governing the investment

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The jurisdiction of the Center shall extend to any legal dispute arising directly out of an investment, between a Contracting State (or any constituent subdivision or agency of a Contracting State designated to the Center by that State) and a national of another Contracting State, which the Parties to the dispute consent in writing to submit to the Center. When the parties have given their consent, no party may withdraw its consent unilaterally.
dispute. In other words, the jurisdiction of ICSID arbitration depends on the answer to the question whether or not the foreign investment that led to the investment dispute arbitration is an ‘investment’ in line with the ICSID Convention. ICSID arbitral practice have recognized and applied certain elements in the determination of an ‘investment’ because the term is undefined in the ICSID Convention. In spite of the considerable consensus on certain elements that have been applied by arbitral practice in the determination of the meaning of investment, the jurisprudence of ICSID comprising scholars, academics and ICSDI arbitral Tribunals are split on the definition of ‘investment’. Part of the debate revolves around the question whether there should be a separate consideration of ‘contribution to economic development’ of the host State of FDI as an element or characteristics of the meaning of an ‘investment’ as the term is understood in the context of investment treaty arbitration in ICSID arbitral practice. However, the debate and propositions for a broader meaning of ‘investment’ without a consideration whether the ‘investment’ contributes to the economic development of the

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2 For e.g. see David A. R. Williams & Simon Foote, *Recent Developments in the Approach to Identifying an “Investment” Pursuant to Article 25(1) of the ICSID Convention* in EVOLUTION IN INVESTMENT TREATY LAW AND ARBITRATION 42, 47-8 (Chester Brown & Kate Miles eds., Cambridge Univ. Press, 2011). (The authors addressed the piecemeal approach to the identifying an investment pursuant to the ICSID Convention. They observed that ‘…the progressive development of international investment law on the topic of investment has led, perhaps inevitably, to piecemeal and sometimes inconsistent approaches to determining whether there is an investment as the term is used in Article 25(1)’).  
3 CHRISTOPH H. SCHREUER, LORETTA MALINTOPPI, AUGUST REINISCH & ANTHONY SINCLAIR, THE ICSID CONVENTION: A COMMENTARY 133 (Cambridge Univ. Press, 2d ed. 2009)(2001). See also Salini Construttori S.P.A and Italtrade S.P.A v. Kingdom of Morocco, ICSID Case No. ARB/00/4, Decision on Jurisdiction, (Jul. 29, 2001), http://italaw.com/cases/documents/959 (last visited May 1, 2013). The Salini ICSID Tribunal espoused what is now commonly known as the ‘Salini Criteria’ in the determination of an ‘investment’ in the context of the ICSID Convention. The decision of the Tribunal contributed immensely to the intellectual foundation of the debate over the meaning of ‘investment’ in the ICSID Convention. At paragraph 52 the Tribunal held inter alia that ‘… [t]he doctrine generally considers that investment infers: Contributions, certain duration of performance of the contract and participation in the risks of the transaction. In reading the Convention’s preamble, one may add the contribution to the economic development of the host State as an additional condition. In reality, these various elements may be interdependent. Thus, the risks of the transaction may depend on the contribution and duration of the performance of the contract. As a result these various criteria should be assessed globally, even if, for the sake of reasoning the Tribunal considers them individually here’. The prescriptions of the ‘Salini criteria’ have been criticized because the criteria espoused by the decision are not supported by the ICSID Convention. Thus it has been argued that applying the Salini criteria could lead to challenging the jurisdictional requirements of the ISCID Convention as a matter of law. See also A Martin, *Definition of Investment: Could a Persistent Objector to the Salini Tests be found in ICSID Arbitral Practice?* 11 GLOBAL JURL. 1, 2 (2011) [hereinafter Martin].
host State forgoes a critical objective of the ICSID Convention.\(^4\) In this respect, the proponents appear to be more obsessed with extending the meaning of ‘investment’ to include any conceivable economic activity in the host State. The analysis in this article is focused on the element of ‘contribution to economic development’ from the standpoint of what may be considered the main objective of the ICSID Convention and the legitimate expectation of hosts States in ICSID arbitration and international investment law.\(^5\) In carrying out the tasks in this article, it is pertinent to briefly comment on the concept of law and international development. A case could be made that an analysis of the relationship between law and international development may be utilized in understanding the circumstances and considerations that led to the negotiation and ratification of the ICSID Convention.

It has been argued that, the rule of law with reference to development, ‘has become significant not only as a tool of development policy, but as an objective for development policy in its own right’.\(^6\) This article queries the mechanism of investment treaty arbitration and Foreign Direct Investment (FDI) in the context of the protection and promotion of foreign investment within the framework of the ICSID Convention.\(^7\) The ICSID Convention is part of an international mechanism for the arbitration of investment disputes negotiated by sovereign States to promote and protect foreign investment for economic development.

It is trite to state that economic development is the outcome of a successful relationship between law and economics. For example Clarke, Murrell and Whiting have argued that, China’s economic development and transformation success could be traced

\(^{4}\) For e.g, see Julian D. Mortenson, *Quiborax SA et al v Plurinational State of Bolivia: The Uneasy Role of Precedent in Defining Investment* 28 (2) ICSID Review, 254-261 (2013) (arguing that Article 25 of the ICSID Convention ‘should properly be understood to reach any plausible economic activity or asset’).

\(^{5}\) In the context of investment treaty arbitration, investment disputes may arise from the violations of foreign investment agreements or contracts as a result of the interference or the omission of the host State to act in a manner envisaged by the applicable legal regime or international investment agreements.


\(^{7}\) *The ICSID Convention, supra* note 1.
to the important role and process of law. These commentators find support in Justice Ocran who, writing extra judicially, posited that the study of law and development should be consciously used to meet the challenges of economic development. The process of economic development involves the interplay of law and economics that impact the quality of life and infrastructural development of a sovereign State. Promoting and sustaining the economic development of a State challenges the political and economic activities of all sovereign States. Indeed, the phenomenon of globalization continues to make economic development a major challenge in developing countries. Developing countries strives to catch up with global economic development through the creation of international wealth for the benefit of its citizens and the international economy. The recent economic downturn in the United States that spread to Europe and other parts of the world is a testament to the reality of the inter-connectivity of the global economy. From a legal perspective, the process of economic development makes the relationship between law and development relevant to the challenges of economic development.

The reference to law in the context of this article implies the combination of efficient domestic and international laws including statutes, systems, international norms and treaties designed to promote and sustain economic development. The thesis of Trubek and Santos is that, the theory of law and development ought to be examined as ‘the intersection of current ideas in the spheres of economic theory, legal ideas, and the policies and practices of development institutions’. In spite of the recognition of some

9 TAWIA M. OCRAN, LAW IN AID OF DEVELOPMENT: ISSUES IN LEGAL THEORY, INSTITUTION BUILDING, AND ECONOMIC DEVELOPMENT IN AFRICA 17 (Ghana Publishing Corporation 1978).
11 See Robert Pritchard, The Contemporary Challenges of Economic Development in ECONOMIC DEVELOPMENT, FOREIGN INVESTMENT AND THE LAW 1, 3 (Robert Pritchard ed., Kluwer Law International 1996) (arguing that ‘[a]ll countries aim to be as “sovereign” and economically self-sufficient as they can possibly can. They have a need therefore for domestic financial institutions and mechanisms to encourage the highest possible level of domestic savings and to develop efficient domestic capital markets...’).
12 The reference to development in this article is in the context of economic development.
13 Trubek & Santos, supra note 6, at 4.
scholars of the relationship between law and development, there is still considerable debate on the actual role of law in economic development particularly with reference to international economic development. In other words, there is no consensus on the precise nature of the relationship between law and development. Pritchard puts the issue this way, ‘[d]espite the consensuses which have emerged on many of these issues [economic development and foreign investment] the development process remains something of an international intrigue… many of the cast of this intrigue are very suspicious of each other’. However, this article hypothesizes that, the place and role of law cannot be divorced from the process of economic development because law and development are mutually reinforcing factors. According to Morgan, ‘[t]he relationship between law and development, in the context of an integrated global economy, has moved from a niche area of study to an increasing central location in scholarly inquiry over the past several decades’. The intrigue complained about by Pritchard may be unraveled by the progressive development or reform of the international norms, systems or laws that interpret the process and the factors that impact economic development. Economists believe that, one of the factors that can influence and contribute to economic development is FDI in the territory of the host nation. Most developing countries, solicit FDI to attract foreign capital that will in turn contribute to the economic development of the domestic economy.

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15 Trubek & Santos, supra note 6 at 5.
16 Pritchard, supra note 11 at 4. The cast of the intrigue referred to by Pritchard comprises foreign investors and the host State with respect to the relationship between law and economic development.
19 See Emma Ujah, Foreigners Invest $20 billion in Nigeria within 3 Years-Onokjob-Iweala, Vanguard Newspaper (Lagos), Nov. 12, 2013, http://issuu.com/vanguardngr/docs/12112013/1. (Ujah reported, quoting Nigeria’s coordinating Minister for the Economy, Dr. Ngozi Okonjo-Iweala, that Nigeria’s effort at attracting FDI has been successful in the last 3 years with the country up USD$20
Put simply, FDI is the acquisition of assets, the transfer of capital or the direct participation by a foreign investor in the economic activities of the host State.\textsuperscript{20} FDI inflows into developing countries in Africa and Asia have increased since the 1980s.\textsuperscript{21} The legal regime regulating FDI facilitates access to international market, higher exports and a means of importation of foreign capital into the local economy. It is intended to create employment and impact infrastructural development of the host economy.\textsuperscript{22} In other words, the inflow of FDI should contribute to economic development. One reason for the need and increase of FDI to developing countries is that, regardless of the abundance of human and natural resources in these countries, such countries lack the necessary capital and technology to promote economic activities that can effectively develop the domestic economy.

