

## Investor-State Arbitration

### *Evaluating Australia's Evolving Position*

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#### Abstract

This article examines Australia's contentious 2011 Trade Policy Statement in which the Federal Government indicated that it will no longer provide for investor-state arbitration (ISA) in future bilateral and regional trade agreements (BRTAs), choosing instead to rely on alternatives to ISA. These are likely to vary from encouraging investor-state parties to negotiate contracts that provide mechanisms for dispute resolution to providing by treaty that domestic courts resolve such disputes. Notwithstanding a change in Australia's Federal Government in 2013, two years after the Policy Statement was announced, the new Liberal Government has retreated from that Policy notably by including ISA in the Korea-Australia Free Trade Agreement (KAFTA) concluded on 5 December 2013. However, it has not rejected the Policy, but has indicated instead that it will consider ISA in its treaties on a case-by-case basis. As a result, the Policy could still have significant ramifications for Australia in negotiating BRTAs; it could have a material impact on Australia's inbound and outbound investors, as well as upon other states and investors directly or indirectly impacted by Australia's Policy. It is also conceivable that other states will follow Australia's initiative and reconsider whether to agree to ISA in their BRTAs. In analysing the policy shift against ISA, the paper evaluates the nature of foreign direct investment (FDI) and its economic and legal significance to host and home states, as well as to inbound and outbound foreign investors. Following this analysis, the paper outlines the rationale behind Australia's rejection of ISA in 2011. It evaluates the perceived advantages and disadvantages of alternatives to ISA, such as diplomatic intervention in investor-state disputes and conciliation proceedings between investor-state parties. However, it focuses on the most likely alternative to ISA, namely, reliance on domestic courts to resolve investment disputes. The paper argues against the complete rejection of ISA. It illustrates the challenges of Australia relying on domestic

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courts to resolve investor-state disputes in light of the impending Investment Chapter of the Trans-Pacific Partnership Agreement (TPPA) and the preservation of Australia's investment interests in Asia.

As an alternative, the article proposes the adoption of a BIT policy which would provide investor-state parties with a choice among dispute-avoiding measures, including access to either domestic courts or ISA. The rationale is that such an approach is likely to preserve the national interests of Australia, while also gaining support within the international community of states and among foreign investors.

## Keywords

Investment treaties, arbitration, litigation – ICSID – Transpacific Partnership Agreement – Australia – China

## Introduction

In a 2011 Trade Policy Statement, the Federal Government of Australia stated that Australia would no longer agree to the inclusion of ISA in its future BRTA's.<sup>1</sup> While the Trade Policy Statement implicitly acknowledged a variety of dispute avoidance and resolution options for investor-state disputes, not limited to domestic courts, it is evident that domestic courts of law serve as the primary means of resolving such disputes due to limitations associated with alternatives to ISA, such as negotiation and conciliation.

Although Australia's 2011 policy shift is not without precedent, it raises a range of potential concerns in the international investment community. One reason why the announcement has attracted such wide international coverage is due to the fact that ISA has become the predominant method of dispute

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<sup>1</sup> Craig Emerson, *Gillard Government Trade Policy Statement: Trading Our Way to More Jobs and Prosperity* <[www.dfat.gov.au/publications/trade/trading-our-way-to-more-jobs-and-prosperity.html#investor-state](http://www.dfat.gov.au/publications/trade/trading-our-way-to-more-jobs-and-prosperity.html#investor-state)> (11 December 2013) (hereafter "Policy"). For a comment on the Australian Government's Policy announced on 12 April 2011 see Luke Peterson, *Australia Rejects ISA Provision in Trade Agreements* <[dontradeourlivesaway.wordpress.com/2011/04/19/australia-rejects-investor-state-arbitration-provision-in-trade-agreements/](http://dontradeourlivesaway.wordpress.com/2011/04/19/australia-rejects-investor-state-arbitration-provision-in-trade-agreements/)> (10 December 2013). For comments on the Policy by the Liberal Government elected in 2013 see e.g., Rowan Callick, 'Korea Ready to Talk Turkey After FTA Hurdle Removed' (1 November 2013) <[www.theaustralian.com.au/business/economics/korea-ready-to-talk-turkey-after-fta-hurdle-removed/story-e6frg926-1226750841630#](http://www.theaustralian.com.au/business/economics/korea-ready-to-talk-turkey-after-fta-hurdle-removed/story-e6frg926-1226750841630#)> (10 December 2013). See generally Leon E. Trakman, 'Foreign Direct Investment: Hazard or Opportunity?' (2010) 41 *Geo. Wash. Int'l L. Rev.* 1.

resolution in cases involving investment claims against foreign governments. Particularly germane is the fact that Australia is the only developed state to have announced that it would reject ISA in its future BRTAs. Other developed states may follow Australia's example in the future, even if Australia itself varies from its 2011 Policy.

In order to evaluate the significance of this Policy, several questions will be considered. Namely, what legal and economic consequences are likely to arise from this Policy? Will the Policy further or impede other objectives of the Federal Government, such as encouraging or discouraging the growth of inbound and outbound foreign investment? Do the legal, economic and political benefits of Australia rejecting ISA outweigh its advantages? Are domestic courts, including the domestic courts of states with whom Australia will negotiate future BITs, ideal institutions for the resolution of investor-state disputes? Finally, if the costs of ISA outweigh its benefits, how might Australia adopt a more effective mechanism for resolving investment disputes, consistent with its domestic public interests? These questions are central to the analysis in this article.

In developing its analysis, the paper begins with a brief introduction of ISA and its continuing appeal to the international community. Part 2 of the paper undertakes a detailed analysis of the 2011 Trade Policy Statement, and Part 3 considers alternative dispute resolution options proposed by international organizations that could be more extensively utilized in the absence of ISA. Part 4 considers the economic reasoning behind the Trade Policy Statement, originating in the Australian Productivity Commission. It also considers whether domestic courts are the most suitable institutions to hear investment complaints lodged against host states. Part 5 examines whether Australia's rejection of ISA is likely to attain the economic goals advocated by the Federal Government in 2011. The paper highlights reasons why a complete rejection of ISA might not best serve Australia's national interests. Part 7 proposes the adoption of a BIT policy with model BIT provisions, including dispute avoidance measures such as negotiations and conciliation. The proposal also argues for parties to exercise a choice among dispute resolution measures, in particular a choice between ISA and domestic courts. The aim of the proposed policy is to reconcile Australia's domestic public policy interests with its countervailing international interests on grounds that both are in the public good.

## **1 The Dominance of Investor-State Arbitration**

The dominance of ISA as a means of resolving investor-state disputes is grounded in global economic developments. Domestic and international

investment markets are becoming increasingly interdependent. A corollary to this development is that a healthy flow of FDI into and out of investment markets impacts markedly on various economic sectors.<sup>2</sup> FDI is also a key means of facilitating economic growth, as an increase in FDI share ordinarily leads to “higher additional growth in financially developed economies.”<sup>3</sup> FDI has grown even more significant following the Global Financial Crisis of 2008 and the worldwide economic slowdown that followed. Market-based competition is growing among states to attract cross-border investment, including capital and infrastructure investments directed at promoting the financial stability and liquidity of international investments. These observations are apparent in relation to Australia in particular. Australia has developed a competitive, economically efficient and technologically advanced resource sector; it has also become a global supplier of agricultural goods and raw materials thanks significantly to inbound FDI flows. As a result, it has a material interest in promoting sustainable and stable FDI flows into and out of Australia.

By its nature, FDI that entails the growth in number and size of cross-border investment flows may lead to cross-border disputes between states and their investors. Historically, such investment disputes were resolved either through diplomatic intervention, by which states would settle disputes on behalf of their outbound investors, or by submitting the disputes to the domestic courts in the country in which the foreign investor operated.<sup>4</sup> These avenues for resolving investment disputes demonstrated significant shortcomings. In particular, they subjected investors to backdoor state-to-state diplomacy and put them at the mercy of domestic courts in countries that had variable conceptions of law and justice and that scored low on “rule of law” indices.

The international community of states has responded to the deficiency in state-to-state dispute resolution in different ways. In particular, a number of states have developed and refined a specialized international dispute resolution process known as investor-state arbitration, which is directed at promoting a healthy cross-border flow of FDI and providing investors with a

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2 See generally Leon E. Trakman and Nick Ranieri (eds.), *Regionalism in International Investment Law* (OUP 2013) 1, 24.

3 Laura Alfaro, Areendam Chanda, Sebnem Kalemli-Ozean and Selin Sayek, ‘Does Foreign Direct Investment Promote Growth? Exploring the Role of Financial Markets on Linkages’ (2010) 91:2 *J. Dev. Econ.* 242.

4 See Andreas F. Lowenfeld, ‘Diplomatic Intervention in Investment Disputes’ (1967) 61 *Proceedings of the American Society of International Law* 96–107.

viable and fair platform for dispute resolution. Under this system, a foreign investor can lodge a claim against a host state to be resolved through a specialized and expert international investment tribunal. This resort to ISA is now widely utilized by foreign investors; it is also incorporated into various bilateral and regional trade agreements worldwide, including in Asia, which has traditionally resisted ISA due to various market-based ideological and economic development considerations.<sup>5</sup>

ISA is perceived to have some distinct benefits over the alternatives. For example, ISA that is provided for by treaty can insulate states from involvement in investment disputes by giving investors an alternative pathway to resolve their grievances against host states. ISA can obviate the need for foreign investors to seek domestic law remedies which they may view as less impartial than international investment arbitration.<sup>6</sup> ISA can also confer substantive protections on foreign investors by treaty or investor-state contract, such as most-favoured-nation (MFN) or national treatment guarantees under international investment law. In addition, ISA can limit the inconsistent effect that the decisions of domestic courts can have upon investors operating within different legal systems with dissimilar legal traditions and cultures.<sup>7</sup> ISA can also reduce reliance on competing domestic rules of evidence and procedure, such as adversarial evidentiary rules in common law systems and inquisitorial methods of adducing evidence in civil law systems.<sup>8</sup> In addition, ISA can limit the perceived social and political costs associated with domestic litigation by allowing investor-state parties to control public access to proceedings.

As a result, ISA can serve as a “delocalized” process of resolving disputes between foreign investors and host states. Outbound investors can rely on ISA provided for in BITs and FTAs and avoid having to rely on the domestic courts and laws of host states about which they have qualms.

5 See Luke Nottage and J. Romesh Weeramantry, ‘Investment Arbitration in Asia: Five Perspectives on Law and Practice’ (2012) 28:1 *Arb. Int.* 19.

6 See Jürgen Kurtz, ‘Australia’s Rejection of Investor–State Arbitration: Causation, Omission and Implication’ (2012) 27:1 *ICSID Rev.* 65; Leon E. Trakman, ‘Investor State Arbitration or Local Courts: Will Australia Set a New Trend?’ (2012) 46:1 *J. World Trade* 83.

7 On the significance of legal cultures, including regionally, in international investment law see Colin B. Picker, ‘International Investment Law: Some Legal Cultural Insights’ in Trakman and Ranieri (eds.), *supra* note 2, p. 120.

8 See Leon E. Trakman, ‘Legal Traditions and International Commercial Arbitration’ (2006) 17 *Am. Rev. Int. Arb.* 1, 119–120, 126–128.

However, despite its continuing use, in recent years a small number of developing states, including in Asia, have become critical of ISA and rejected it in favour of alternative dispute resolution models.<sup>9</sup> For example, in response to negative perceptions of ISA, in 2007 the Philippines negotiated to exclude investment arbitration from its FTA with Japan.<sup>10</sup> In that same year, Bolivia withdrew from the forerunning investor-state arbitration centre, the International Centre for Settlement of Investment Disputes (ICSID).<sup>11</sup> Ecuador followed in 2009 and Venezuela did so in 2012.<sup>12</sup> The Republic of Argentina announced in 2012 that it will withdraw from the ICSID,<sup>13</sup> while South Africa has signalled that it will no longer include ISA in its future BITs.<sup>14</sup> In contrast,

