An Appellate Mechanism for Review of Arbitral Decisions In Investor - State Disputes: Prospects and Challenges

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During the past few years there has been increasing discussion of a new "appellate body" --or better (to avoid confusion with the WTO) an "appellate mechanism"-- for reviewing arbitral decisions in investor - state disputes.[1] While the current interest in the concept appears to have originated in the debate leading up to and in the United States' Trade Promotion Authority legislation (enacted in 2002), Professor Thomas Walde indicates that the idea goes back at least to 1991.[2] The most recent concrete proposal, subsequently recanted and now in limbo, was offered in an October 2004 ICSID Secretariat document.[3]

However, the appellate mechanism issue is no longer simply an academic or theoretical one. Once the Dominican Republic - Central American Free Trade Agreement ("CAFTA-DR")[4]

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[1] *See* William H. Knull III & Noah D. Rubins, *Betting the Farm on International Arbitration: Is it Time to Offer an Appeal Option*, 11 Am. Rev. Int'l Arb. 531 (2000) (suggesting that internal appeals processes for investment disputes have a role for high-stakes and complex arbitrations); Susan D. Franck, *The Legitimacy Crisis in Investment Treaty Arbitration: Privatizing Public International Law Through Inconsistent Decisions*, 73 Fordham L.R. 1521 (2005) (arguing that the expanding volume of investor-state arbitral decisions call for, *inter alia*, an appellate court to discourage inconsistent decisions).

[2] OGEMID Message of Nov. 7, 2004, giving credit for the idea to Sir Eli Lauterpacht.

[3] ICSID Secretariat Discussion Paper, *Possible Improvement of the Framework for ICSID Arbitration*, Oct. 22, 2004, Part VI; [hereinafter "ICSID Discussion Paper"]. The principal drafter of that paper, Antonio R. Parra, explained at a June 2005 ICSID conference that the proposal for an ICSID-based investment dispute appellate mechanism had been "premature," and the subsequent version of the discussion paper makes no mention of that proposal. *See Suggested Changes to the ICSID Rules and Regulations,* Working Paper of the ICSID Secretariat, May 12, 2005, *available at* http://www.worldbank.org/icsid/sug-changes.htm (visited Aug. 8, 2005) [hereinafter "ICSID Suggested Changes"]

[4] United States - Dominican Republic - Central American Free Trade Agreement (United States, Costa Rica, Dominican Republic, El Salvador, Guatemala, Honduras, Nicaragua), Aug. 5, 2004 (hereinafter "CAFTA-DR"), *available at* http://www.ustr.gov/Trade_Agreements/Bilateral/CAFTA/CAFTA-DR_Final_Texts/Section_Index.html (visited Aug. 8, 2005).

enters into force on January 1, 2006[5], an annex to CAFTA-DR requires the Parties to establish a negotiating group for an "appellate body or similar mechanism" within three months (April 1, 2006) and to prepare a suitable amendment to CAFTA-DR within a year thereafter.[6] It is thus reasonably possible that some sort of more concrete proposal for an appellate mechanism will evolve in the CAFTA-DR context. Should the process in CAFTA-DR be successful, there will undoubtedly be renewed pressure on the Parties to the North American Free Trade Agreement ("NAFTA")[7] (United States, Canada, Mexico), and to signatories to other recent U.S. bilateral investment treaties ("BITs) and free trade agreements ("FTAs") with investment provisions to agree on a similar mechanism.

Actual implementation of an investment appellate mechanism for CAFTA-DR, NAFTA or other FTAs or BITs is of course another matter entirely. That process, requiring an amendment to each of the agreements by each Party through its constitutional processes, could take years, or may never reach fruition. The controversial nature of the appellate mechanism and, even more, the political sensitivity post CAFTA-DR of submitting *any* trade agreement or amendment thereto to the U.S. Congress or other legislatures, make prompt creation of an appellate mechanism highly problematic, even assuming that the CAFTA-DR negotiating group actually produces a "draft amendment" in a timely manner.

In this essay I discuss how the investment appellate mechanism concept originated; review the current "appeal" process for investor-state arbitral decisions, with particular attention to the three NAFTA Chapter 11 arbitral decisions that have been reviewed to date; set forth the

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[5] As of September 2005, CAFTA-DR had been ratified by the United States, Guatemala, El Salvador, Honduras and the Dominican Republic.. (*See US Trade Representative Rob Portman Statement Regarding Dominican Republic's Passage of CAFTA-DR*, Sept. 6, 2005, *available at* http://www.ustr.gov/Document_Library/Press_Releases/2005/September/US_Trade_Representative_Rob_Portman_Statement_Regarding_Dominican_Republics_Passage_of_CAFTA-DR.html (visited Sept. 7, 2005) (discussing the current state of CAFTA-DR ratification). Costa Rica was not expected to approve the agreement until the first quarter of 2006. (Email from former Costa Rican negotiator Roberto Echandi, Aug. 2, 2005; copy on file with author.) Passage in Nicaragua is likely to be delayed due to an internal political crisis. *See Costa Rica, Other Countries Face Difficulties in Approving DR-CAFTA*, Inside US Trade, Aug. 19, 2005, *available at* http://www.insidetrade.com (visited Sept. 7, 2005). Although a final decision had not been made as of mid-September, political and economic considerations suggest that CAFTA-DR is very likely to go into effect for at least five of the seven Parties as of January 1, 2006, presumably triggering to the appellate mechanism annex.

[6] CAFTA-DR, *supra* note 3, Annex 10-F.

[7] North American Free Trade Agreement, December 17, 1992, U.S.-Can.-Mex., 32 I.L.M. 289 (1993).

rationale supporting an appellate mechanism; consider what is perhaps the key legal issue, standard of review; and review some of the other political, procedural and legal hurdles. I conclude with a few comments and recommendations.

I. The Genesis of the Appellate mechanism Concept

The current impetus in the United States for an investment appellate mechanism for investor-state dispute arbitration comes primarily from non-governmental organizations, several domestic government agencies (EPA, Justice) and Congressional concerns regarding NAFTA Chapter 11. Chapter 11 contemplates the likelihood of disputes between a foreign investor or service provider and the host government or an agency thereof. Foreign investors may seek arbitration under Chapter 11 of any of the obligations guaranteed under Section A of Chapter 11, such as most favored nation treatment, fair and equitable treatment freedom from export or local content performance requirements, the right to make most financial transfers, and restrictions against expropriation whether direct or indirect.[8] Among the concerns that NGO and Congressional critics have raised is that "normal" regulatory actions, including but not limited to those in the environmental/health fields, would be as compensable takings in such cases as *Methanex*[9] and *Sunbelt Water*[10].

With regard to "regulatory" takings, the focus has been on *Methanex.* The Canadian firm Methanex challenged the action of the State of California in banning the gasoline additive, MTBE, because of the perceived risks of MTBE pollution of the underground water supply.[11] Methanex manufactures methanol, which is the principal ingredient in MTBE, and argued that

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[8] NAFTA, *supra* note 7, arts. 1103, 1105, 1106, 1109, 1110, respectively; procedures for international arbitration between NAFTA nationals and the NAFTA governments are contained in Section B.

[9] *Methanex Corp. v. United States*, Partial Award, (NAFTA Arb. Trib. (Aug. 7, 2002)), *available at* http://www.state.gov/documents/organization/12613.pdf (last visited Mar. 11, 2003). *See* the pleadings, orders and other documents at http://www.naftaclaims.com/disputes_us_6.htm (currently ending with the hearing transcripts dated Jun2 3004).

[10] *Sunbelt Water, Inc. v. Canada,* Notice of Claim and Demand for Arbitration, Oct. 12, 1999, *available at* http://naftaclaims.com. The action, claiming that Canada had discriminated against the firm in denying it the right to export water from Canada, was never pursued. (This proprietary website is the best single source of documentation for NAFTA, Chapter 11 claims.)

[11] Exec. Order D-5-99 of the State of California, Mar. 25, 1999, as modified by Exec. Order D-52-02, Mar. 14, 2002, *available at* http://www.governor.ca.gov (visited May 1, 2003).

the measures taken by California constituted a "substantial interference and taking of Methanex US' business and Methanex's investment in Methanex US. These measures were characterized both directly and indirectly tantamount to expropriation."[12] The original tribunal did not reach the question of whether California's action constituted a compensable taking under Article 1110, dismissing the original complaint on grounds that the connection between the California MTBE ban and Methanex' operations was not "legally significant" so as to satisfy the "relating to" language in NAFTA, Article 1101.[13] All claims against the United States contained in a revised claim, both jurisdictional and substantive, were also dismissed, and the United States awarded attorneys' fees and court costs that will likely exceed $4 million.[14]

The concerns raised by *Methanex* were ultimately unfounded. However, NGOs and other NAFTA critics are continuing to argue that were a future tribunal reviewing similar facts to require compensation, it could lead to a chilling effect on national and state government regulation in these areas.[15] Some, including a majority of the Congress, as noted below, have felt that an appellate mechanism to review investment decisions could deal with the possible "rogue" arbitral decision, although others have argued that this would not be a panacea for the many perceived shortcomings of Chapter 11.[16] Whether members of the business/investment

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[12] Methanex Notice of Intent, available at http://www.naftaclaims.org at 3.

[13] *Methanex,* Partial Award*, supra* note 9, para. 172(2).

[14] *Methanex Corporation v. United States of America* (Final Award), Aug. 3, 2005, at 300, *available at*http://www.naftaclaims.com/disputes_us_6.htm (visited Aug. 11, 2005); *see* State Dept. Press Release, *NAFTA Tribunal Dismisses Methanex Claim*, Aug. 10, 2005, *available at* http://www.state.gov/r/pa/prs/ps/2005/50964.htm (visited Sept. 7, 2005) (noting that Methanex is required to pay the United States "more than $4 million in legal costs and arbitral expenses).

[15] *See, e.g.,* Public Citizen, *U.S. Dodging Bullet in Methanex Ruling Does not Remedy Threats from NAFTA Chapter 11 Foreign Investment Protection Mechanism,* Aug. 10, 2004, *available at* http://www.citizen.org/pressroom/release.cfm?ID=2017 (visited Aug. 16, 2005) (stating that "Today's dismissal of a NAFTA "Chapter 11" challenge to California's phase-out of MTBE does little to ease public concerns about the extraordinary foreign investor protection rules in NAFTA-style agreements and does nothing to alleviate the unusual and radical threat to other local, state and federal public interest policies . . . .").

[16] *See* Letter to USTR Robert Zoellick from the Center for International Environmental Law ("CIEL") and other NGOs, Dec. 7, 2004, *available at* http://www.ciel.org/Tae/CAFTA_7Dec04.html (stating that "it is vital to emphasize at the outset that the introduction of an appellate mechanism fails to address the significant underlying problems with both the substantive and procedural provisions in the investment chapter of CAFTA . . . .")

community will support the idea of an appellate mechanism remains to be seen. Presumably, this will turn in large part on the scope of appellate review, the likelihood that payment of an award will not be unduly delayed by appeal, as has happened on some occasions with the ICSID Annulment Committee Process[17], the belief by some claimants that "betting the farm" high-stakes arbitrations of very complex matters require a solid and predictable appellate process,[18] and whether support for such a mechanism might head off efforts to weaken substantively the Chapter 11 protections in subsequent bilateral investment treaties ("BITs") and in free trade agreements ("FTAs"). However, the objectives of the proponents for an investment appellate mechanism are clearly broader than this; they relate to the desirability of greater consistency among the increasing volume of ICSID, UNCITRAL and other investment tribunal decisions[19] that increasingly are adopting conflicting interpretations of similar treaty provisions on "fair and equitable treatment" or indirect expropriation.[20]

The most extreme example of a conflict is the so-called "Lauder" cases, involving a dispute between a U.S. investor and the Czech Government. One action was brought by Ronald S. Lauder under the United States - Czech BIT in London, while the other was brought in Stockholm by CME Czech Republic B.V. (Dutch company owned by Lauder) under the Netherlands Czech BIT. The two tribunals reached radically different results despite the similarity of the two BITs; most significantly, the London tribunal declined to find an expropriation, while the Stockholm tribunal, on the same facts, determined that an arbitration had indeed taken place.[21] A Swedish court reviewing the Stockholm decision concluded that it

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[17] *See* Anthony F.T. Fernando, *The Requirement to Provide a Bank Guaranty, In Return for a Continuation of the Provisional Stay of Enforcement of the Award Under Article 52(5) of the ICSID Convention – Can This be Justified?,* at 4 (2004) (unpublished paper on file with author) (noting that in several ICSID arbitrations subject to multiple tribunal and Annulment Committee review the entire arbitration process required seven and ten years).