The emergence and the interaction of the variables of FDI investment treaty arbitration and economic development in the paradigm of international investment law is the product of the need to create a system of international law to attract investment to developing countries as a means to advance economic development.\textsuperscript{23} As a result, the improvement of the international investment climate through the protection of foreign investment became one of the principal objectives of international investment law.\textsuperscript{24} Accordingly, the World Bank created a Multilateral Investment Guarantee Agency (MIGA) as an incentive to attract private international investment for the purpose of promoting economic development in developing countries.\textsuperscript{25} To be clear, the protection
of foreign investment is based on the theory that, the protection of foreign investment will encourage private international investment in developing economies. In what appears to be a tacit support of this theory, the World Bank also initiated a concerted effort to design and establish a mechanism for international arbitration of investment disputes between State Parties and foreign investors. The investment treaty arbitration mechanism initiated by the World Bank was created through the successful negotiation of the ICSID Convention.26

The tasks of this article are hinged on the theoretical assumption that host States connotes developing countries that offers investment arbitration in exchange for FDI into their domestic economies. The underpinnings of the ICSID Convention were designed to enable developing countries give assurances for the settlement of investment disputes through arbitration in order to attract private international investments. This article analyzes the matrix of FDI and contribution to economic development in investment treaty arbitration under the ICSID Convention with reference to the jurisprudence of ICSID arbitral practice. Part II-III of the article is devoted to the examination of the history of the ICSID Convention through a critical analysis of the travaux préparatoires and the law applicable in ICSID arbitration. In Part IV, the article argues that the mechanism for investment treaty arbitration attracts FDI. This connection between FDI and investment treaty arbitration should make considerations for the independent consideration of contribution to economic development imperative in arbitral practice with respect to the ICSID Convention. Part V examines the classical theory of FDI as the intellectual foundation why ‘contribution to economic development’ should be the core element in investment treaty arbitration. The article hypothesizes that the purpose of the ICSID Convention is the protection and promotion of foreign investment for economic development in host States. Accordingly, it draws inferences from the classical theory to theorize that economic development is the fundamental objective of FDI and the legitimate expectation of hosts States with respect to the ICSID Convention. Part VI reviewed the decisions of the SGS cases with reference to the definition of ‘investment’

26 The ICSID Convention, supra note 1.
as the term is understood under the ICSID Convention.27 This part of the article advances the argument that ‘contribution to economic development’ should and ought to be the core element in investment treaty arbitration in the context of the ICSID Convention. In conclusion, the article acknowledges the difficulty that may be associated with the determination of an ‘investment’ that contributes to economic development, but contends that relegating the element of ‘contribution to economic development’ to the back seat of investment treaty arbitration endangers the main objective of the ICSID Convention in host States. This endangerment could generate dissatisfaction among hosts States against the ICSID Convention.

I. A Brief History of the ICSID Convention and the Promise of Economic Development

At the end of the Second World War, there was a worldwide need to promote policies and programs that could spread international development particularly in less developed countries in the third world. The attainment of political independence by third world countries from erstwhile colonial masters that included Great Britain, France, Belgium, Portugal and Spain also made international development imperative in developing countries. Against this background, the United Nations commissioned a report by the Secretary General on the international flow of private capital pursuant to Resolution 622 C (VII) passed in 1952.28 Taking note of the latter, this august body consequently passed a Resolution to promote the international flow of private capital for the economic development of underdeveloped countries at its 510th Plenary Meeting of 11 December 1954.29 This Resolution received overwhelming support from the international community. It was passed on the basis that the flow of private international investment to

27 The SGS Cases were better known for bringing the debate over the scope and interpretation of umbrella clauses to the fore of ICSID arbitration. Umbrella Clauses are provisions in BITs or investments agreements that create an international obligation on the host State to guarantee the observance of the investment contract it entered with the foreign investor. See generally Jarrod Wong, Umbrella Clauses in Bilateral Investment Treaties: Of Breaches of Contract, Treaty Violations, and the Divide Between Developing and Developed Countries in Foreign Investment Disputes, 14 GEO. MASON L. REV. 135-77 (2006).
host States contributes to economic development. The premise of the Resolution is that productive activities resulting from the international flow of private capital contributes to the standard of living and the development of human and natural resources. The Resolution confirmed that, ‘…the flow of private investment has not been commensurate with the needs in those areas where rapid development is essential for economic progress.’ Based on the necessity to attract foreign investment for proportionate international economic development, the Resolution recommended that countries seeking foreign investment should:

1 (a) Re-examine, wherever necessary, domestic policies, legislation and administrative practices with a view to improving the investment climate; avoid unduly burdensome taxation; avoid discrimination against foreign investment; facilitate the import by investors of capital goods, machinery and component materials needed for new investment; make adequate provision for the remission of earnings and repatriation of capital

(b) Develop domestic and foreign information services and other means for informing potential foreign investors of business opportunities in their countries and of the relevant laws and regulation governing foreign enterprise.

In what may be a confirmation of the purpose of creating a viable international investment climate for foreign investment as stated above, the Resolution declared that… ‘in order for new foreign investments to be an effective contribution to the economic development of the under-developed countries, it is advisable to take into account among other things, the situation with regard to previously established enterprises so as not to affect their normal development with the national interest’. Furthermore, under Article 1 (a-b), the Resolution recommended policy initiatives that might encourage and protect foreign investment in the territory of the host State. Admittedly, it appears that the declaration in Article 6 of the Resolution points to the overall responsibility and purpose of foreign investment. This perspective may be justified by the Article’s apparent reference to and emphasis of the economic growth of developing countries as the natural consequences of the implementation of the recommendations under Article 1 (a-b).

30 id. at preamble.
31 id. at para 1 (a-b).
32 id. at para 6.
A. Options and Limitations of the Settlement of Investment Disputes under Customary International Law.

The Resolution passed by United Nations significantly influenced the promotion of foreign investment through private international investment. It may have laid the foundation for the relationship of the variables of foreign investment and economic development. The efforts of the United Nations contributed to the principles of customary international law regulating the principal actors in international investment law.\(^{33}\) However, the traditional principles of customary international law regulating foreign investment subjected foreign investors to various barriers in their home courts as well as the courts of the host State of their investments. Foreign investors lacked legal standing under international law. Since States are the traditional subject of international law, foreign investors must go through their home State and host States’ legal systems to settle foreign investment disputes. Also, as Judge Tomka rightly noted, under customary international law, a State is only responsible for a breach of an international obligation occasioned by an unlawful act inimical to the principles of customary international law.\(^{34}\) As a result, private disputes between foreign investors and State Parties became very difficult to pursue.\(^{35}\)

It has been suggested that under customary international law, a State may assert sovereign immunity to restrict the jurisdiction or judicial power of a foreign court in respect of claims against the State or protect that State’s property against foreign enforcement measures.\(^{36}\) In a case where sovereign immunity is asserted, a foreign investor is left with limited options to pursue foreign investment claims. Similarly, a foreign investor may also be denied legal process to assert investment claims based on

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\(^{33}\) See Muchlinski, *supra* note 24 at 6. (Stating that ‘[t]he earliest legal rules concerning foreign investors and investment assumed a tripartite set of actors: the home state, the host, and the investor’).

\(^{34}\) Peter Tomka, *Are States Liable for the Conduct of Their Instrumentalities?: Introductory Remarks in IAI SERIES ON INTERNATIONAL ARBITRATION NO. 4, STATE ENTITIES IN INTERNATIONAL ARBITRATION* 7, 8-9 (Emmanuel Gaillard and Jennifer Younan eds., Juris Publishing 2008).

\(^{35}\) See *INVESTOR-STATE ARBITRATION* 11, 20 (Christopher F. Dugan, Don Wallace, Jr., Noah D. Rubins & Borzu Sabahi eds., Oxford Univ. Press 2008) (The editors explained that the assertion of sovereign immunity by the host State is absolute to prevent foreign investment claims against the State Party).

the ‘act of state doctrine’. By operation of this doctrine, the home State of the foreign investor denies the latter access to its court system on the ground that the cause of action is the act of a foreign state that is not subject to the jurisdiction of the investor’s home state. Therefore, the only clear avenue for the foreign investor to pursue investment claims against foreign states was through diplomatic intervention or what was generally referred to as ‘gunboat diplomacy. Diplomatic intervention or gunboat diplomacy is practiced because of the international law obligation of States to protect alien property for the development of trade and investment in developing countries. In other words, this obligation under customary international law is placed under the rubric of the ‘Responsibility of States for injuries to Aliens’. Gunboat diplomacy is a process that allowed foreign investors to obtain relief in respect of foreign investment claims through their government diplomatic intervention or the use of armed force. Gunboat diplomacy was mainly employed by capital exporting countries mostly in cases of expropriation of alien property or investments. Gunboat diplomacy brought limited

37 See David L. Jones, Act of Foreign State In English Law: The Ghost Goes East, 22 VA. J. INT’L L. 433, 435–6 (1982) (discussing the rule of non-justiciability in the context of the act of a foreign State). See also Banco Nacional de Cuba v. Sabbatino, 176 U.S. 398 (1964) where the United States Supreme Court held inter alia in an expropriation case that: ‘However offensive to the public policy of this country and its Constituent States an expropriation of this kind may be, we conclude that both the national interest and progress towards the goal of establishing the rule of law among nations are best served by maintaining intact the act of state doctrine in this realm of its application.’


39 Id. See also Edwin M. Borchard, Theoretical Aspects of International Responsibilities of States, Max-Planck Institute for Comparative Public Law and International Law 223, 224–30 (1929), http://www.zaoev.de/01_1929/1_1929_1_a_223_250.pdf (last visited Jan.24, 2014)(discussing the theories and foundation of the international Responsibilities of State for injuries to alien property as a part of international law).


