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The Nature of Investor-State Arbitration Dispute and its Role in the Interpretation of Bilateral Investment Agreement Provision

Bilateral international investment agreements are the main driving force of international investment law. Depending on the complexity of investment relations, the dispute often arises between the foreign investor and the host state. In this case the most effective dispute resolution mechanism is an international arbitration. The challenge of the dispute is the vague provisions of the investment agreement, based on which the dispute should be resolved. Therefore, within the arbitration competence will be the interpretation of the provision. In this case the greatest difficulty is the scope of discretionary powers of the tribunal, as it may not exceed the competence of the state and has to protect the foreign investor's interests properly. Through the presented article is demonstrated the nature of the Investor-State Investment Arbitration Dispute and the role of the Arbitration Tribunal in the interpretation of the Bilateral Investment Agreement Provisions.

Key words: *investment agreements, interpretation of investment treaties, investor-state arbitration dispute, role of arbitration tribunal.*

1. Introduction

In the last decades, the importance of investment and their regulatory provisions has increased the interest towards international investment law. Today, investing requires a complex approach and its regulation cannot be fully implemented within one particular direction of international or national order.[26] International investment agreements are an effective mechanism for regulating complex investment relations. The latter is particularly effective when a bilateral investment agreement is signed between two States which regulates an investment relationship between the Contracting States. Based on the theoretical and practical grounds it is approved, that bilateral investment agreements are guarantees for foreign direct investment in developing countries.[27] However, their overall regulation is a major challenge for international investment law. It is difficult to find a balance between protecting the investor's rights and the state's regulatory function.

As a rule, the state interferes with the establishment of appropriate regulations in the activities of the investor. But it is difficult to raise the degree of transparency and foreseeability of the regulatory norms of investment law. This is especially important because through the foreseeable and unvague norms is increasing trustworthiness to the investment environment. This creates an excellent opportunity for investors to foresee future perspectives.[28] In order to achieve this, it is necessary to interpret international investment agreements, which is one of the main problematic and topical issues that remains in the hands of the international arbitration tribunal while resolving disputes between the foreign investor and the host state. In this case, arbitration tribunal's discretion involves finding the appropriate balance for interpreting the legal provision in order to avoid the interference in the state competence. It is because that the tribunal is somewhat similar to the ‘’creator’’ of provision and as rights of the investor should be protected. Present article explains about the arbitration tribunal in which cases and in what extant interferes in the interpretation of the investment legal provisions which is shown with several examples.

The present work describes the nature of dispute between the state and foreign investor through the international arbitration and the role of the arbitration tribunal in the interpretation of the investment legal

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26 *Tsertsvadze G.,* Introduction in International Investment Law Tbilisi, 2013, 9 (In Georgian).

27 *Vekua G. ,* Political-Legal Analyse of Georgian Bilateral Investmnet Treaties, Tbilisi, 2016, 4, (In Georgian).

28 *Tsertsvadze G.*, Introduction in International Investment Law Tbilisi, 2013, 11, (In Georgian).

provision. To illustrate these clearly further are given existing approaches about some principles of investment treaties and problematic circumstances about the interpretation.

2. An Investment Arbitration Dispute between the Investor and the Host State

The current investment regime offers many international rights to the investor, but does not require any obligations from the investor. Bilateral investment treaties provide direct foreign investments in the developing countries and reinforce the investment environment, underline the stability of the country and well-being of the investor. However, on the other hand, investors rights are not properly protected, which causes disputes between the state and the investor.[29]

Foreign investors who carry out direct investments, usually stay for a long time in the host state and are supported by the state. In such case negotiation is favorable for dispute resolution, but it is not often successful. In this case, foreign investors often rely on local courts, which are not always an effective method to resolve the dispute. The risk of this particularly exists in developing countries because of the following possible reasons: inefficient qualification of the judges in respect of such specific disputes, extended processes in time, the less familiarity of investor regarding the procedural issues of host country, the partiality of the judge in investment dispute between state and foreign investor, sovereign immunity of the state in relation to lawsuit of the investor or at least to the enforcement mechanisms.[30]