[18] Knull & Rubin, *supra* note 1, at 564.

[19] The ICSID Secretariat reports that of the 159 cases submitted to ICSID from the outset until mid-2004, 85 were before the Centre in one form or another during 2004, and 30 new cases were registered during the year. ICSID Annual Report 2004, at 3-4 (Sep. 10, 2004), *available at* http://www.worldbank.org/icsid/pubs/1998ar/2004_icsid_ar_en.pdf (visited Aug. 16, 2005).

[20] For a discussion of some of the jurisprudence in these areas, *see* David A.Gantz, *The Evolution of FTA Investment Provisions: From NAFTA to the United States - Chile Free Trade Agreement,* 19 AM. U. INT'L L. REV. 679, 708-740 (2004).

[21] *See* Susan Franck, *supra* note 1, at 1565, 1559-65 (discussing the Lauder cases in detail); Ronald S. Lauder v. Czech Republic, LCIA no. , Sept. 3, 2001, *Available at* http://www.cetv-net.com/iFiles/1439-lauder-cr_eng.pdf (visited Aug. 23, 2005).

lacked jurisdiction to reconcile the two decisions, in part because the awards involved different parties (Lauder in the London action, the Dutch company in the Swedish case).[22] However, numerous other conflicts among tribunals considering the same BIT language exist.[23]

For many commentators, the question is not simply whether one is for or against an appellate mechanism, but whether one favors a particular mechanism and standard of review, and how one would deal with the practical problems in making the concept a reality. Even within a particular government, it seems reasonable to assume that there may be differences of views among agencies, with those principally responsible for protection of foreign investment world-wide perhaps less enthusiastic about *de novo* review than the domestic agencies responsible for implementing environmental policies or defending the government against foreign investor claims.[24]

Insofar as I have been able to determine, the appellate mechanism concept– in the United States at least– appears formally for the first time in the Trade Promotion Authority provisions of the Trade Act of 2002 "[T]he principal negotiating objectives of the United States regarding foreign investment are . . . to secure for investors important rights comparable to those that would be available under United States legal principles and practice, by . . . providing for an *appellate body or similar mechanism* to provide coherence to the interpretations of trade agreements . . . ."[25]

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[22] *See id.,* at 1567 (recounting the rationale of the Svea Court of Appeal in declining to resolve the conflict between the two awards); Czech Republic v. CME Czech Republic B.V., 42 I.L.M. 919 (Swedish Court of Appeals 2003).

[23] *See, e.g.,* SGS v. Islamic Republic of Pakistan, Decision on Jurisdiction, ICSID (W. Bank) Case No. ARB/01/13 (2003) [hereinafter Pakistan Award], available at http:// www.worldbank.org/icsid/cases/SGS-decision.pdf, holding that an "umbrella clause" in a BIT does not convert a contract breach into a treaty breach, and SGS v. Republic of the Philippines, ICSID (W. Bank) Case No. ARB/02/6 (Jan. 29, 2004) [hereinafter Philippines Award], available at http://www.worldbank.org/icsid/cases/SGSvPhil-final.pdf, reaching the opposite conclusion, both discussed in Susan Franck, *supra* note 1, at 1569-1574.

[24] When the author suggested in a telephone conversation with one of the U.S. officials involved of the discussions of an appellate facility agreement within the U.S. Government may have been more difficult than the upcoming negotiations with the other CAFTA-DR parties, the official did not disagree. [hereinafter "U.S. Official's Observations"] (Memorandum of conversation, Aug. 23, 2005; copy on file with author.)

[25] Bipartisan Trade Promotion Authority Act of 2002, 19 U.S.C. § 3802(b)(3)(G)(iv) (2002) [hereinafter "TPA"]; emphasis supplied.

The Senate Report provides the rationale:

> [N[egotiators should seek to establish a single appellate body to review decisions in investor-state disputes. As the United States enters into more investment agreements and the number of investor-state disputes grows, the need for consistency of interpretation of common terms– such as expropriation and fair and equitable treatment– will grow. Absent such consistency, key terms may be given different meanings depending on which arbitrators are appointed to interpret them. This will detract from the predictability of rights conferred under investment agreements. A single appellate mechanism to review the decisions of arbitral panels under various investment agreements should help to address this issue and minimize the risk of aberrant interpretations.[26]

The "Trade Negotiating Objectives" set out on the President's Trade Promotion Authority provide in pertinent part that "

> [T]he principal negotiating objectives of the United States regarding foreign investment are to reduce or eliminate artificial or trade-distorting barriers to foreign investment . . . and to secure for investors important rights comparable to those that would be available under United States legal principles and practice, by–
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> . . .
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> (G) seeking to improve mechanisms used to resolve disputes between an investor and a government through–
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> . . .
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> (iv) providing for an appellate body or similar mechanism to provide coherence to the interpretations of investment provisions in trade agreements . . .[27]

Accordingly, the first two FTAs concluded under TPA, The U.S.-Chile FTA and the U.S.-Singapore FTA, provide:

> Within three years after the date of entry into force of the Agreement, the Parties

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[26] *See* Bipartisan Trade Promotion Authority Act of 2002, 19 U.S.C. §§ 3801 et seq., Senate Rept. 107-139, 107th Cong., 2d Sess., Feb. 28, 2002, at 16 [hereinafter "TPA Senate Report"].

[27] TPA, *supra* note 25, 19 U.S.C. § 3802(b)(3)(G)(iv) (2002).

> shall consider whether to establish a bilateral appellate body or similar mechanism to review awards rendered under Article 10.25 in arbitrations commenced after they establish the appellate body or similar mechanism.[28]

Similar language is found in the U.S. - Morocco Free Trade Agreement and in the 2004 U.S. - Model BIT(in the latter case the provision is entitled, "Possibility of a Bilateral Appellate Mechanism," a somewhat lukewarm endorsement).[29] Such appellate mechanism language might also find its way into an FTAA investment chapter if an FTAA is ever concluded– an increasingly remote possibility-- and if the agreement covers investment, which is even more remote.[30]

CAFTA-DR, possibly because of Congressional dissatisfaction with the bare-bones formulation in the Singapore and Chile FTAs and the lack of a short deadline for negotiations, offers a much more detailed instruction on developing an appellate mechanism:

> 1. Within three months of entry into force of the Agreement, the [Fair Trade] Commission shall establish a Negotiating Group to develop an appellate body or similar mechanism to review awards rendered by tribunals under this Chapter. Such appellate body or similar mechanism shall be designed to provide coherence to the interpretation of investment provisions in the Agreement. The Commission shall direct the Negotiating Group to take into account the following issues, among others:
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> (a) the nature and composition of an appellate body or similar mechanism;
> (b) the applicable scope and standard of review;
> (c) transparency of proceedings of an appellate body or similar

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[28] *See* United States - Chile Free Trade Agreement, June 6, 2003, Annex 10-H, United States - Singapore Free Trade Agreement, May 6, 2003, exchange of letters between USTR Robert Zoellick and Minister for Trade and Industry George Yeo, May 6, 2003, *all available at* http://www.ustr.gov.

[29] *See* United States - Morocco Free Trade Agreement, Jun. 15, 2004, Annex 10-D, *available at* http://www.ustr.gov. ; 2004 U.S. Model BIT, Nov. 2004, Annex E, *available at* http://www.state.gov/e/eb/rls/othr/38602.htm (visited Aug. 8, 2005).

[30] *See* For a discussion of the FTAA and its possibly fatal negotiation problems, see David A. Gantz, *The Free Trade Area of the Americas: An Idea Whose Time has Come– and Gone?,* 1 LOYOLA INT'L L. REV. 179 (2004); Kevin C. Kennedy, *The FTAA Negotiations: A Melodrama in Five Acts*, 1 LOYOLA INT'L L. REV. 121 (2004) (both discussing the problems that have led to a suspension of negotiations).

> mechanism;
> (d) the effect of decisions by an appellate body or similar mechanism;
> (e) the relationship of review by an appellate body or similar mechanism to the arbitral rules that may be selected under Articles 10.16 and 10.25; and
> (f) the relationship of review by an appellate body or similar mechanism to existing domestic laws and international law on the enforcement of arbitral awards.
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> 2. The Commission shall direct the Negotiating Group to provide to the Commission, within one year of establishment of the Negotiating Group, a draft amendment to the Agreement that establishes an appellate body or similar mechanism. Upon approval of the draft amendment by the Parties, in accordance with Article 22.2 (Amendments), the Agreement shall be so amended.[31]

The entry into force of CAFTA-DR, expected January 1, 2006, will as noted earlier trigger a one-year process that may result in some sort of an agreement contemplating the establishment of an appellate mechanism, at least for the seven CAFTA-DR partners. The CAFTA-DR language, however, leaves open key issues, including whether the appellate mechanism is to guard against aberrant interpretations of the treaty or international law that jeopardize major public policy objectives, correct erroneous arbitral decisions on law and/or fact, or both. Most significantly, despite the short deadline proffered for initiating and completing the negotiations, there is no time table for submission of the agreement as an amendment to the Parties' congresses for approval. Thus, it is entirely possible that the CAFTA-DR language regarding negotiation of an appellate mechanism agreement could be fully complied with, without any implementing action being taken by the Parties for months or even years.

Presumably, the Senate Report, and extended inter-agency discussions, have provided the necessary guidance to the U.S negotiators in this respect, but it is unclear whether the proponents in Congress and elsewhere have given much thought as to how the concept would be implemented. It is also difficult to see how negotiators from only seven nations, parties to a single FTA, could themselves establish an appellate mechanism with broader jurisdiction, without the active participation of other interested nations, or the ICSID Secretariat. Even so, an all CAFTA-DR appellate mechanism could be a significant first step, and the agreement could always provide for an *ad hoc* appellate mechanism initially, use under other U.S. BITs and FTAs to the extent such agreements are negotiated and, ultimately, for folding this mechanism into one at ICSID if and when one is established there.

It is also notable that all seven CAFTA-DR Parties are also parties to the ICSID

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[31] CAFTA-DR, *supra* note 3, Annex 10-F.

Convention, providing a respected and widely used framework for investor-state disputes,[32] while the use of the Convention provisions and ICSID Arbitral Rules are impossible under NAFTA because neither Canada nor Mexico are parties to ICSID.[33] The ICSID facilities are, however, available to some non-Parties under the ICSID Additional Facility Arbitral Rules, as long as either the government of the investor claimant or the respondent government is a Party to ICSID.[34] The provisions of the ICSID Convention, including those that relate to the Annulment Committee, do not apply to Additional Facility proceedings.[35] However, a non-ICSID appellate mechanism may create a conflict with the CAFTA-DR Parties' obligations to use the Annulment Committee for ICSID Arbitrations, should the parties to a dispute elect to arbitrate under the ICSID Convention, one of the options under the investment chapter.[36] (This problem could be avoided if the scope of the appellate mechanism were limited to non-ICSID Convention arbitrations, leaving ICSID arbitrations for review by the Annulment Committee.)