41 The allegation of expropriation of alien property or foreign investment against the host State is one of the most critical factors that define the nature of foreign investment disputes from the prism of investment treaty arbitration. Expropriation or nationalization of foreign investments in the territory of the host State is permissible under international investment law. However, it must be for a public purpose, in accordance with due process of law and payment of compensation. The payment of adequate compensation has, more often than not, been the bone of contention in cases where expropriation is alleged against the host State by the foreign investor. Expropriation may be direct or indirect. Expropriation may be considered direct and easily ascertained, where an allegation of the actual taking of the alien property or foreign investment in the territory of the host State can be sustained against the latter. See generally Homayoun Mafi, Controversial Issues of Compensation in
ssuccor to some foreign investors. There are notable examples where it has been employed by the United States and France on behalf of their foreign investors in Venezuela and Mexico respectively in the 1860s.42

However, recourse to gunboat diplomacy to settle foreign investment disputes subjects the foreign investor to proving that the local remedies available in the host State have been exhausted to no avail. A foreign investor may also be required to prove citizenship to his home government. Exhaustion of local remedies subjected the foreign investor to the jurisdiction of the legal system of the host State. On the exhaustion of local remedies, Borchard explains that ‘the government of the complaining citizen must give the offending government an opportunity of doing justice to the injured party in its own regular way, and thus avoid, if possible, all occasion for international discussion’. 43 The home State of the foreign investor may refuse to directly seek relief on behalf of an investor for political reasons regardless of whether or not the foreign investor has a good claim under international law. From the perspective of the foreign investor, subjecting investment claims to the jurisdiction of the host government may lead to a conflict of interest between the host government, the home government and the foreign investor creating an institutional bias. The conflict of interest between the foreign investor and the home State may also arise because of political expediency in the diplomatic relationship between the home State and the host State. Salacuse has expressed the frustration of foreign investors this way:

The potential for conflict among the three parties [the foreign investor, the host country and the home country] is ever present. In most instances, conflicts arising out of foreign investments, results in disputes between the investor on the one hand, and the host country government, on the other. The home country of the investor may become engaged at the encouragement or request of its national. In such conflicts, the host country often considers the dispute to be subject to the host country law and host country legal and judicial process… [the] host government tends to see foreign laws and foreign courts as irrelevant to any issues.

42 Dugan et al supra note 35 at 27.
43 EDWIN M. BORCHARD, DIPLOMATIC PROTECTION OF CITIZENS ABROAD OR THE LAW OF INTERNATIONAL CLAIMS 817 (Banks Law Publication Company 1915). See also Dugan et al supra note 35 at 30.
of disagreement with foreign investors and may view any potential interference as an outright challenge to national sovereignty.\textsuperscript{44}

In addition to the issue of conflict of interest, there may also be serious questions about the impartiality and the credibility of the host country’s legal system because of the probable influence or prejudice of the host government against the foreign investor.\textsuperscript{45} At the same time, the foreign investor has no recourse to the home country legal system because of the doctrine of state sovereign immunity in customary international law. Consequently, the difficulties presented by the limitations of the options to settle investment disputes made foreign investors to be wary and skeptical about the prospects of their investments abroad.

Ultimately, the protection of foreign investment became a problematic issue in the international efforts aimed at promoting foreign investment for economic development. The economic development of the host State and the home State of the foreign investor could have been gravely affected if something was not done to address the legitimate concerns of foreign investors. Foreign investors from developed countries desire bigger foreign markets for investment in order to maximize FDI and repatriate profits that contribute to economic development in their home States. In contrast, developing countries desire to attract foreign investment through private international investment for economic development. Therefore, there arose a potential peril of the variables of foreign investment and economic development because a mechanism for the protection of foreign investment was ineffective or could not overcome its limitations with reference to the settlements or adjudication of foreign investment claims. In other words, the absence of a generally acceptable system for the resolution of foreign investment disputes became the weakest link in the international quest for the promotion and protection of foreign investment. The problem became a huge issue for international organizations charged with international development including the World Bank.

B. The World Bank, The ICSID Convention and the Resolution of Investment Disputes

\textsuperscript{44} See JESWALD W. SALACUSE, THE LAW OF INVESTMENT TREATIES 40-1 (Oxford Univ. Press 2010).
\textsuperscript{45} id.
The World Bank\textsuperscript{46} was established in 1944 to assist European postwar reconstruction and development at the end of World War II. With its success in Europe, the bank’s responsibilities metamorphosed into pursuing programs for the global reduction of poverty and promotion of development in third world countries.\textsuperscript{47} In the 1960s, the World Bank became concerned about the problem of the settlement of disputes between foreign investors and host governments as an issue affecting the promotion of foreign investment. On several occasions, the World Bank was approached to mediate in the settlement of investment disputes between foreign investors and host governments.\textsuperscript{48} These overtures to the Bank to intervene were made against the background of the limited and unacceptable options open to foreign investors and governments under customary international law. In a note to the Executive Directors of the World Bank on ‘Settlement of Disputes between Government and Private Parties’ the General Counsel of the World Bank suggested the establishment of an international arbitration as a way out of the imbroglio. The General Counsel phrased the problem this way:

1. The many studies which have been undertaken in recent years concerning ways and means to promote private foreign investment have almost invariably discussed the problem of the settlement of disputes between foreign private investors or entrepreneurs and the Government of the country where the investment is made. In many cases these studies have recommended the establishment of international arbitration and/or conciliation machinery.

2. The absence of adequate machinery for international conciliation and arbitration often frustrates attempts to agree on an appropriate mode of settlement of disputes. Tribunals set up by private organizations such as the International Chamber of Commerce are frequently unacceptable to governments and the only


The General Counsel then proposed the establishment of an international mechanism for the conduct of arbitration of investment disputes through the creation of a permanent tribunal and the provision of facilities for conciliation as an alternative to arbitration. The General Counsel’s suggestions were based on the premise that States should recognize the possibility of direct access by foreign investors to an international platform for the settlement of disputes and that agreement to submit such disputes to international agreements are binding international obligations. On September 19, 1961 recognizing that the World Bank is not fully equipped to resolve investment disputes, the President of the World Bank re-echoed the urgent need for an international arbitration system for investment disputes. The President declared that:

At the same time, our experience has confirmed my belief that a very useful contribution could be made by some sort of a special forum for the conciliation or arbitration of these disputes. The results of an inquiry made by the Secretary General of the United Nations showed that this belief is widely shared. The fact that governments and private interests have turned to the Bank to provide this assistance indicates the lack of any other machinery for conciliation and arbitration which is regarded as adequate by investors and governments alike. I therefore intend to explore with other institutions and other member governments whether something might not be done to promote the establishment of a machinery of this kind.

The proposal and the suggestions of the General Counsel to the Executive Directors of the World Bank thus laid the foundation for the process leading to the negotiation of the ICSID Convention.

The ICSID Convention is a product of three stages of intense negotiations that included a World Bank internal drafting stage, regional meetings of legal experts from participating States and convocation of member-states delegates. The convocation of delegates constituted the ‘Legal Committee’ that prepared the Convention final draft for

49 Id. at 2.
50 Id.
51 Id. at 3.
approval by the World Bank Executive Directors. The most critical consideration for the birth of the Center came out of the need to look for innovations that could accelerate international economic development. The discussions started in June of 1962 when a World Bank working group was commissioned under the leadership of Aaron Broches, the General Counsel of the Bank. The World Bank working group was mandated to produce a draft Convention for internal consideration. The first draft Convention produced by the working group extended jurisdiction to any dispute between the parties with a minimum amount in dispute of $100,000.00 without reference to any subject matter restrictions. Upon review of the initial draft produced by the World Bank working group, questions were raised concerning the need to separate political or commercial disputes from disagreements over legal and contractual rights.

The questions raised in the initial draft laid the foundation for the exclusion of political or commercial disputes from the jurisdiction of the ICSID. The second internal draft submitted in October of 1963 limited the jurisdiction of the Center to ‘any existing or future investment dispute of a legal character’. Having specified and distinguished political or commercial disputes from foreign investments, why was the term ‘investment’ not defined? There was a consensus among members of the World Bank working group that investment disputes to be adjudicated by the Tribunals constituted pursuant to the ICSID rules, must be purely of a legal character. The earliest omission to define ‘investment’ occurred when officials of the World Bank involved in the process at the time declared their keenness, not to create a process that could lead to incessant disputes over foreign investments. The view was particularly expressed that ‘to include a more precise definition would tend to open the door to frequent disagreements as to the applicability of the Convention to a particular undertaking, thus undermining the primary objective’. It is evident from the preamble of the ICSID Convention that the need for

53 id.
54 History of the ICSID Convention, supra note 48 at 33-4.
55 Id. at 19-46.
economic development through private international investments is the main purpose of the ICSID Convention. This article contends that the following propositions are discernible from the preamble of the ICSID Convention: (i) to give assurances in writing to foreign investors mostly from the developed economies of the protection of foreign investment (ii) encourage international economic development through private investments.

In support of the discernible propositions on the objective of the ICSID Convention, the history of the Convention confirmed that ‘if the plans established for the growth in the economies of the developing countries were to be realized, it would be necessary to supplement the resources flowing to these countries from bilateral and multilateral government sources by additional investment originating in the private sector’.

Therefore, the hypothesis is this: a mechanism that does not reflect or mandate the consideration of economic development of the host State is contrary to the primary purpose of the ICSID Convention. This article contends that, once there is the admission of foreign investment, there should be a corresponding determination of contribution to economic development. But, the deliberate omission to define ‘investment’ under the ICSID Convention appears to relegate the requirement of economic development to a back seat, and prioritizes assurances given to foreign investors within the framework of the ICSID Convention. The situation could make it difficult for developing economies to maximize the benefits associated with the purpose of the ICSID Convention.

1. The Council of the Legal Experts

This stage of the history of the Convention involved consultative meetings of legal experts of the negotiating parties that took place in Addis Ababa, Santiago, Geneva, and Bangkok between December 1963 and May 1964. During this phase the contentious issue of the meaning of ‘investment’ created a dichotomy between capital-importing countries and capital-exporting countries. Capital importing countries wanted a precise definition of investment while the capital-exporting countries preferred an unrestricted

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58 Mortenson, supra note 56 at 263.
approach to the nature of disputes the Center could adjudicate. It is on record that Sweden, canvassed for the exclusion of the term altogether.

To resolve the opposing contentions represented above, the World Bank proposed a definition of ‘investment’ for the first time. ‘Investment’ was defined as ‘any contribution of money or other asset of economic value for an indefinite period or, if the period be defined for not less than five years’. The developed nations contended that the proposed definition is too restrictive, in that it could create impediments to investment agreements. In contrast, developing countries articulated a narrower definition of ‘investment’. Some developing countries, wanted a regulatory framework that could guarantee the exercise of sovereignty through control of internal affairs that might overlap with the conduct of FDI.