- 9 For a general overview of this trend see Michael Waibel, Asha Kaushal, Kyo-Hwa Chung and Claire Balchin (eds.), *The Backlash Against Investment Arbitration: Perceptions and Reality* (Kluwer Law International 2010).
- 10 See Ministry of Foreign Affairs of Japan, *Japan-Philippines Economic Partnership Agreement* (September 2006) <[www.mofa.go.jp/policy/economy/fta/philippines.html](http://www.mofa.go.jp/policy/economy/fta/philippines.html)> (10 December 2013). See generally Shotaro Hamamoto and Luke Nottage, 'Foreign Investment In and Out of Japan: Economic Backdrop, Domestic Law, and International Treaty-Based Investor-State Dispute Resolution' (2011) 5 *TDM*.
- 11 On Bolivia's denunciation and withdrawal from the ICSID see ICSID News Release, *Bolivia Submits a Notice under Article 71 of the ICSID Convention* <[icsid.worldbank.org/ICSID/FrontServlet?requestType=CasesRH&actionVal=OpenPage&PageType=AnnouncementsFrame&FromPage=NewsReleases&pageName=Announcement3](http://icsid.worldbank.org/ICSID/FrontServlet?requestType=CasesRH&actionVal=OpenPage&PageType=AnnouncementsFrame&FromPage=NewsReleases&pageName=Announcement3)> (10 December 2013).
- 12 On Ecuador's withdrawal from the ICSID see ICSID News Release, *Ecuador Submits a Notice under Article 71 of the ICSID Convention* <[icsid.worldbank.org/ICSID/FrontServlet?requestType=CasesRH&actionVal=OpenPage&PageType=AnnouncementsFrame&FromPage=NewsReleases&pageName=Announcement20](http://icsid.worldbank.org/ICSID/FrontServlet?requestType=CasesRH&actionVal=OpenPage&PageType=AnnouncementsFrame&FromPage=NewsReleases&pageName=Announcement20)>; Karsten Nowrot, *International Investment Law and the Republic of Ecuador: From Arbitral Bilateralism to Judicial Regionalism*, 5 <[papers.ssrn.com/sol3/papers.cfm?abstract\\_id=1620424](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1620424)> (10 December 2013).
- 13 On Argentina's proposed withdrawal from the ICSID see Nicolas Boeglin, *ICSID and Latin America: Criticisms, Withdrawals and Regional Alternatives* <[cadtm.org/ICSID-and-Latin-America-criticisms](http://cadtm.org/ICSID-and-Latin-America-criticisms)> (4 July 2013).
- 14 For commentary on these events, as well as investment arbitration in Latin America see *Argentina to Withdraw from the ICSID*, <[www.presstv.com/detail/2013/01/24/285299/argentina-to-withdraw-from-icsid/](http://www.presstv.com/detail/2013/01/24/285299/argentina-to-withdraw-from-icsid/)> (24 Jan 2013); Sergey Ripinski, *Investment Treaty News: Venezuela Withdrawal from ICSID: What It Does and Does Not Achieve* <[www.iisd.org/itn/2012/04/13/venezuelas-withdrawal-from-icsid-what-it-does-and-does-not-achieve/](http://www.iisd.org/itn/2012/04/13/venezuelas-withdrawal-from-icsid-what-it-does-and-does-not-achieve/)> (13 April 2012); Luke Eric Peterson, *South Africa Pushes Phase-out of Early Bilateral Investment Treaties After at Least Two Separate Brushes with Investor-State Arbitration* <[www.iareporter.com/articles/20120924\\_1](http://www.iareporter.com/articles/20120924_1)> (10 December 2013). See generally Scott Appleton, *Latin American Arbitration: The Story Behind the Headlines* <[www.ibanet.org/Article/Detail.aspx?ArticleUid=78296258-3B37-4608-A5EE-3C92D5DoB979](http://www.ibanet.org/Article/Detail.aspx?ArticleUid=78296258-3B37-4608-A5EE-3C92D5DoB979)> (10 December 2013).

Romania attempted to withdraw from the Swedish-Romanian BIT, only to be subjected to a 2008 ISA award that purported to bind it “irrevocably” to arbitration under that BIT.<sup>15</sup>

Other states, rather than reject ISA entirely, have qualified how it applies to them.<sup>16</sup> This was particularly common during the first generation of BITs in which states reserved extensive regulatory powers and accorded limited protections to foreign investors. For example, while China acceded to the ICSID Convention and provided for investor protections in its first and second Model BITs, it often failed to incorporate those protections in its negotiated BITs.<sup>17</sup> In particular, China has traditionally declined to grant ISA tribunals the jurisdiction to determine whether an expropriation has occurred, restricting ISA to determining the nature and extent of compensation. In addition, China often has declined to provide foreign investors with protection in accordance with the “national treatment” standard. China also has stipulated that foreign investors had to have resort to domestic administrative review before referring their cases to ISA and imposed a waiting period of three to nine months in order to provide parties with the opportunity to reach a settlement. Only after having

15 See *Micula v. Republic of Romania*, ICSID Case No. ARB/05/20, Decision on Jurisdiction, 24 September 2008, paras. 28–32. The investor claim against Romania was brought under the Sweden–Romania BIT. It dealt with the cancellation and withdrawal of a favourable customs and tax regime by Romania relating to a food production enterprise. See further Jurisnet, *Ioan Micula, Viorel Micula, S.C. European Food S.A, S.C. Starmill S.R.L. and S.C. Multipack S.R.L. v. Romania, ICSID Case No. ARB/05/20 (Sweden/Romania BIT), Decision on Jurisdiction and Admissibility* (2011) ArbitrationLaw.com <arbitrationlaw.com/library/ioan-micula-viorel-micula-sc-european-food-sa-sc-starmill-srl-and-sc-multipack-srl-v> (14 December 2013).

16 On the EU’s proposal to restrict investment treaties being concluded by individual EU members see European Commission, *Proposal for a Regulation of the European Parliament and of the Council: Establishing a Framework for Managing Financial Responsibility Linked to Investor-State Dispute Settlement Tribunals Established by International Agreements to which the European Union is Party* <trade.ec.europa.eu/doclib/docs/2012/june/tradoc\_149567.pdf> (10 December 2013). See also Nathalie Bernasconi-Osterwalder, *Analysis of the European Commission’s Draft Text on Investor-State Dispute Settlement for EU Agreements* <www.iisd.org/itn/2012/07/19/analysis-of-the-european-commissions-draft-text-on-investor-state-dispute-settlement-for-eu-agreements/> (10 December 2013).

17 See International Centre for Settlement of Investment Disputes, *ICSID Convention, Regulations and Rules*, pp. 95–96 <icsid.worldbank.org/ICSID/StaticFiles/basicdoc/CRR\_English-final.pdf> (10 December 2013). On the recognition and enforcement of international commercial arbitration awards see Margrete Stevens, ‘The ICSID Convention and the Origins of Investment Treaty Arbitration’ in A. van den Berg (ed.), *50 Years of the New York Convention* (Kluwer Law International 2009) 69.

exhausted local remedies and these waiting periods could foreign investors initiate ISA proceedings against China under its early BITs.<sup>18</sup>

While China has liberalized its BITs significantly in recent years, other states with liberalized BITs have begun to restrict investor protections in their BITs and expand on state defences. For example, the US Model BIT has extended the scope of a state's right to engage in regulatory activities.<sup>19</sup> It has restricted the rights of foreign investors under standards of "fair and equitable treatment", "minimum standard of justice" and "national treatment" and provided for a subjective national security test by which state parties to BITs are free to define their own national interests, as distinct from being accountable to objective criteria.<sup>20</sup> In addition, the US Model BIT reserves the rights of state parties to impose governmental measures to protect public health, environmental safety and related public interests.<sup>21</sup>

18 On China's evolving BIT policies see Leon E. Trakman, 'China and Foreign Direct Investment' (2013) (1)2 *CJCL* 1093; Leon E. Trakman, *China and Foreign Direct Investment: Looking Ahead* <papers.ssrn.com/sol3/papers.cfm?abstract\_id=2244634> (2 April 2013); Yang Shu-Dong, 'Investor Arbitration and China: Investor or Host State?' (2011) 2 *Opinio Juris in Comparatione* Paper No. 6, 1 <papers.ssrn.com/sol3/papers.cfm?abstract\_id=1973744> (10 December 2013).

19 Office of the United States Trade Representative, *The United States Model Bilateral Investment Treaty* (2012) <www.state.gov/documents/organization/188371.pdf> (10 December 2013). See also Kenneth J. Vandavelde, 'Model Bilateral Investment Treaties: The Way Forward' (2011) 18 *Sw. J. L. & Trade Americas* 307. Contrast U.S. Department of State, *American Model Bilateral Investment Treaty* (2004) <www.state.gov/documents/organization/117601.pdf> (10 December 2013). On Canada's Model Investment Treaty see Andrew Newcombe, *Canada's New Model Foreign Investment Protection Agreement* (August 2004) <ita.law.uvic.ca/documents/CanadianFIPA.pdf> (10 December 2013).

20 See Article 6 (expropriation and compensation); Article 3 (national treatment); Article 4 (most-favored-nation-treatment) and Article 5 (minimum standards of treatment) in *The United States Model Bilateral Investment Treaty* (2012). On the 'self-judging' nature of 'national security' under the 2012 US Model BIT, in contradistinction to the 2004 US Model BIT see Lise Johnson, 'The 2012 US Model BIT: and What the Changes (or Lack Thereof) Suggest for Future Bilateral Investment Treaties' (2012) VIII-2 *Political Risk Insurance Newsletter* 1-4 <www.vcc.columbia.edu/files/vale/content/Political\_Risk\_Insurance\_Newsletter\_-\_The\_2012\_US\_Model\_BIT\_-\_Nov\_2012.pdf> (10 December 2013).

21 It should be noted that even before the US adopted its 2012 Model BIT, it has begun to limit the scope of ISA in its FTAs. For example, the 2009 US-Peru Free Trade Agreement subjected foreign investors to significant regulation by the host state. See *Peru Trade Promotion Agreement*, US-Peru, signed 12 April 2006 (entered into force 1 Feb 2009) art 10.21; *Free Trade Agreement*, US-Colombia, signed 22 November 2006 (entered into force 15 May 2012) art 10.21; *Free Trade Agreement*, Korea-US, signed 30 June 2007 (approved by Congress, 12 October 2011) art 11.21.



There has nevertheless been some concern that ongoing ISA proceedings can have a negative impact on the willingness of states to engage in public interest legislation. The concern is that the threat of an ISA claim by a foreign investor can discourage states from engaging in public interest regulation, in effect producing a “regulatory chill” on public interest action by states.<sup>22</sup> ISA has also fallen out of favour in Latin America in particular as Governments there have emphasized national self-reliance over foreign investment protections. A more pervasive concern among some developing countries, beyond Latin America, is that ISA awards favour investors from developed states over developing countries and that various ISA conventions such as the ICSID will perpetuate those disadvantages.<sup>23</sup>

Notwithstanding these criticisms, state parties to international conventions on investment arbitration, such as the ICSID, have not withdrawn from such conventions *en masse*. The vast majority of the more than 3,000 BITs negotiated to date provides for ISA, with a dramatic increase in the inclusion of ISA provisions until several years ago.<sup>24</sup> Developed countries in general have provided for ISA in their BITs and FTAs (with the noticeable exception of the Australia–United States FTA, which refers investor-state disputes to domestic courts).<sup>25</sup>

22 See Kyla Tienhaara, ‘Regulatory Chill and the Threat of Arbitration: A View from Political Science’ in C. and K. Miles (eds.), *Evolution in Investment Treaty Law and Arbitration* (CUP 2012) 606–628.

23 These concerns are not entirely novel. They were reflected in the Calvo Doctrine enunciated decades ago by the Argentine Republic. That doctrine stipulated that domestic authorities, not limited to local courts, should resolve disputes, including matters arising over FDI that had previously been submitted to international tribunals. See generally Wenhua Shan, ‘From “North-South Divide” to “Private-Public Debate”: Revival of the Calvo Doctrine and the Changing Landscape in International Investment Law’ (2007) 27 *Nw.J. Int’l L. & Bus.* 631; Bernardo Cremades, ‘Resurgence of the Calvo Doctrine in Latin America’ (2006) 7 *Business L. Int’l* 53.

24 On the UNCTAD’s “country specific list of bilateral investment treaties”, including links to each treaty see UNCTAD, *Country-Specific Lists of Bilateral Investment Treaties* <[unctad.org/en/Pages/DIAE/International%20Investment%20Agreements%20%28IIA%29/Country-specific-Lists-of-BITs.aspx](http://unctad.org/en/Pages/DIAE/International%20Investment%20Agreements%20%28IIA%29/Country-specific-Lists-of-BITs.aspx)> (10 December 2013).

25 That Treaty provided for investors of either partner state to have access to the domestic courts of the other, based on the rationale that the courts in both countries adhered to a “rule of law” tradition. See also Leon E. Trakman, *Foreign Direct Investment: An Australian Perspective* (2010) 13 *Int’l Trade & Business L. Rev.* 31, 79–81; Peter Drahos and David Henry, ‘The Free Trade Agreement between Australia and the United States’ (2004) *Brit. Med. J.* 1271; See generally William S. Dodge, ‘Investor-State Dispute Settlement between Developed Countries: Reflections on the Australia-United States Free Trade Agreement’

China also serves as a useful illustration of ISA's sustainability in an evolving FDI marketplace. As a developing country, China was initially cautious about adopting ISA and sought to limit recourse to it in relation to inbound investments into China. However, in recent years China has expanded the scope of ISA consistent with its growth as an outbound investment originating state. The expanded scope of ISA is evident, most recently, in its bilateral agreement with Canada and its trilateral agreement with Japan and Korea.<sup>26</sup> Consistent with its role as a growing capital exporter, China has extended investor protections in its BITs and FTAs in order to protect its rising number of outbound investors from the regulatory defences of host states<sup>27</sup>

As a result, notwithstanding the perceived limitations of ISA, ISA remains the preferred mechanism for resolving FDI related disputes, and Australia is the only developed country to completely reject ISA in its future BRTAs. The question thus arises: why, given the endorsement of ISA in the vast majority of existing BITs, has Australia chosen to reject it?

## 2 The Significance of Australia's 2011 Policy Statement

In its Trade Policy Statement released in April 2011, the then Gillard Government declared that Australia will no longer agree to the adoption of international investment arbitration in its bilateral and regional trade agreements.<sup>28</sup> Specifically, the Policy Statement provides that Australia will no longer negotiate treaty protections "that confer greater legal rights on foreign businesses than those available to domestic businesses" or rights that would "constrain the ability of the Australian Government to make laws on social, environmental

(2006) 39 *Vand. J. Transnat'l L.* 1 (commenting on the exhaustion of local remedies); Thomas Westcott, *Foreign Investment Issues in the Australia-United States Free Trade Agreement* <archive.treasury.gov.au/documents/958/PDF/06\_Foreign\_investment\_policy\_AUSFTA.pdf> (10 December 2013).

