

# *Navigating Jurisdictional Expansion: An Analysis of ICSID's Role in Bolstering Foreign Investment Protection*

Jacqueline Wang

*Faculty of Law, University of Macau, Macau S. A. R, China*

**Keywords:** ICSID; BITs; Foreign Investment Protection; Jurisdictional Expansion; Fork-in-the-Road Clause; Most-Favored-Nation Clause; Umbrella Clause

**Abstract:** Under the Convention on the Settlement of Investment Disputes, the International Centre for Settlement of Investment Disputes (ICSID), affiliated with 165 member countries, holds exclusive jurisdiction over state-foreign investor disputes. ICSID arbitral tribunals frequently expand their jurisdiction and amplify protection for foreign investments through broad interpretation of jurisdictional conditions, enlarged application of the Most-Favored-Nation and Umbrella Clauses, and adaptability of the Fork-in-the-Road provision. This paper scrutinizes these strategies and underscores the tribunals' role in shaping investment protection while considering their impact on the delicate balance between international arbitration and local remedies. It concludes by advocating for a more balanced approach that respects local remedies while safeguarding foreign investment interests.

## **1. Introduction**

Article 26 of the Convention on the Settlement of Investment Disputes between States and Nationals of Other States ("the Convention") represents a strategic compromise in reconciling differences between Northern and Southern nations. The rule for applying local remedies stipulated in this Article diverges significantly from that of traditional international law. According to Article 26, the International Centre for Settlement of Investment Disputes (ICSID) holds exclusive arbitral jurisdiction over investment disputes between states and foreign investors. Additionally, the provision allows concerned nations to select local remedies as a precondition for accepting ICSID arbitration. However, such a request must be explicitly made, or the application of local remedies would be considered forfeited.

Since the 1990s, the number of disputes between investor countries submitted to ICSID has increased substantially. This uptick, particularly in applications related to Article 26 of the Convention, has been driven by a desire to attract foreign investment and stimulate national economic growth. This has prompted contracting countries, especially those in the developing world, to sign a large number of bilateral or multilateral investment treaties, most of which broadly accept the jurisdiction of ICSID. Concurrently, the ICSID arbitral tribunal exhibits a trend towards expanding its jurisdiction by broadly interpreting jurisdictional conditions, enlarging the application scope of the Most-Favored-Nation (MFN) Clause and the "Umbrella Clause", and circumventing the "Fork-in-the-Road Clause". Therefore, once an investment dispute arises, the host country is typically susceptible to the jurisdiction of ICSID.

## 2. Broad Interpretation of the Conditions of ICSID Jurisdiction

Article 26(1) of the Convention asserts, "Unless otherwise stated, consent of the parties to arbitration under this Convention shall be deemed consent to such arbitration to the exclusion of any other remedy." This provision underscores the centrality of "party consent" in establishing ICSID jurisdiction, which is explicitly exclusive. Additionally, the fundamental criteria for ICSID jurisdiction are outlined in Article 25 of the ICSID Convention. Primarily, only those investment disputes embodying the subject element, the object element, and the subjective element simultaneously can be submitted to ICSID. Hence, in practice, the expansion of ICSID jurisdiction and the exclusion of local administrative or judicial remedies predominantly occur through broad interpretation of these three elements.

In terms of the broad interpretation of the subject element of investment disputes, the focus is primarily on expanding investor qualifications, especially enlarging the scope of shareholders entitled to demand arbitration. The arbitral tribunal's approach to rulemaking transitioned from the traditional treaty interpretation of Article 25 to directly citing the definition of "investor" in Bilateral Investment Treaties (BITs). For instance, in the *Case of Azurix Corp. v. Argentine Republic* [1], the tribunal held that investor rights should encompass shareholder rights based on BITs. This stance was reiterated in the *Case of Siemens A.G. v. Argentine Republic* [2], where the tribunal expanded the scope of shareholders from qualified to all in the *Case of Lanco International Inc. v. Argentina Republic* [3].