To avoid above-mentioned risks arbitration is considered as one of the most flexible and convenient mechanism to resolve international business disputes. Therefore, nowadays almost all investment treaties provide dispute mechanisms through the arbitration between investor and state. Only a small amount of bilateral investment treaties does not consider dispute settlement through the arbitration process.[31] As a rule, dispute settlement through the arbitration depends on the mutual consent of the parties, but the most common feature of modern investment arbitration is that in case of dispute the arbitration proceedings are held despite the investor's will. This implies that there is no arbitration agreement between the parties about the commencement of the arbitration proceedings. Such approach has been extended in bilateral investment treaties. That is, in case of dispute between host state and foreign investor the arbitration tribunal will be guided with the provisions of international investment agreement concluded between the host state and home-country of foreign investor.

The mechanism represents new standard for investor's protection. The main positive aspect of this mechanism is the security of the investor, i.e. the guarantee that his rights are protected. In addition, it should also be emphasized that the latter does not imply that the arbitration decision will be made in favor of the investor.[32] Nowadays, Investor-state arbitration disputes based on an investment agreement are one of the most common areas in terms of state control.[33] Indeed, the consideration of arbitration as a dispute settlement mechanism between investor and state by bilateral investment treaties is a key opportunity for the following: to enforce a legal provision, to establish a free investment environment and to provide a favorable investment climate.

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29 *Schreider E.M.,* The Role of the State in Investor-State Arbitration, in: *Lalani Sh., Polanco Lazo R. (Editors)*, The Role of the State in Investor-State Arbitration, Nijhoff International Investment Law Series, Vol. 3, Brill, Nijhoff, Leiden, Boston, 2015, 3.

30 *Vandevelde J., Kenneth,* Bilateral Investment Treaties (History, Policy, and Interpretation), Oxford University Press, New Yorl, 2010, 427.

31 *Ratz P*., International and European Law Problems of Investment Arbitration Involving the EU, 1st Edition, Nomos, Baden-Baden, 2017, 159.

32 *Schreider E.M*., The Role of the State in Investor-State Arbitration, in: *Lalani Sh., Polanco Lazo R.* (Editors), The Role of the State in Investor-State Arbitration, Nijhoff International Investment Law Series, Vol. 3, Brill, Nijhoff, Leiden, Boston, 2015, 3.

33 *Schreider E.M.,* The Role of the State in Investor-State Arbitration, in: *Lalani Sh., Polanco Lazo R*. (Editors), The Role of the State in Investor-State Arbitration, Nijhoff International Investment Law Series, Vol. 3, Brill, Nijhoff, Leiden, Boston, 2015, 6.

3. The Role of Arbitration Tribunal in the Interpretation of Bilateral Investment Agreement Provision

According to the United Nations report dated on May, 2018 more than three thousand investment agreements are in force.[34] Many of them contain obscure conditions that give to arbitrationtribunal insufficient guidelines and leave the states undefended to an unintended interpretation. Many investment treaties contain extensive standards and vague provisions that allow arbitration tribunals to resolve disputes related to the investment treaty with full discretion. This discrepancy leads to unpredictable interpretations, because various arbitrators may come to different conclusions about identical facts. In a broader definition of state obligations by the arbitrators, the States may find it interpreted more in favor of investor which was not state's intention at the time of treaty conclusion. Also, the problem is the absence of unified understanding of the conditions of international investment treaties that negatively impact the diversity of decisions made by the arbitration tribunals. Herewith, important is the correct distribution of responsibility between state and arbitration tribunals while interpreting international investment agreements because of the following: Governments are guided in the interests of their citizens in interpretation of treaties and arbitrators in accordance with the delegated authority which has been transmitted in the case of a specific case.