The Working Group reported that, there was an impasse between the contending blocs and within the Working group on how to define ‘investment’. It would appear that, the World Bank favored a broad definition of ‘investment’ to protect international investments. This is because there was a consensus on the need to spread development to emerging economies; the protection of foreign investment was the problematic issue. It is debatable, whether the interests of foreign investors would be better served by a broader meaning of ‘investment’, but this perhaps explains the reason why the initial draft sent to the Committee of Legal Experts did not contain a proposed definition of ‘investment’. There is no contrary reason in the history of the Convention except the reservations expressed by the Working Group of the World Bank at the drafting stage. The UK broke the impasse by proposing a solution that allows a broader reference to ‘investment’ with

59 See Consultative Meetings of Legal Experts cited in History of the ICSID Convention, supra note 48 at 395-470. See also Mortenson, supra note 56 at 285.
60 See History of the ICSID Convention, supra note 48 at 400-401. The delegate from Sweden ‘doubted the wisdom of including in Article II [of the working draft emphasis added] the reference to “investment”. He suggested that it should be transferred to the preamble’. At 469-470, the delegate from India agreed with the reservations shared by Thailand and Ceylon and argued that the lack of a precise meaning of the investment disputes to be referred to the Center is a profound weakness.
61 Draft Convention on the Settlement of Investment Disputes between States and Nationals of other States (11 September 1964) cited in History of the ICSID Convention, supra note 48 at 623. See also Mortenson, supra note 56 at 286.
62 id.
powers given to State parties to stipulate their own definition of ‘investment’. The UK’s proposition was widely supported and accepted. The Convention was eventually passed for ratification in March of 1965. The UK’s proposal did not define ‘investment’ per se but may have deferred the issue to State parties in their conduct of FDI.⁶⁴

On the notification mechanism, Article 25 (4) of the ICSID Convention provides that ‘[a] ny Contracting State may, at the time of ratification, acceptance or approval of this Convention or at any time thereafter, notify the Center of the class or classes of disputes which it would or would not consider submitting to the jurisdiction of the Center’. The solution proposed by the United Kingdom on the definition of ‘investment’ may be contrary to one of the primary purposes of the Convention. It appears to be tailored to cater for the protection of foreign investments without any economic development considerations from the perspective of the host State. There was considerable agitation that the meaning of ‘investment’ ought to be in accordance with the public interest. According to the General Counsel of the World Bank, ‘nearly all the definitions [of investments] which had been proposed were in fact definitions of what the delegates concerned believed their governments would in fact wish to submit to the center’.⁶⁵

Similarly, the consent provisions under Article 25 (4) enables host States to limit foreign investments in areas they wish not to submit to the jurisdiction of the Center to protect the State advancement of economic development. Ultimately, the consent provisions could foreclose investment opportunities that may lead to economic development. Either way, the consideration for economic development as the fundamental purpose of the ICSID Convention was defeated. Commenting on the controversy surrounding the omission to define ‘investment’, Mortenson argued that there was an unsuccessful attempt to define investment. He stated that the consequence of the ‘failed’ definition of ‘investment’ is to give State parties to the ICSID Convention the freedom to define the term in their individual transactions.⁶⁶ Mortenson’s analysis is incomplete because it fails to give adequate consideration to the implication of his

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⁶⁴ See Schreuer, supra note 57 at para 82. The UK compromise is the basis of the notification mechanism in Article 25(4) of the Convention.

⁶⁵ Summary Proceedings of the Legal Committee Meeting (Nov.27, 1964) cited in History of the ICSID Convention, supra note 48 at 707.

⁶⁶ Mortenson, supra note 56 at 292.
argument on ‘contribution to economic development’ as one of the main objectives of the ISCID Convention. The commentator was more frustrated about the failure of the Convention to define ‘investment’ in much broader terms to include ‘any plausible economic activity’ because he saw the compromise in Article 25 (4) as appeasement to an influential Latin American Executive Director of the World Bank.67

2. The International Center for the Settlement of Investment Disputes

The ICSID Convention is a multilateral treaty that provides for settlement of investment disputes through arbitration. The Center was established to provide facilities for conciliation and arbitration of investment disputes between State Parties and Nationals of the signatories to the Convention according to the provisions of the ICSID Convention.68 In other words, the Center facilitates the resolution of investment disputes and does not by itself directly adjudicate investment disputes between contending parties. Through the ratification of the ICSID Convention, State Parties assent to the enforcement of the protections of foreign investments in exchange for private international investments to develop the host economy.69 Sornarajah contends that, a critical factor that influenced the negotiation of the ICSID Convention was the desire of developed economies to increase protections for their investors abroad.70 It has been held that, the Center is conducive to the security of foreign investments through the provision of the mechanism for investment treaty arbitration.71 Therefore, it may be argued that the Center was established as part of a mechanism for the protection of foreign investments.

The primary seat of the Center is at the principal office of the World Bank in Washington, DC located in the United States of America. But, the seat of the Center for the purpose of investment treaty arbitration may be moved from place to place on the

67 id.
68 See the ICSID Convention, supra note 1 at Art. 1(2).
69 See Susan D. Franck, Foreign Direct Investment, Investment Treaty Arbitration and the Rule of Law, G’BAL BUS. & DEV. L. J. 337, 338 (2007)(analogously nothing that ‘treaties offer foreign investors a series of economic rights, including the right to arbitrate claims, in hopes of attracting Foreign Direct Investment that will bring a country...economic stability’).
approval of the administrative council.\textsuperscript{72} The Center maintains a panel of Conciliators and Arbitrators that may be selected to arbitrate investment treaty claims between State parties and foreign investors. The Center was established principally to address the shortcomings of customary international law in the resolution of investment disputes between private and State parties in the mechanics of foreign investment through private international investment. The advent of the Center made it possible for the first time under international law, for a foreign investor to litigate claims directed against foreign states.\textsuperscript{73} Thus, Article 25 (1) provides that:

\begin{quote}
The jurisdiction of the Center shall apply to any legal dispute arising directly out of an investment between a Contracting State (or any constituent subdivision or agency of a Contracting State designated by that State to the Center) and a national of another Contracting State which the parties in dispute consented in writing to submit to the Center. When the parties have given their consent, no party may withdraw its consent unilaterally.\textsuperscript{74}
\end{quote}

According to the ICSID Convention, the national of another Contracting State includes natural and juridical persons in law.\textsuperscript{75} Based on Article 25 (1) of the ICSID Convention, a Tribunal constituted under the Rules of the Center may exercise jurisdiction over investment claims based on consent and agreement of the State Party and the foreign investor.\textsuperscript{76} It should be noted that, the task of investment arbitration and conciliation within the framework of the Center is the responsibility of Conciliation and Arbitration Tribunals constituted pursuant to the ICSID Convention. In other words, the Center does not directly settle foreign investment disputes through arbitration or conciliation.\textsuperscript{77}

\begin{footnotesize}
\begin{itemize}
\item[72] The ICSID Convention, \textit{supra} note 1 at Art. 2.
\item[73] This statement may also be interpreted to mean that the right of investors to arbitrate claims against the host State may no longer be stymied by the host State legal system or the assertion of sovereign immunity.
\item[74] The ICSID Convention, \textit{supra} note 1 at Art. 25 (1).
\item[75] \textit{id.} at Art. 25(2) a-b.
\item[76] The consent of the host State and the foreign investor to arbitrate investment claims is the bedrock of the jurisdiction of ICSID with respect to the ICSID Convention. Pursuant to the ICSID Convention, once there is consent to submit investment disputes to arbitration, that consent in itself excludes every other remedy in law. See ICSID Convention, \textit{supra} note 1 at Art.26. For a more detailed examination of the element of consent in investment treaty arbitration see Christoph Schreuer, \textit{Consent to Arbitration} 1, 5 (2007), \url{http://www.univie.ac.at/intlaw/con_arbitr_89.pdf} (last visited Jan. 9, 2013).
\item[77] Report of the Executive Directors, \textit{supra} note 52 at para 15.
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However, the ICSID Regulations and Rules that include the Rules of Procedure for Arbitration Proceedings (Arbitration Rules) are not the only process for settlement of investment disputes through arbitration. There are other internationally recognized arbitration rules that may be utilized to institute investment arbitration. Examples include the United Nations Commission on International Trade Law (UNCITRAL) Rules, the Stockholm Chamber of Commerce (SCC) Rules and the International Chamber of Commerce (ICC) Arbitration Rules. However, most international investment agreements provide for ICSID arbitration. Further analyses of these other Rules that may be utilized for investment arbitration are outside the scope of this article for obvious reasons. However, the analysis of the law applicable in ICSID arbitration should recognize economic development considerations in the host State.

II. The Law Applicable in ICSID Arbitration

The law applicable in ICSID arbitration comprises substantive law and procedural rules. It is trite that substantive law must be distinguished from procedural rules where both regimes are applicable in the resolution of disputes between parties. Substantive law determines the rights and obligations while procedural rules provide the framework for the enforcement of the rights and obligations defined by substantive law. The State party and the foreign investor choose the law applicable to ICSID arbitration based on the doctrine of party autonomy, but ICSID arbitration procedural law or rules are dictated by

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78 See RUDOLF DOLZER & CHRISTOPH SCHREUER, PRINCIPLES OF INTERNATIONAL INVESTMENT LAW 255 (Oxford Univ. Press, 2008); Christoph Schreuer, Travelling the BIT Route: Of Waiting Periods, Umbrella Clauses and Forks in the Road, 5 J. WORLD INVESTMENTS & TRADE LAW 231, 231 (2004).