The appellate mechanism idea is not solely a U.S./CAFTA-DR concept, even if the inclusion of appellate mechanism negotiating commitments in U.S. FTAs is likely driving discussions elsewhere. Presumably to stake out its claim as a logical situs for a single investment appellate mechanism, the ICSID Secretariat, in October 2004, issued its own proposal for an appellate mechanism to be located at ICSID.[37] The ICSID "Discussion Paper" asks "whether an appellate mechanism is desirable to ensure coherence and consistency in case law generated in ICSID and other investor-to-state arbitrations initiated investment treaties"[38] and concluded that the answer is indeed "yes." The paper further asserted that

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[32] Convention for Settlement of Investment Disputes Between States and Nationals of Other States, Mar. 18, 1965, 17 U.S.T. 1270, T.I.A.S. 6090, 575 U.N.T.S. 159 [hereinafter "ICSID Convention"].

[33] *See* List of Contracting States and Other Signatories to the Convention, updated May 25, 2005, *available at*http://www.worldbank.org/icsid/constate/c-states-en.htm (visited Aug. 8, 2005).

[34] Additional Facility Rules, Rule 2(a), *available at* http://www.worldbank.org/icsid/facility/facility.htm (visited Aug. 11, 2005). This means the Additional Facility is not available under CAFTA-DR, since all seven Parties are also Parties to the ICSID Convention, despite the inclusion of the Additional Facility in the list of alternative mechanism open to the parties to a dispute. CAFTA-DR, *supra* note 3, art. 10.16(3)(b).

[35] *Id.,* art. 3.

[36] CAFTA-DR, *supra* note 3, art. 10:16:3(a).

[37] *See* ICSID Discussion Paper, *supra* note 2, Annex.

[38] *Id.* at 4.

> it would seem to run counter to the objectives of coherence and consistency for different appeal mechanisms to be set up under each treaty concerned. Efficiency and economy, as well as coherence and consistency, might best be served by ICSID offering a single appeal mechanism as an alternative to multiple mechanisms.[39]

While the ICSID paper, as noted earlier, no longer formally exists, it was quite useful bureaucratically in making a forceful argument for locating any investment appellate mechanism at ICSID, and many of the ideas espoused will undoubtedly be revived, and at least be considered by the CAFTA-DR negotiators, if the negotiations under CAFTA-DR move forward as mandated.

II. **Review of Arbitral Tribunal Decisions**

An initial question is why a new or separate appellate mechanism for investment disputes is needed when tribunal awards are already subject to review by the ICSID Annulment Committee or by national courts. As indicated below, a limited form of review is currently a feature of investor-state arbitration.

A. Review of ICSID Arbitral Awards

An award by a tribunal operating under the ICSID Convention Arbitration Rules is already to subject to limited review, to annulment "on one or more of the following grounds":

> (a) that the Tribunal was not properly constituted;
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> (b) that the *Tribunal has manifestly exceeded its powers*;
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> (c) that there was corruption on the part of a member of the Tribunal;
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> (d) that there has been a serious departure from a fundamental rule of procedure; or
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> (e) that the award has failed to state the reasons on which it is based.[40]

An *ad hoc* committee of three is appointed from a panel of arbitrators, with the authority to annul the award or any part of it; if the award is annulled either party to the arbitration may request that the dispute be submitted to a new tribunal.

The ICSID Annulment Committee overturned some ICSID decisions in favor of investors, particularly in the early years; the first three awards reviewed by the Committee were

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[39] *Id.* at 15.

[40] ICSID Convention, *supra* note 32, Art. 52; emphasis added.

set aside.[41] It has been suggested that this was less a result of "appellate scope or systemic weakness" than inexperience of the arbitrators and the committee with ICSID rules.[42] Several recent annulment committee decisions have found in the investor's favor. For example, in *Wena Hotels, Ltd. v. Egypt*[43], the Committee rejected Egypt's claims that the ICSID tribunal had failed to apply the applicable law, or had departed from a fundamental rule of procedure. In *Vivendi Annulment*[44], the Committee accepted the investor's claim and annulled the Tribunal's refusal to exercise jurisdiction even where its jurisdiction existed, determining that by so refusing the Tribunal had manifestly exceeded its powers under ICSID Conv., art. 52(1)(b). One observer has concluded that "[I]f there were any doubt before, there is no doubt now that parties cannot routinely expect to be able to annul ICSID awards.[45]

However, the Annulment Committee has its shortcomings. First, like the ICSID Convention itself, it is available only for disputes in which both the investor and the home state are parties to the Convention.[46] Secondly, the Annulment Committee is not a single body, but a panel of arbitrators from which an *ad hoc* committee is chosen in each instance.[47] Thus, the likelihood of consistency among decisions of the Annulment Committee is at best moderate, since different arbitrators are deciding different cases.

B. Court Review of NAFTA Chapter 11 Awards

Of course, the ICSID Annulment Committee procedures are not available for arbitral awards rendered under NAFTA, since as noted earlier neither Mexico nor Canada are Parties to the ICSID Convention. Arbitration under NAFTA must proceed under either the UNCITRAL Rules or the ICSID Additional Facility Rules.[48] While the use of the ICSID Additional Facility

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[41] *See Holidan, Klockner, et al. v. Cameroon*, ICSID Case NO. ARB/81/2, 1 ICSID REV. FOR. INV. L. J. 90 (1986); *Amoco v. Indonesia,* ICSID Case no. ARB/81/1 (Nov. 20, 1984), 25 ILM 1441 (1986).

[42] Knull & Rubins, *supra* note 1, at 553.

[43] ICSID Case no. ARB/98/4 (Jan. 28, 2002), 14 ILM 933 (2002).

[44] Compania de Aguas del Aconquija S.A. and Vivendi Universal v. Argentine Republic (Jul. 3, 2002), 41 ILM 1135 (2002).

[45] Daniel Q. Posin, *Recent Developments in ICSID Annulment Procedures*, 13 WORLD ARB. & MEDIATION REP. 170, 171 (2002).

[46] ICSID Convention, *supra* note 32, art. 25.

[47] *Id.*, art. 52(3).

[48] NAFTA, art. 1120.

has historically been largely limited to NAFTA cases, arbitration under the UNCITRAL Arbitration Rules is common in investor-state arbitration under both NAFTA and BITs.[49]

In either instance, a court proceeding may be brought to set aside or annul the award, in the state which is the situs (place) of the arbitration.[50] It appears to be largely as a result of expediency that Canada had been designated as the situs of most arbitrations under NAFTA to date[51], although arbitration under NAFTA Chapter 11 can be held in any nation that is a party to the New York Convention on the Recognition and Enforcement of Arbitral Awards.[52] It is generally accepted that the national courts in the place of arbitration cannot be deprived of jurisdiction over arbitral decisions rendered in their territories (except to the extent that the Parties to the ICSID Convention have agreed otherwise as, for example, in their acceptance of the Annulment Committee as the sole body for review).

However, some states do restrict the scope of court review of arbitral decisions within their territories (in part because those involved in international commercial arbitration tend to avoid siting arbitral proceedings in states where the scope of review is broad). Many, including several jurisdictions in Canada, have have adopted the UNCITRAL Model Law on International Commercial Arbitration:

> (1) Recourse to a court against an arbitral award may be made only by an application for setting aside in accordance with paragraphs (2) and (3) of this article.
>
> (2) An arbitral award may be set aside by the court specified in article 6 only if:
>
> > (a) the party making the application furnishes proof that:
> >
> > (i) a party to the arbitration agreement referred to in article 7 was under some incapacity; or the said agreement is not valid under the

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[49] *See* Occidental Exploration and Production Company v. Republic of Ecuador, (Final Award), Jul. 1, 2004 (arbitration under the U.S. - Ecuador BIT administered by the London Court of Arbitration under UNCITRAL Rules), *available at* http://www.asil.org/ilib/OEPC-Ecuador.pdf (visited Aug. 23, 2005); Lauder/CMS cases, *supra* note 22 and accompanying text.

[50] *See* NAFTA, *supra* note 7, art. 1136:3.

[51] For example, in *Feldman v. United Mexican States*, 42 I.L.M. 625 (2003) (ICSID (W. Bank) Dec. 16, 2002), where the Claimant was a United States citizen and the Respondent was Mexico, it seemed logical to the Tribunal (and, apparently, to the parties), to choose Ottawa, Ontario, Canada as the place of arbitration, and that is what happened. (*See* ¶ 26.)

[52] New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards, Jun. 10, 1958, 21 U.S.T. 2517, T.I.A.S. No. 6997, 330 U.N.T.S. 38. *See* NAFTA, Art. 1130:1.

> law to which the parties have subjected it or, failing any indication thereon, under the law of this State; or
>
> (ii) the party making the application was not given proper notice of the appointment of an arbitrator or of the arbitral proceedings or was otherwise unable to present his case; or
>
> (iii) *the award deals with a dispute not contemplated by or not falling within the terms of the submission to arbitration, or contains decisions on matters beyond the scope of the submission to arbitration*, provided that, if the decisions on matters submitted to arbitration can be separated from those not so submitted, only that part of the award which contains decisions on matters not submitted to arbitration may be set aside; or
>
> (iv) the composition of the arbitral tribunal or the arbitral procedure was not in accordance with the agreement of the parties, unless such agreement was in conflict with a provision of this Law from which the parties cannot derogate, or, failing such agreement, was not in accordance with this Law; or
>
> (b) the court finds that:
>
> (I) the subject-matter of the dispute is not capable of settlement by arbitration under the law of this State; or
>
> (ii) *the award is in conflict with the public policy of this State.*[53]

* * *

Article 34 of the Model Law, which closely follows Article V of the New York Convention[54], thus sets forth a very limited scope of review. Investors are likely to seek as the situs of arbitration states which have adopted the UNCITRAL Model Law, where experience indicates that the courts will undertake only that limited review and not a *de novo* review of either the facts or the law as determined by the tribunal. However, despite this attempt at uniformity of approach, national court review is not likely to provide a high level of consistency,

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[53] UNCITRAL Model Law on International Commercial Arbitration, 1985, art. 34, *available at* http://www.uncitral.org/uncitral/en/uncitral_texts/arbitration/1985Model_arbitration.html (visited Aug. 8, 2005);emphasis added.

[54] United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards, Jun. 10, 1958, *available at* http://www.jus.uio.no/lm/un.arbitration.recognition.and.enforcement.convention.new.york.1958/doc.html (visited Aug. 8, 2005).

even in a particular country, because inevitably different judges sit on different cases, and some have more experience with arbitral award review than others.

Under NAFTA Chapter 11 to date, all three annulment actions have been brought in Canadian provincial or federal courts– in the province designated as the situs of the arbitration-- where the courts have applied the grounds set forth in Article 34 of the UNCITRAL Model Law on Commercial Arbitration, as adopted in Canada.

1. In *United Mexican States v. Metalclad*, before the British Columbia Supreme Court [a court of first instance], the court concluded that the Tribunal acted beyond the scope of the submission to arbitration by finding a transparency requirement in Chapter 11 as the basis for determining that Mexico had violated arts. 1105 (fair and equitable treatment) and 1110 (expropriation) of NAFTA.[55] (The tribunal's finding of indirect expropriation was upheld on other grounds.) The decision does raise some confusion as to the proper scope of review under Article 34 of the UNCITRAL Model Act as applied in Canada; the principal arbitral holding was characterized as a "misstatement of the applicable law."[56] In so finding, the court implicitly determined that it had jurisdiction to review alleged errors of law.