26 China has over 130 BITs, becoming the state with the second largest number of BITs signed, after Germany that has signed the most BITs. For an overview of China's BITs see generally China FTA Network, *FTA News Release* <fta.mofcom.gov.cn/english/index.shtml> (10 December 2013).

27 On China's shifting position in regard to investment arbitration see generally Nils Eliasson, 'China's Investment Treaties: A Procedural Perspective' in V. Bath and L. Nottage (eds.), *Foreign Investment and Dispute Resolution Law and Practice in Asia* (Routledge 2011) 90–111; Leon E. Trakman, 'China and Investor-State Arbitration' in W. Shan and Q. Liu (eds.), *China, Trade and Investment* (CUP 2014) (forthcoming).

28 See Policy, *supra* note 1, p. 1.

and economic matters in circumstances where those laws do not discriminate between domestic and foreign businesses.”<sup>29</sup>

The Australian Policy Statement did not challenge the ICSID as a creature of the World Bank and as a supplicant of the United States, unlike Ecuador, Bolivia and Venezuela.<sup>30</sup> For Australia, the central consideration was to impede foreign investors from invoking ISA to challenge Australian sovereignty over public safety, health and the environment.<sup>31</sup> Such concerns have merit. The fact that Australia is a resource rich country sets the stage for foreign investors to invoke ISA to challenge public policy laws and regulations directed at containing environmental damage in the mining, oil and gas industries, in which foreign entities are often significant investors.<sup>32</sup> By declining to incorporate ISA in its BRTAs, Australia would have greater latitude in designing sustainable measures to preserve its public interests. It would also be better able to avoid succumbing to the “regulatory chill” arising from having to defend itself against costly and intrusive ISA claims.<sup>33</sup>

These concerns are illustrated in part by Philip Morris’s ISA claim against Australia under the Hong Kong-Australia BIT over Australia’s decision to

29 *Ibid.*, pp. 1–2.

30 See Leon E. Trakman, ‘The ICSID in Perspective’ in Trakman and Ranieri (eds.), *supra* note 2 p. 253 (discussing these withdrawals from the ICSID); Markus Burgstaller and Charles B. Rosenberg, ‘Challenging International Arbitral Awards: To ICSID or not to ICSID?’ (2011) 27 *Arb. Int.* 91; R. Zachary Torres-Fowler, ‘Undermining ICSID: How The Global Antibribery Regime Impairs Investor-State Arbitration’ (2012) 52:4 *Va. J. Int’l L.* 995; Antonios Tzanakopoulos, ‘Denunciation of the ICSID Convention under the General International Law of Treaties’ in R. Hofmann and C.J. Tams (eds.), *International Investment Law and General International Law: From Clinical Isolation to Systematic Integration?* (Nomos Publishing 2011) 75; Waibel et al. (eds.), *supra* note 9; Tor Krevier, ‘The Legal Turn in Late Development Theory: The Rule of Law and the World Bank’s Development Model’ (2011) 52 *Harv. Int’l L. J.* 287; Ignacio A. Vincentelli, ‘The Uncertain Future of ICSID in Latin America’ (2010) 16 *Law & Bus. Rev. Am.* 409; United Nations Conference on Trade and Development (UNCTAD), *Denunciation of the ICSID Convention and BITS: Impact on Investor-State Claims* <[unctad.org/en/Docs/webdiaeia20106\\_en.pdf](http://unctad.org/en/Docs/webdiaeia20106_en.pdf)> (10 December 2013); Appleton, *supra* note 14. See also ICSID, *Venezuela Submits a Notice under Article 71 of the ICSID Convention, Washington DC* <[icsid.worldbank.org/ICSID/Servlet?requestType=CasesRH&actionVal=OpenPage&PageType=AnnouncementsFrame&FromPage=Announcements&pageName=Announcement100](http://icsid.worldbank.org/ICSID/Servlet?requestType=CasesRH&actionVal=OpenPage&PageType=AnnouncementsFrame&FromPage=Announcements&pageName=Announcement100)> (10 December 2013).

31 See Luke Nottage, ‘Investor-State Arbitration Policy and Practice after *Philip Morris Asia v. Australia*’ in Trakman and Ranieri (eds.), *supra* note 2, p. 452.

32 Tienhaara, *supra* note 22, pp. 606–628.

33 *Ibid.*

require the plain packaging of cigarettes on public health grounds<sup>34</sup> and Ukraine's more recent WTO challenge against Australia over this same issue.<sup>35</sup> Australia's related concern is that foreign drug companies could invoke ISA to contest restrictions on foreign manufactured drugs under Australia's Pharmaceutical Benefits Scheme (PBS), which selectively restricts public access to some pharmaceuticals while subsidizing others.<sup>36</sup> Finally, the Government also has ongoing concerns about foreign investors securing a controlling interest in the Australian media and in core financial markets such as the stock exchange.<sup>37</sup>

The Gillard Government's announcement implies that domestic courts and not investment tribunals are the appropriate bodies to resolve investment disputes between host states and foreign investors. However, the Policy Statement does not explicitly identify domestic courts as *the* alternative to ISA.<sup>38</sup>

- 34 See generally Nottage, *supra* note 312, p. 452; Andrew D. Mitchell and Sebastian M. Wurzberger, 'Boxed in? Australia's Plain Tobacco Packaging Initiative and International Investment Law' (2011) 27 *Arb. Int.* 623; Tania Voon and Andrew Mitchell, 'Implications of WTO Law for Plain Packaging of Tobacco Products' in A. Mitchell, T. Voon and J. Liberman (eds.), *Public Health and Plain Packaging of Cigarettes: Legal Issues* (Edward Elgar 2012) 109 On Philip Morris: ongoing action against Australia under the Australia-Hong Kong Free Trade Agreement see Phillip Morris International, *News Release: Philip Morris Asia Initiates Legal Action Against the Australian Government Over Plain Packaging* <[www.pmi.com/eng/media\\_center/press\\_releases/pages/PM\\_Asia\\_plain\\_packaging.aspx](http://www.pmi.com/eng/media_center/press_releases/pages/PM_Asia_plain_packaging.aspx)> (10 December 2013); On Philip Morris: unsuccessful litigation against the Prime Minister of Australia see *Philip Morris Limited v. Prime Minister* [2011] AATA 556; On the earlier claim brought against the Republic of Uruguay under the Switzerland-Uruguay BIT see *FTR Holdings S.A. (Switzerland) v. Oriental Republic of Uruguay*, ICSID Case No. ARB/10/7, Request for Arbitration, 19 February 2010 <[smoke-free.ca/eng\\_home/2010/PMIvsUruguay/PMI-Uruguay%20complaint0001.pdf](http://smoke-free.ca/eng_home/2010/PMIvsUruguay/PMI-Uruguay%20complaint0001.pdf)> (10 December 2013) FTR Holding S.A. is a subsidiary of Philip Morris International Inc (PMI). PMI's Operation's Centre is in Switzerland.
- 35 See Dispute Settlement DS434, *Australia — Certain Measures Concerning Trademarks and Other Plain Packaging Requirements Applicable to Tobacco Products and Packaging* <[www.wto.org/english/tratop\\_e/dispu\\_e/cases\\_e/ds434\\_e.htm](http://www.wto.org/english/tratop_e/dispu_e/cases_e/ds434_e.htm)> (10 December 2013). See generally Tania Voon and Andrew Mitchell, 'TDM Special Issue on Legal Issues in Tobacco Control' (2012) 5 *TDM*.
- 36 On the PBS see Australian Government: Department of Health and Ageing, *Pharmaceutical Benefits Scheme: PBS News Updates* [www.pbs.gov.au/](http://www.pbs.gov.au/) (11 December 2013).
- 37 See Leon E. Trakman, 'National Good No Issue in ASX Deal', *The Australian*, 2 November 2010 <[www.theaustralian.com.au/business/national-good-no-issue-in-asx-deal/story-e6frg8zx-1225946362212](http://www.theaustralian.com.au/business/national-good-no-issue-in-asx-deal/story-e6frg8zx-1225946362212)> (10 December 2013).
- 38 See Trakman, *supra* note 30, pp. 48–53; Westcott, *supra* note 25; Leon E. Trakman, 'Australia and the Future of Investor-State Arbitration' in M. Legg (ed.), *The Future of Dispute Resolution* (Lexis/Nexis 2012) 228–239.

Nor does it dismiss alternative dispute prevention and avoidance measures to resolve investor-state disputes, such as negotiation and conciliation. Indeed, it is arguable that the Policy statement may encourage investor-state parties to negotiate contracts in which they provide for their own preferred dispute resolution mechanisms, as this would provide greater certainty than relying upon BITs that include dispute avoidance and conciliation measures but do not provide for ISA.

There are economic reasons which justify a policy of incentivizing outbound Australian investors to conclude investment contracts with their host countries. Firstly, Australia is a net capital importer in which capital inflows are largely directed at the extraction of resources. Secondly, the companies in those resource sectors possess sufficient bargaining power to protect their interests without having to rely on dedicated investor guarantees in treaties between Australia and a host state. In asserting that the duty should fall upon outbound investors to protect their own economic interests when investing abroad, the Government's 2011 Policy Statement explicitly states: "if Australian businesses are concerned about sovereign risk in Australian trading partner countries, they will need to make their own assessments about whether to commit to investing in those countries."<sup>39</sup> This suggests that the Government intended for large scale investors in particular, such as in the resource extraction industry, to negotiate investor-state contracts that address the risks of conflict with host states rather than rely upon either diplomatic intervention by Australia or investor protections in BITs.

Notably, however, it is precisely the large scale outbound investors who are most likely to secure the diplomatic assistance of the Australian Government in order to protect their investments abroad. The problem is thus that the Australian Policy may force outbound investors who lack both the political influence to secure diplomatic intervention from the Australian Government and the bargaining power to negotiate investor-state contracts to rely on foreign domestic courts in which those investors lack confidence. While reliance on domestic courts may not pose difficulties in countries with well-developed legal systems, the Policy Statement does not distinguish between countries that do and do not subscribe to "rule of law" traditions as Australia conceives of them. Rather, the Statement adopts an all-encompassing position. In effect, Australia's position against ISA applies to all future BITs and FTAs that it may negotiate, regardless of the size or capacity of its outbound investors, regardless of the destination of their investments, and

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<sup>39</sup> *Ibid.*

without differentiating between so called “rule of law” host states and other jurisdictions.<sup>40</sup>

Whether or not the Policy Statement against ISA, if preserved, will apply even-handedly to all outbound investors, the Policy nevertheless has some economic support. In formulating it, the Gillard Government relied significantly on a 2010 report issued by the Australian Productivity Commission (APC), a public commission charged by the Federal Treasurer with the specific task of advising on future trade policy directions. The APC attributed significant costs and limited benefits to including ISA in its BRTAs.<sup>41</sup> It contended that “current processes for assessing and prioritising BRTAs lack transparency and tend to oversell the likely benefits.”<sup>42</sup> The Report added tersely: “At a minimum, the economic value of Australia’s preferential BRTAs has been over-sold.”<sup>43</sup> As a result, the APC recommended that Australia should cease using ISA to resolve disputes in its BRTAs.

There is also anecdotal support for the Australian Policy. A group of influential judges, lawyers and academics from predominantly British Commonwealth jurisdictions have publicly declared their support for Australia’s Policy Statement in challenging the proposed investment chapter of the Transpacific Partnership Agreement that provides for ISA.<sup>44</sup> In particular, they objected to the MFN provision that would enable investors “to avoid the deliberate decision of [TPPA negotiating Governments] that require investors to pursue remedies in the domestic courts of the host nation...” They expressed dissatisfaction with the rotating roles of arbitrators and advocates “in a manner that would be unethical for judges”. They argued, further, that the exclusion of “non-investor litigants and other affected parties” from participating in ISA proceedings was contrary to basic principles of “transparency, consistency and due process”.<sup>45</sup>

Perhaps in part due to this support, and irrespective of whether the 2011 Trade Policy Statement proves to be an effective means of resolving

40 On Australia’s Policy Statement generally see Trakman, *supra* note 6. See also Leon E. Trakman, ‘Foreign Direct Investment: An Australian Perspective’ (2010) 13 *International Trade & Business Law Review* 31, 48–53.

41 See Australian Productivity Commission, *Bilateral and Regional Trade Agreements: Final Report*, pp. 1, 271–272 <[www.pc.gov.au/projects/study/trade-agreements](http://www.pc.gov.au/projects/study/trade-agreements)> (10 December 2013).

42 Australian Productivity Commission, *Research Report*, p. xiv (on file with author).

43 *Ibid.*, p. xxii.

44 See TPP Legal, *An Open Letter from Lawyers to the Negotiators of the Trans-Pacific Partnership Urging the Rejection of Investor-State Dispute Settlement*, 8 May 2012. <[tpplegal.wordpress.com/open-letter/](http://tpplegal.wordpress.com/open-letter/)> (10 December 2013).