From the above-mentioned, it is indisputable that the arbitrator's discretionary authority is of great importance in regulating the legal conflict. It is crucial as tribunal decides it will take or not responsibility of provision interpretation, which will influence the final decision content. There are many reasons why is the problem to give to arbitration the discretion for the interpretation of provisions. For example, the fluent knowledge of language is important because the arbitrator may not be able to accurately reflect the desired result because of the language barrier. In addition, the arbitrator may not be properly qualified and experienced, which lead to a probability of interpreting legal provision in an inappropriate way. The vaguer the provision is, the higher the degree of arbitrator's freedom is and therefore the responsibility itself.[35]

From the above-mentioned, it is clear how complex is the interpretation of the investment legal norm and how big the arbitration tribunal's responsibility is to find the golden intermediate in the process of interpretation so that the state's and investor's interests should be balanced.

3.1. The Existing Approaches about the Interpretation of Bilateral Investment Treaty Provisions

International treaties play a central role in the system of states' international law, but in spite of this nowadays knowledge is less about the approaches of interpretation of international treaties. Controversy arises when the states have different approaches about the interpretation of treaties. But it is also worth to mention, that the States' treaties have different contents and objectives.[36] The development of investment law has led to questioning the existence of executive power of legal bodies. Investment tribunals have decreased the power of states as governments often not only lose their authority, but they also in many cases are represented as defendants in foreign courts.[37] Therefore, they can not be represented in the arbitration proceedings as the interpreter of the norm, as this will lead to the inequality of the parties in the arbitration process. This will be caused by the fact that the state may clarify the provision in its favor, which will infringe the rights of foreign investors and will result in incompetence of the arbitration decision.

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[34] Recent Developments in International Investment Regime, International Investment Agreements Issues Notes, United Nations, 2018, 2, <https://unctad.org/en/PublicationsLibrary/diaepcbinf2018d1_en.pdf>, [17.07.2019].

[35] *Tsertsvadze G.,* Introduction in International Investment Law Tbilisi, 2013, 27, (In Georgian).

[36] *Ginsburg T.,* Objections to Treaty Reservation – A Comparative Approach to Decentralized Interpretation, in: *Roberts A., Spephan B.P., Verdier P.H., Versteeg M. (Editors)*, Comparative International Law, Oxford University Press, New York, 2018, 231.

[37] *Tucker T.,* The Concept of the State in Investor-State Arbitration – A Social Sciene Perspective, in: *Lalani Sh., Polanco Lazo R.* (Editors), The Role of the State in Investor-State Arbitration, Nijhoff International Investment Law Series, Vol. 3, Brill, Nijhoff, Leiden, Boston, 2015, 138.

Arbitration decisions are often the subject of discussion because of inadequate, extensive or narrow interpretations of treaty provisions. The arbitration tribunals criticize the decisions taken by each other as the tribunals interpret provisions outside the scope than it is intended by the states. One of the main obstacles to this is that there is no precedence of an international commercial arbitration decisions and there is no hierarchy between arbitration tribunals. Treaties define identical rights regardless of its variety, what creates possibility of precedent development in international investment arbitration. Even if the formulation of the provision differs from one another, the purpose and promotion of investment are the same in every treaty. Professor Stephen Schill notes that the decisions made by the arbitration tribunal should be uniform and consistent and not different and fragmented.

Making various controversial arbitration decisions on the same facts cause the dissatisfaction of experts. Professor Susan Franck suggests to divide inconsistent decisions in three directions: 1. The cases with the same factual circumstances, the Parties are related to each other and have similar investment rights; 2. Cases contained similar commercial factual circumstances and similar investment rights; 3. Cases in which different parties participate and have different commercial factual circumstances, but have the same investment rights.

Specialists believe that the absence of the interpretation standards of investment treaties lead to conflicting arbitration decisions. This problem is caused by subjective approach of arbitrators. Professor Sornaraja notes that arbitrators' have two approaches. In his opinion, some arbitrators preferred subjective approach, while others chose a neutral approach when making decisions. The ones who are in favor of neutral approach explain the terms of investment treaties widely. Sornaraja has emphasized another tendency of arbitrators' approach. According to his observations, arbitrators take into consideration the views expressed by the lawyers what are based on the content of the treaty and not on the intention of the states which they had at the time of treaty conclusion.