2. In *S.D. Myers v. Mexico*, a federal court sitting in Ottawa upheld the arbitral tribunal.[57] The court declined to review a jurisdictional challenge based on Canada's allegation that there was no "investment" by S.D. Myers in a very formalistic approach. Since Canada raised a jurisdictional issue without labeling it as such in its Statement of Defense, according to the court Canada effectively waived its right to submit the issue as a "jurisdictional" challenge. More broadly, the court applied what it said was a "correctness" standard of review for legal issues (such as the meaning of the word "investor") and a "reasonableness" standard for application of facts to legal issues: "Article 34 of the *Code* [UNCITRAL Model Code as adopted in Canada] does not allow for judicial review if the decision is based on an error of law or an erroneous finding of fact if the decision is within the jurisdiction of the Tribunal."[58]

If the court in *Metalclad* had applied this standard it presumably would have affirmed the tribunal. Also, in *S.D. Myers*, presumed concerns over court review led to determinations "in the alternative." Subsequent to the issuance of the court's opinion, S.D. Myers and Canada apparently both accepted the judgment.

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[55] *United Mexican States v. Metalclad*, 2001 BCSC 664 (May 2, 2001).

[56] *Id.,* ¶¶ 70, 72.

[57] *Attorney General of Canada and S.D. Myers, Inc. and the United Mexican States,* 2004 FC 38 (Jan. 13, 2004), ¶77.

[58] *Id.,* ¶ 42.

3. In *United Mexican States v. Feldman,* an Ontario court of first instance, in dismissing the challenge, afforded the tribunal a high degree of deference: "In my view, a high level of deference should be accorded to the Tribunal, especially in cases where the Appellant Mexico is in reality challenging a finding of fact. The panel who has heard the evidence is best able to determine issues or credibility, reliability and onus of proof."[59] The Court also indicated that the public policy exception to enforcement should be invoked only when the award "must fundamentally offend the most basic and explicit principles of justice and fairness in Ontario, or evidence intolerable ignorance or corruption on the part of the arbitral Tribunal."[60] The Mexican government's appeal resulted in an affirmation by the appellate court.[61] Interestingly, the Court of Appeal for Ontario (Ontario's highest court), despite the continued participation of the Attorney General of Canada in support of Mexico, noted that "Quite Apart from principles of international comity, our domestic law in Canada dictates a high degree of deference for decisions of specialized tribunals generally and for awards of consensual arbitration tribunals in particular."[62]

III. The Rationale for an Appellate Mechanism

As noted earlier, some members of the U.S. Senate and Congress, government agencies and NGOs have been concerned about the lack of an appellate process under NAFTA Chapter 11, so that *ad hoc* arbitrators cannot be controlled, and any legal errors are made cannot be effectively corrected for the current or for future cases. The fears are particularly acute where major public policy issues are being decided, e.g., whether regulatory action can be considered expropriatory (*Methanex*), or whether imposition of unfair trade remedies (anti-dumping and countervailing duties) are subject to challenge under NAFTA, Chapter 11 (*Canfors*[63]). Concerns over tribunal errors are not unknown among foreign investors themselves, particularly in "bet the company" arbitrations with foreign states.

Under NAFTA, Article 1131:2, "An interpretation of the [Fair Trade] Commission of a

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[59] *United Mexican States v. Marvin Roy Feldman Karpa*, Ontario Superior Court of Justice, File no. 03-CV-23500 (Dec. 2, 2003), ¶ 77.

[60] *Id.,* ¶ 87.

[61] United Mexican States v. Marvin Roy Feldman Karpa, Court of Appeal for Ontario, Jan. 12, 2005, *available at* http://naftaclaims.com (visited Aug. 8, 2005).

[62] *Id.* at para. 37.

[63] *Canfor Corp. v. United States*, May 23, 20002. This action alleges that the United States violated various provisions of NAFTA, Chapter 11, in assessing anti-dumping and countervailing duties against softwood lumber imported from Canada.

provision of this Agreement shall be binding on a Tribunal established under this Section." This power of interpretation may offer some relief from such errors, but its utility is uncertain. For an Interpretation to be issued, the three NAFTA governments must agree that an Interpretation is appropriate regarding the affected issue, *and* agree on the text. Only one Interpretation has been issued during the first twelve years of NAFTA.[64] Also, at least one tribunal (*Pope & Talbot*[65]) has suggested that it was appropriate for the tribunal to determine whether the Interpretation really an *ultra vires* effort by the Parties to amend NAFTA. (The tribunal in *Mondev*[66] disagreed.) While the NAFTA Parties who are not parties to a particular Chapter 11 arbitration are free to "make submissions to a Tribunal on a question of interpretation of this Agreement" (Article 1128), the tribunal has no obligation to accept such views.

Moreover, despite the lack of formal precedential value of earlier arbitral decisions– NAFTA, Art. 1136:1 states that "An award made by a Tribunal shall have no binding force except between the disputing parties and in respect of the particular case"– prior decisions *are* being regularly cited by parties to arbitrations, which effectively requires tribunals to discuss, distinguish and/or follow those earlier decisions. This increases the risk for concerned governments, NGOs or private investor groups in leaving an allegedly erroneous decision unchallenged.

There is obviously some dissatisfaction with national court review (particularly in recent Canadian NAFTA cases), either because courts have only limited experience with the issues or themselves make flawed interpretations of complex treaty provisions or principles of international law, or because the courts are giving too much (or too little) deference to the tribunals. Judges in general, except for the few that regularly deal with such issues as enforcement of foreign arbitral awards and sovereign immunity (e.g., those in the Southern District of New York or sitting on the Court of Appeals for the Second Circuit, or perhaps on the federal courts in Washington, D.C.), have at best limited expertise in such issues, certainly less than one could reasonably expect from an appellate mechanism of investment law experts. After the Canadian experiences some of the pending NAFTA arbitrations have selected Washington, D.C. as the situs, but to date there have been no reviews in Washington, D.C. courts of NAFTA arbitral decisions. With court annulment procedures, the result may ultimately be a three step process (as in *Feldman*), an arbitral award under ICSID Additional Facility or UNCITRAL Rules; appeal to a court of first instance, followed by an appeal of the court decision to an appellate court in the same jurisdiction. The cost and time burdens for the parties are potentially

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[64] *See Notes of Interpretation of Certain Chapter 11 Provisions*, (Jul. 31, 2001), *available at* <http://www.dfait-maeci.gc.ca/tna-nac/NAFTA-Interpr-en.asp?format=print> (visited Mar. 31, 2003).

[65] *Pope & Talbot v. Canada*, (Award on Damages) (May 31, 2002), 41 ILM 1342 (2002).

[66] *Mondev v. United States* (Oct. 11, 2002), 42 I.L.M. 85 (2003).

significant.

For major companies and governments, there is probably less concern with time and cost considerations for an extended arbitral process (including an appeal) when the issues are of broad public interest (governments) or involve "bet the company" issues (private investors). Few today few really believe that international arbitration, particularly between private investors and states, is any quicker or cheaper than, for example, U.S. federal court litigation, even though the discovery process is more circumscribed in an international arbitration. However, small investors (e.g., Marvin Feldman) or developing country governments may be discouraged from using the process by the existence of a more formal appellate process and the greater prospect that it will be used on a regular basis.

Consideration of the investment appellate mechanism concept has and will continue to be influenced by the general success of the WTO's Appellate Body[67] in resolving international trade disputes. During the past nearly eleven years, the WTO Appellate Body has generally proved itself able to produce consistent decisions in a very timely (90 days) fashion, with a high level of expertise and analysis. A total of 67 appeals to the Appellate Body were filed between 1995 and the end of 2004, although none were filed in 1995.[68] The number of appeals peaked in 2000, with thirteen; they increased each year from 1995 to 2000, and have decreased each year since 2000. Over the period 1995-2003, 67% of all panel reports were appealed to the Appellate Body.[69] (The total number of consultations under the Dispute Settlement Understanding[70] reached 332 by mid-August 2005.[63]) Many, including some high U.S. government officials and members of Congress– some of whom are currently supporting an investment appellate mechanism– have been critical of some of the WTO Appellate Body decisions, but few have

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[67] The Appellate Body is created by Article 17 of the Understanding on Rules and Procedures Governing the Settlement of Disputes ("DSU" or "Dispute Settlement Understanding") and Annex 2 to the Marrakesh Agreement Establishing the World Trade Organization. World Trade Organization, *Understanding on Rules and Procedures Governing the Settlement of Disputes*, art. 2 [hereinafter *DSU*] *at* http ://www.wto.org/english/docs_e/legal_e/28-dsu_e.htm (last visited Apr. 14, 2005); Marrakesh Agreement Establishing the World Trade Organization [hereinafter Marrakesh Agreement], Annex 2, (1994) *at* http://www.wto.org/english/docs_e/legal_e/legal_e.htm.

[68] WTO, Report of the Appellate Body, *Annual Report for 2004*, Annex 2 WTO Doc. WT/AB/3 (Jan. 2005) [hereinafter Appellate Body *2004 Report*.

[69] *Id.* at Annex 3.

[70] *See* DSU, *supra* note 67, art. 4 (establishing that trade dispute resolution under the DSU begins with consultations between the affected WTO Members).

[63] WTO Secretariat, Dispute Settlement: The Disputes - Disputes, Chronologically, *at* http://www.wto.org/english/tratop_e/dispu_e/dispu_status_e.htm (last visited Aug. 11, 2005).

attacked the concept in general. While the experience of the WTO is not fully transferable to the investment appellate mechanism concept– in particular, the WTO's Appellate Body is applying a limited number of international trade agreements while an ICSID Appellate Body could ultimately be applying the differing provisions of hundreds of BITs and FTAs– there are obvious useful parallels.

IV. **Standard of Review - Level of Deference to Tribunals**

Perhaps the single most important issue facing negotiators of an appellate mechanism, upon which governments and private investors are likely to differ, is the standard of review. The possible range of standards runs the gamut from the high degree of deference and narrow standards of review incorporated in the ICSID and UNCITRAL Model Law standards, discussed earlier, to a *de novo* review at the opposite end of the spectrum. As noted above, the ICSID Annulment Committee normally vacates an arbitral decision only when "the Tribunal has manifestly exceeded its powers." Under UNCITRAL Model Law, Article 34, a court is to annul the tribunal's award when "[T]he award deals with a dispute not contemplated by or not falling within the terms of the submission to arbitration, or contains decisions on matters beyond the scope of the submission to arbitration...." and on a few other grounds, such as the award being contrary to public policy.

In Canadian practice, where the UNCTRAL Model Law standards have been adopted, this has been interpreted as correctness on law, reasonableness on applying the law to facts (*S.D. Myers)*; and a "high degree of deference" (*Feldman*) although the application of the standard has not been fully consistent, as noted above.

Where the arbitral situs is outside the United States, the international provisions of the Federal Arbitration Act (the same grounds as apply to enforcement under the New York Convention) would apply for review by U.S. courts.[64] Where the situs of the international arbitration is in the United States– in Washington, D.C., for example, as in several pending NAFTA cases– both the domestic and international sections of Federal Arbitration Act would be applicable, including the criterion of "manifest disregard of law".[65] While no U.S. court decisions reviewing NAFTA arbitrations exist to date, it is reasonable to expect that U.S. court review will afford a high degree of deference to NAFTA and similar investment arbitrations, as occurs with review of other types of arbitral awards, or in enforcement actions under the New York Convention.

Presumably, the NGOs and at least some government supporters of the appellate mechanism concept have in mind a broader scope of review. For example, Canada, the respondent in *S.D. Myers*, argued unsuccessfully that the appropriate standard of review is

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64 *See* 9 U.S.C. § 201, et seq.

65 *See* Knull & Rubins, *supra* note 1, at 544.