45 *Ibid.*

investor-state disputes globally or a toothless tiger, the Australian Government demonstrated a serious intention to implement it. This is evidenced by the absence of ISA in Australia's FTA with Malaysia, concluded in May 2012, and in the more recent amendment to the investment protocol in the Australia-New Zealand Closer Economic Trade Relations Agreement.<sup>46</sup>

Equally importantly, despite the controversial nature of the proposed Policy, the Liberal Government that replaced the Labour Government in 2013 appears willing to vary from the Policy Statement only on a case-by-case basis, such as in its Free Trade Agreement with South Korea concluded on 5 December 2013, while still preserving that Policy on economic and political grounds.

### 3 Dispute Resolution Options in the Absence of ISA

Given that domestic litigation is not the only alternative to ISA, the first step in analysing the consequences of Australia's rejection of ISA is to examine alternative dispute resolution mechanisms by which Australia and its inbound and outbound investors can avoid or resolve disputes with host states.

As one option, Australia may negotiate for resort to diplomatic channels to resolve investor-state disputes. In effect, foreign investors would request diplomatic assistance from their home states in resolving investor-state disputes with host states. As was noted in Part 1 of this paper, interstate diplomacy is not a novel method of resolving investment disputes and was commonly utilized in decades past.<sup>47</sup> However, this method of dispute resolution is far less sustainable today, given that governments are increasingly reluctant to so intervene. In light of the growing number and size of inbound and outbound investments, state intervention is likely to be cost prohibitive. Home states are likely to avoid intervening in investor-state disputes in order not to damage their relations with host states. In addition, states may make a cost benefit analysis in which they implicitly acknowledge the cost to small and medium sized foreign investors who may lack the economic and political leverage of more powerful outbound investors who can mobilise their home states to intervene on their behalf.

As a further alternative, investor-state parties could be required to initiate formal negotiations and conciliation as a precondition to a foreign investor initiating a domestic court case. The problem is that such negotiations often

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46 For the full text of the ANZCERTA see <[www.dfat.gov.au/fta/anzcerta/](http://www.dfat.gov.au/fta/anzcerta/)> (10 December 2013).

47 See Nottage and Weeramantry, *supra* note 5, p. 19.

serve as little more than mandatory waiting periods: they delay investors from filing ISA claims rather than serve as effective means of resolving an investor-state dispute. Such measures may also compound the cost and delay the process by which investor-state disputes are ultimately resolved by domestic courts or by ISA tribunals.

Yet another alternative is for Australia to rely on individual private investors to enter into contracts with foreign states, providing for international commercial arbitration as distinct from investor-state arbitration. The parties could adopt this option in an investor-state agreement, conceivably reinforced by an umbrella clause in a BIT or FTA. While this approach gives Australia maximum flexibility in managing its relations with foreign investors, it has two major limitations. First, investor-state contracts may be one-sided, favouring the host state, or alternatively, a powerful investor. This is especially likely when small and middle-sized investors from developing home states proceed against developed states, and when developing states defend against claims from better resourced foreign investors. Second, insofar as such investor-state contracts include choice of jurisdiction and choice of law clauses, these clauses are likely to refer disputes to domestic legal systems and their courts for resolution. The result may be resort to the domestic courts and laws of the host state if the dominant contracting party is the host state, or to the courts and laws of the investor's home state or a third-party state if the foreign investor is the dominant party. In addition, while most states are signatories to the 1958 New York Convention on the Recognition and Enforcement of Foreign Judgements, it is often difficult to enforce arbitration awards against determined and recalcitrant host states or state owned entities.

In summary, options such as diplomatic intervention and investor-state contracts remain available to foreign investors. However, they are often difficult for investors to access and utilize. Furthermore, investors may not have sufficient knowledge and financial resources to evaluate their legal options in resolving disputes with host states. They may resort to dispute avoidance measures such as negotiation and conciliation, but only if they have the economic and political capacity to influence a host state. The upshot is that, in the absence of ISA, foreign investors are most likely to rely on domestic litigation to resolve disputes with their host states.

#### 4 Balancing Domestic Courts Against ISA

An important question relates to whether domestic courts are more appropriate institutions to hear investment disputes than allegedly specialized ISA



tribunals appointed under the ICSID Convention or guided by the UNCITRAL Rules. This question is dealt with in the sub-sections below.

#### 4.1 *In Defence of Domestic Courts*

A perceived benefit of designating domestic courts to decide investor-state disputes is that they have a better understanding of domestic law, including important public policy considerations, than ISA tribunals. Domestic proceedings are ordinarily open to the public; domestic courts often provide for third-party submissions on public interest matters; and verdicts in some domestic courts are reached by juries. Domestic judicial systems are also often touted as being independent arms of government in a constitutional democracy, with authority to decide cases free of legislative and executive intervention. In support of domestic courts as democratic institutions, judgments are usually published and freely available to ordinary citizens, and losing parties usually have the right to appeal a decision to a higher court. As a result, well-respected domestic courts are viewed as being able to reach decisions impartially between foreign investors and the domestic state, to take account of the legitimate interests of both litigants, and to consider dispassionately important public policy considerations and investor protections that are in issue.

When the quality of justice is measured against these criteria, ISA may appear to be deficient. ISA proceedings are generally confidential; third-party interventions in ISA proceedings are often restricted; and awards are sometimes either unpublished or published in part only.<sup>48</sup> While ISA parties often agree to open ISA proceedings in whole or in part to the public, such decisions require the explicit consent of both sides. This consent is sometimes difficult to secure from investors who object to open hearings and published awards because they fear the disclosure of issues that are commercially confidential. States, in turn, may wish to avoid publicity over sensitive public policy issues. ISA may also lead to unduly broad liability findings and excessive damages awards in favour of foreign investors at the expense of host states. In addition, commercially trained international arbitrators may be more receptive to investor claims than to host state defences based on national security, environmental protection and public health.<sup>49</sup>

48 See Trakman, 'The ICSID in Perspective' in Trakman and Ranieri (eds.), *supra* note 2, p. 253.

49 In response to these concerns, some scholars have contemplated the possibility of some form of appellate review of ISA awards. See e.g., Jack J. Coe Jr, 'Domestic Court Control of Investment Awards: Necessary Evil or Achilles Heel within NAFTA and the Proposed FTAA' (2002) 19 *J. Int'l Arb.* 185; David A. Gantz, 'An Appellate Mechanism for Review of Arbitral Decisions in Investor-State Disputes: Prospects and Challenges' (2006) 39 *Vand. J.*

One implication of these criticisms of ISA is that it may potentially produce a regulatory “chill,” causing states to forego passing public interest legislation for fear of being subject to an ISA challenge.<sup>50</sup> This concern is reinforced by the fact that grounds for annulling an ISA award, such as under the ICSID Convention, are limited to serious procedural deficiencies and challenges to the impartiality of arbitrators, e.g. on grounds of conflicts of interest. Given the narrowness of these grounds for annulment,<sup>51</sup> few ISA decisions are set aside in fact.

#### 4.2 *The Case for ISA*

While concerns with ISA are justifiable, it is important to emphasize that many of these criticisms can apply equally to domestic legal systems. For example, it is true that ISA proceedings are often resource intensive, leading to significant awards in favour of foreign investors and against host states, particularly developing states. However, litigation in domestic courts may also be costly, delivering devastating blows to foreign investors. This was well illustrated by the *Loewen* case, in which a Canadian investor was forced into bankruptcy as a result of an outlandish punitive damages award issued by a jury in a domestic US court with which an ISA tribunal declined to interfere on grounds that it lacked jurisdiction.<sup>52</sup>

Similarly, even though ISA awards are not subject to challenge on the merits, ISA annulment proceedings are not necessarily under-inclusive solely because they are limited to procedural matters. Asserting that appeals from domestic courts are wider in scope than annulment proceedings also ignores the extent to which domestic judicial systems diverge over the availability of and grounds for an appeal and also over the success rate of appellants on the merits.

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*Transnat'l L.* 39; *But see* William S. Dodge, ‘Case Report: Waste Management, Inc v Mexico’ (2001) 95 *Am. J. Int'l L.* 186 (presenting the case for modelling Chapter 11 on the WTO appellate process); *See also* Gary R. Saxonhouse, ‘Dispute Settlement at the WTO and the Dole Commission: USTR Resources and Success’ in R.M. Stern (ed.), *Issues and Options for U.S.-Japan Trade Policies* (University of Michigan Press 2002) 363.

50 *See, e.g.*, Tienhaara, *supra* note 22, p. 606.

51 *See* Bernardo M. Cremades Román, B. Cremades y Asociados, *The Use of Preliminary Objections in ICSID Annulment Proceedings* <[kluwerarbitrationblog.com/blog/2013/09/04/the-use-of-preliminary-objections-in-icsid-annulment-proceedings-2/](http://kluwerarbitrationblog.com/blog/2013/09/04/the-use-of-preliminary-objections-in-icsid-annulment-proceedings-2/)> (10 December 2013).

52 On the *Loewen* case *see* Charles Brower and Lee Steven, ‘NAFTA Chapter 11: Who then should Judge? Developing the International Rule of Law under NAFTA Chapter 11’ (2001) 2 *Chi. J. Int'l L.* 193, 193–195.

In addition, the criticism that ISA tribunals diverge in applying standards of treatment, such as “fair and equitable” treatment to foreign investors, ignores the extent to which domestic courts apply diverse domestic rules of evidence and procedure to resolve disputes, including against states.<sup>53</sup> Domestic courts also domesticate conceptions of public policy differently from state to state.<sup>54</sup>

Beyond these criticisms and responses, it is disputable whether ISA is inherently incompatible with rule of law-based adjudicatory ideals such as transparency and openness. Moreover, there are structural and functional benefits of ISA over domestic courts, making it a more appropriate forum for the resolution of investor-state disputes. For example, while a small number of ISA arbitrators are repeatedly appointed from a list of panellists nominated by member states, it is difficult to conclude that domestic judges appointed by nation states invariably act independently from those states.<sup>55</sup> ISA arbitrators who are appointed because of their investment law expertise are ordinarily more experienced than domestic court judges, who lack such specialized experience. In addition, awards reached by arbitrators who are chosen by the parties, including by the foreign investor, arguably act with the consent of both investors and their host states – as distinct from domestic judges, who are appointed (or sometimes elected) solely by domestic actors within the host state.

It is true that investor-state parties can often make a choice of law before a domestic court, including the choice of another legal system or of international investment law. However, the choice by investors of diverse domestic laws may impede the resolution of FDI disputes. In contrast, customary international law is likely to provide ISA tribunals with more consistent principles, standards and rules than the laws of a plethora of domestic legal systems.<sup>56</sup> Even though domestic courts may sometimes apply international law to an

53 For a debate on this issue see Leon E. Trakman and M. Sornarajah, ‘A Polemic: The Case For and Against Investment Liberalization’ in Trakman and Ranieri (eds.), *supra* note 2, Appendix p. 499.

54 On such issues see generally Foreign Investment Review Board, *Current International Investment Issues - OECD Investment Committee* <[www.firb.gov.au/content/international\\_investment/current\\_issues.asp?NavID=60](http://www.firb.gov.au/content/international_investment/current_issues.asp?NavID=60)> (10 December 2013).

55 See Leon E. Trakman, ‘A Plural Account of the Transnational Law Merchant’ (2011) 2(3) *Transnational Legal Theory* 309, 335.

56 On this public-private tension see Alex Mills, ‘The Public-Private Dualities of International Investment Law and Arbitration’ in C. Brown and K. Miles (eds.), *Evolution in International Investment Treaty Law and Arbitration* (CUP 2011) 97; Catherine A. Rogers, ‘International Arbitration’s Public Realm’ in A.W. Rovine (ed.) *Contemporary Issues in International Arbitration and Mediation: The Fordham Papers* (Martius Nihoff Publishers 2010) 165.

investor-state dispute, ISA tribunals are likely to have a firmer grasp of principles of investment law and public international law.<sup>57</sup> They are also likely to produce a more uniform system of international investment laws and procedures than diverging domestic laws and procedures. In fact, over the thirty years of ICSID and UNCITRAL-governed proceedings, ISA jurisprudence has developed a sophisticated degree of coherence.<sup>58</sup> This is so notwithstanding the fact that ISA decisions are *ad hoc*, that they bind only the direct parties to the dispute, and that ISA tribunals sometimes do diverge amongst themselves in applying certain international investment law standards, such as in applying the state defence of “necessity”.<sup>59</sup>

ISA has also established institutional roots that are widely recognized by nation states. A majority of ISA cases are administered by established international institutions, such as the ISCID, to which the vast majority of states are signatory parties. As a result, the ICSID rules are derived from the collective action of those signatory states and are interpreted and applied by ISA tribunals appointed by the disputing investor-state parties. This subjects ISA tribunals to standardised institutional rules and international oversight, such as under the ICSID Convention and the UNCITRAL Rules.

In addition, ISA awards are ordinarily enforceable domestically. As a formal matter, states that are signatories to ISA conventions such as the ICSID

57 See *e.g.*, Susan Franck, ‘The Legitimacy Crisis in Investment Treaty Arbitration: Privatizing Public International Law through Inconsistent Decisions’ (2004–5) 73 *Fordham L. R.* 1521, 1543–44; Guillermo A. Alvarez and William W. Park, ‘The New Face of Investment Arbitration: NAFTA Chapter 11’ (2003) 28 *Yale J. Int’l L.* 365.