79 The ICSID Arbitration Rules and the UNCITRAL Rules are the most commonly used Rules in investment arbitration. State Parties and foreign investors often define ‘investment’ in BIT(s) and other international investment agreements that may be applicable to the investment disputes. Under the other arbitration Rules such as UNCITRAL, ICC, SCC, a definition of investment only need to satisfy the BIT or investment agreement definition, whereas an ICSID claim would need to satisfy both the definition in the BIT itself and the ICSID Convention. The test whether an ‘investment’ exists in an ICSID claim is often referred to as the ‘double barreled’ test or the ‘double keyhole approach’. For a further discussion of the ‘double barreled’ test in ICSID arbitral practice see K Yannaca-Small, Definition of “investment”: An Open-ended Search for a Balanced Approach” in ARBITRATION UNDER INTERNATIONAL INVESTMENT AGREEMENTS: A GUIDE TO THE KEY ISSUES 249-50 (Yannaca-Small ed., Oxford Univ. Press 2010).


the relevant provisions of the ICSID Convention. In other words, while the parties to international arbitration within the framework of the ICSID Convention may agree on the applicable procedural law, such agreement cannot be contrary to the procedural provisions of the ICSID Convention. This limitation applies even where a particular procedural provision could only be read into the letters of the ICSID Convention in the context of investment treaty arbitration. A typical example is afforded by the principle of public policy in the application of procedural rules to regulate international arbitration. Along this line, Hirsch elaborates that the doctrine of ‘public policy’, ‘prohibits an arbitration tribunal from applying rules that are contrary to the public policy of the state in which an arbitration is being conducted or that of the international community’.\(^\text{82}\) Hirsch’s analogy is a common principle acceptable in international commercial arbitration, but it may be applicable to investment treaty arbitration on the theory that arbitral Tribunals may not apply a procedural rule that may violate a peremptory norm of international law. In what appears to be an attempt to justify the extension of the doctrine of public policy to ICSID arbitration, this article is drawn to the instructive hypothesis of Schreuer who notes that:

> The matter is different with regard to certain basic international tenets that may be described as the public policy of the international community. These principles would include but not be restricted to the peremptory rules of international law. Examples are the prohibition of slavery, piracy, drug trade, terrorism and genocide, the protection of the basic principles of human rights and the prohibition to prepare and wage an aggressive war. Otherwise applicable rules, whether contained in the investment agreement itself or adopted by reference, which violate these basic principles would have been disregarded by an ICSID tribunal. If any theoretical justification is needed for this conclusion, it can be found in the foundation of ICSID in the Convention and hence in international law which, in a wider sense, is the *lex fori* of ICSID arbitration.\(^\text{83}\)

Schreuer’s postulation above is significant to the theme of this article in two ways. First, it alludes to an international public policy with reference to investment arbitration in the context of the ICSID Convention. Secondly, it references the foundation of the ICSID Convention as the premise of the consideration of public policy. It seems self-evident that the foundation of the ICSID Convention and by extension ICSID arbitration

\(^{82}\text{id. at 113.}\)
\(^{83}\text{Schreuer, supra note 57 at para 33.}\)
is international economic development and the protection of foreign investment. Therefore, it would seem that the determination of the law applicable in ICSID arbitration should recognize considerations for contribution to economic development and the protection of foreign investment. More so, it is a basic tenet of the interpretation of treaties that a treaty like the ICSID Convention should be interpreted according to its object and purpose.\(^{84}\)

The substantive law applicable to ICSID arbitration is determined in accordance to the provision of Article 42(1) of the ICSID Convention which provides:

\[\text{The Tribunal shall decide disputes in accordance with such rules of law as may be agreed by the parties. In the absence of such agreement, the Tribunal shall apply the law of the Contracting State party to the dispute (including rules on the conflict of laws) and such rules of international law that may be applicable.}\]

Article 54(1)\(^{85}\) of the ICSID Additional Facility Rules confirms the salient provisions of Article 42 (1) of the ICSID Convention.

Regardless of the clear provision of Article 42(1), it has been suggested that in practice, arbitral Tribunals employs a combination of the intention of the parties and the law that has a reasonable connection to the investment dispute in the determination of the substantive law that is applicable in international arbitration.\(^{86}\) This suggestion is supported by the opening sentence of Article 42(1), which accords, with the doctrine of party autonomy and encourages the State parties and foreign investors to express their intention with reference to choice of law to enable a Tribunal to give effect to that intention. When read in full, Article 42 (1) draws a sharp distinction between the applicable law chosen by the State party and the foreign investor and the responsibility bestowed on the Tribunal to apply the domestic law of the host State and principles of


\(^{85}\) Article 54 (1) provides:

The Tribunal shall apply the rules of law designated by the parties as applicable to the substance of the dispute. Failing such designation by the parties, the Tribunal shall apply (a) the law determined by the conflict of laws rules which it considers applicable and (b) such rules of international law as the Tribunal considers applicable.

\(^{86}\) Hirsch, *supra* note 81 at 117.
international law subject to conflict of law rules. Pursuant to Article 42(1), the choice of law agreed by the State party and the foreign investor may be in a self-contained investment agreement or national investment legislation. ICSID jurisprudence is consistent with the principle that where there is a conflict between domestic and international law, the latter prevails.\textsuperscript{87} Similarly, one author explains that ‘where the tribunal can find no guidance from the investment agreement on a particular issue, this may be treated by the tribunal as an ‘absence of agreement’ on the applicable law concerning that particular question’.\textsuperscript{88} Once a Tribunal determines that there is an absence of agreement on the choice of law, that Tribunal must be guided by the second sentence of Article 42(1) which mandates an ICSID arbitration Tribunal to apply domestic law and the rules of international law that may be applicable. The connection of foreign investment to domestic law may arise out of a contract between the State party and the foreign investor.\textsuperscript{89} Once there is a clear choice of law between the investor and the State Party in the investment contract, the Tribunal should respect the intention of the parties pursuant to the first part of Article 42(1).\textsuperscript{90}

However, the language of the second sentence of Article 42 (1) appears to give ICSID arbitration Tribunals the discretion to determine the applicable law through an analysis of the relevant law of the host state and principles of international law. On one hand and with reference to the second sentence of Article 42 (1), the host state law is relevant only to the extent that it is not in conflict with the principles of international law. On the other hand, the exercise of discretion conferred on arbitral Tribunals by the second sentence of Article 42 (1) could be unpredictable and lead to inconsistency of arbitral Tribunals in the interpretation of the second sentence of Article 42 (1) of the ICSID Convention. The

\textsuperscript{87}For e.g. see CME Czech Republic B.V. v. The Czech Republic, UNCITRAL Arbitration Proceedings, Final Award, Mar.14, 2003) 9 ICSID Reports 291, para 91 where the Tribunal held inter alia that ‘[t]o the extent that there is a conflict between a national law and international law, the arbitral tribunal shall apply international law’.


\textsuperscript{90}See Emmanuel Gaillard, \textit{The Role of the Arbitrator in Determining the Applicable Law in THE LEADING ARBITRATORS GUIDE TO INTERNATIONAL ARBITRATION} 185 (Lawrence W. Newman ed., Juris Publishing Inc. 2003).
major driving force of this distinction is the extent of the application of domestic law and rules of international law. Banifatemi comments that a fundamental problem for Tribunals may be striking a balance of the law applicable in investment arbitration in the absence of an unequivocal choice of law clause.\textsuperscript{91} Two ICSID arbitration cases demonstrate the unpredictability of arbitral Tribunals and find support in Banifatemi’s skepticism with reference to the second sentence of Article 42 (1).

In Wena Hotels Ltd v. Arab Republic of Egypt\textsuperscript{92} the ad hoc committee considered whether the Tribunal applied the applicable Egyptian law pursuant to the second sentence of Article 42(1). In the absence of a clear choice of law pursuant to Article 42(1), the ad hoc Committee held that in determining the applicable law, the history of the ICSID Convention allowed for both domestic and international law to have a role. It added that both legal orders could be applied where there is justification and likewise, international law can be applied by itself.\textsuperscript{93} This decision is in sharp contrast with the ruling of the Tribunal in Klockner Industrie-Anlagen GmbH v. Republic of Cameroon\textsuperscript{94}. In this annulment proceeding, the ad hoc Committee considered the question whether the application of domestic law pursuant to Article 42 (1) can be fulfilled by reference to one basic principle. The ad hoc Committee apparently examined this query against the second sentence of Article 42 (1) of the ICSID Convention. In response to the question, the ad hoc Committee held that ‘Article 42 (1) clearly does not allow the arbitrator to base its decision solely on the rules or principles of international law’.\textsuperscript{95} According to the ad hoc Committee, the ‘arbitrators may only have recourse to the principles of international law only after having inquired into and establish the content of the law of the state party to the dispute and after having applied the relevant rules of the State’s law’.\textsuperscript{96}

\textsuperscript{91} Banifatemi, supra note 89 at 201.
\textsuperscript{92} Wena Hotels Ltd v. Arab Republic of Egypt, ICSID Case No ARB/98/4, Decision on Application for Annulment (Feb. 5, 2002) 41 International Law Materials 933, 933
\textsuperscript{93} id at 941.
\textsuperscript{94} Klockner Industrie-Anlagen GmbH and Others v. Republic of Cameroon, ICSID Case No. ARB/81/2, Decision on Annulment Proceedings (May 3, 1985) 2 ICSID Reports 95, 95-163.
\textsuperscript{95} id at para 69.
\textsuperscript{96} id.
III. Does Investment Treaty Arbitration Mechanism attract FDI?

On the hypothesis that FDI contributes to economic development, it is fair to ask whether investment treaty arbitration mechanism attracts FDI. It has been suggested that the substantive or procedural right to investment treaty arbitration is one of the strongest incentives for the protection of foreign investment in the host State.\(^\text{97}\) As mentioned earlier, investment arbitration is designed to restore investors’ confidence and promote foreign investment against the limitations presented by the traditional methods of investment dispute resolution under customary international law. The protection of foreign investment is one of the most critical components of the international investment regime.\(^\text{98}\) It is unlikely that a foreign investor will engage in FDI in the host State without concrete assurances for the protection of foreign investment. One way this has been done is through consent to investment treaty arbitration, a means by which the foreign investor can enforce their substantive and procedural rights against the host State.

Before embarking on the journey that metamorphosed into the ICSID Convention, the World Bank also espoused the view that ‘improved methods for the settlement of investment disputes would contribute to an improvement in the investment climate and would thereby tend to promote the flow of private capital’.\(^\text{99}\) It was against this background that the World Bank took steps to study an international arrangement to facilitate the settlement of investment disputes between State parties and foreign investors that eventually midwifed the ICSID Convention. However, protection of foreign investment is not the only factor that may stimulate FDI. Potential foreign investors may also consider economic and political factors like market size, production costs and political stability of the host State. But the protection of foreign investment appears to be one of the most critical considerations in the conduct of FDI from the perspective of the foreign investor. It would seem that if there is no protection mechanism, the consideration of the other factors may become unnecessary.


\(^{99}\) See Note by the President to the Executive Director 28 December 1961 in History of the ICSID Convention, supra note 48 at 4.
The influence of the dispute settlement mechanism in attracting FDI is a contested issue. Some commentators believe that dispute settlement mechanisms, such as arbitration attracts FDI but others insist that isolating investment arbitration from other substantive treaty rights may be impracticable. There is limited empirical evidence in favor or against either position of the debate. However, based on the antecedents of the ICSID Convention, the limitations of customary international law on the settlement of disputes between the foreign investor and the State party and the relationship of FDI to economic development, a brief examination of the hypothesis on the issue is relevant to the task of this article.