"correctness" not only with regard to the law but to the application of facts to the law, a broader standard than that applied to review of arbitrations involving only private parties.[66] One possibility is the WTO Appellate Body standard for review of Panel decisions, empowering the Appellate Body to review "issues of law covered in the panel report and legal interpretations developed by the panel."[67] In practice, the WTO Appellate Body has essentially followed this approach. The panels are given relatively little leeway with regard to issues of law, but considerable discretion with regard to their factual determinations.[68]

The *Chevron v. Natural Resources Defense Council*[69] standard, which calls for deference to the expert tribunal below, contemplating affirmation even where the reviewing court might have reached a different conclusion, but reversal where the tribunal below makes legal errors, is certainly one which could logically be adapted in principle for an appellate mechanism for investment disputes, given the obvious specialized expertise of most investor-state arbitration tribunals. Effectively, that standard has been adopted for panel review of administering agency decisions under the WTO's Antidumping Agreement.[70]

One interesting approach to the standard of review approach is found in the ICSID Secretariat's Discussion Paper, which proposes the following:

> An award could be challenged pursuant to the Appeals Facility Rules for a clear error of law or on any of the five grounds for annulment of an award set out in Article 52 of the ICSID Convention.[71] A further ground for challenging an award might consist in serious errors of fact; this ground would be narrowly defined to

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[66] *S.D. Myers*, *supra* note __, ¶ 33.

[67] WTO Understanding on Rules and Procedures Governing the Settlement of Disputes, Art. 17:6, *available at* http://www.wto.org (visited Aug. 8, 2005).

[68] Thus, in *Japan - Measures Affecting the Importation of Apples,* WT/DS245/AB/R, AB-2003-4 (issued Nov. 26, 2003, adopted Dec. 10, 2003), rejected certain challenges to the Panel's fact-finding, indicating that it "would not base a finding of inconsistency with [DSU] Article 11 simply on the conclusion that we might have reached a different factual finding from the one the panel reached." *Id.,* ¶ 222(quoting *EC- Asbestos Appellate Body Report,* ¶ 159). It also suggested that certain other panel conclusions were within the panel's "margin of discretion" in evaluating the relevant evidence. *Id.,* ¶ 221. For a comprehensive analysis of WTO standard of review practice, *See* Claus-Dieter Ehlermann and Nicholas Lockhart, *Standard of Review in WTO Law*, 7 J. INT'L ECON. L. 491 (2004).

[69] *Chevron v. Natural Resources Defense Council,* 468 U.S. 1227 (1984).

[70] [I]n its assessment of the facts of the matter, the panel shall determine whether the authorities' establishment of the facts was proper and whether their evaluation of those facts was unbiased and objective. If the establishment of the facts was proper and the evaluation was unbiased and objective, even though the panel might have reached a different conclusion, the evaluation shall not be overturned." WTO Anti-dumping Agreement, Art. 17.6(i).

[71] *See* discussion at Part II(A), *supra.*

preserve appropriate deference to the findings of fact of the arbitral tribunal.[72]

The inclusion of "errors of law" is consistent with the earlier discussion, and is likely to be found in any appellate mechanism proposal that reaches fruition. However, it is doubtful that there could be review of "serious errors of fact" without the review process leading to an effective *de novo* review by the appellate mechanism. There is obviously a significant risk that this could become a "Pandora's Box" for either or both parties to the proceedings at the tribunal level to reintroduce existing facts or introduce new ones to buttress its case that the tribunal had made "serious" errors, by submitting a voluminous factual record. Surely, any factual error important enough, if proven, to change the result would necessarily be considered "serious" by the party allegedly adversely affected.

Accordingly, inclusion of the broad power by the appellate mechanism to review factual determinations made by the original arbitral tribunal is likely to be strenuously opposed by the investment bar, although it might well be supported by Canada and Mexico, among other state respondents, as a means of further reducing the risk of an adverse tribunal ruling directing the government to pay money to a foreign investor.

It is reported that the U.S. government, in preparation for the CAFTA-DR negotiating group, has agreed internally on a middle ground. Review of legal issues would not be either *de novo* or subject to the more limited *Chevron* standard but, rather, to an intermediate "clear legal error" standard.[73] Review of alleged factual errors would be narrow, limited to situations where the complaining party could demonstrate that "no reasonable trier of facts" could have reached the conclusion found by the tribunal.[74] If this approach could be negotiated with the other CAFTA-DR parties, it would represent a reasonable compromise among divergent interests both in the United States and in the other Party nations.

V. **Other Hurdles in Creating an Appellate Mechanism**

The legal and practical challenges to the idea are also significant. In addition to choice of the appropriate standard of review, many other questions arise. These relate, *inter alia*, to the power of the appellate mechanism to confirm, set aside and remand; issues relating to choice of law; the relationship of the appellate mechanism process to national court review; the appropriateness of bonding requirements for appeals; and the complexities of structuring one or more appellate bodies to deal with multiple agreements. It could be very difficult to reach agreement on these issues among investor groups, civil society and governments.

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72 ICSID Discussion Paper, *supra* note 2, Annex, at 4.

73 U.S. Official's Observations, *supra* note 24.

74 *Ibid.*

A. **Procedural and Jurisdictional Issues**

There is no reversal authority for NAFTA, Chapter 19 (unfair trade disputes), only the authority to affirm or remand.[75] The ICSID Annulment Committee may affirm or annul, but not effectively remand; at the request of either part, the dispute is to be submitted to a new tribunal, presumably to start over.[76] The WTO Appellate Body has no remand authority to panels, but only to "uphold, modify or reverse the legal findings and conclusions of the panel."[77] (Among the reforms of the DSU being considered by the WTO as part of the Doha Development Round is authority for the Appellate Body to remand cases to the panels for further proceedings in appropriate circumstances.[78])

Under NAFTA, a claimant may not enforce an award until 120 days have elapsed without a party seeking annulment under ICSID, or three months have elapsed without any disputing party having sought revision or annulment under the ICSID Facility Rules or UNCITRAL Arbitration Rules.[79] (CAFTA-DR contains similar language.[80]) The ICSID Annulment Committee is granted specific authority to stay enforcement of the underlying award pending the committee decision.[81]

Is, as most assume, the investment appellate mechanism to be a substitute for situs court review, or would it be an *additional* step? If part of the problem with the current system is court review in the state of the situs, shouldn't that step be eliminated, effectively to be replaced with the appellate mechanism? One selling point of an appellate mechanism to the investment community is the possible elimination of two situs court appeals, to the court of first instance and then to the appellate level, a costly process in both time and money. However, some NGO groups opposed to NAFTA Chapter 11 in general have expressed their "strong opposition to any provisions in an appellate mechanism that would eliminate domestic legal review of arbitral provisions,"[82] even though such court review is very circumscribed today, as discussed in Part II, above.

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[75] NAFTA, *supra* note 7, art. 1904(8).

[76] ICSID Convention, *supra* note 32, art. 52(6).

[77] Dispute Settlement Understanding, *supra* note 67, art. 17(13).

[78] *See* Report by the Chairman to the Trade Negotiations Committee, Special Session of the Appellate Body (Jun. 6, 2003), at 8, *available at* http://docsonline.wto.org/DDFDocuments/t/tn/ds/9.doc (visited Aug. 16, 2002) (suggesting the amendment of art. 17(12) of the DSU to permit the complaining party in a WTO dispute to request the Dispute Settlement Body to remand an issue to the original panel where the factual findings by the panel were insufficient to permit the Appellate Body to fully address the issue).

[79] NAFTA, *supra* note 7, art. 1136(3).

[80] CAFTA-DR, *supra* note 3, art. 10.26(6).

[81] ICSID Convention, *supra* note 32, art. 52(5).

[82] CIEL/NGO Letter, *supra* note 16, at 1.

B. Transparency of the Proceedings

NAFTA itself provides that the final award may be made public if either the government or the private party wishes to do so (in the case of Canada or the United States), or in accordance with the applicable arbitration rules (Mexico).[83] Even the formal notice initiating arbitration may not be public if neither party decides to release it. Most of the NAFTA transparency rules were add-ons. In July 2001, the NAFTA Parties stated that "nothing in NAFTA imposes a general duty of confidentiality" and agreed that they would "make available to the public in a timely manner all documents submitted to, or issued by, Chapter 11 tribunals" subject to certain exceptions for confidential or privileged information. In October 2003, Canada and the United States, but not Mexico, issued statement indicating that they would consent– and request disputing investors and tribunals to consent– to holding hearings that are open to the public, subject to measures to protect confidential business information.[84] In October 2003, Canada and the United States, again without Mexico, issued a statement indicating that they would consent– and request disputing investors and tribunals to consent– to holding hearings that are open to the public, subject to measures to protect confidential business information.[85] At the same time, a statement was issued setting forth procedures for non-disputing party (*amicus curiae*) participation in Chapter 11 proceedings.[86]

Subsequent agreements, such as CAFTA-DR and the 2004 U.S. Model BIT, incorporate similar transparency and third-party participation language directly in the text of the agreements.[87] They also reflect transparency requirements in the TPA.[88] NGOs, in commenting on the appellate mechanism concept, have urged, *inter alia*, that it incorporate provisions for *amicus curie* briefs and open hearings.[89] Even the ICSID Secretariat has proposed modifications

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[83] NAFTA, *supra* 7, Annex 1137.4.

[84] NAFTA Free Trade Commission, *Notes of Interpretation,* parts A(1), A(2) (Jul. 30, 2001), *available at* http://www.ustr.gov.
Transparency rules are written into the investment chapter of CAFTA-DR, *supra* note 3, art. 10.21.

[85] *Statement on Open Hearings in NAFTA Chapter Eleven Arbitrations,* Oct. 7, 2003, *available at* http://www.ustr.gov; Statement of Canada on Open Hearings in NAFTA Chapter Eleven Arbitrations (Oct. 2003), *available at*http://www.dfait-maeci.gc.ca.

[86] *See Statement of the Free Trade Commission on non-disputing party participation* (Oct. 2003), *available at*< http://www.ustr.gov>; *NAFTA Commission Meet, Announces New Transparency Measures*, USTR Press Release, Oct. 7, 2003, at 1.

[87] CAFTA-DR, *supra* note 3, art. 10.21; Model BIT, art. 29.

[88] The principal negotiating objectives include, "[E]nsuring the fullest measure of transparency in the dispute settlement mechanism . . . ." TPA, *supra* note 25, 19 U.S.C. § 3802(b)(3)(H) (2002).

[89] Int'l Institute for Sustainable Development, *Comments on ICSID Discussion Paper, "Possible Improvement of the Framework for ICSID Arbitration"* (Dec. 2004), at 8-9, *available at* http://www.iisd.org.

in the Arbitration Rules which would facilitate open hearings and the receipt of *amicus* briefs when the tribunal so determined after consultation with the parties.[90] It can thus be reasonably assumed that any appellate mechanism agreement negotiated by the CAFTA-DR parties will incorporate transparency provisions similar to applicable in CAFTA-DR to the conduct of tribunal proceedings, perhaps simply by reference.[91]

C. **Bonding Requirements**

Also, to protect investors, should an appealing government be required to post a bond equal to the amount of the arbitral tribunal's award pending appeal? This is a common requirement in U.S. courts, as a precondition for appeal, due to the lengthy delays that occur when review takes place. The bonding requirement was a key element in *Loewen.* Because the claimant allegedly could not meet bonding requirements for an appeal, set at $625 million, Loewen settled the case for $175 million, "under conditions of extreme duress" and brought a Chapter 11 claim.[92]

There is no specific provision in ICSID for such a requirement, which would apply in most instances to an appealing government. However, at least four of the *ad hoc* ICSID Annulment Committees have continued the stay for enforcement for the tribunal's award only on condition that the applicant for the stay (the respondent government) provide a bank guarantee or bond for payment of the Award,[93] and a stay has been continued only once under circumstances where no bond or other security was required.[94] The ICSID Discussion Paper proposes that the appealing state be required to post a bank guaranty or bond in the amount of the award.[95] (The bonding issue would not likely arise where the investor is seeking review of the tribunal's award, since she would not be appealing unless her request for compensation had been denied.) This feature of the proposal would likely be strenuously opposed by the ICSID member governments negotiating an appellate mechanism. However, it may well be a make-or-break issue with the investment bar.[96] Thus, it makes eminent sense for the United States to include the bonding requirements in its negotiating proposal for CAFTA-DR.[97]

D. **Choice of Law**

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[90] ICSID Discussion Paper, *supra* note 2, at 10-11.