58 On the variability of international investment treaty law see Stephan W. Schill, *The Multilateralization of International Investment Law* (CUP 2009) 363; M. Sornarajah, ‘The Case Against an International Investment Regime’ in Trakman and Ranieri (eds.), *supra* note 2, p. 475.

59 On allegedly inconsistent ICSID decisions in a series of investment claims against Argentina, commencing with the *CMS, Enron* and *Sempra* cases see *CMS Gas Transmission Co v. The Argentine Republic*, ICSID Case No. ARB/01/8, Award, 12 May 2005; *Enron Creditors Recovery Corporation and Ponderosa Assets, L.P. v. Argentine Republic*, ICSID Case No. ARB/01/3, Award, 22 May 2007; *Sempra Energy International v. The Argentine Republic*, ICSID Case No. ARB/02/16, Award, 28 September 2007. See further August Reinisch, ‘Necessity in International Investment Arbitration – An Unnecessary Split of Opinions in Recent ICSID Cases? Comments on *CMS v. Argentina* and *LG&E v. Argentina*’ (2007) 8 *JWIT* 191; Stephan W. Schill, ‘International Investment Law and the Host State’s Power to Handle Economic Crises: Comment on the ICSID Decision in *LG&E v. Argentina*’ (2007) 24 *J. Int’l Arb.* 265; Michael Waibel, ‘Two Worlds of Necessity in ICSID Arbitration: *CMS* and *LG&E*’ (2007) 20 *Leiden J. Int’l L.* 637. See Clint Peinhardt and Todd Allee, ‘Devil in the Details? The Investment Effects of Dispute Settlement Variation in BITS’ in K. Sauvart (ed.), *Yearbook on International Investment Law & Policy 2010–2011* (OUP 2011) 833–854.

Convention are required to enforce ISA awards in accordance with their undertakings as signatory states.<sup>60</sup> In contrast, the decisions of domestic judges are comparatively more difficult to enforce in foreign jurisdictions than ISA awards, given the limited endorsement of the Hague Convention on the Recognition and Enforcement of Foreign Judgements and the Draft Hague Principles on Choice of Law,<sup>61</sup> as compared with the plethora of state signatories to the ICSID Convention.<sup>62</sup>

None of this is to assert that institutional rules embodied in Conventions such as the ICSID are invariably even-handed in their treatment of signatory states and their investors. Many states became signatories to the ICSID long after its rules were devised. However, given the growing number of developing state signatories to the ICSID and the availability of alternative institutional rules such as those promulgated by the UNCITRAL, an institution like the ICSID is strongly motivated to demonstrate the transparency and effectiveness of its rules and procedures to its membership at large.

While the ICSID rules have proven remarkably well-suited to the resolution of investor-state disputes, concern over the perceived lack of transparency of some ISA proceedings remains controversial. The historical rationale for the confidentiality of ISA proceedings and awards was to protect the confidences of the investor-state parties. Closed ISA hearings, the denial of interpleader status to third parties and unpublished awards avoided media coverage that was often associated with the publicised decisions of domestic courts of law. Nowadays, however, ISA proceedings are increasingly open to the public; intervenor status is sometimes granted to public interest organizations; and

60 See Kenneth Vandeveld, 'A Brief History of International Investment Agreements' (2005) 12 *UC Davis J. Int'l & Pol'y.* 157, 172. See also UNCTAD, *World Investment Report 2010*, xxv <[www.unctad.org/en/docs/wir2010\\_en.pdf](http://www.unctad.org/en/docs/wir2010_en.pdf)> (10 December 2013).

61 On the draft Hague Principles on Choice of Law see Hague Conference on Private International Law, *Draft Hague Principles on the Choice of Law in International Contracts* <[www.hcch.net/upload/wop/contracts2012principles\\_e.pdf](http://www.hcch.net/upload/wop/contracts2012principles_e.pdf)> (10 December 2013); See also *Hague Convention on the Recognition and Enforcement of Foreign Judgments in Civil and Commercial Matters* <[www.hcch.net/index\\_en.php?act=conventions.text&cid=78](http://www.hcch.net/index_en.php?act=conventions.text&cid=78)> (10 December 2013); See also Stevens, *supra* note 17, p. 69. On the list of state and other signatories of the ICSID Convention see ICSID, *List of Contracting States and Other Signatories of the Convention* <[icsid.worldbank.org/ICSID/FrontServlet?requestType=ICSIDDocRH&actionVal=Contractingstates&ReqFrom=Main](http://icsid.worldbank.org/ICSID/FrontServlet?requestType=ICSIDDocRH&actionVal=Contractingstates&ReqFrom=Main)> (10 December 2013); See also Hague Conference on Private International Law, *The Hague Convention of 30 June 2005 on Choice of Court Agreements* <[www.hcch.net/upload/conventions/txt37en.pdf](http://www.hcch.net/upload/conventions/txt37en.pdf)> (10 December 2013).

62 On the ICSID membership see ICISD <[icsid.worldbank.org/ICSID/FrontServlet?requestType=ICSIDDocRH&actionVal=Contractingstates&ReqFrom=Main](http://icsid.worldbank.org/ICSID/FrontServlet?requestType=ICSIDDocRH&actionVal=Contractingstates&ReqFrom=Main)> (10 December 2013).

ISA awards are published in whole or part. In issue is political sensitivity about the need for transparency, particularly among developing states, in taking account of domestic public policy. Consequently, there is now far greater public access to ISA proceedings and records than there was a decade ago.<sup>63</sup> For example, the ICSID now provides for third-party intervener status in ISA proceedings and for the publication of ISA awards.<sup>64</sup>

In addition, disputing parties increasingly issue statements on their ISA positions to the public, which institutional rules permit, provided these statements do not disclose information marked in proceedings as “confidential”. Those statements provide public information on contentious issues, including issues of national significance. Furthermore, these public releases encourage investor-state parties to agree to open ISA proceedings to the public, to admit public interest interventions and to allow the publication of awards, in order to offset the impact of public statements made by one disputing party in the absence of a public record. Thus, while ISA has a number of limitations, it is able to accommodate domestic public policy, not unlike investor-state litigation before domestic courts.

#### 4.3 *Converging Domestic and International Investment Laws*

Under a pure monist legal system, pre-existing differences among domestic and international investment laws are harmonized within a single system, obfuscating inconsistencies and contradictions among the two legal orders.<sup>65</sup> However idealized such a monist legal system may be, experience suggests that it is unlikely to eventuate in practice. The concept of state sovereignty is simply too resilient to succumb to a unifying international jurisprudence.

Nevertheless, the question remains whether certain practices associated with legal monism can help to avoid the dislocation caused by legal dualism, or pluralism, among legal systems regulating FDI.<sup>66</sup> It is difficult to answer this

63 See e.g., Aurélie Antonietti, ‘The 2006 Amendments of the ICSID Rules and Regulations and the Additional Facility Rules’ (2006) 21 *ICSID Rev.* 427; Edward Baldwin, Mark Kantor and Michael Nolan, ‘Limits to Enforcement of ICSID Awards’ (2006) 23 *J. Int’l Arb.* 1.

64 On this amendment to the ICSID Rules see Antonietti, *supra* note 63, p. 427. See also Statement by the OECD Investment Committee, *Transparency and Third-party Participation in Investor-State Dispute Settlement* <[www.oecd.org/daf/inv/investment-policy/34786913.pdf](http://www.oecd.org/daf/inv/investment-policy/34786913.pdf)> (10 December 2013).

65 For a comparative analysis of dualism and monism in international law see Brindusa Marian, ‘The Dualist and Monist Theories: International Law’s Comprehension of these Theories’ (2007) 28–29 *The Juridical Current Journal* <[revcurentjur.ro/arhiva/attachments\\_200712/recjurid071\\_22F.pdf](http://revcurentjur.ro/arhiva/attachments_200712/recjurid071_22F.pdf)> (10 December 2013).

66 On a dualist conception of international law see, e.g., Hans Kelsen, *Principles of International Law* (2<sup>nd</sup> ed., Holt Rinehart & Winston 1966) 551–552.

question in the abstract. What is apparent, however, is that if a blend of legal monism and dualism is left to evolve unchecked, the result is likely to be a patchwork quilt of marginally to substantially different legal systems,<sup>67</sup> or even an un-cohesive ‘spaghetti bowl’ of disparate domestic and international investment laws and procedures.<sup>68</sup> As a result, some priority is necessary between domestic and international investment law, as between ISA tribunals and domestic courts, in order to promote greater certainty and transparency in resolving investor-state disputes.

#### 4.4 *Finding a Balance Between ISA and Domestic Courts*

As this paper has argued, whether ISA is deemed more efficient or fairer than domestic litigation is likely to hinge on the normative values and risks that are ascribed to each. If normative priority is given to legal coherence, the risk of ISA tribunals and domestic courts adopting narrow literal methods of treaty interpretation in order to arrive at coherent results by coherent means applies to both. Similarly, both domestic courts and ISA tribunals may construe treaties liberally, while ascribing different purposes to those treaties. Domestic courts may highlight the need to protect domestic public policy values. Yet ISA tribunals may also prioritize state defences over investor claims, deciding in favour of the host state on national security, environmental protection, or public health grounds. Conversely, ISA tribunals may deny such state defences in order to protect the commercial interests of foreign investors. So, too, may domestic courts construe state defences restrictively in favour of foreign investors.

If normative priority is accorded to investment expertise, ISA arbitrators are likely to be perceived as having a greater comprehension of investment law than most domestic judges.<sup>69</sup> If emphasis is given to the transparency of legal procedures, ISA is likely to prevail over domestic courts in jurisdictions that

67 On the tension arising from this patchwork quilt of BITs and ISA awards, particularly in relation to developed and developing states and their investors see Leon E. Trakman and M. Sornarajah, ‘International or National Investment Law? A Polemic’ in Trakman and Ranieri (eds.), *supra* note 2, Appendix p. 499.

68 On “swimming in the spaghetti bowl” to describe the economic effect of multiple “free” trade agreements see Jagdish Bhagwati, *Free Trade Today* (Yale University Press 2002).

69 On the expertise of investor-state arbitrators, among various other factors in support of ISA see generally Christopher Dugan, Don Wallace Jr. and Noah Rubins, *Investor-State Arbitration* (OUP 2008); Peter Muchlinski, Federico Ortino and Christoph Schreuer (eds.), *Oxford Handbook of International Investment Law* (OUP 2008); Campbell McLachlan, Lawrence Shore and Matthew Weiniger, *International Investment Arbitration: Substantive Principles* (OUP 2008).

score low on corruption, transparency, and rule of law indices.<sup>70</sup> If priority is given to the binding force of precedent, as common lawyers conceive of it, a preference is likely to be expressed for ISA arbitrators who treat past ISA awards as binding or at least influential.<sup>71</sup>

The problem is that ISA tribunals may diverge over the priorities they accord to each of these values. They may prioritize the transparency of ISA proceedings disparately. They may diverge in the value they accord to legal precedent, or encompass it within a more pervasive *opinion juris*.

As a result, domestic courts and ISA tribunals may subscribe to similar or different normative preferences in response to comparable or dissimilar normative presuppositions. Even the presupposition that ISA tribunals are more likely to prioritise the commercial interests of foreign investors, while domestic courts are more likely to prioritise the public policy concerns of the host state, is not self-evident. Indeed, an examination of ISA panels demonstrates a growing balance between commercially trained and public international lawyers on panels of ISA arbitrators, such as the ICSID panel.<sup>72</sup> Even so, it remains the case that commercially trained arbitrators are more frequently appointed to ISA tribunals.

Other normative presuppositions about the effectiveness of ISA compared to domestic courts are also subject to quantitative analysis. For example, it is possible to quantify the presupposition that ISA jurisprudence is more consistent in its scope of application than a multiplicity of different domestic laws applied by local courts to govern foreign investment in light of localised laws and procedures.<sup>73</sup> However, such quantitative measures do not take account of the value priorities that are ascribed to particular domestic laws which are applied by local courts compared to international investment standards that are applied by ISA tribunals.

70 On Transparency International's Corruption Perceptions Index 2012 see Transparency International, *Corruption Perceptions Index 2012* <[www.transparency.org/cpi2012/results](http://www.transparency.org/cpi2012/results)> (10 December 2013). On doubts about the reliability of such indexes see Theresa Thompson and Shah Anwar *Transparency International's Corruption Perceptions Index: Whose Perceptions Are They Anyway?* <[web.worldbank.org/WBSITE/EXTERNAL/WBI/EXTWBIGOVANTCOR/0,,contentMDK:21482059~menuPK:1977002~pagePK:64168445~piPK:64168309~theSitePK:1740530~isCURL:Y,00.html](http://web.worldbank.org/WBSITE/EXTERNAL/WBI/EXTWBIGOVANTCOR/0,,contentMDK:21482059~menuPK:1977002~pagePK:64168445~piPK:64168309~theSitePK:1740530~isCURL:Y,00.html)> (10 December 2013).

71 See e.g., Christoph Schreuer and Rudolf Dolzer, *Principles of International Investment Law* (OUP 2008) 357.

72 On the ICSID Panels of Arbitrators and Conciliations see ICSID, *Search ICSID Panels*: <[icsid.worldbank.org/ICSID/FrontServlet?requestType=ICSIDDataRH&reqFrom=Main&actionVal=PanelStates&range=A~B~C~D~E](http://icsid.worldbank.org/ICSID/FrontServlet?requestType=ICSIDDataRH&reqFrom=Main&actionVal=PanelStates&range=A~B~C~D~E)>.

