South Carolina Law Review

Volume 16 | Issue 3 Article 2

1964

Foreign Investment Protection: The Arbitration Aspect

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FOREIGN INVESTMENT PROTECTION: THE ARBITRATION ASPECT

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Sir George Jessel—not the American entertainer raised to spurious Hollywood knighthood, but the erudite, quick-witted 19th century English Master of the Rolls—once said, "I may be wrong and sometimes am, but I never have any doubts."

It is unfortunately difficult *not* to have doubts about the most effective way of encouraging and protecting foreign investment in newly developing nations in Latin America, Asia and Africa. The relatively new Act for International Development[1] makes it part of United States foreign policy to encourage private investment in these nations.

There is substantial agreement, however, that one of the deterrents to a greater flow of private investment capital to newly developing nations is the considerable non-business risk involved. This risk (in some, not all, newly developing nations) stems from (1) "creeping" or outright expropriation of property without adequate, prompt and effective compensation; (2) currency controls and inconvertibility; (3) export and import controls; and (4) political and social instability.

There have been several suggestions for minimizing this risk. One suggestion is termed unilateral. This requires assurances (constitutional provisions, legislative enactments, executive policy statements) by newly developing nations that private foreign capital will be permitted to develop safe from confiscation and harassment within the legal, political and economic framework of the country in which the investment is made. Investment insurance or guarantees by the government of the private investor, such as the United States investment guarantee program, also are included in this concept.

A second suggestion uses a bilateral approach. It includes any agreement between two nations affording an opportunity for and protection of private foreign investment. For example, the numerous bilateral treaties of "friendship, commerce and navigation" the United States has concluded with other nations fall within this concept. In addition, if an investment insurance

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1. 75 Stat. 438 (1961), 22 U.S.C.A. 2351 (a) (1961 Supp.).

or guarantee program is shared in a treaty between a capital exporting and a capital importing nation, the approach is bilateral.

A third suggestion visualizes a multilateral approach. It encompasses either (1) an investment insurance or guarantee program; or (2) an agreement or code or convention among a group of capital exporting and importing nations (ideally the program or agreement would be worldwide) to facilitate the flow of private investment capital from nations having it to nations needing it.

Some work has been done in both these directions. For example, in March, 1962, The World Bank completed a study on the feasibility of a multilateral insurance program.[2] The bank does not at present contemplate further action, however, in the belief that its function is that of an impartial banking-lending agency, not an initiator or promoter of a somewhat controversial world-wide investment insurance program. Several organizations—among them the International Chamber of Commerce and the Organization for Economic Cooperation and Development—have drafted proposed multilateral conventions for encouraging and protecting foreign investment. Although they have generally been acceptable to capital exporting nations, newly developing nations have not shown great interest in becoming signatories to them.

Each of the three basic approaches, unilateral, bilateral, and multilateral, has advantages and disadvantages; each, of course, has its supporters and detractors. But underlying them all is the mordant fact that no matter what means are used to facilitate movement of private investment capital to newly developing nations, there will be disputes and controversies between investors and nations in which investments are made. Any other view is simply a pathological belief in the occurrence of the impossible.

A way must be found to resolve these disputes before they escalate into acrimonious proportions discouraging further desirable private investment in nations desperately needing it.

One suggestion for doing this is international arbitration of foreign investor-newly developing nation disputes. Moreover, it has been suggested that the arbitration procedure be institutionalized in an international convention or conventions. This

2. *Multilateral Investment Insurance, A Staff Report, Int'l Bank for Reconstruction and Development,* Washington, D. C. (March 1962).

should give greater opportunity for widespread acceptance and use of arbitration, something that *ad hoc* arbitration has not had in the past.

At first impression, arbitration of foreign investment disputes may seem a far-fetched means of encouraging and protecting private investment. But will not fair and expeditious settlement of foreign investment disputes strongly encourage nations in which investments are made to be considerate and thoughtful in their treatment of these investments? Is not this also one of the factors that might encourage responsible private investors to move capital to newly developing nations?[3]

Why Arbitration?

There is, of course, the possibility that foreign investment disputes might be resolved by diplomacy, mediation or conciliation. Diplomacy has not, however, proven to be effective. Nations are reluctant to espouse claims of their national investors against newly developing nations. Political considerations are often overweighing. Mediation and conciliation are potentially useful. But where vital economic interests of investors and nations are at stake, it is difficult to mark out an area of acceptable, voluntary compromise. (Mediation and conciliation can be used where this is possible, however.)