Regarding the object element – the "investment" in investment disputes – the lack of a clear definition of "investment" in the Convention and the broad scope provided by BITs results in the tribunal typically making investment decisions on a case-by-case basis. A landmark instance of this approach is the *Case of Fedax NV v. Republic of Venezuela*. [4] With the expanded scope of arbitration, ICSID progressively broadens the definition of "investment," leveraging it as a condition for surrendering the host country's jurisdiction. While this serves to protect the interests of foreign investors from developed nations, it risks overlooking or even jeopardizing the interests of host countries (primarily developing nations).

Concerning the subjective element – the "consent of the parties" – the form of "consent" has evolved from requiring explicit consent to encompassing implied consent in arbitral proceedings, as reflected in the *Case of AMCO v. Indonesia* [5].

## 3. Broadening of the Most-Favored-Nation (MFN) Clause

Foreign investors often invoke the MFN Clause of BITs to bypass local administrative or judicial remedies and instead, present their investment disputes to ICSID for arbitration. While the foundational principle of the MFN Clause remains constant, four primary variations of the MFN clauses can be found in BITs. [6, 7] The second broad clause category typically refers to "all matters," "all rights," or "treatment," without explicit reference to dispute settlement provisions. [8] This forms the crux of the controversy surrounding whether the MFN Clause can be applied to the procedures of investment dispute settlement mechanisms.

In practice, the arbitration tribunal has demonstrated a propensity to rule, as evidenced in the *Case of Maffezini v. Spain*, [9] that unless BITs limit the application scope of the MFN Clause, it should ensure equitable treatment at all stages of foreign investments, including the dispute settlement mechanism.

## 4. Broadening of the "Umbrella Clause"

The "Umbrella Clause" functions to safeguard investments by incorporating obligations or commitments that the host state has made concerning a foreign investment under the protective

"umbrella" of the BIT. The clause's significance lies in the principle that any breach of an investment contract equates to a violation of the "Umbrella Clause". This places the host country's commitments under the protective shield of an international investment treaty. In other words, if the host country infringes upon the investment contract, the investors can obtain international relief based on the BIT, thereby bypassing local remedies. As a result, disputes might arise over the "Umbrella Clause" within the context of investment disputes.

With two contrasting rulings in the *Case of SGS v. Pakistan* [10, 11] and the *Case of SGS v. Philippines* [12] handed down by the tribunal, it becomes apparent that the tribunal tends to adopt a broad interpretation of the "Umbrella Clause" to enhance its jurisdiction. However, for host investment countries, particularly developing countries, the most advantageous approach may be to avoid including the "Umbrella Clause" in their BITs or MITs.

## 5. Bypassing the "Fork-in-the-Road Clause"

The arbitral tribunal in an investment treaty case often invokes what is known as a "fork-in-the-road" provision. Under this provision, an investor's decision to submit disputes either to local courts or to international arbitration is considered final and excludes the other option.[13] This situation arises as developed countries and investors frequently cite the inadequacies of the host investment country's legal system and the inefficiency of its dispute resolution process as reasons to oppose the inclusion of exhaustion of local remedies in the international investment treaty. As a result, developing countries have found themselves compromising by accepting the "Fork-in-the-Road Clause".

However, in practical terms, foreign investors typically prefer to use this clause to select international arbitration as their dispute resolution mechanism rather than relying on local courts. This preference for a broader choice by investors is also backed by ICSID. The tribunal focuses on whether two different proceedings are the same case (or the same dispute), as illustrated in the cases of *Olguín v. Paraguay*[14], *Genin v. Estonia*[15], and *Enron v. Argentina*[16,17]. The tribunal employed a strict interpretation when assessing the applicability of the "Fork-in-the-Road Clause". Consequently, this clause has virtually no chance of being applied, and the tribunal's approach favors the expansion of ICSID's jurisdiction while sidelining the jurisdiction of local remedies.