73 On the development of international investment norms around conceptions of efficiency see Foreign Investment Review Board, *supra* note 54.



In summary, neither quantitative nor qualitative assessments of ISA compared to domestic courts provide any definitive conclusion about the perceived virtues or pitfalls of either. It is therefore desirable to evaluate Australia's rejection of ISA in its 2011 Trade Policy Statement in light of its potential global political, economic and legal effect, not limited to its impact on Australia.

## 5 How Will The Rejection of ISA Protect Australia's National Interests?

There are various measures by which to determine whether Australia's 2011 Policy Statement is likely to accomplish its intended goals. In particular, will Australia's selective rejection of ISA reduce the risk of ISA claims being brought against Australia? Will it alleviate the risk of Australia being subject to a regulatory "chill" in passing public interest legislation?

Australia faces a particular problem in that the lodging of ISA actions against it is almost unavoidable, notwithstanding its Policy Statement against incorporating ISA into its BRTA's. Given the resource intensive nature of the Australian economy and the size of the foreign entities invested in resource markets, it is likely that Australia will be unable to inhibit foreign investors from lodging ISA claims against it under its existing investment treaties, even if it repudiates ISA in all future treaties.

One way for foreign investors to bring ISA claims against Australia is by shifting their places of residence or incorporation to foreign states in order to mount ISA actions against Australia from there and to avoid Australia's domestic court system. The Philip Morris case against Australia is an illustration: in order to avoid Australian courts, the company shifted its operations from Australia to Hong Kong and filed a claim against Australia under the Hong Kong-Australia BIT,<sup>74</sup> thus bypassing Australia's domestic courts. Should Philip Morris lose its ISA claim against Australia on the jurisdictional ground that Hong Kong constitutes a mere forum of convenience, other inbound investors may be discouraged from forum shopping for ISA. However, ISA tribunals do not generally refuse to hear claims submitted to them.<sup>75</sup> What is more likely is

74 The Agreement is titled: 'Agreement between the Government of Hong Kong and the Government of Australia for the Promotion and Protection of Investments'. On proceedings in *Philip Morris Asia Limited v. The Commonwealth of Australia*, UNCITRAL PCA Case No. 2012-12 <[www.italaw.com/cases/851](http://www.italaw.com/cases/851)> (10 December 2013).

75 On the ICSID Caseload Statistics see <[icsid.worldbank.org/ICSID/FrontServlet?requestType=ICSIDDocRH&actionVal=CaseLoadStatistics](http://icsid.worldbank.org/ICSID/FrontServlet?requestType=ICSIDDocRH&actionVal=CaseLoadStatistics)> (10 December 2013).

that foreign investors will rely on forum shopping in mounting their challenges against Australia, or any other country that stipulates that domestic courts must resolve investor-state disputes.

In addition, ISA claims against Australia are indeed likely to lead to a regulatory “chill”, not only in Australia, but also in other states contemplating comparable public interest or other regulatory action. The underlying concern for such states is to avoid being exposed to the risks of spiraling ISA claims brought by claimants with sufficiently deep pockets to sustain them. An illustration of a recurrent ISA claim is Philip Morris’s claim against Uruguay under the Switzerland-Uruguay Free Trade Agreement, prior to its claim against Australia under the Australia-Hong Kong BIT.<sup>76</sup> Should other states enact plain packaging legislation before Philip Morris’s ISA claim against Australia is decided, Philip Morris, or another international tobacco company, may well lodge ISA claims against those other states as well. In issue is more than the prospect of international tobacco companies winning or losing ISA cases. In issue is the fact that the mere lodging of such claims can extend the “chilling” effect of public health legislation for the duration of each case, and if successive ISA actions are brought against multiple states, possibly indefinitely.

Australia’s further dilemma is in balancing the need to protect itself from claims by inbound investors against preserving its attractiveness as a destination for FDI. If it is to reject ISA, it may fail to attract and retain foreign investors that contribute to the infrastructure and operation of its important resource sector. It may encourage foreign investors to relocate their offices to intermediary states such as the Netherlands Antilles and Mauritius<sup>77</sup> in order to avoid Australian BITs that render them reliant on Australian domestic courts in which they lack confidence. This could dampen Australia’s attractiveness as an inbound investment destination and reduce tax revenues generated from such investments. Australia’s unwillingness to provide for ISA in its BRTAs is also unlikely to shield it from ISA claims. In particular, should Australia persist in rejecting ISA and require that domestic courts resolve investor-state disputes in future BITs and FTAs, it may increase, not reduce, its exposure to claims from foreign investors who relocate to states in which Australia has pre-existing BRTAs that provide for ISA.

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76 See *Philip Morris Brands Sàrl, Philip Morris Products S.A. and Abal Hermanos S.A. v. Oriental Republic of Uruguay*, ICSID Case No. ARB/10/7 <[www.italaw.com/cases/460](http://www.italaw.com/cases/460)> (10 December 2013).

77 On the tax and related protection accorded to foreign investors in tax havens such as the Netherlands Antilles see <[www.escapeartist.com/Special\\_Reports/What\\_Is\\_A\\_Tax\\_Haven/](http://www.escapeartist.com/Special_Reports/What_Is_A_Tax_Haven/)> (10 December 2013).

Moreover, should other states replicate Australia's reliance on domestic courts to resolve investor-state disputes, either through their future BITs or FTAs with Australia, or more expansively through their own BIT programs, investor-state claims may mushroom across multiple domestic judicial systems. A likely result is the burgeoning of disparate judicial procedures and domestic laws that are applied to investor-state disputes and the creation of further confusion over the global regulation of FDI.

## 6 Geopolitical Hazards in Rejecting ISA

As was illustrated in prior sections, there is no assurance that ISA is preferable to domestic litigation. Cost-benefit assessments of each may well favour one over the other. Qualitative indices used to measure the value of each may hinge on normative priorities that are subjectively informed more than objectively verified.

Notwithstanding these observations, it is difficult to argue convincingly that domestic courts are the most appropriate institutions in which to decide investor-state disputes. It is also questionable whether the Australian Government is likely to achieve its stated goals by repudiating ISA.

In addition to these issues, there are two further geopolitical and economic barriers to Australia implementing the 2011 Policy Statement. The first barrier is Australia's position as a party to the impending Trans-Pacific Partnership Agreement (TPPA). The second barrier is that Australia's immediate neighbours may refuse to enter into BITs and FTAs with Australia if it refuses to endorse ISA. This barrier is currently an issue in Australia's trade and investment negotiations with China, Japan and South Korea.

### 6.1 *ISA and the Trans-Pacific Partnership Negotiations*

A particular geopolitical challenge for Australia lies in the contest between Australia's 2011 Policy Statement favouring domestic courts over ISA and TPPA member countries favouring ISA.<sup>78</sup> Officially, Australia commenced

<sup>78</sup> See Meredith K. Lewis, 'The Trans-Pacific Partnership: New Paradigm or Wolf in Sheep's Clothing?' (2011) 34 *B. C. Int'l & Comp. L. Rev.* 27, 34; Patricia Ranald, 'The Trans-Pacific Partnership Agreement: Contradictions in Australia and in the Asia Pacific Region' (2011) 22:1 *Econ. Lab. Relat. Rev.* 81 <search.informit.com.au/documentSummary;dn=013448300672307;res=IELBUS> (10 December 2013). On the US negotiating position generally see David Gantz, *Trans-Pacific Partnership Negotiations: Progress, But No End in Sight* <kluwerarbitrationblog.com/blog/2012/06/22/trans-pacific-partnership-negotiations-progress-but-no-end-in-sight/> (10 December 2013).

negotiating the TPPA with the understanding that it will be exempt from any ISA provisions in the TPPA. Granting Australia such an exemption is not exceptional on its face. Country-specific reservations and exemptions are part and parcel of multilateral negotiating processes. Furthermore, the parties negotiating the TPPA have rejected a one-size-fits-all TPPA in order to accommodate the domestic interests of negotiating states.<sup>79</sup> Thus, on the surface, the exemption which Australia sought from ISA is justifiable, given the likelihood of other country-specific exemptions from other provisions in the TPPA. Nevertheless, the costs of Australia securing an exemption from ISA may outweigh its anticipated benefits.<sup>80</sup>

First, reservations and exemptions from treaties are often strategically determined by state parties to such treaties in general and by states seeking specific reservations and exemptions in particular. As a result, participating countries are likely to grant exemptions depending on the perceived benefit to them of doing so. However, a TPPA that is replete with country-specific exemptions can neutralize its value as an umbrella agreement, undermine its uniformity, and lead to multiple side-agreements that are inconsistent with it. This risk of exemptions undermining the TPPA is not limited to the proposed Investment Chapter of the TPPA. It is likely to arise in relation to intellectual property rights and export compliance requirements, among others.

A further risk to TPPA negotiating parties exempting Australia from ISA is that they will embark on a slippery slope in which other parties follow suit by also adopting country-specific reservations. The potential drawback of a TPPA that obfuscates a one-size-fits-all agreement is that it will be downgraded to a loose framework agreement with multi-tiered exemptions and side agreements. Such an eventuality could seriously undermine its economic and legal stature as a multilateral agreement purporting to rival in part a faltering WTO.

In addition, if Australia is to secure an exemption from ISA under the TPPA, its courts are likely to decide ISA cases inconsistently with ISA tribunals appointed under the TPPA. This is due in part to Australia's dualist tradition of according primacy to domestic law over international law, unless the latter is

79 State-by-state negotiations notwithstanding, each "round" of TPPA negotiations includes all participating countries. The 18th Round of TPP Negotiations will take place in Kota Kinabalu, Malaysia on July 15–24, 2013. See further Leon E. Trakman, 'The Transpacific Partnership Agreement: Significance for International Investment' (2013) 4(4) *J. Int'l Commercial Law* (forthcoming).

80 For arguments in support of Australia opting out of investor-State arbitration see e.g. Kyla Tienhaara, *Submission to the Department of Foreign Affairs and Trade: Investor-State Dispute Settlement in the Trans-Pacific Partnership Agreement* <[www.dfat.gov.au/fta/tpp/subs/tpp\\_sub\\_tienhaara\\_100519.pdf](http://www.dfat.gov.au/fta/tpp/subs/tpp_sub_tienhaara_100519.pdf)> (10 December 2013).

expressly incorporated into domestic law. A further likely outcome, if Australia concludes side-agreements with other states that subscribe to a blend of legal monism and dualism domestically, is the accentuation of inconsistencies both between domestic and international investment law and among the domestic legal systems of TPPA member states.<sup>81</sup>

For many observers, the TPPA represents an attempt to revive the Doha Round of trade negotiations and promote greater harmonization among various standards that were created in the spaghetti bowl of BRTAs. International investment is one of the disparate contents of that spaghetti bowl. While the TPPA falls short of a WTO style agreement, its proponents envisage that it will lead to greater harmony in trade and investment, offsetting disparities among pre-existing investment treaties, improving dispute resolution processes, and involving key states in these decision-making processes. If Australia secures an exemption from ISA in the TPPA, it risks isolating itself from other negotiating parties who want to maintain ISA in their treaties with all significant trade and investment partners. Australia may thus lose its voice in the negotiating process over the future of the regional and global investment regime. If Australia withdraws its request for an exemption from ISA, such as in return for access to US sugar and beef markets, it would avert these risks in relation to the TPPA in particular. However, if it negotiates side agreements with TPPA partner states that exclude ISA, the result may still be a “spaghetti bowl” of BITs and FTAs.

## 6.2 *ISA in Australia's Neighborhood*

Australia is fortunate to have inherited a sophisticated legal system that emphasizes the separation of governmental powers and the rule of law. Unfortunately, many of Australia's neighbours are developing nations that have not yet built up comparably developed legal systems.<sup>82</sup> Despite the lack of rooted, liberalized investment regimes in the region, Asia has become increasingly appealing to Australian investors, and it is reasonable to assume that the Asian region will become essential to Australia's future economic development, as is already increasingly the case.

Statistics on Australia's outward investment flows illustrate the economic importance of the Asian region to Australia. According to 2011 Federal Government Statistics, Australia's combined investment in Asia was AUD

81 See Leon E. Trakman, 'International Investment Law and the Transpacific Partnership Agreement' in T. Voon (ed.), *The Transpacific Partnership Agreement* (forthcoming 2013).

82 On the prospect of foreign investors resorting to intermediary states to bring claims against host states see the references cited *supra* notes 76–77.

150 billion, accounting for 13% of its total FDI.<sup>83</sup> While this number is not self-evidently significant, the rate of Australian investment in the Asia region has doubled since 2001.<sup>84</sup> When one examines Australia's trade in goods, the statistics are much more staggering: two-third of Australian trade flows into the Asian region.<sup>85</sup> Similarly, investment from Asia into Australia grew to AUD 300 billion in 2011, which is double what it was 10 years earlier.<sup>86</sup> Although different inferences may be drawn from this data, it is clear that Asia is of immense importance to the economic wellbeing of Australia and is likely to become the primary channel for its future trade and investment flows.