Franck employed three hypothetical models with some evidence to explain the likely impact of investment treaty arbitration in attracting FDI to developing and host States. These models are: The Place Holding Model, The Political and Economic Reality Model and the Market Liberalization Model. Frank adopts these models to describe the overriding consideration of foreign investors that determines the flow of private international capital compared to the hypothesis that investment treaty arbitration mechanism attracts FDI. With reference to ‘Place Holding Model’, the author theorized that foreign investors may overlook the consideration of investment treaty arbitration mechanism to invest in a country that will provide an opportunity for them to establish a place in the economy of the host country. The author cited China as a typical example of this model. Franck conceded that an empirical evaluation of China’s BITs may give a better picture the effect of its BITs. But China’s success with attracting FDI has been traced to its extensive treaty network offering an investment treaty arbitration mechanism to foreign investors for settlement of investment disputes. However, Frank’s theory may be true prior to China’s reform and expansion of its investment treaty network including its unconditional consent to arbitration under the ICSID Convention. On the hypothesis of the Political and Economic Reality Model, the Frank articulated that

101 Franck, supra note 69 at 364-375.
102 id. at 357.
political and economic stability of the host State will make provisions for investment
treaty arbitration unnecessary. Frank referred to Australia as an example citing the Free
Trade Agreement between Australia and the United States that retains permission with
the Contracting Parties to permit arbitration of investment claims between the foreign
investor and the State party. It is conceivable that a stable economic and political
environment may positively impact FDI in the host state, but the premise of this model
appears to be based on the presumption that in a stable political environment investment
disputes are rare and unlikely. Even where they occur, the decision to authorize
investment arbitration lies with the Contracting Parties as in the case between Australia
and the United States concerning the Australian-United States Free Trade Agreement
(AUSFTA). 104 In fact, Article 11.16 (1) of AUSFTA provides:

If a [Contracting] Party considers that there has been a change in circumstances
affecting the settlement of disputes on matters within the scope of this chapter and
that, in the light of such change, the Parties should consider allowing an investor
of a party to submit to arbitration with the other Party a claim regarding a matter
within the scope of this chapter, the Party may request consultations with the
other Party on the subject, including the development of procedures that may be
appropriate. On such a request, the Parties shall promptly enter into consultations
with a view towards allowing such a claim and establishing such procedures.

Notwithstanding the above provision, Article 11.16 (2) of AUSFTA, allows an
investor to bring or arbitrate an investment claim directly against the other Party to the
extent that it is permitted under that Party’s law. The provision in the AUSFTA may be
likened to diplomatic intervention. The requirement of consultation at the instance of
either of the State Parties, may subject investors to the same limitations under customary
international law that negatively impacted FDI. The conflict of interests that may result
through diplomatic intervention spurred consideration for an alternative international
arrangement for the settlement of investment dispute that was championed by the World
Bank. Under international law, the espousal of diplomatic intervention and protection in
the context of international investment law is absolutely within the discretion of States. 105
The exercise of this discretion, more often than not, is subject to overriding political

104 Australia-United States Free Trade Agreement, AUSFTA, signed May 18, 2004 (entered into force
105 Kuusi, supra note 98 at 46.
interests that may be at variance with the interests of the foreign investor. Furthermore, through the Market Liberalization Model, Franck explains that reformation and modernization of an international investment regime in the host State will attract FDI regardless of whether or not there exists a mechanism for investment treaty arbitration. The author relied on the limited or the absence of investment treaty arbitration mechanism in the international investment regimes of countries such as Brazil and Ireland. Franck made her strongest point with the examples of Brazil\textsuperscript{106} and Ireland\textsuperscript{107} that have had a commendable attraction of FDI in spite of the near absence of provisions for investment treaty arbitration in their respective international investment regimes. But as the author noted, some trading countries are still skeptical and have been urging Brazil for example, to reform its international investment regime to reflect international standard and best practices that includes investment treaty arbitration.\textsuperscript{108}

There is no question that investment treaty arbitration mechanism is an incentive that can attract FDI to host States. Justice Mohammed Uwais, a former Chief Justice of Nigeria, argued that the mechanism for investment arbitration is a critical element to attract foreign investments into Nigeria, a developing country. According to Justice Uwais, ‘[t]he importance of international arbitration as the preferred choice of settlement of commercial and investment disputes cannot be over-emphasized’.\textsuperscript{109} Some commentators have merely suggested that an investment treaty arbitration mechanism should not be isolated from other treaty rights contained in international investment agreements. Even if one concedes to the reservations of the ‘non-isolationists’, it is hypothesized that the concept of the protection of foreign investment is incomplete without a mechanism for investment treaty arbitration. This article contends that investment treaty arbitration mechanism attracts FDI. One of the major reasons for the

\textsuperscript{106} Brazil has no BIT in force. Resolution of foreign investment disputes are regulated by national investment legislation.


\textsuperscript{108} Franck, \textit{supra} note 69 at 364.

proliferation of investment treaties is the procedural and substantive rights it offers to foreign investors to arbitrate investment claims directly against the host State.

IV. A Brief Analysis of the Classical Theory of FDI

The classical theory of foreign investments explains the relationship between foreign investment and economic development. The classical theory of foreign investment theorizes that the purpose of foreign investment is to develop the host economy. The premise of this theory is that foreign investments ought to be utterly beneficial to the host economy. This theory supports the hypotheses of this article on the relationship between foreign investment and economic development. Ball conveyed a convincing thesis on what appears to be the basis of the classical theory when he noted that, ‘nations that elect to pursue policies that tend to eliminate the private sector or discriminate against outside investment should be aware that they are denying themselves a source of capital that could otherwise greatly speed their own economic development’. Finding support in Ball, Sornarajah explains that the classical theory is supported by the fact that foreign capital exported into the host State through the process of foreign investment could be used for the public good which translates to economic development. In this regard Schreuer added that the impact of foreign investment on the host State economy accelerates creation of employment, infrastructural development, technology transfer and positively impacts facilities such as health care and transportation for the benefit of the investor and the domestic economy. The main gist of the classical theory is in accord with development economics, which encourages the economic interaction of local resources with private international capital to maximize the benefit of foreign investment to the domestic economy.

Development economics is a study of a branch of economic theory with a specific focus on institutions and policies that regulates the process of economic development in

110 See generally Sornarajah supra note 70 at 48-52.
111 George Ball, Address to the United Nations Conference on Trade and Development, 1964 extracted from Kuusi, supra note 98 at 37.
112 Sornarajah, supra note 70 at 51.
113 id.
less-developed countries.\textsuperscript{114} It is a form of economic liberalism that has been described as a theory of economic development that metamorphosed from a movement that arose from an international concern to end international poverty. The theory of economic liberalism is based on the assumption that industrialization is the path to economic development and that developing countries should create an environment for the capital that will facilitate industrialization for economic development.\textsuperscript{115} The classical theory is further strengthened by the notion that no meaningful economic development can take place in developing countries in the absence of foreign investment. As a result, the standing of foreign investment as a critical component of the international development agenda cannot be overemphasized.\textsuperscript{116}

Furthermore, it seems evident that the place and importance of foreign investment created the need for concerted efforts by international institutions not only to facilitate the flow of international investment but to create measures and international policies that might guarantee the protection of investments. Sornarajah’s thesis articulates that, ‘focus on these beneficial aspects of the foreign investment flows enables the making of the policy-oriented argument that foreign investment must be protected by international law’.\textsuperscript{117} The prescriptions of the classical theory may also be reflected in international instruments regulating the conduct of international investment law. The preamble of the ICSID Convention that alludes to the promotion and protection of foreign investment for the economic development of the host State is a classic expression of the classical theory of foreign investment. Similarly, the purpose and object of most international investment treaties are expressed in accordance with the hypotheses of the classical theory of foreign investment.\textsuperscript{118} The classical theory may also find eloquent expression in what Yusuf describes as the progression from the ‘rules of abstention’ to the ‘rules of international co-operation’ in the development of the rules of international law to reflect the

\textsuperscript{115} KENNETH J. VANDEVELDE, \textit{BILATERAL INVESTMENT TREATIES: HISTORY, POLICY, AND INTERPRETATION} 90 (Oxford University Press, Oxford 2010).
\textsuperscript{117} Sornarajah, \textit{supra} note 70 at 52.
\textsuperscript{118} \textit{id}. 

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emergence of a legal framework for economic development in developing countries. Yusuf uses his thesis to argue the case for a special treatment for low-income countries as the basis to address the reality of economic inequality. In Yusuf’s analysis, ‘the rules of abstention’, created a system where interaction between sovereign States was dominated by the politics of avoidance of war that was based on reciprocity with little or no emphasis on international cooperation between States. The premise of the ‘rules of international co-operation’, is a progression from the theory of abstention that recognizes the need for the maximization of international collaborative efforts ‘which in turn may widen the perception of these common interests and of the collaborative efforts to be undertaken in their pursuit’. Yusuf added that the emergence of the international co-operation was necessitated by the occurrence of international events that shaped the character of international law in the nineteenth and twentieth century. The author alluded to the Russian Revolution of 1917 and the emergence of the socialists States in Eastern Europe, a massive trend of independence of former colonies in Asia and Africa and the greater involvement of States in the control of economic activities in pre-World War II.

Nevertheless, the classical theory of foreign investment has been criticized for promoting inequality in the host State and for not doing enough for the eradication of poverty among the poor in the host State. In this sense, poverty is a symptom of underdevelopment in the host State. There are also legitimate concerns that the repatriation of capital by the foreign investor from the host State is much more than the capital inflow associated with the particular investment, thereby denying the host economy much needed capital that could be reinvested into the local economy to promote economic development. Similarly, the presumed advantage of technology transfer to the host State through foreign investment may not be the case. According to Sornarajah, ‘technology that has spent its cycle in its state of origin is introduced in the developing states where the product may be new’. Indeed, the transfer of management skills to local workers is uncommon with foreign investors in hosts States. The social corporate

120 id at 25.
121 Vandevelde, supra note 113 at 97.
122 Sornarajah, supra note 70 at 63.
responsibility of foreign investors in the form of infrastructural development that may include provision of healthcare, education, energy and social services are illusory in most cases.\textsuperscript{123} The criticisms of FDI in this respect are valid. For example, the presence of Shell Global and American oil giant, Chevron Oil operating in Nigeria’s oil rich Niger Delta has done little to improve the economic development of the region.