Van Harten also expresses its position on arbitrators' interpretation methods in commercial arbitration. In his opinion, arbitrators are more likely to use the theory of private law in commercial arbitration rather than the principles that are more relevant to public law. In addition, he criticizes the approach according to which the investor's protection is the main goal of the investor-state arbitration dispute system as it contradicts democratic principles and the ability of the state to exercise discretionary power.[38]

According to some experts, the provisions of investment treaties are interpreted as "the original goal of the norm is not considered.~ Professor Sornarajah has studied the norms of the various treaties and concluded that the arbitration tribunal's interpretations are beyond the scope of their real content. For example, he criticized the arbitration tribunal in the interpretation of Most-Favored Treatment[39] given in case *Emilio Augustin Mafezzini v. The Kingdom of Spain*[40] and noted that the provision by the tribunal is widely interpreted and it is beyond the scope of the norms defined by the States. Similarly, the definition of Fair and Equitable Treatment[41] is broadly defined.

In contrast to this, other specialists believe that the narrow definition of a Fair and Equitable Treatment cannot be fully compatible with the approaches of Vienna Convention on Contract Law[42] about the interpretation of legal norms. E.i., the common content of the provision is the basis for correct interpretation.[43] The latter implies that in case of investment arbitration, the decision should be made according to the interests of the investor and the intentions of the state.

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38 *Hai Yen T.*, The Interpretation of Investment Treaties, Volume 7, Brill Nijhof, Leiden,Boston, 2014, 23-25.

39 Most-Favored Treatment principle is regulated by many international treaties and it provides the protection of investor's from the discrimination on the national basis.

40 International Center for Settlement of Investment Disputes, dated 13 November, 2000, Case Emilio Agustín Maffezini v. The Kingdom of Spain, ICSID Case No. ARB/97/7, <https://www.italaw.com/sites/default/files/case-documents/ita0481.pdf>, [21.04.2019].

41 Equal treatment to foreign and local investor.

42 Vienna Convention on the Law of Treaties, 23/05/1969, <http://www.supremecourt.ge/files/upload-file/pdf-/aqtebi78.pdf>, [23.04.2019].

43 *Hai Yen T.,* The Interpretation of Investment Treaties, Volume 7, Brill Nijhof, Leiden, Boston, 2014, 23-24

International investment arbitration decisions made by arbitrator Michael Reisman is a clear example of this approach. For the sake of example may be named two cases A*G Fraport Airport Services Worldwide v.Philippines*[44] and *GAMI Investment Inc. v. Mexico.*[45] In both arbitration decisions are considered as the legal system of the respondent states as well as the principles of conventional international law and the investor's interests for protecting their investments. In case *AG Fraport Airport Services Worldwide v. Philippines* clearly and in case of *GAMI Investment Inc. v. Mexico* is implicitly acknowledged the main political basis of the state liability regime in the International Investment Law. In this is implied the respect to the host state justice without damaging foreign investments.[46]

It is also problematic to explain the concept of investment, namely, the phrases that are formulated as follows: "all disputes related to investment" or "any legal dispute related to investment~. In recent times, arbitration tribunals often interpret the concept of investment and imply in them various assets and transactions. The Tribunals interpreted an investment at the time of interpretation bilateral investment treaties which covered construction agreements, agreements on loan, shares, debt obligations and property transferred to State. It is also interesting that the assets are divided into categories, as there are different opinions about whether or not the following ones may be considered as an investment a) Pre-investment expenses; B) possession of shares; C) indirect ownership.[47]

From the above-mentioned is sheer in how many ways treaty provisions may be interpreted which influences the result of final decision. Arbitration tribunal has huge responsibility, because its creativity in the interpretation of investment provision will lead to significant contribution to the improvement and development of state's investment law.