China is a noteworthy example of Australia's growing trade and investment relationships within Asia. China is a major investor in Australia and is heavily involved in its natural resources sector. While Australia's investment in China still lags behind other states in the region, in 2010 Australia's FDI in China reached AUD 17 billion.<sup>87</sup> Although China only invested AUD 19 billion in Australia at that time, this rate is three times higher than what it was in 2007.<sup>88</sup> To put it in perspective, FDI flows from China into Australia are growing exponentially and are making a major contribution to Australia's recent high economic growth, commonly referred to as the natural resources boom. Considering China's demand for natural resources, it is unlikely that this trend will be reversed in the near future as China acquires more of Australia's natural resources.

While the Asian region has immense economic opportunities, Australia's outbound investment into some Asian countries is not without risks. According to the 2012 Transparency International Corruption Perceptions Index, the majority of countries in Asia scored between 10 and 50 points out of a possible 100.<sup>89</sup> Other studies conducted by the World Justice Project provide similarly troubling

83 See Business Council of Australia, *Assessing Australia's Trade and Investment with Asia* <[www.bca.com.au/publications/assessing-australias-trade-and-investment-with-asia](http://www.bca.com.au/publications/assessing-australias-trade-and-investment-with-asia)> (14 December 2013).

84 *Ibid.*

85 See Australian Government Department of Foreign Affairs and Trade, *Australia's Trade in Goods and Services 2012* <[www.dfat.gov.au/publications/tgs/](http://www.dfat.gov.au/publications/tgs/)> (10 December 2013).

86 See Australian Government, *Australia in the Asian Century, Foreign Direct Investment Fact Sheet*, Oct 2012 <[asiancentury.dpmc.gov.au/sites/default/files/fact-sheets/20.-Foreign-investment-in-Australia.pdf](http://asiancentury.dpmc.gov.au/sites/default/files/fact-sheets/20.-Foreign-investment-in-Australia.pdf)> (11 December 2013).

87 *Ibid.*

88 *Ibid.*

89 See Transparency International, *2012 Corruption Perception Index Results* <[cpi.transparency.org/cpi2012/results/](http://cpi.transparency.org/cpi2012/results/)> (20 September 2013).

assessments.<sup>90</sup> The World Bank's Ease of Doing Business rankings of East Asia and the Pacific paints an even bleaker picture: only four countries in the region managed to score in the top 20, with other key regional economic partners of Australia falling behind by a significant margin.<sup>91</sup> While the methodology of these rankings is not without controversy,<sup>92</sup> these surveys portray a similar story: Asia is still lagging behind other parts of the world in the development of its legal institutions and in the protections accorded to foreign investors.

In the absence of ISA, Australia's outbound investors located in Asia may encounter resistance in securing relief from host states, including before local courts. While some investors may move their businesses to intermediary states to avoid the courts of partner states, many smaller Australian investors lack such mobility and will have to resolve their disputes in the local courts of their host states.<sup>93</sup> Thus, one of the practical challenges that Australia faces, if it remains determined to retire ISA, lies in protecting its outbound investors in Asia who lack the capacity to protect themselves.

Of further importance, while many states in Asia do not have a strong rule of law tradition as it is understood in Australia, these countries place increasing emphasis on ISA in their trade and investment relations with other states. This affirmation of ISA stems, in part, from the fact that Asian countries are growing into significant capital exporters with strong economic incentives to protect their outbound investors from local courts in BIT and FTA partner states. China is an illustration of this development. According to unconfirmed reports, Australia is under pressure from China to include access to ISA in the current free trade agreement under negotiation.<sup>94</sup>

China's position on the matter is understandable. Appreciating some "rule of law" limitations in its domestic legal system, China wants to make sure that it remains an attractive FDI destination. Furthermore, Chinese investors have

90 See The World Justice Project, *2012–2013 Rule of Law Index Scores and Rankings* <[worldjusticeproject.org/rule-of-law-index-data](http://worldjusticeproject.org/rule-of-law-index-data)> (20 September 2013).

91 See The World Bank, *Ease of Doing Business 2012 Rankings* <[www.doingbusiness.org/rankings](http://www.doingbusiness.org/rankings)> (20 September 2013).

92 See *e.g.*, Theresa Thompson and Anwar Shah, "Transparency International's Corruption Perceptions Index: Whose Perceptions Are They Anyway?" World Bank Discussion Draft 2005 <[siteresources.worldbank.org/INTWBIGOVANTCOR/Resources/TransparencyInternationalCorruptionIndex.pdf](http://siteresources.worldbank.org/INTWBIGOVANTCOR/Resources/TransparencyInternationalCorruptionIndex.pdf)> (14 December 2013).

93 Investors may base these decisions on various grounds, including but not limited to corruption, transparency and rule of law indices. See *supra* notes 89–90.

94 See Rick Wallace, 'Free-trade Push May Open Door to China', *The Australian*, 18 July 2013 <[www.theaustralian.com.au/national-affairs/foreign-affairs/free-trade-push-may-open-door-to-china/story-fn59nm2j-1226681027576](http://www.theaustralian.com.au/national-affairs/foreign-affairs/free-trade-push-may-open-door-to-china/story-fn59nm2j-1226681027576)> (10 December 2013).

made a number of high profile investments in Australia and it is reasonable to surmise that China lacks confidence in the impartiality of Australian courts. This is especially so in sensitive matters concerning national security, public health and the environment, which are closely related to investment in natural resource sectors and which the Australian government has strong eco-political reasons to protect.

China may also prefer to preserve other dispute resolution options, beyond both ISA and domestic courts, including diplomatic state-to-state measures. As an illustration, China initiated diplomatic measures in response to Australia's exclusion of the Chinese Company, Huawei, from Australia's broadband program over allegations that Huawei had engaged in cyber-espionage.<sup>95</sup> Highlighting the significance of such diplomatic measures was the inference that China had conspired with Huawei in such actions, prompting the US and EU to blacklist Huawei and the UK to reconsider its pre-existing investment relationships with Huawei.<sup>96</sup> Whatever the legal significance of relying on ISA or domestic courts, providing for diplomatic measures is an unavoidable component in BIT reform, not only as a dispute avoidance option, but also in relation to resolving disputes.

In summary, Asian investors may have good reason to anticipate that Australian courts, however strenuously they apply the "rule of law", will also be sensitive to Australia's public policies. Smaller foreign investors in Australia are also likely to encounter significant costs and delays in suing Australia before its local courts.

Australian investors in Asia may also be vulnerable to regulatory excesses due to the developing nature of the region and the lack of sophisticated regulatory regimes in significant parts of it. Furthermore, as Asian economies grow increasingly interdependent, a number of states in the region have shown interest in negotiating BRTAs with Australia, accelerating greater economic integration with it. Due to the relatively protectionist nature of their economies,<sup>97</sup> negotiations between these states and Australia are likely to be protracted, as illustrated by the failure of Australia to conclude an FTA with China

95 Mike Hibberd, 'Huawei Blocked from Australia NBN Bid', *telecoms.com*, 26 March 2012 <[www.telecoms.com/41633/huawei-blocked-from-australian-nbn-bid/](http://www.telecoms.com/41633/huawei-blocked-from-australian-nbn-bid/)> (10 December 2013).

96 See e.g., Jill Stark, 'US Follows Australia in Naming Huawei as a Possible Security Threat', *Sydney Morning Herald*, 9 October 2012 <[www.smh.com.au/it-pro/security-it/us-follows-australia-in-naming-huawei-as-a-possible-security-threat-20121008-277ad.html](http://www.smh.com.au/it-pro/security-it/us-follows-australia-in-naming-huawei-as-a-possible-security-threat-20121008-277ad.html)> (10 December 2013); Christopher Joye, 'Huawei Spies for China, Says ex-CIA Chief', *Financial Review*, 19 July 2013 <[www.afr.com/p/national/huawei\\_spies\\_for\\_china\\_says\\_ex\\_cia\\_QoPS9JWsvg6bMYqmPbtqLK](http://www.afr.com/p/national/huawei_spies_for_china_says_ex_cia_QoPS9JWsvg6bMYqmPbtqLK)> (10 December 2013).

97 On the topic see generally Christopher Dent, 'Free Trade Agreements in the Asia Pacific a Decade On: Evaluating the Past, Looking to the Future' (2009) 10:2 *Int. Relat. Asia Pac.* 201.



and Korea. Australia's seemingly intractable stance on ISA may further aggravate these negotiations, since many of its regional partners view ISA not just as a means to an end, but as a broader symbolic instrument by which to commit to the protection of FDI. Thus, Australia's continuing rejection of ISA will prove to be hazardous in light of the need to protect Australian investors located in Asia and Australia's long term trade interests in the region.

## 7 A Proposed Policy to Regulate Investor-State Disputes

A key task for Australia, in considering whether to persist in rejecting ISA, will be to weigh the "national interest" benefits underlying the 2011 Policy Statement against the benefits of utilizing ISA. This will entail designing an investor-state regulatory regime that satisfies the expectations of the Government and also addresses the pitfalls arising from the Policy. The options proposed below are presented as a spectrum, ranging with the rejection of ISA on the one end to its unconditional reinstatement on the other. In the middle are various ISA configurations that contracting states could potentially negotiate.

As one option, Australia may withdraw from its announced intention to reject ISA. A strong economic and political reason to do so would be to secure treaty concessions from negotiating partner states with which Australia values its investment relationships. These concessions might include, among others, Australian outbound investors gaining access to profitable U.S. markets under the TPPA or to Chinese markets under a China-Australia trade and investment agreement.<sup>98</sup> However, if Australia's announced rejection of ISA is irreversible, including for a number of legitimate reasons, the unqualified re-instatement of ISA may not be viable. Even so, upholding the status quo and maintaining a complete opposition to ISA may come at a high cost and could undermine Australia's national interests.

Alternatively, Australia could reaffirm ISA on a country-by-country basis, according to the nature of its trade and investment relationships, the perceived rule of law standards in its partner states, and the quality of protections that are accorded to foreign investors there. However, employing this approach could damage relations between Australia and those states it deems to lack "rule of law" traditions. Additionally, as was explored in Part 3 of the paper, placing the burden upon investors to employ a contract-based approach to dispute resolution in certain countries is cumbersome, resource intensive and

<sup>98</sup> On the TPPA *see supra* Part VI.A and note 78; on the extent of inbound investment from and outbound to China *see supra* Part VI.B.

one-sided, since it ordinarily favours the stronger negotiating parties. Australia would be the stronger negotiating party in a number of cases involving inbound investments into Australia, but far less so in its negotiations with powerful multinationals from countries like China, Japan, the EU and the US.

A preferable approach is for Australia to modify its 2011 Policy Statement to provide for a multi-tiered, qualified access to ISA. This would be embodied in an overarching Australian BIT policy that would serve as a flexible template for negotiating FTAs and BITs, including with dominant states that have their own model BITs. Such a multi-tiered dispute resolution process may include negotiations between states, including possible referral of disputes to the International Court of Justice, should such negotiations fail. Australia could also develop model clauses to incorporate into its BITS that encourage dispute prevention and avoidance measures, such as requiring investor-state parties to undertake negotiations and/or conciliation prior to resorting to either domestic litigation or ISA. Such a pragmatic approach is not inconsistent with international trade and investment practice. Given that ISA is a party driven process of dispute resolution, treaty signatories are free to design dispute avoidance and resolution measures to suit their needs and those of their investors.

This multidimensional dispute resolution option may further encourage state parties to investment treaties to evaluate different dispute resolution options in light of the costs, timing, duration and effectiveness of each option. It can also help home and host states and disputing investor-state parties to identify their differences and to find common ground. In addition, it may assist disputing parties to consider a wide menu of dispute prevention and resolution options without being locked into any one particular option. Affected parties may opt for negotiations, conciliation and, where appropriate, diplomatic intervention by a home state with a host state partner on behalf of an investor. In doing so, they can avoid protracted litigation, which is costly to all parties involved in an investment dispute.<sup>99</sup>

For comparable reasons, Australia may develop model rules of procedure to apply during formal ISA proceedings that include: setting limits on the standing of foreign investors to bring ISA claims; requiring public notice of ISA complaints; providing for public participation in ISA proceedings, and requiring publication of ISA awards. It may also design model BIT clauses that provide for interim measures; create budgetary limits on the costs of ISA in order to avoid cost overruns; and address dilatory ISA processes including lengthy adjournments. In addition to modification of the procedural rules regulating ISA, Australia may provide for the stay of ISA proceedings to allow for

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99 See *supra* Part III.

investor-state settlement. In addition, to ensure that ISA proceedings do not produce absurd or unjust decisions, it could provide for bilateral challenge committees to hear challenges to ISA decisions, including rules to govern the functioning of such challenge committees.<sup>100</sup>

This multi-tiered approach to resolving investor-state disputes has the advantage of allowing the Australian Government to redress many of the limitations associated with ISA, while avoiding the problems arising from a complete rejection of it. For example, one of the broader benefits of resort to illustrative BIT rules and clauses governing ISA is a greater commitment to transparency, not only for foreign states and their foreign investors, but also for Australian investors abroad. A comprehensive BIT policy could also serve as a signal to both states and investors that Australia has adopted a balanced approach to dispute resolution in its BITs, including support for stable trade and investment relations, which it shares with other states and impacted investors.

Importantly, Australia's adoption of a BIT policy and illustrative BIT clauses could provide inducements for foreign investment in the domestic Australian economy such as by adopting a market-based definition of "investment" and by espousing an investor-sensitive conception of a "direct or indirect expropriation". Conversely, it could provide for Australia's public interest defences to foreign investor claims in order to protect its predominately resource-based economy from foreign investor incursions.