[91] U.S. Official's observations, *supra* note 24.

[92] Loewen Group v. United States (Award), para. 6 (Jun. 26, 2003), Decision on Request for Consideration (Sep. 13, 2004), *both available at* http://www.naftaclaims.com (visited Aug. 8, 2005).

[93] Anthony F.T. Fernando, *supra* note 17, at 1.

[94] *Id.* at 2.

[95] ICSID Discussion Paper, *supra* note 2, Annex, at 6.

[96] Informal conversation with then ICSID Deputy Secretary General, Antonio Parra, at ICSID, Jun. 3, 2005.

[97] U.S. Official's observations, *supra* note 24.

If the investment appellate mechanism is to review issues of law decided by investment tribunals, it, like the tribunals, will have to decide what law applies. One of the differences between the WTO Appellate Body and any proposed for investment disputes is the fact that the WTO Appellate Body is applying in all cases a defined body of international trade law, the "covered agreements."[98] Reference to outside international law sources, other than the Vienna Convention on the Law of Treaties for interpretative purposes, has been rare[99]

The issues tend to more complex even under individual bilateral investment treaties and free trade agreements. Even NAFTA is less straightforward than might be imagined from the text: Chapter 11 tribunals are directed to "decide the issues in dispute in accordance with this Agreement and applicable rules of international law."[100] Yet, this has led under NAFTA to considerable litigation over the concept of "international law." For example, Article 1105 states that "Each Party shall accord to investment of investors of another Party treatment in accordance with international law, including fair and equitable treatment and full protection and security."[101] The scope of the concept "fair and equitable treatment" under international law has never been clear, and the water was muddied early on when the Tribunal in *Pope & Talbot* initially determined that this quoted language provided claimants with a right that was *in addition to* rather than limited by the phrase "treatment in accordance with international law."[102]

The concerns of the NAFTA Parties over this *Pope & Talbot* deviation prompted the first and to date only binding "Interpretation" of NAFTA Chapter 11,[103] which, *inter alia*, stated that "The concepts of 'fair and equitable treatment' and 'full protection and security' do not require treatment in addition to or beyond that which is required by the *customary* international law

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[98] DSU, *supra* note 67, art. 1(1). These agreements consist of the Marrakesh Agreement Establishing the World Trade Organization and its more than twenty annexed agreements dealing with trade in goods, trade in services, trade-related intellectual property rights, and resolution of disputes.

[99] In *EC - Hormones*, the Appellate Body considered whether the "precautionary principle" used in part by the EC to justify its ban on imports of hormone-fed beef was a principle of customary international law, deciding in the negative. *EC Measures Concerning Meat and Meat Products*, WT/DS 26, 48/AB/R, adopted Feb. 13, 1998, *available at* http://www.wto.org.

[100] NAFTA, *supra* note 7, art. 132(1).

[101] *ID.*, art. 1105(1).

[102] *Pope & Talbot v.* Canada (Merits, Phase II) (Apr. 10, 2001), para. 110, *available at* http://naftaclaims.com/Disputes/Canada/Pope/PopeFinalMeritsAward.pdf (visited Sep. 8, 2005).

[103] NAFTA, art. 1131(2) provides that "An interpretation by the [Free Trade] Commission of a provision of this Agreement shall be binding on a Tribunal established under this Section."

minimum standard of treatment of aliens."[104] In subsequent agreements such as the FTA with Chile, the governing law is explicitly "customary international law,"[105] and customary international law is explicitly defined as resulting from "a general and consistent practice of States that they follow from a sense of legal obligation,"[106] presumably to discourage tribunals from relying too extensively on other agreements and arbitral decisions as a source of customary international law. The 2004 Model BIT and the CAFTA-DR FTA both contain essentially identical language.[107]

However, even in U.S. FTAs this is not the end of the matter. In the U.S.- Chile FTA, for example, the governing law for general claims is "this Agreement and applicable rules of international law," as in NAFTA; however, when a claims is submitted based on a specific investment agreement or investment authorization, the tribunal is directed to decide the manner,

> in accordance with the rules of law specified in the pertinent investment agreement or investment authorization . . . If the rules of law have not been specified or otherwise agreed, the tribunal shall apply the law of the respondent (including its rules on the conflict of laws), the terms of the investment agreement or investment authorization, such rules of international law as may be applicable, and this agreement.[108]

A similar bifurcation– and challenge to the tribunal and any reviewing body– appears in the CAFTA-DR FTA.[109]

Such differences obviously would not raise major problems if there is a separate appellate mechanism for each FTA and BIT, as is contemplated with CAFTA-DR. However, if a single appellate mechanism, at ICSID or elsewhere, is ultimately created with jurisdiction over dozens or hundreds of BITs and FTA investment provisions, or even covering only the nearly fifty U.S. FTAs and BITs,[110] the level of complexity will be high.

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[104] *See Notes of Interpretation of Certain Chapter 11 Provisions*, (Jul. 31, 2001), *available at* <http://www.dfait-maeci.gc.ca/tna-nac/NAFTA-Interpr-en.asp?format=print> (visited Mar. 31, 2003).

[105] U.S. - Chile FTA, *supra* note 28, art. 10.4(1).

[106] *Id.,* annex 10-A.

[107] 2004 Model BIT, *supra* note 29, art. 5, annex A; CAFTA-DR FTA, *supra* note ___, art. 10.5, annex 10-B.

[108] U.S. - Chile FTA, *supra* note 28, arts. 10.21(1) and 10.21(2).

[109] US - CAFTA-DR FTA, *supra* note 3, arts. 10.22(1) and 10.22(2).

[110] Once those already approved by Congress (CAFTA-DR, Morocco) enter into force, the United States will have FTA based investment protection with eleven nations (Canada, Mexico, Chile, Singapore, Dominican Republic, El Salvador, Guatemala, Honduras, Nicaragua, Costa Rica, Morocco); As of March 2005, the United States had negotiated 47 BITs and 40 were in force. U.S. Dept. of State, *U.S. Bilateral Investment Treaty Program*,

E. Structure and Membership of an Appellate Mechanism

Should there be permanent members (as with the WTO Appellate Body) or an *ad hoc* tribunal in each instance formed from a standing roster (as with the ICSID Annulment Committee)? The WTO Appellate Body calls for a standing roster of seven members, three of whom serve on each case, in rotation.[111] However, in "a practice of collegiality," all seven members review briefs, attend hearings, and participate to some extent in the decision-making process, an approach which adds to the consistency of decisions.[112] For the WTO's Appellate Body, there have been 6-12 cases a year, and the members are effectively kept busy by the WTO at least half-time.

The ICSID Annulment Committee actions, in contrast, are rare; only a handful in forty years.[113]

The case load of an investment appellate mechanism will ultimately depend not only on how many investor - state disputes are filed, but on how many of the more than 2000 BITs and dozens of FTAs with investment provisions replace the ICSID Annulment Committee and situs court review with exclusive jurisdiction for the appellate mechanism, if and when a mechanism is created under ICSID auspices. A potentially large volume exists, but the number of cases in actual practice is very difficult to predict.

Of course, if there are separate appellate mechanisms for each agreement or even group of agreements the case load for any individual agreement could be very small. With NAFTA, there have been about 40 investment cases filed in eleven years,[114] with roughly half brought under the

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http://www.state.gov/e/eb/rls/fs/22422.htm (visited Aug. 9, 2005). Several others FTAs are in various stages of negotiation or ratification (Morocco, Bahrain, Panama, Ecuador, Colombia, Peru).

[111] DSU, *supra* note 67, art. 17(1).

[112] Debra P. Steger & Peter Van Den Bossche, *WTO Dispute Settlement: Emerging Practice and Procedure,* 92 Am. Soc'y Int'l L. Proc. 79 (1998)

[113] *See* ICSID, List of Concluded Cases, *passim, available at* http://www.worldbank.org/icsid/cases/conclude.htm (visited Aug. 11, 2005).

[114] Based on the best information available (the Todd Weiler website, http://naftaclaims.com) , approximately forty-one Chapter 11 actions had been filed as of September 2005, including those which may be dormant. While this is believed to be a comprehensive list, the secrecy surrounding the Chapter 11 filing process does not assure that disputes and the documents filed during the proceedings will be made public. NAFTA has no such requirements. However, an "Interpretation" issued by the Parties July 31, 2001, requires all documents relating to Chapter 11 provisions, excepting those containing confidential information, to be made "available to the public in a timely fashion." Compliance by the governments (and/or the claimants) appears to be very good.

UNCITRAL Arbitration Rules[115], and the rest under the ICSID Additional Facility Rules.[116] Had there been an appellate mechanism with jurisdiction, there might have been more referrals than there have been to date (3) to the reviewing courts, all involving the relatively rare monetary awards against the NAFTA Parties.[117] If an appellate mechanism existed and had been authorized to exercise a broader standard of review than Article 34 of the UNCITRAL Model Law, at least some of the investor claimants whose claims against the NAFTA Parties have been rejected[118] might have brought appeals. However, even then, it is unlikely that more than an additional handful of cases would have been appealed.

Since the CAFTA-DR mechanism will likely cover that FTA alone, it would make little sense to create a standing body as in the WTO. Rather, as the United States is likely to propose,[119] the only cost-effective option would be a roster system similar to that used in the ICSID Annulment Committee, in which each CAFTA-DR member government nominates a list of acceptable individuals, and when an award is referred to the appellate mechanism, three members are chosen from the rosters. Presumably, if normal practice is followed, one member would be nominated by the claimant - investor, one by the responding state, and the third chosen by the two or, failing agreement, by the appointing authority, presumably the ICSID Secretary

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[115] UNCITRAL Arbitration Rules (1976), *available at* http://www.uncitral.org/uncitral/en/uncitral_texts/arbitration/1976Arbitration_rules.html (visited Aug. 9, 2005).

[116] ICSID Additional Facility Rules (Jan. 2003), *available at* http://www.worldbank.org/icsid/facility/facility.htm (visited Aug. 9, 2005).

[117] Only four cases– *Metalclad, S.D. Myers, Pope & Talbot* and *Feldman*– have resulted in monetary damages awards against Canada or Mexico, and there have been no monetary damages awarded to date against the United States. Metalclad Corporation v. United Mexican States, Case no. ARB(AF)/97/1 (Aug. 26, 2000), 40 I.L.M. 36 (2001); Pope & Talbot v. Canada, Award in Respect of Damages (May 31, 2002), 41 ILM 1347 (2002); S.D. Myers, Inc. v. Government of Canada (Nov. 13, 2000) (Partial Award); Marvin Feldman v. United Mexican States, Case no. ARB(AF)/99/1 (Dec. 16, 2002). All except *Pope & Talbot* were appealed, unsuccessfully. An earlier case was settled after the Government of Canada agreed to change certain regulations and pay costs. Ethyl Corporation v. Government of Canada, Jun. 24, 1998, 38 I.L.M. 708 (1999)

[118] The rejected claims include Waste Management, Inc. v. Mexico (Final Award) (Apr. 30, 2004); Methanex v. United States (Final Award) (Aug. 9, 2005); Robert Azinian, Kenneth Davitian & Ellen Baca. v. United Mexican States, Case no. ARB(AF)/97/2 (Nov. 1, 1999), 39 I.L.M. 537, 555 (2000); Mondev v. United States, Case no. ARB(AF)/99/2 (Oct. 11, 2002); ADF Group, Inc. v. United States, Case no. ARB(AF)/00/1 (Jan. 9, 2003); UPS v. Canada (Award on Jurisdiction) (Nov. 22, 2003)[hereinafter *Feldman*]; Loewen Group v. United States (Award) (Jun. 26, 2003), Decision on Request for Consideration (Sep. 13, 2004) [hereinafter *Loewen I* and *Lowen II*, respectively]; Gami Investments v. United Mexican States (Award) (Nov. 15, 2004) *all available at* http://naftaclaims.com

[119] U.S. Official's observations, *supra* note 24.