For obvious reasons, a foreign investor is reluctant to allow adjustment of his grievance before a tribunal of a nation allegedly causing a grievance, or in which a grievance arises. As long ago as 1938, at the biennial International Law Association conference in Amsterdam, one international jurist noted: "The indispensable objectivity and impartiality [of national courts] are sometimes jeopardized by consideration of national inter-

3. For a generally affirmative answer see U.N. Doc. No. E/3492, *The Promotion of the Int'l Flow of Private Capital* (18 May 1961) p. 100: ". . . In effect, the consultations carried out in the course of the preparation of this Report tend toward the conclusion that apprehension of non-business risks constitutes an impediment to foreign private investment which may be substantially lessened by the assurance of an effective machinery for the adjustment of investors' claims arising from disputes with the government of the country of investment. In order to be effective, such machinery should be international in character, so as to assure complete independence in interest from both parties to the dispute. . . ." To the same effect, U.N. Doc. No. E/3365, *The Promotion of the Int'l Flow of Capital* (28 June 1962) p. 41. In the limited context of oil investment in the Middle East see Levy, *Issues in International Oil Policy,* 35 FOREIGN AFFAIRS 454, 468 (1957): ". . . It is becoming imperative that we insist more energetically . . . that disputes be arbitrated rather than unilaterally resolved in favor of Middle East governments under the threat of expropriation. . . ."

ests; this occurs especially in cases in which considerable interests are at stake."[4]

The plain fact is that no international tribunal or system of international tribunals exists by which these disputes may be decided. Only international organizations and nations may be litigants before the International Court of Justice at the Hague. The Permanent Court of Arbitration, which also has its seat at the Hague, now permits its staff and premises to be used for arbitration of disputes between a nation and a private corporation, providing the nation involved is a signatory of the Hague Convention for the Pacific Settlement of International Disputes of 1899 or 1907.[5]

This is helpful, of course, but it does not provide an arbitral tribunal to resolve foreign investment disputes; it simply provides premises and staff. Moreover, the nation must be a signatory of one of the conventions mentioned. Most newly developing nations are not signatories of either convention.

What is needed, as the then Attorney General, Herbert Brownell, said at the American Bar Association convention in London, July 24, 1957, is ". . . a tribunal or system of tribunals which will command general confidence as to the fairness of their judgment and whose procedure will be supported by a public opinion which will not tolerate a departure from them." Contrary to popular belief, this idea is neither new nor revolutionary.[6]

Arbitration has been defined as "the voluntary submission of a dispute by the interested parties to a disinterested person or persons for final determination."[7] It has advantages over judicial settlement of disputes as well as settlement by diplomacy, mediation and conciliation. Its flexibility, imprimatur of impartiality and speed, when properly conducted, seem unobtainable by overburdened national courts. It is not so cumbersome as judicial settlement of disputes. It adheres to basic principles of law while preserving the flexibility of rational standards of commercial fairness. It is concerned more with common sense and justice and less with political nuances than

4. INT'L L. ASS'N, REPORT OF THE FORTIETH CONFERENCE 174-75.
5. Circular Note of the Secretary-General, Permanent Court of Arbitration (March 3, 1960). An unofficial translation of this note appears in 54 AM. J. INT'L L. 933 (1960).
6. See, *e.g.*, the history of this idea in SOHN, PROPOSAL FOR THE ESTABLISHMENT OF A SYSTEM OF INTERNATIONAL TRIBUNALS IN INTERNATIONAL TRADE ARBITRATION 63 (Domke ed. 1958).
7. AM. ARBITRATION ASS'N, COMMERCIAL ARBITRATION RULES 3 (1954).

diplomacy, mediation or conciliation. It allows an individual or business entity to act as litigant.

True, there is little past experience or precedent in the settlement of foreign investment disputes by international arbitration. On balance, this may be an advantage. It permits room in which to move forward into new areas that appear to be workable and practicable without offending *stare decisis*. It allows opportunity for regional institutional arbitration with permanent administrative machinery. It permits adoption of a new, more generally acceptable basis for awards. It allows establishment of *ad hoc* tribunals composed of arbitrators of different nationalities chosen from among respected, competent, knowledgeable jurists and businessmen. It permits establishment of an appellate arbitral tribunal to aid in maintaining reasonable uniformity of legal bases of awards.

Why Regional Arbitration?