Despite the legitimate questions and criticisms of the classical theory of foreign investment, its underpinnings still dominate the phenomenon of globalization. As shown above, the classical theory is at the heart of the progressive development of international investment law. The purpose of FDI from the perspective of the host State is not in doubt; the protection of international investments in the host State was the issue because of the limitations for the protection of foreign investment created for the foreign investor by the nuances of customary international law. The promotion and protection of international investment should not be divorced from the purpose of international investments. The criticisms of the classical theory of foreign investment perhaps demonstrate that the problem with the classical theory is how to properly harness its tenets to ensure protection and promotion of foreign investment for economic development. If there is evidence that foreign investment promotes economic growth, then there is a stronger case why it ought to be recognized and considered that foreign investment should ‘contribute to the economic development’ of the host State in the context of investment arbitration.

V. The SGS Cases Revisited: Why there should be consideration of ‘contribution to economic development’ in ICSID Arbitration.

It is important to understand the divergent interests of the major players in the conduct of foreign investment with reference to the definition of ‘investment’.\textsuperscript{124} These interests may be reflected by two important considerations. Firstly, foreign investors either directly or within the framework of an applicable international investment agreement usually ensure that foreign investments are structured beyond a mere

\textsuperscript{123} id.
\textsuperscript{124} From an investment treaty arbitration perspective, the major players connected with conduct of FDI within the framework of Bilateral Investment Treaties and other international investment agreements are: The foreign investors (which is either a natural or legal person from the State party), the host government and ICSID. See STEPHEN D. COHEN, MULTINATIONAL CORPORATIONS AND FOREIGN DIRECT INVESTMENT (Oxford Scholarship Online, Oxford 2007).
contractual relationship to maximize the advantages offered by international arbitration. Such safeguards are mostly determined through an assessment of the definition of ‘investment’ in an investment agreement or other laws that forms part of the host State’s legal framework for the conduct of foreign investment relating to the transaction in issue.\(^{125}\) Secondly, host States prefer a definition of ‘investment’ that could stimulate the flow of foreign investments that have the potential to impact economic development. In what appears to be a confirmation of these contrasting interests, it has been argued that, ‘treaties [BITs] offer foreign investors a series of economic rights, including the right to arbitrate claims in hopes of attracting FDI that will bring a country infrastructure projects, financing, know-how, new jobs and, economic reality’.\(^{126}\)

These contrasting interests on the definition of ‘investment’ under the ICSID Convention were played out in the ICSID arbitration case of SGS Societe Generale de Surveillance S.A. v. Republic of the Philippines.\(^{127}\) In this case, the Republic of the Philippines entered into an agreement with Societe Generale de Surveillance S.A. (SGS), a Swiss company, to carry out, on an exclusive basis, Pre-Shipment Inspection (PSI) in any country of export to the Philippines. Under the contract, inspection would cover quality, quantity and price comparisons. The relevant articles of the agreement required SGS to maintain a liaison office in the Philippines and to provide free of charge: training courses for the Philippines Bureau of Customs (BOC), the provision of customs equipment to the BOC and maintenance thereof, intelligence/investigative consultant and a library stocked with the most comprehensive trade publications from the twenty leading exporting countries to the Philippines. The agreement at issue provided that all provisions were to be governed in all respects and construed in accordance with the laws of the Philippines and all disputes in connection with the obligations of either party to the agreement shall be filed in the Regional Trial Courts of Makati or Manila. In exchange for the performance of SGS’s obligations, the Philippines agreed to pay SGS, in Swiss

francs, a fee amounting to 0.6 percent of the Free On Board (FOB) value declared on the exporter’s final settlement invoice covering each shipment inspected. The Philippines and Switzerland have a binding treaty agreement for the Promotion and Reciprocal Protection of Investments.\textsuperscript{128}

SGS commenced investment treaty arbitration for alleged breaches of the agreement between it and the Republic of the Philippines by relying on the provisions of the Swiss-Philippines BIT. Citing relevant provisions of the BIT, SGS initiated arbitration under Article 25 (1) of the ICSID Convention contending that: there is a dispute of a legal nature; arising directly out of an investment; between a contracting State and a national of another contracting State and; the parties have consented in writing to ICSID arbitration.\textsuperscript{129} The Republic of the Philippines challenged the jurisdiction of the Tribunal contending that there was no ‘investment’ in the Philippines in accordance with the purpose of the ICSID Convention. The Philippines also argued that the dispute is purely contractual.\textsuperscript{130} The Tribunal found for SGS holding that the circumstances and elements of the services provided by SGS were sufficient to qualify the service as one provided in the Philippines. According to the Tribunal ‘[s]ince it was a cost to SGS to provide it, this was enough to amount to an ‘investment’ in the Philippines within the BIT’.\textsuperscript{131}

Similarly, in the earlier case of SGS Societe Generale de Surveillance S.A. v. Islamic Republic of Pakistan,\textsuperscript{132} SGS and the Islamic Republic of Pakistan entered into a PSI Agreement signed in 1994 similar to the service agreement signed with the Philippines. The PSI Agreement included an arbitration clause that provided that all disputes must be settled in Pakistan. The dispute in this case arose when SGS alleged a breach of contract against Pakistan for not making timely payments under the contract. When

\begin{footnotesize}
\begin{enumerate}
\item Art. 25(1) of the ICSID Convention established the jurisdictional requirements of investment treaty arbitration.
\item SGS v. Philippines, \textit{supra} note 127 at para 51(a) and (d).
\item \textit{id} at para 103.
\item SGS Societe Generale de Surveillance S.A. v. Islamic Republic of Pakistan, ICSID Case No. ARB/01/13, Decision of the Tribunal on Objections to Jurisdiction, Aug. 6, 2003, \url{http://www.worldbank.org/icsid/cases} (last visited Feb. 9 2003).
\end{enumerate}
\end{footnotesize}
communications initiated by the parties to resolve the issue failed, SGS filed suit against Pakistan in the Swiss Court of First Instance in Switzerland. Pakistan prevailed in the Swiss courts when it contended that in the PSI Agreement, the parties had chosen to arbitrate any disputes arising out of the contract before an arbitration tribunal in Pakistan. SGS later brought a claim against Pakistan at the Center in accordance with Article 9 (2) of the Swiss-Pakistan BIT that provides for arbitration within the framework of the ICSID Convention. Before the Tribunal, SGS contended that Pakistan violated Article 11 of the BIT by failing to guarantee observance of its contractual commitments. The tribunal while siding with Pakistan that it had no jurisdiction over contractual claims, decided conclusively in favor of SGS that it has jurisdiction over SGS BIT claims.

The focus of this article is the decision of the Tribunals on the definition of ‘investment’ with respect to considerations of contribution to economic development. It is apparent that, the Tribunals in the SGS cases adopted a broad interpretation of the BITs in question to determine that the service contracts, subject matter of the disputes, were protected ‘investments’ in the applicable BITs. SGS prevailed on the issue of jurisdiction in the Philippines case because that Tribunal was of the view that, since ‘a substantial and non-severable aspect of the overall service was provided in the Philippines … SGS entitlement to be paid was contingent upon that aspect’. The basis of the definition of ‘investment’ ought to be the intention of the State party and the foreign investor on what constitute an ‘investment’ within the framework of the ICSID Convention and not on the discretion of arbitral Tribunal unsupported by any concrete rules of interpretation within the enabling ICSID Convention with reference to the definition of ‘investment’. It is a truism that, the foreign investor has had no part in the negotiation of the ICSID

133 id at para 23. The Swiss Courts rejected SGS claim because of the arbitration in the PSI agreement.
134 id at para 22-25.
137 SGS v. Philippines, supra note 127 at para 102.
Convention. This fact raises the issue of investment ‘Arbitration without Privity’ and undermines the relevance of the intention of the State party and the foreign investor in the context of ICSID arbitration and treaty law. Generally, the agreement to arbitrate is a contract binding on the parties that have agreed to it. However, this article contends that, the investor-State relationship with reference to ICSID arbitration integrates the concept of privity because the ICSID Convention was formulated between States for the benefit of the States parties and nationals of other States.

In the Philippines case, the Tribunal accepted SGS argument that its assets in the Philippines pursuant to the contract, juxtaposed with the BIT under review, fell within the ‘non exhaustive definition of [foreign] investments under Article 1(2) of the BIT’. In that Tribunal’s determination of an ‘investment’, this paper contends that the Tribunal should have made a ‘contribution to economic development’ consideration of the protected investment in accordance with the purpose of the ICSID Convention. Once the issue of whether or not there is an ‘investment’ in the territory of the host State is raised by either the State party or foreign investor, a Tribunal should consider ‘contribution to economic development’ of the investment in issue. The protection of foreign investments and the attraction of foreign capital to promote domestic economic development are paramount to the conduct of foreign investment in host States. The protection of foreign investments through the mechanism of the ICSID Convention makes it imperative to consider why States enter into International Investment Agreements (IIAs). On the intentions of States in entering IIAs and in international investment law, Garcia-Bolivar opined that States enter into IIAs to protect foreign investments with the expectation to attract foreign capital to promote domestic economic development. Garcia-Bolivar argued that, the expectation of States should be interpreted to include the protection of foreign investment and the anticipated domestic economic development of the host economy.