General, as in CAFTA-DR arbitrations.[120]

A related issue is whether party nationals should be permitted to serve, as on investment tribunals under ICSID and NAFTA, or excluded, as with ICSID Annulment Committee and with WTO panels (but not with the Appellate Body). Given the relative shortage of highly experienced arbitrators, excluding those from the countries whose nationals are the more frequent claimants (such as the United States) could make the process difficult or impossible to administer.

Would 15 (or more) outstanding investment arbitrators be willing to accept nomination to serve on an appellate mechanism under CAFTA-DR? Probably, as long as listing on the roster did not foreclose their continued work as arbitrators? The ICSID Secretariat had proposed a panel of 15 persons of "recognized authority, with demonstrated expertise in law, international investment and investment treaties", each from a different nation, with three sitting on each appeal.[121] With the CAFTA-DR appellate mechanism, it would make sense initially to require each government to nominate at least two (and probably not more than five) individuals, who need not be nationals of the CAFTA-DR nations. Having non-nationals on the roster would provide alternatives for chairperson who were perceived as independent from any of the parties, and the U.S. negotiating proposal apparently contemplates such nominations.[122]

If there is a large roster, should some of the members be persons with some experience in environmental law or labor law in addition to or instead of international investment law? There is no general bar to such appointments for a roster– as distinct from a standing body– as the parties could presumably influence the selection or non-selection of the roster members for individual disputes. The investment bar in the United States would, however, almost certainly oppose the appointment of roster members other than recognized international investment law experts with prior arbitral experience.

Presumably, the costs of individual appeals would be borne by the parties, as is now the case at ICSID for both tribunals and the Annulment, at the ICSID rate– currently $300 per hour– or some higher agreed rate. Certainly, the CDN$800 per day rate currently paid to NAFTA Chapter 19 and 20 arbitrators[123] would not attract the skilled arbitrators required to make a CAFTA-DR appellate mechanism a success.

F. Conflicts of Interest

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[120] CAFTA-DR, *supra* note 3, art. 10.19(2).

[121] ICSID Discussion Paper, *supra* note 2, Annex, at 3. These criteria are similar to those required under the WTO's DSU, *supra* note 67, art. 17(3).

[122] Telephone conference with a member of the State Department's advisory committee on investment, Aug. 24, 2005; memorandum on file with author.

[123] Email communication from the U.S. Secretary, NAFTA Secretariat, Aug. 25, 2005; copy on file with author.

The problem of actual and potential conflicts of interest arises wherever *ad hoc* arbitrators are used. Unless the appellate mechanism effectively becomes a permanent tribunal, the members are all likely to be part-time. When they are not engaged in work for the appellate mechanism they are likely to be involved in their area of expertise, i.e., investment disputes, either as arbitrators or counsel in investor-investor or investor-state disputes. The potential for conflicts is thus significant.

The ICSID Convention and Arbitral Rules encompass no code of conduct as such. Instead, Rule 6 provides a declaration by the arbitrators disclaiming any reasons for non-service or lack of independence.[124] Apparently because of some dissatisfaction with such a bare-bones approach, the ICSID secretariat has proposed a requirement for a much broader disclosure requirement designed to identify possible conflicts at the outset:

> Attached is a statement of (a) my past and present professional, business and other relationships (if any) with the parties is attached hereto and (b) any other circumstance that might cause my reliability for independent judgment to be questioned by a party. I acknowledge that by signing this declaration I assume a continuing obligation promptly to notify the Secretary-General of the Centre of any such relationship or circumstance that subsequently arises during this proceeding.[125]

Because of the obvious sensitivity of the appellate mechanism process, particularly in the earlier year, a stronger code of conduct would be appropriate, perhaps patterned after the NAFTA Code of Conduct[126] or the WTO DSU Rules.[127] For example, the NAFTA Code of Conduct(which is not applicable in Chapter 11 investment disputes but only to those arising under other chapters) requires, *inter alia*, that

A candidate shall disclose any interest, relationship or matter that is likely to

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[124] [ICSID] Rules of Procedure for Arbitration, Rule 6(2), *available at* http://www.worldbank.org/icsid/basicdoc/partF.htm (visited Sep. 8, 2005).

[125] Suggested Changes to the ICSID Rules and Regulations, May 12, 2005, at 12, *available at* http://www.worldbank.org/icsid/sug-changes.htm (visited Aug. 9, 2005).

[126] Code of Conduct for Dispute Settlement Procedures Under Chapters 19 [unfair trade disputes] and 20 [disputes among the Parties] [hereinafter "NAFTA Code of Conduct"] *available at* http://www.nafta-sec-alena.org/DefaultSite/index_e.aspx?CategoryId=75 (visited Aug. 9, 2005).

[127] WTO Appellate Body, "Rules of Conduct for the Understanding of Rules and Procedures Concerning the Settlement of Investment Disputes," Annex II to the Working Procedures for Appellate Review (Jan. 4, 2005), *available at* http://www.wto.org/english/tratop_e/dispu_e/ab_e.htm#20 (visited Sep. 8, 2005) [hereinafter "WTO Code of Conduct"].

> *affect the candidate's independence or impartiality or that might reasonably create an appearance of impropriety or an apprehension of bias in the proceeding*. To this end, a candidate shall make all reasonable efforts to become aware of any such interests, relationships and matters.
>
> . . .
>
> Once appointed, a member shall continue to make all reasonable efforts to become aware of any interests, relationships or matters referred to in section A and shall disclose them. The obligation to disclose is a *continuing duty*which requires a member to disclose any such interests, relationships and matters that may arise during any stage of the proceeding. [128]

The WTO requires self-disclosure by panelists or members of the Appellate Body of "any information that could reasonable be expected to be known to them at the time which, coming within the governing principles of these rules, is likely to affect or give rise to justifiable doubts as to their independence or impartiality."[129] The rules include "an illustrative list (Annex 2) of examples of the matters subject to disclosure," as well as a continuing obligation to "also disclose any new information . . . ."[130]

G. **Situs**

For efficiency and consistency reasons, a single multilaterally-supported appellate mechanism, as contemplated in the Senate Report, would be preferable to separate bodies for various agreements, *if* the volume is likely to be sufficient to justify such bureaucracy. ICSID is an obvious situs for a broadly based appellate mechanism, assuming that there is a significant number of ICSID Convention Parties who are interested in an alternative (or addition) to the Annulment Committee. Among other things, there is a highly competent ICSID secretariat. Even if that staff were to require augmentation for such new responsibilities, this would be much more cost-effective than starting from scratch. Unfortunately, there does not seem to be much support among ICSID Members for an investment appellate mechanism, either instead of or more likely in addition to the Annulment Committee, as indicated by the Secretariat's withdrawal of the proposal, noted earlier. (Those that likely most concerned– Canada and Mexico– are not members of ICSID.)

In some respects this may be just as well. Because amendment of the ICSID Convention requires unanimous approval of the now more than 140 members,[131] it would be impractical to incorporate the appellate mechanism as an amendment to the Convention. Rather, as the ICSID

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128 NAFTA Code of Conduct, *supra* note 126, Part II(A, C) emphasis added.

129 WTO Code of Conduct, *supra* note 127, art. VI(2).

130 *Id.,* annex 2, art. VI((5).

131 ICSID Convention, *supra* note 32, art. 66.

Secretariat suggested, it would be preferable to have the earlier proposed "ICSID Appeals Facilities Rules" approved by ICSID's Administrative Council (as the Additional Facility Rules were some years ago).[132] If the Appeals Facilities Rules were drafted in a manner similar to the Additional Facility [Arbitral] Rules, they would be largely procedural in nature. Consent to the use of the Appellate Facilities Rules, agreement to forego the use of the Annulment Committee, and the substantive law rules to be applied, would presumably be determined by the underlying bilateral investment treaties or FTA investment chapters,[133] as the availability of the Additional Facility Rules is determined.[134] Another alternative might be to conclude a "plurilateral" protocol to the ICSID Convention, rather than an amendment, which provided that as among the parties to the protocol the Appellate Facilities Rules would be substituted for the Annulment Committee.

The Organization of Economic Cooperation and Development ("OECD")– a group of rich countries plus South Korea, Mexico and a few in Eastern Europe)[135]– in some respects is another logical home for a broadly-based Appellate mechanism. Presumably, an agreement creating an appellate mechanism– entirely procedural in nature– would be be easier to negotiate than the failed Multilateral Agreement on Investment.[136] As such it could be made available to non-OECD members, although some might be reluctant to participate in an instrument prepared largely by capital-exporting nations, and the failure of the OECD's efforts to conclude the Multilateral Agreement on Investment in 1998 may make the OECD locus unattractive to others. Because there are hundreds of BITs in force similar to the OECD model, between developed and developing nations, this nexus might provide a rationale for non-OECD member accession.

One commentator has suggested that the WTO's Appellate Body might be given jurisdiction over investment disputes as well as trade disputes.[137] While attractive from an efficiency point of view, this option has a number of disadvantages, including the fact that WTO Appellate Body members are chosen for trade law rather than investment law expertise (although a number of present and former members have investment law experience). Most WTO

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132 ICSID Discussion Paper, *supra* note 2, annex, at 1.

133 *Ibid.*

134 *See, e.g,* 2004 Model BIT, *supra* note 29, art.24(3) ; CAFTA-DR, *supra* note 3, art. 10.16(3) (providing the usual three alternative fora, ICSID Arbitral Rules, ICSID Additional Facility Rules, or UNCITRAL Arbitral Rules, and, in the case of the Model BIT, any other forum agreed to by the parties to the dispute, which is of course possible with CAFTA-DR as well).

135 *See* "About OECD," http://www.oecd.org/about/0,2337,en_2649_201185_1_1_1_1_1,00.html (visited Aug. 11, 2005) (explaining the objectives of the OECD, its work and members).

136 [Draft] Multilateral Agreement on Investment (1995-1998), *available at* http://www.oecd.org/document/35/0,2340,en_2649_201185_1894819_1_1_1_1,00.html (visited Aug. 9, 2005).

137 Manitoba Law School Professor Brian Schwartz. The suggestion was made in a conference at American University on NAFTA Chapter 11, in March 2004.

Members, who have opposed a comprehensive WTO investment agreement as one of the "Singapore Issues" in the Doha Development Round of WTO negotiations,[138] would likely strenuously oppose giving the WTO Appellate Body jurisdiction over investment disputes, viewing it as an undesirable first step in expanding the WTO's current very limited coverage of investment issues[139]. This reluctance seems likely even if the agreement creating an investment appellate mechanism were a "plurilateral" agreement, with accession optional for the WTO Members.

There are, of course, *ad hoc* alternatives, and this is undoubtedly the most practical arrangement for an appellate mechanism that may have very few cases before it from year to year, as the U.S. government apparently intends.[140] One could, for example, envision an appellate mechanism created by the seven CAFTA-DR parties, and then opened up to other parties to U.S. FTAs containing investment provisions, or to BITs with similar provisions now being negotiated by the United States. If, for example, the NAFTA Parties were to decide to amend NAFTA, Chapter 11 to include an appellate mechanism in lieu of court review in Additional Facility and UNCITRAL cases– a political Pandora's Box of considerable dimension– they could graft on to the CAFTA-DR appellate mechanism. Assuming that within a few years the United States has treaty relationships (FTA or BIT) contemplating binding investor-state arbitration with at least 50 nations[141], such a limited appellate mechanism might be reasonable in terms of efficiency, although probably less efficient cost-effective and politically acceptable than an ICSID body.