## 6. Conclusion

In the dynamic sphere of arbitration activities, arbitral tribunals often lean towards expanding their jurisdiction with a primary aim to fortify protection for investors and investments. This bias sparks apprehensions among sovereign states, particularly those hosting investments. The ICSID arbitral tribunal has been observed to adopt an extensive approach to enhance its jurisdictional coverage by utilizing bilateral investment treaties, flexibly interpreting scope terms, and emphasizing unilateral protection of the foreign investor. The Most-Favored-Nation Clause and the "Umbrella Clause" have also been applied innovatively to expand the jurisdictional purview and bolster investor protection. Key instances such as the *Azurix Corp. v. Argentine Republic* case, the *SGS v. Pakistan* case, and the *AMCO v. Indonesia* case exemplify the tribunal's progression towards expanded jurisdiction.

Moreover, through the strict interpretation of the "Fork-in-the-Road Clause", the tribunal permits foreign investors to seek international arbitration even after opting for local remedies, further broadening its jurisdiction.

However, this expansionist approach, while presenting certain advantages, also raises concerns. The tribunal's seemingly singular focus on foreign investor protection can inadvertently overshadow the principle of exhaustion of local remedies, which could potentially harm the interests of host countries, especially those in the developing world. Certain cases, such as *Lanco International Inc. v.*

*Argentina Republic* and *SGS v. Philippines*, illustrate the potential detriment to host countries.

Thus, in evaluating the role of arbitral tribunals, it is imperative to consider not only their contributions to strengthening foreign investment protection but also their impacts on the balance between international arbitration and local remedies. This comprehensive perspective will help inform balanced policies and practices that cater to both foreign investor interests and host country needs.

By examining the extensive interpretation of jurisdictional conditions, the expansion of the MFN and "Umbrella" clauses, and the circumvention of the "Fork-in-the-Road" clause, the paper underscores the pivotal role of the tribunal in shaping foreign investment protection. Yet, it also calls for more nuanced, balanced approaches that respect the importance of local remedies.

## References

- [1] ICSID Case No. ARB/01/12, *Azurix Corp. v. The Argentine Republic*.
- [2] ICSID Case No. ARB/02/8, *Siemens A. G. v. The Argentine Republic*.
- [3] ICSID Case No. ARB/97/6, *Lanco International Inc. v. The Argentine Republic*.
- [4] ICSID Case No. ARB/96/3, *Fedax N. V. v. Republic of Venezuela*.
- [5] ICSID Case No. ARB/81/1, *Amco Asia Corporation and others v. Republic of Indonesia*.
- [6] Newcombe, A. P., & Paradell, L. (2009). *Law and practice of investment treaties: standards of treatment*. Kluwer Law International BV.
- [7] Rubins, N. (2008). *MFN clauses, procedural rights, and a return to treaty text*. *Investment treaty arbitration and international law*, 1, 213-229.
- [8] Parker, S. L. (2012). *A BIT in Time: The Proper Extension of the MFN Clause to Dispute Settlement Provisions in Bilateral Investment Treaties*. *Arbitration Brief*, 2, iii.
- [9] ICSID Case No. ARB/97/7, *Emilio Agustín Maffezini v. The Kingdom of Spain*.
- [10] ICSID Case No. ARB/01/13, *Société Générale de Surveillance S. A. v. Islamic Republic of Pakistan*.
- [11] Grane, P., & Bombassaro, B. (2013). *Umbrella Clause Decisions: The Class of 2012 and a Remapping of the Jurisprudence*.
- [12] ICSID Case No. ARB/02/6, *Société Générale de Surveillance S. A. v. Republic of the Philippines*.
- [13] Petsche, M. A. (2019). *The fork in the road revisited: an attempt to overcome the clash between formalistic and pragmatic approaches*. *Washington University Global Studies Law Review*, 18, 391.
- [14] ICSID Case No. ARB/98/5, *Eudoro Armando Olguín v. Republic of Paraguay*.
- [15] ICSID Case No. ARB/99/2, *Alex Genin, Eastern Credit Limited, Inc. and A. S. Baltoil v. The Republic of Estonia*.
- [16] ICSID Case No. ARB/01/3, *Enron Creditors Recovery Corporation (formerly Enron Corporation) and Ponderosa Assets, L. P. v. Argentine Republic*.
- [17] Dundas, H. R. (2008). *The Oxford Handbook of International Investment Law*.