3.2. Institutional Arbitration Body and its Role in the Interpretation of Bilateral Investment Treaty Provision

Depending on the complexity of the investment arbitration, institutional arbitrations are more favorable for investors than Ad Hoc arbitration.[48] Ad hoc tribunals are criticized for lesser availability to accountable, transparent and democratic processes in comparison to permanent arbitration tribunals. This is not a fair, independent and balanced approach to resolve the investment dispute. Specialists express the opinion that the arbitration decisions regarding the interpretation of investment treaties can be solved by establishing a new international court by which will be reviewed the enforceability of the arbitration decisions.

Investor-state arbitration disputes point out that its existence is essential because the state guarantees more the fulfillment of liabilities.Through the existing mechanism the balance could be maintained between the state sovereignty and investment rights.[49]

Therefore, we conclude that because of the arbitration nature as it does not belong to any legal system is undoubtedly difficult and perhaps impossible to develop a precedent by Ad hoc tribunal decisions. As a result of this institutional investment arbitration will create more favorable consequences in the creation of common standards in investment arbitration.

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44 International Center for Settlement of Investment Disputes, dated 16 August, 2007, Case Fraport AG Frankfurt Airport Services Worldwide v. The Republic of the Philippines, ICSID Case No. ARB/03/25, <https://-www.italaw.com/sites/default/files/case-documents/ita0340.pdf>, [21.04.2019].

45 International Center for Settlement of Investment Disputes, dated 4 November, 2004, Case Gami Investments, Inc. v. The Government of the United Mexican States, <https://www.italaw.com/sites/default/files/case-documents/ita0353_0.pdf>, [20.104.2019].

46 *Caron D.D.,* The Interpretation of National Foregn Investment Law as Unilateral Acts Under International Law, in: *Arsanjani H. M., Cogan Katz J., Sloane D.R., Wiessner S. (Editors),* Looking to the Future, Martinus Nijhoff Publishers, Leiden/Boston, 2011, 579-581.

47 *Hai Yen T.*, The Interpretation of Investment Treaties, Volume 7, Brill Nijhof, Leiden, Boston, 2014, 23-24.

48 *Ad hoc* Arbitration is a proceeding that is not administered by others and requires parties to make their own arrangements for selection of arbitrators. The parties are under discretion to choose designation of rules, applicable law, procedures and administrative support.

49 *Hai Yen T.,* The Interpretation of Investment Treaties, Volume 7, Brill Nijhof, Leiden, Boston, 2014, 23-24.

4. Conclusion

The majority of modern bilateral investment treaties provide the provision about the settlement of a dispute. According to this the foreign investor is entitled to present a claim to international arbitration tribunal against e host state in respect of the obligations undertaken by the investment treaty.[50] It can be said that the international arbitration is the most convenient mechanism between the foreign investor and the state. But the problem arises when the provision of investment contract is vague and the arbitration tribunal becomes the interpreter of provision.

In the present case, the main problem is the maintenance of balance, on the one hand, the overriding of the state discretion and, on the other hand, the fair protection of the foreign investor's interests. Furthermore, there is no precedent or universally recognized standards for the interpretation of provision, which would not allow the arbitration for greater discrepancy and would give the possibility to make decisions in a systematic way. It is also evident from the present work that the State is a party in the arbitration dispute which excludes participation in the provision interpratation in order not to be infringed the interests of the foreign investor and not to be an investor in an unequal position.

From above-mentioned, we come to the conclusion that the arbitrator's responsibility, qualification and experience is of great importance in making fair decisions. These are decisive to balance the tribunal interests of the parties and not toexercised with excessive discretionary powers in the interpretation of the provision that will lead to the invasion of the state competence.

With the the increase of investment arbitration popularity will continue the increasement of the arbitration decisions' number, which refers to the same standards of protection and of the same or similar issues considered by bilateral or multilateral investment treaties. They in turn will further increase the importance and the contribution of the tribunals in the interpretation of investment treaty's vague and incomplete norms.

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12. 12.Vekua *G*., Political-Legal Analyse of Georgian Bilateral Investmnet Treaties, Tbilisi, 2016, 4.
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