One of the problems of an *ad hoc* appellate mechanism is the need for secretariat services. However, arrangements could likely be made with the ICSID Secretariat to conduct the

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[138] The "Relationship Between Trade and Investment" was among the topics included in the Ministerial Declaration (Nov. 14, 2001) initiating the Doha Development Round of WTO negotiations, although the decision as to whether to include negotiations on investment issues was explicitly left for later. Doc. WT/MIN(01)/DEC/1, ¶ 20. Disagreement over the inclusion of the so-called "Singapore Issues" (competition law, investment, transparency in government procurement and trade facilitation) in the negotiations was partially responsible for the collapse of the negotiations at the Cancun Ministerial in September 2003. The "Doha Work Programme" adopted August 1, 2004, contains an explicit understanding that competition, investment and government procurement issues "will not form part of the Work Programme . . . and therefore no work towards negotiations on any of these issues will take place within the WTO during the Doha Round." Doc. WT/L/579, ¶ 1(g).

[139] *See* WTO Agreement on Trade Related Investment Measures, arts. 3, 6, annex, in Annex 1A of the Marrakesh Agreement Establishing the World Trade Organization (1994), *available at* http://www.wto.org (visited Aug. 9, 2005) (applying the GATT principles of national treatment, transparency and restrictions on quantitative restraints to investment, and prohibiting most performance requirements).

[140] U.S. Official's observations, *supra* note 24.

[141] *See* note 110, *supra.*

CAFTA-DR appeals on a case-by-case basis, as has been done with a number of NAFTA Chapter 11 cases brought under the UNCITRAL rules.[142] This would effectively limit any operational costs to the actual appeals filed, and important feature of the appellate mechanism given the likely great reluctance among the CAFTA-DR member governments– including the United States– to funding an entity that may have no cases for a number of years.

Other convenient options are few. There are of course many commercial arbitration sites, such as the International Chamber of Commerce in Paris[143], or the London Court of Arbitration[144], but neither are well-suited to disputes involving the United States and Central American or the Dominican Republic governments compared to the use of the ICSID facilities in Washington, D.C. In theory, at least, the CAFTA-DR parties could call upon the facilities of the Canadian or Mexican sections of the NAFTA Secretariat. Those secretariats, designed to manage NAFTA Chapter 19 and 20 cases,[145] are generally under-utilized, particularly in Canada, where no Chapter 19 or Chapter 20 cases are even pending.[146] Canada, in particular, would provide a reasonably well-staffed secretariat in a neutral country, probably at costs below those charged by the ICSID Secretariat.[147]

H. **Modifications to Existing BITs and FTAs**

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[142] *See* International Thunderbird Gaming Corporation v. United Mexican States, Procedural Order no. 1 (Jun. 27, 2003), para. 4, *available at* http://naftaclaims.com/Disputes/Mexico/Thunderbird/ThunderbirdProceduralOrder1.pdf (visited Aug. 24, 2004) (stating that the "Secretariat of ICSID shall render administrative services in relation to the arbitral proceedings similar to those rendered in arbitrations under the ICSID Facility Rules"); Grand River Enterprises et al v. United States of America (NAFTA/UNCITRAL Arbitration), Minutes of the First Session of the Tribunal (Mar. 31, 2005), at 3-4, *available at* http://naftaclaims.com/Disputes/USA/GrandRiver/Grand%20River%20v.%20USA_Minutes%20First%20Session.pdf (visited Aug. 24, 2005) (indicating that ICSID is providing administrative services to the tribunal).

[143] ICC, International Court of Arbitration, http://www.iccwbo.org/index_court.asp (visited Aug. 24, 2005).

[144] London Court of International Arbitration, http://www.lcia-arbitration.com/ (visited Aug. 24, 2005).

[145] NAFTA, *supra* note 7, art. 2002(3).

[146] NAFTA Secretariat, Status of Panel Proceedings, *available at* http://www.nafta-sec-alena.org/DefaultSite/index_e.aspx?DetailID=11 (visited Aug. 24, 2005) (listing no Canadian section cases, and only four cases being administered by the Mexican section).

[147] As far as the author is aware, the Canadian secretariat has never provided secretarial services for an investor-state arbitration, and has never published a schedule of rates that might be applicable.

Incorporating an appellate mechanism would require amendment of bilateral investment treaties the investment provisions of NAFTA and other FTAs, as CAFTA-DR explicitly contemplates.[148] In most instances, changes in domestic law would also be required.[149] Where an investment treaty contemplates the use of ICSID arbitral rules, with exclusive resort to the ICSID Annulment Committee, modifications in ICSID party obligations would likely be required to substitute an appellate mechanism for the Annulment Committee. The amendment of BITs would be easier politically than amending investment provisions of NAFTA and FTAs, since it could be difficult, if reopening NAFTA or FTAs, to limit the modifications to inclusion of an appellate mechanism, but given the need for Senate advice and consent to protocols to existing BITs, the process could take years to implement, unless the legislation creating one or more appellate mechanisms could be included with other, important but less controversial trade or trade-related legislation.

VI. **Conclusions and Recommendations**

Overall, the appellate mechanism concept seems to be more generally favored by some states, including the United States, than by private investors and their counsel, although there are indications that with the right structure an appellate mechanism would be preferred over substantial delays at ICSID or review by multiple national courts.[150] This is not surprising, given that historically, most (but not all) of the requests for court or ICSID Annulment Committee review are brought be respondent states, not by investors. Also, there appears to be some concern among states that are already reassessing the desirability of BITs that the existence of an ICSID (or some other) appellate facility would effectively pressure states concluding BITs to include the facility in new agreements.

In the author's view, the investment appellate mechanism is a proposal which, *if* it can be properly implemented, could be beneficial to both governments and the investment community. A well-structured and staffed appellate mechanism could improve the jurisprudence in investment-related arbitration by increasing consistency and annulling the occasional wrong decision. A CAFTA-DR mechanism, in particular, would provide some modest increase in consistency over the current national court process. There, one can be reasonably sure that one of several U.S. roster members would sit on most or all of the cases, regardless of whether a U.S. investor was seeking compensation from one of the other CAFTA-DR governments (the most likely scenario) or vice-versa. As such, the appellate mechanism could allay some of the fears of investment agreement critics without detracting from the generally high level of investor

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[148] CAFTA-DR, *supra* note 3, Annex 10-F.

[149] In the United States, the Federal Arbitration Act (**9 U.S.C. §§ 1-14**) would have to be amended to deprive federal courts of jurisdiction to review arbitral awards rendered where the situs of the arbitration (as at ICSID in Washington) were the United States.

[150] Telephone conversation with a member of the State Department's advisory committee on investment, Aug. 24, 2005; memorandum on file with author.

protection in NAFTA, the recent FTAs and BITs, assuming of course– and this is a major assumption– that those critics were supportive of the 2-3 persons selected for the American roster.

An investment appellate mechanism is not, however, a cure-all for all or even most of the problems (real or apparent) that emerge in investor-state arbitration. Even if, as hoped, the appellate mechanism would substitute a single appellate step for what today may be multiple levels of court proceedings when arbitral decisions are reviewed by national courts, it probably would not significantly reduce expenses, particularly if the appellate mechanism has the authority to review key facts on a *de novo* basis. Nor it would satisfy those groups that are broadly opposed to NAFTA Chapter 11 and similar mechanisms in BITs and FTAs,[151] nor assure that governments unhappy with decisions against them would receive relief.

Moreover, putting the idea into practice is fraught with practical and legal problems, and the potential for enormous political controversy, even if the scope of review is limited largely to legal issues in a manner that gives considerable deference to the determinations of arbitral tribunals. Those with significant interest in the creation and operation of an investment appellate mechanism– nations, foreign investors, and NGOs, among others– will not likely see eye to eye on the major structural and procedural issues. No mechanism satisfactory to the foreign investment community is likely to be fully acceptable to governments in their defendant roles, or to environmental and other NGOs, particularly with regard to standard of review, posting of bonds, eliminating the role of national courts, and choice of roster members.

CAFTA-DR is the likely laboratory for an initial effort to create appellate mechanism, once the agreement goes into effect January 1, 2006. Whether it is realistic for the CAFTA-DR nations to conclude negotiations regarding such a novel concept within one year remains to be seen. Nor can those in the U.S. Congress who supported the concept of an appellate mechanism in the Trade Promotion Authority legislation in 2002, but opposed CAFTA-DR in 2005, be expected to support an amendment to CAFTA-DR to establish an appellate mechanism. It would also be unreasonable to assume that the Bush Administration, having won CAFTA-DR in the House of Representatives only by putting the full prestige of the presidency (and some "carrots") behind it[152], would have any strong interest in proposing a CAFTA-DR amendment to Congress, for an appellate mechanism or any other purpose. Thus, under the best of circumstances– prompt agreement on an appellate mechanism by the CAFTA-DR Parties in the mandated negotiations– it could be some years (if at all) before the CAFTA-DR is amended, and even longer before the first case reaches the appellate mechanism.

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[151] *See* CIEL/NGO Letter, *supra* note 16 (setting out the objections to an appellate mechanism that does not, *inter alia*, permit national court review, apply local law and assure that not only investment experts are appointed to the body).

[152] *See* Sophie Walker, *CAFTA Win Sends Mixed Signals on U.S. Govt-Analysts*, Jul. 28, 2005 (Reuters).

Notwithstanding these very substantial political challenges in the United States, and legal drafting and negotiating complexities, CAFTA-DR does have several advantages as a "guinea pig": there will be seven nation parties (eventually), rather than only two as in most other FTAs or three in NAFTA. All seven CAFTA-DR Parties are already parties to ICSID (unlike Canada and Mexico), which will allow flexibility in designating ICSID as the *ad hoc* secretariat or even ultimately as the seat of a broader appellate facility. Having accepted the existing investment provisions in CAFTA-DR, none of the other six Parties are likely to have significant opposition to an appellate mechanism, as it should have modest cost advantages (at least over a multiple level situs court review process) and lead to greater predictability than national courts. Since several CAFTA-DR Parties– Costa Rica and Nicaragua in particular– have a history of expropriation or other adverse actions against American investors[153], it is reasonable to predict that an appellate mechanism applicable to investment disputes under CAFTA-DR will eventually be utilized if it ever becomes operational. There will be cases, although probably not many. A well-structured investment appellate mechanism negotiated in the CAFTA-DR context should also serve as the model for broader applicability of the concept. Is an appellate mechanism really worth all the effort, up to now and in the future, to the governments, the investment communities and civil society?

Is it really cost-effective in the broadest sense to create an investment appellate mechanism when the benefits over the existing system (ICSID Annulment Committee for ICSID arbitrations, national courts for the rest) – primarily a modest increase in the likelihood of consistency and the elimination of multi-layer appeals in the national court systems– are so limited? Certainly, in retrospect, there is serious doubt. However, the process has by now gained sufficient momentum to be likely to continue through at least a good faith attempt at the drafting of a CAFTA-DR amendment. However, for adoption and implementation, don't hold your breath!

DRAFT: September 8, 2005

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[153] *See* U.S. Department of State, Background Notes: Costa Rica (Aug. 2004) ("There have been some vexing issues in the U.S.-Costa Rican relationship, principal among them longstanding expropriation and other U.S. citizen investment disputes, which have hurt Costa Rica's investment climate and produced bilateral tensions."); Dept. of State, Background Note: Nicaragua (Feb. 2005) ("The resolution of U.S. citizen claims arising from Sandinista-era confiscations and expropriations still figures prominently in bilateral policy concerns."), *available at* http://www.state.gov/r/pa/ei/bgn/ (visited Aug. 11, 2005).