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139 SGS v. Philippines, supra note 127 at para 48-49.
140 Omar E. Garcia –Bolivar, Economic development at the core of the international investment law regime in EVOLUTION IN INVESTMENT TREATY LAW AND ARBITRATION 587 (Chester Brown & Kate Miles eds., Cambridge Univ. Press 2011).
In the face of the inconsistent approach of arbitral practice to ‘contribution to economic development’ as a core element in investment treaty arbitration,\textsuperscript{141} the arbitral panel in Malaysian Historical Salvors Sdn Bhd v. Malaysia (MHS) case held that for a foreign investment to come under the adjudicative mechanism of the ICSID, it must be shown that there is a substantial contribution to the economic development of the recipient State.\textsuperscript{142} Prior to this case, the panel in Ceskoslovenska Obchodni Banka, A.S v. Slovak Republic,\textsuperscript{143} relied on the preamble of the ICSID Convention to infer that: ‘an international transaction which contributes to cooperation designed to promote the economic development of a Contracting State may be deemed to be an investment as that term is understood in the Convention’.\textsuperscript{144}

Other Tribunals have disagreed with the approach of the arbitral Tribunals in the \textit{Malaysian Historical Salvors} and the \textit{Slovak Republic} cases. As shown in this article, inconsistent views have been registered by arbitral Tribunals in respect of how to define investment. On the other hand, Garcia-Bolivar’s proposition was based on what ought to be the basic core element of the adjudicative principle of treaty investment arbitration. Still, it is argued that, international investment agreements should contain express provisions that reflect the intentions of the State parties that execute BITs. The purpose and preamble of investment agreements are insufficient to convey the intention of the State parties of BITs. A system of arbitration that leaves room for speculation on the intention of the State parties in the context of investment treaty arbitration is bound to produce inconsistencies that could negatively impact the credibility of the process. The

\textsuperscript{141} For example in Patrick Mitchell v. Democratic Republic of Congo, ICSID Case No. ARB/99/7, Decision on annulment, Nov. 1, 2007, \url{http://www.worldbank.org/icsid/cases} (last visited May 22, 2013). At para 33, the Tribunal stated that ‘[t]he existence of a contribution to the economic development of the host state as an essential-although not sufficient-characteristics or unquestionable criterion of the investment, does not mean that this contribution must always be sizable or successful; and, of course ICSID tribunals do not have to evaluate the real contribution of the operation in question. It suffices for the operation to contribute in one way or another to the economic development of the Host State, and this concept of economic development is, in any extent extremely broad and also variable depending on the case’.


\textsuperscript{144} \textit{id} at para 64.
conduct of FDI through BITs though revolutionary, cannot sustain the development of
international investment law if its purpose is intended only to correct the limitations of
multilateral treaties to resolve the uncertainties of customary international law in favor of
foreign investors from developed economies.

Garcia-Bolivar’s thesis is in accord with the dissenting opinion of Judge
Shahabuddeen in *Malaysian Historical Salvors v. Malaysia*. Judge Shahabuddeen
pointed out that, a proper consideration of ICSID objective jurisdiction with reference to
the definition of ‘investment’ includes a requirement for a consideration of ‘contribution
to the host State’s economic development’. According to Judge Shahabuddeen, ‘the
need for a contribution to the economic development of the host State is consistent with
both the formative documents of ICSID and with case law’. Indeed, the preamble of
the ICSID Convention states inter alia that, the ICSID Convention was formulated
‘considering the need for international co-operation for economic development, and the
role of private international investment therein; bearing in mind that from time to time disputes may arise in connection with such investments between Contracting States and nationals of other Contracting States’. Commenting on the preamble of the ICSID Convention, the Tribunal in *CSOB v. The Slovak Republic* stated that ‘[t]his language permits an inference that an international transaction which contributes to the co-operation designed to promote the economic development of a Contracting State may be deemed to be an investment as that term is understood in the Convention’. Similarly, in *Mr Patrick Mitchell v. Democratic Republic of the Congo (DRC)* the Tribunal cited the opinion of Schreuer on the interpretation of the preamble of the ICSID Convention, that contribution to economic development is the ‘only possible indication of an objective meaning of the term investment’.

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146 *id* at para 21-24.
147 *Malaysian Historical Salvors case, supra* note 69 at para 15.
149 *Ceskoslovenska Obchodni Banka, A.S. v. The Slovak Republic, supra* note 139.
150 *id* at para 64.
151 *Patrick Mitchell v Democratic Republic of the Congo, supra* note 139.
152 *id* at para 31.
If the *raison d’être* of the host States for entering IIAs is to attract capital that would finance and promote economic development, a consideration of whether or not a particular transaction is an ‘investment’ within the scope of Article 25(1) of the ICSID Convention ought to include ‘contribution to economic development’. This article contends that, the objective requirements of Article 25(1) of ICSID Convention with reference to the definition of ‘investment’ when considered together with the purpose of the ICSID Convention put economic development and the protection of foreign investments at the core of ICSID arbitration and the international investment law regime. Therefore, in the absence of a concrete definition of ‘investment’ in the ICSID Convention, an ‘investment’ should not be determined under the ICSID Convention in the absence of a consideration of ‘contribution to economic development’ contrary to the object and purpose of the ICSID Convention. The view of the Tribunal in *Joy Mining Machinery Limited v Arab Republic of Egypt*¹⁵³ ought to be a guide to Tribunals established according to the rules of the Center. This Tribunal made a convincing point when it held that for the purpose of ICSID jurisdiction, the parties to an investment dispute cannot by agreement define ‘investment’ outside the objective requirements of Article 25 of the Convention, otherwise Article 25 with reference to the meaning of ‘investment’ will be nugatory even if the term is undefined.¹⁵⁴ If the SGS Tribunals have considered ‘contribution to economic development’ of the host State, substantial parts of the contract in the SGS cases that were performed outside the host State might have been critical in the determination of the meaning of ‘investment’ with reference to Article 25(1) of the ICSID Convention.

However, a fundamental weakness of the consideration of ‘contribution to economic development’ within the meaning of Article 25 (1) of the ICSID Convention is how to determine investments that contributes to the domestic economic development of the host State. Does it have to be ‘substantial’, ‘significant’, or ‘minimal’? ICSID case law on the consideration of ‘contribution to economic development’ has been inconsistent on the issue. Some Tribunals that have attempted to consider ‘contribution to economic

¹⁵⁴ *id* at para 50.
development' in the context of Article 25 (1) of the ICSID Convention have applied
different paradigms on what transaction constitutes a contribution to the economic
development of the host State. In the *Malaysian Historical Salvors case*¹⁵⁵, the Tribunal
held that for a transaction to contribute to the economic development of the host State,
the 'contract must have made a significant contribution to the development of the
respondent'.¹⁵⁶ According to this Tribunal,¹⁵⁷ ‘where there is not the requirement of
significance any contract which enhances the Gross Domestic Product of an economy by
any amount, however small, would qualify as an investment’. However, in the *CSOB case*,
the Tribunal considered the benefits of a loan contribution to the host State’s public
interests to reach a decision that the loan, even though devoid of visible transfer of
resources, is an ‘investment’ that contributed to the economic development of the Slovak
Republic.¹⁵⁸ In the more recent case of *Inmaris v Ukraine*¹⁵⁹ consideration for
‘contribution to economic development’ was disregarded altogether. The investment
dispute in this case arose over a contract to renovate and operate a ship owned by the
Respondent for tourism and training purposes. This Tribunal, rejected a formal approach
to apply the test and held instead that ‘[t]he State Parties to a BIT agree to protect certain
types of economic activity, and when they provide that dispute between investors and
States relating to that activity may be resolved through, inter alia, ICSID arbitration, that
means that they believe that the activities constitute an investment within the meaning of
the ICSID Convention as well’.¹⁶⁰

The majority of the annulment Tribunal in the *Malaysian Historical Salvors case*
annulled the award of the sole arbitrator because consideration of ‘contribution to
economic development elevated the criteria to a jurisdictional requirement that excluded
‘small contributions of a cultural and historical nature’ not supported by the ICSID
Convention.'¹⁶¹ Still, in the opinion of this article, the difficulty and inconsistency

¹⁵⁶ *id* at para 124.
¹⁵⁷ *id* at 123.
¹⁵⁸ *Ceskoslovenska Obchodni Banka, A.S. v. The Slovak Republic*, supra note 141 at para 76.
¹⁶⁰ *id* at para 130.
expressed by some Tribunals in the analysis of the criteria should not be construed to mean that ‘contribution to economic development’ is irrelevant with reference to the meaning of ‘investment’ in the ICSID Convention. In the absence of a concrete definition of ‘investment’ under Article 25 (1) of the ICSID Convention, the Convention will be meaningless if Article 25 (1) is construed to exclude ‘contribution to economic development’ contrary to the purpose of the ICSID Convention from the perspective of the host States. As a Tribunal rightly noted, ‘there exists a definition of an investment within the meaning of the ICSID Convention’.162

VI. Conclusion

In view of the preceding analysis, the mechanism of foreign investment and investment treaty arbitration particularly under the ICSID Convention should not to be divorced from the goal of ‘contribution to economic development’. The expectation of host States in international investment law is the utilization of foreign capital to promote and advance economic development. This expectation with reference to the ICSID Convention cannot be fully achieved in the absence of an independent consideration of the element of ‘contribution to economic development’ in the determination of an ‘investment’ in ICSID arbitral practice. It has been argued in this article that the presence of the principles of the classical theory of FDI in international investment agreements is a testament to the paramount importance of economic development.163 This article contends that there is no logical reason to the contrary that ‘contribution to economic development’ is not the reason why developing countries as host States embraced the idea of the ICSID Convention. The expectation of ‘contributing to economic development’ explains the positive attitude shown by most developing countries in the process leading to the conclusion of the ICSID Convention and the establishment of ICSID. For example, Tunisia was the first State to sign the ICSID Convention on 5 May 1965 and Nigeria was


163 See Part IV above.
the first State to ratify the ICSID Convention on August 23, 1965. While it may be conceded that the inconsistent jurisprudence of investment arbitration on the definition of ‘investment’, may have contributed to the relegation of consideration of ‘contribution to economic development’ to the bleachers, it is submitted that the embracing rubric of the ICSID Convention should be interpreted by arbitral Tribunals beyond the protection of foreign investment to include consideration for ‘contribution to economic development’ of the State. This will ensure a balanced approach to the interpretation and application of the principal objective of the ICSID Convention that might create a better opportunity for host States to maximize the benefits of the ICSID Convention in the context of investment treaty arbitration.

The reasoning of most arbitral Tribunals that, international investment arbitration mechanism has the final say on the adjudication of investment disputes make it more imperative for host States to reform their international investment regimes to reflect their legitimate expectations. It is hoped that such a normative and legislative approach might bring the issue of ‘contribution to economic development’ to the altar of international arbitration to get the proper attention in the context of the ICSID Convention. Ignoring considerations for ‘contribution to economic development’ in investment treaty arbitration could fuel dissatisfaction among host States against the ICSID Convention.

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