Most lawyers will agree that it is unreasonable to expect a litigant in San Francisco, for example, to be required to go all the way to Washington, D. C. to litigate an action against the United States. Is it not equally unreasonable to expect a litigant in, say, Lima, Peru, Lagos, Nigeria, Aukland, New Zealand or New York City to go all the way to the Hague, London or Colombo, Ceylon, to litigate an action against a nation which he asserts is derelict with respect to his investment?

Moreover, is not one worldwide arbitral tribunal too large and unwieldy if it is to be, as it must, if worldwide, representative of all capital exporting and importing nations and large enough to handle the expected volume of worldwide business?

Are sensitive, sovereign, newly developing nations amenable to one tribunal physically distant and located in a capital exporting nation? Are investors in capital exporting nations amenable to one tribunal physically distant and located in a newly developing nation?

A reasonable solution seems to lie in the establishment of a system of regional arbitral tribunals. A somewhat analogous suggestion was made as long ago as 1924 by members of the Hungarian branch of the International Law Association; this occurred at the 33rd conference of the Association. The suggestion, in slightly different form, was renewed by members of the

French branch in 1934 at the 38th conference of the Association.[8]

Selecting the regions is a difficult task. Insofar as possible, they should follow geographic and ethnic lines. On this bases the noncommunist world might be divided into seven regions: (1) Turkey, Iran, Morocco, Algeria, Tunisia, Libya, United Arab Republic, Iraq, Saudi Arabia; (2) remainder of Africa; (3) Afghanistan, Pakistan, Nepal, India, Ceylon, Burma, Thailand, Cambodia, Laos, South Vietnam, Malaya, Indonesia, Philippines, Taiwan, Japan; (4) Australia, New Zealand, and the rest of Australasia; (5) Europe, Great Britain, Ireland, Israel; (6) South and Central America (excluding Mexico); (7) North American continent (including Mexico).

Some of these regions may be cumbersome and unworkable. Others may be neither ethnically similar nor geographically contiguous. To a degree, this may be inevitable. But the selection is not intended to be inflexible. If further reflection and experience indicate that other regional groupings are more desirable, those should prevail.

The important points are to (1) form reasonably compatible groups of states following geographic and ethnic lines where feasible; (2) form groups of states with at least a modicum of economic, political and cultural ties; and (3) give a component state a feeling of basic confidence in the fairness with which its disputes will be approached.

Arbitration Process

Selection of arbitrators is extremely important. It is commonplace to say that they should be highly competent, mature, knowledgeable, respected and impartial—but it is nonetheless urgently true.

A three-man tribunal in which each of two party-litigants chooses an arbitrator and the two arbitrators choose a presiding

8. The Hungarian suggestion in 1924 was for "an International Tribunal for civil matters competent for litigous civil matters between a private individual and a foreign State or between private individuals having their domicile in different States. The French conception [in 1934] advocates the creation of a mixed tribunal set up always by two States only and competent for differences between those two States or between one State and a subject of the other or between subjects of the respective States. Professor de La Pradelle has a regional solution in view. *No doubt it is easier to create regional organizations than universal ones.*" (Emphasis added) INT'L L. ASS'N REPORT OF THE 38TH CONFERENCE 79 (1934). Compare Inter-Parliamentary Union Doc. No. C/EF/58/5 (Ext.) 4 (1958).

arbitrator, should be adequate. The presiding arbitrator must not be a national of, nor the same nationality as, a party-litigant. (If there is more than one party-litigant on each side, then all litigants on one side choose one arbitrator and all on the other side choose another.)

It has been suggested that the two arbitrators be businessmen of judicial temperament who are knowledgeable in foreign commercial matters, including foreign investment. The presiding arbitrator should be an international jurist with recognized competence in foreign commercial matters, including foreign investment. A five-man tribunal might be desirable in infrequent instances; but it is arguable whether its desirability warrants the extra expense, on balance.

It is necessary to assure that a recalcitrant litigant to a foreign investment dispute not be allowed to prevent arbitration by refusal to appoint an arbitrator. This has happened in the past; it emasculates the arbitral process. This can be effectively accomplished by a carefully drawn provision in the convention establishing the arbitration tribunal. The provision, for example, could provide for appointment of the arbitrator by an impartial, disinterested, distinguished person of a nationality different from that of any party to the dispute.[9]

The rules of procedure of the arbitral process must be fair, equitable and well-defined. If litigants fail to receive a full and fair hearing and have their dispute equitably and impartially decided on its merits, arbitration becomes a mockery. There may be no effective, impartial method of settling foreign investment disputes.

Bases for Awards

Awards of arbitral tribunals in foreign investment disputes must be based on fundamental legal principles. If a party to the arbitration alleges a breach of either public or private international law, the issues must be decided on the basis of principles of the law involved.

There are two points one should bear in mind, however. One is that principles of public (and to a lesser extent, private) international law are indistinct in some areas and nonexistent in others. The second is that newly developing nations are reluctant

9. The writer has done this in a proposed arbitration convention he has drafted. See Snyder, *Foreign Investment Protection: A Proposed Arbitration Convention*, 11 J. PUB. L. 191, 203 (1963).

to subscribe to an arbitral process basing awards solely on international law, either public or private. Many newly developing nations assert, perhaps wrongly, they had no part in shaping this international law.[10]

One cannot, however, escape the necessity for adhering to such widely accepted international law principles as *pacta sunt servanda*. In this context, then, and with reliance on fundamental principles of public and private international law, awards may be based on (1) tenets agreed upon by the parties; or (2) in the absence of agreement, *ex aequo et bono*. A tribunal basing an award *ex aequo et bono* should be guided by: (1) trade customs; (2) private international law rules; and (3) principles of justice recognized by the principal legal systems of the world.

Enforcement of Awards

There is neither effective world legal order nor properly constituted force to implement that order if it existed. Attitudes of national courts toward enforcement of arbitral awards vary from country to country. For these reasons, enforcement may be difficult, tortuous and time-consuming at best; at worst, it is nonexistent. But if international arbitration of foreign investment disputes is to gain widespread acceptance, it is obvious that there must be effective enforcement of awards.

One of two approaches may be feasible: *First*, it may be possible to incorporate the so-called New York Convention on Rec-

10. See, *e.g.*, Anand, *Role of the New Asian-African Countries in the Present International Legal Order*, 56 AM. J. INT'L L. 383, 384-90 (1962); Brierly, THE LAW OF NATIONS, 42 (4th ed. 1949): "The law of nations had its origin among a few kindred nations of western Europe. . . ."; remarks of Dr. Jorge Castaneda, legal adviser, Permanent Mission of Mexico to the U.N. at Am. Soc. Int'l L., New York Regional Meeting, March 2, 1961, pp. 11-12: "There is another interesting aspect of this problem. . . . Most under-developed countries would rather tend to feel, I think, that the concept of the minimum standard was created by the practice of the highly industrialized nations in the past in their relations with the under-developed countries, in situations of great inequality, especially in the last century and the beginning of this century. . . ."; Porter, *Multilateral Protection of Foreign Investment*, 3 INT'L DEVELOPMENT REV. 23, 26 (1961): "A widely held view was expressed by the Mexican representative, Senor Castaneda: nearly half of the nations represented in the United Nations have come into being since the main body of international law was formulated; they question their obligation to be bound by rules which they had not helped to create. . . ."; compare, Domke, *Foreign Nationalization*, 55 AM. J. INT'L L. 585 (1961): ". . . International law, far from being an outgrowth of only Western concepts, is indeed an expression of fundamental principles embodied in long established legal systems throughout the world. Islamic law, for instance which is of real significance for one sixth of the world population, in the Middle East, Pakistan, Southeast Asia and parts of Africa, clearly embodies the universal maxim of the protection of acquired rights. . . .".

ognition and Enforcement of Foreign Arbitral Awards[11] into the convention establishing regional arbitral tribunals. Or *second*, it may be acceptable to incorporate specific enforcement provisions into the convention establishing regional arbitral tribunals.

Should There be an Appellate Tribunal?

There has never been an international appellate arbitral tribunal. This is no reason why there should not be one now, however. There are three reasons why one seems desirable: (1) to correct errors of regional arbitral tribunals; (2) to aid in establishing a more uniform "arbitral jurisprudence"; and (3) to fulfill the pragmatic, eminently necessary function of allowing an unsuccessful party an opportunity to work off the head of steam his unsuccessful quest engendered.

There should be a *right* of appeal in certain instances. In all other instances, an unsuccessful party should have a *privilege* of appeal. This privilege might be elevated into an appeal in the discretion of either (1) the tribunal which made the original award; (2) the appellate tribunal; or (3) an impartial legal agency connected in some manner with the appellate tribunal.

Moreover, a procedure allowing decision on a question of law certified to the appellate tribunal by a regional arbitral tribunal should exist. This would be analogous to the presently available advisory opinion of the International Court of Justice, except that it would be binding.

The procedural system for lodging and perfecting appeals should not be difficult to establish. It need only work reasonably well and not be cumbersome. It could be the system of appeal used in non-criminal cases in any mature juridical system. Perhaps it might be modeled on the system by which appeal lies in non-criminal cases to: (1) the United States Supreme Court; (2) the House of Lords in Great Britain; or (3) the *Cour de Cassation* in France or Belgium. It is necessary, of course, that the system be one upon which states concerned can agree.

Objections to These Proposals

Doubtless there are objections to some or all of these proposals. One is that they are "visionary." True, but one might answer

11. This convention is set out in Int'l Commercial Arbitration and the Convention of New York, A Study of the Int'l Headquarters of the Int'l Chamber of Commerce, 11 (1960). Defects in this convention, however, have been pointed out in Quigley, *Accession by the U.S. to the U.N. Convention on the Recognition and Enforcement of Foreign Arbitral Awards,* 70 YALE L. J. 1049 (1961). These should be explored carefully before verbatim incorporation is sanctioned.

that trite objection by an equally trite retort: these are "visionary" times. Another is that they are expensive. True, but expense is a relative term. They may not be "expensive" compared to the losses that may be incurred by investors due to precipitant action, sometimes gleefully taken at the expense of "former colonial powers" and their allies, by sensitive, volatile newly developing nations in a headlong dash to industrialize and raise standards of living.

Still another revolves around the background or profession of the arbitrators. Some say that arbitrators should be jurists, not businessmen; others say they should be businessmen, not jurists. It is suggested that the best solution, not simply a compromise, but the best solution for several reasons, is that they be both businessmen and jurists, with special competence and "judicial temperament."

Another objection is that arbitrators should not be chosen from among any persons the parties desire but from a preconstituted panel. It is suggested that at least in the initial stage of international arbitration of foreign investment disputes, each party-litigant will prefer to name an arbitrator without having to select him from a preconstituted panel. Moreover, for reasons that are obvious, selection from a preconstituted panel might not be practicable in the case of regional tribunals. Later, if experience and desire indicate the feasibility of another method of selection of arbitrators, that method can be adopted.

A fifth objection is the supposed difficulty in determining which regional tribunal would have jurisdiction of a particular dispute; for example, a claim of a foreign investor in the United States against, say, Pakistan over an investment in Pakistan.

It is possible for either the regional tribunal including the United States or the one including Pakistan to have jurisdiction. As a matter of policy it might be preferable to require the claimant (United States investor) to assert his claim in the regional tribunal of the respondent (Pakistan). If the situation were the other way around, that is, the government of Pakistan were asserting a claim against a United States investor, the claim would be asserted in the regional tribunal including the United States.

But this is a matter which need not be troublesome. If it seems preferable to decide jurisdiction in a manner contrary to that suggested, there does not seem to be an ovreweighing reason why this could not be done.

Another objection is that an appellate tribunal would only delay the final result. Is not this same objection equally valid in the juridical hierarchy of the United States? Why have appellate courts? Why a United States Supreme Court and a final court of appeal in each of the fifty states? Do they not delay the final result?

Taken as a whole, these objections remind one of the epigram attributed to Lord Denning (an English Law Lord); some lawyers find difficulties for every solution; other lawyers find solutions for every difficulty. The truth is that if there is sufficient desire on the part of foreign investors and nations to solve their disputes by arbitration, difficulties can be overcome.

In any event, international arbitration of foreign investor-newly developing nation disputes is only one part of a possible program for encouraging and protecting a greater flow of private investment capital to newly developing nations. The proposals here may serve as a basis for discussion; they are not intended to be inflexible nor to provide final answers.

CONCLUSION

How can regional tribunals for resolution of foreign investment disputes be established? One possibility is for the Secretary-General of the United Nations to suggest a meeting of nations to consider drafting a convention to establish one regional tribunal. The region chosen might be one where a considerable amount of foreign investment is currently going. This might serve as a basis for testing the feasibility of the proposals. The Secretary-General might be persuaded to offer his "good offices" in selecting a site for the meeting, making necessary arrangements and providing personnel necessary to conduct it.

If this is possible, its implementation requires only the will of the nations of the region chosen and foreign investors investing in those nations. If investors make known, with sufficient vigor, their desire to try this approach, industrially developed nations will almost certainly be willing to try it. A start may be made. This start may serve as the motivating force for nations and foreign investors in other regions to try it.

This is a possibility. Is it not a possibility worth exploring?