Such a proposed BIT policy has strategic benefits for Australia, encouraging further economic integration between Australia and its key economic allies in the region. The fact that China has adopted a similar multi-faceted process for the resolution of investor-state disputes could help both sides to reach consensus on a trade and investment treaty, which continues to be elusive at the time of writing, along with stalled treaties with Korea and Japan. Such a policy would also make it easier for Australia to engage in the TPPA negotiations in which the majority of members have opted for ISA.

This paper presents 18 recommendations that Australia might include in a BIT policy. These recommendations attempt to accommodate international "good practice" in support of ISA, while recognizing Australia's desire to provide for greater involvement of domestic courts in the resolution of FDI-related disputes. The purpose of the proposed BIT policy would be to identify Australia's preferred position in negotiating BITs – including variations to

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<sup>100</sup> On such a challenge process see UNCTAD IIA: Issues Note, *Reform of Investor-State Dispute Settlement: In Search of a Roadmap* 4 <[unctad.org/en/PublicationsLibrary/webdiaepcb2013d4\\_en.pdf](http://unctad.org/en/PublicationsLibrary/webdiaepcb2013d4_en.pdf)> (26 June 2013).

meet specific domestic and/or foreign party requirements – not unlike, but with more flexibility than, the US Model BIT. It would also assist Australian negotiators to frame BIT provisions, and would provide domestic courts and ISA tribunals with a point of reference when applying treaties to specific investor-state disputes. In addition, it would enable Australia to negotiate for its preferred dispute avoidance provisions in concluding BITs with other states. These 18 recommendations are outlined below:

1. The proposed Australian BIT policy would reflect the desire of the Australian Government to protect its fundamental public policy interests, including its national security, public health, environmental safety and related public interests.
2. The BIT policy would include illustrative clauses providing for investor protections, such as national treatment, most-favoured-nation treatment, and fair and equitable treatment, consistent with the interests of Australia's treaty partners and their investors.
3. The BIT policy would provide for the exhaustion of local remedies before resort to either the domestic courts of host states or ISA.<sup>101</sup>
4. The BIT policy would provide for the stay of ISA proceedings to encourage a settlement by creating a waiting period of six months, during which neither party may initiate proceedings either in domestic courts or through ISA.
5. The BIT policy would include provision for negotiations and conciliation between investor-state parties. Such dispute avoidance measures are consistent with the proposals for dispute avoidance enunciated by the UNCTAD.<sup>102</sup>
6. The BIT policy would compromise between Australia's current Policy of rejecting ISA in future BITs and international investment practice in favour of ISA, by enabling investor-state parties to choose between having their disputes resolved by the domestic courts of the host state or through ISA.
7. The BIT policy would allow foreign investors to bring claims against host states under the rules of established arbitration institutions, such as under the ICSID Convention, the UNCITRAL Rules, the rules of one or more international commercial arbitration centres, or on an *ad hoc* basis.

<sup>101</sup> See Klaus Peter Berger, *Private Dispute Resolution in International Business: Negotiation, Mediation, Arbitration* (Kluwer Law International 2006) vol. II, pp. 74–78.

<sup>102</sup> See UNCTAD, *Investor-State Disputes: Prevention and Alternatives to Arbitration* <[www.unctad.org/en/docs/diaeia2009n\\_en.pdf](http://www.unctad.org/en/docs/diaeia2009n_en.pdf)> (10 December 2013).

8. The BIT policy would provide for variations from the Rules identified in point 7 by expressly stipulating for alternative rules, such as in regulating ISA or other arbitration proceedings BIT by BIT.
9. The BIT policy would set forth rules governing the standing of foreign investors to bring investor-state claims, while denying standing to discourage premature, opportunistic and pernicious claims by foreign investors against host states.
10. The BIT policy would stipulate that arbitration proceedings are open to the public and awards are published, while preserving in confidence the commercial secrets and sensitive information of the direct parties to a dispute.
11. The BIT policy would allow the submission of amici curiae briefs and the participation of third-party interveners on public interest grounds. This is consistent with ICSID Rule 37, adopted in 2006, which regulates submissions of non-disputing parties to ISA disputes.<sup>103</sup>
12. The BIT policy would provide for the admission into ISA proceedings of social, economic and environmental impact reports that relate both to the protection of investors and the defences of states. These reports would be publicly available, subject to the requirements of limited confidentiality, as identified in Proposal 10.
13. The BIT policy would provide for interim measures to expedite proceedings and ensure fairness between the parties, such as to impede claimants and host states from engaging in duplicitous, disruptive or otherwise wrongful conduct. Such measures would inhibit host states from implementing fast-track legislation directed at preventing ISA proceedings from being initiated against it. These measures would also discourage investor-claimants from protracting ISA proceedings in order to delay the implementation of governmental measures.
14. The BIT policy would provide that challenges to an investor-state arbitrator are decided by a challenge committee and not by arbitrators sitting on the same panel as the arbitrator who is the subject of the challenge.
15. The BIT policy would provide for ISA costs directed at monitoring legal costs, including but not limited to: the use of contingency fees, the

<sup>103</sup> International Centre for Settlement of Investment Disputes, *ICSID Convention, Regulations and Rules*, April 2006, Rule 37, p. 117: <[icsid.worldbank.org/ICSID/StaticFiles/basicdoc/CRR\\_English-final.pdf](http://icsid.worldbank.org/ICSID/StaticFiles/basicdoc/CRR_English-final.pdf)> (10 December 2013). See also Leon E. Trakman, 'The ICSID under Siege' (2012) 45(3) *Cornell Int'l L.J.* 603, 663–65; Antonietti, *supra* note 63, p. 427; Baldwin, Kantor and Nolan, *supra* note 63, p. 1 (discussing "tactics" that may be employed in attempts to "delay" or "avoid" compliance with ICSID Awards).

capping of arbitrators' fees, and the allocation of costs between investor and state parties, consistent with the rules regulating monitoring of costs under the 2010 UNCITRAL Rules.<sup>104</sup>

16. The BIT policy would include an illustrative "umbrella clause" by which each BIT party would ensure its observance of any specific undertakings it may have given in relation to investments made by the nationals of another BIT party. The purpose of such an "umbrella clause", often incorporated into BITs, would be to extend treaty protection to investors from BIT partner states in connection with claims which arise from contracts and other dealings between those investors and the host state.<sup>105</sup>
17. The BIT policy would provide for a bilateral interpretative committee to interpret BIT treaty language, including ambiguous wording, and to resolve inconsistent constructions of such treaties.
18. Finally, the BIT policy would be subject to modification and development, in keeping with Australia's evolving national interests and its concerns regarding the protection of foreign investors.

While this paper encourages Australia to adopt a detailed BIT policy, the policy should be neither uncompromising nor mechanically applied to all of Australia's ensuing treaties. Some states, like the US, strongly adhere to a Model BIT template in negotiating BITS with partner states. Other states, like China, sometimes diverge extensively from their Model BITs when they negotiate individual BITs. This was the case in China's bilateral investment treaty with Canada, concluded in 2012,<sup>106</sup> and will most likely be repeated in China's investment treaty negotiations with the EU, launched in November 2013.<sup>107</sup>

The proposed BIT policy is that Australia should adopt a middle position by utilizing a BIT policy that includes illustrative and non-binding BIT clauses, given its status as a middle power and the likelihood that it will conclude

<sup>104</sup> UNCITRAL, *UNCITRAL Arbitration Rules* <[www.uncitral.org/uncitral/uncitral\\_texts/arbitration/2010Arbitration\\_rules.html](http://www.uncitral.org/uncitral/uncitral_texts/arbitration/2010Arbitration_rules.html)> (10 December 2013).

<sup>105</sup> See OECD, *Interpretation of the Umbrella Clause in Investment Treaties* (Working Papers on International Investment, number 2006/3) <[www.oecd.org/investment/internationalinvestmentagreements/37579220.pdf](http://www.oecd.org/investment/internationalinvestmentagreements/37579220.pdf)> (10 December 2013).

<sup>106</sup> The China-Canada Bilateral Investment Treaty was concluded on 12 September 2012, although Canada has not yet adopted it. See <[news.xinhuanet.com/english/china/2013-10/18/c\\_132811261.htm](http://news.xinhuanet.com/english/china/2013-10/18/c_132811261.htm)> (10 December 2013).

<sup>107</sup> See Philip Bentley, QC and Frank Schoneveld, *A Giant Leap: EU-China Bilateral Investment Treaty Negotiations to Be Launched Formally*, National Law Review (23 November 2013) <[www.natlawreview.com/article/giant-leap-eu-china-bilateral-investment-treaty-negotiations-to-be-launched-formally](http://www.natlawreview.com/article/giant-leap-eu-china-bilateral-investment-treaty-negotiations-to-be-launched-formally)> (10 December 2013).

negotiations with different kinds of BIT partners in the foreseeable future. Thus, Australia's BIT policy should not be drafted as a declaration upon which Australia's national identity is inextricably dependant.

Furthermore, these proposals are workable only if they are subject to ongoing examination and refinement. In particular, to ensure that the proposed BIT policy is properly adopted and implemented, it would need to be monitored on a continuing basis in light of its application to particular BITs and the subsequent interpretation of those BITs by domestic courts and ISA tribunals. – The policy would also need to be regularly re-evaluated in light of its impact on national policy and the flow of FDI into and out of Australia.

### Conclusion

Australia's 2011 Policy Statement asserted that the Australian Government would no longer negotiate to include ISA in its BRTAs. Since that date, the Australian Government has changed; the new Liberal Government appears willing to distance itself from its predecessor's Policy Statement, but not to reject it outright. As a result, it is uncertain whether the Policy will survive as Australia's long term approach to the resolution of investor-state disputes. In particular, the current Australian Government has not stated that it will seek to withdraw from, or seek the amendment of, existing BITs and FTAs that provide for ISA. In addition, some of its existing BITs may not have ready mechanisms for displacing ISA.<sup>108</sup>

Australia's unilateral withdrawal from ISA in 2011 could have serious political implications, including the risk of undermining its international reputation and economic relations with its BIT and FTA partners. Should the new Liberal Government revert to the widely accepted reliance on ISA, it would incur limited political damage, in light of its capacity to reverse a Policy Statement that it had not initiated.

However, if the Liberal Government intends to proceed with the rejection of ISA, this paper has proposed a further analysis of the economic, political and legal implications associated with that rejection. The assertion is not that ISA is necessarily more efficient or fairer than resort to domestic courts to resolve investor-state disputes. The claim is rather that macro-economic and political arguments favouring the localisation of investment disputes before domestic courts, on balance, are less optimal than the risks to Australia's outbound

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108 This is subject to the provision in a BIT for a state to withdraw its consent as signatory to a BIT.

investors whose investor-state disputes are heard by domestic courts in jurisdictions that score low on corruption, transparency, and rule of law indices.<sup>109</sup> Australia's potential impasse is that, in relying on domestic courts in defending itself from inbound investors who threaten to attack home state values, institutions and processes, such barriers may fail to protect Australia's outbound investors who are left to fend for themselves in unreceptive foreign legal environments.

This paper does not imply that ISA decisions are invariably coherent in nature or that ISA tribunals apply standards of treatment to foreign investors entirely consistently. Nevertheless, these occasional deficiencies in the practice of ISA do not constitute material reasons to reject ISA out of hand. Notwithstanding the difficulty in developing cohesive principles out of *ad hoc* and sometimes unpublished ISA awards, international custom and treaty practice has helped to both clarify and crystalize international investment jurisprudence.<sup>110</sup> While ISA does not lead to judicial precedent as common lawyers conceive of it, it is more stable than the plethora of different local laws and procedures that domestic courts apply to foreign investment. Moreover, ISA tribunals ordinarily have significantly more experience in weighing investor protections against state defences than domestic courts, which have limited exposure to investor-state disputes.

The paper does not assert that Australia, in its Policy Statement against ISA, was oblivious to the countervailing risks that foreign courts would treat Australian investors abroad unfairly. The Australian Government may well have considered these risks, but gave more credence to the capacity of large-scale outbound investors to protect their investments through investor-state contracts with host states or to proceed against those states through intermediaries.

Nevertheless, Australia's 2011 announced treaty movement away from ISA and towards domestic courts to resolve international investment disputes may have materially negative economic, social and legal consequences for Australia and its outbound investors. In particular, an exodus of investors from Australia to so-called "investor-friendly" intermediary states is but one consequence which the 2011 Policy Statement could have on investor practice as investors seek certainty and security in their business operations.

The paper has concluded that ISA has some systematic economic, political and legal advantages over submitting investor-state disputes to domestic courts, although a case can be made for both. If ISA is to prevail while also

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109 See Transparency International, *supra* note 70.

110 See Franck, *supra* note 57, pp. 1521, 1543–1544.



responding to Australia's public policy and economic concerns, ISA provisions in its BITs and FTAs should protect essential national security, public health, and the environment, among other public interests. It should also provide sufficient investor protection to attract foreign investors to Australia and retain those that are here. Establishing a balance between public interests and the commercial expectations of foreign investors is likely to be challenging, whether or not Australia subscribes to ISA. However, that challenge ought not to discourage Australia from pursuing such a balance in light of the constantly changing regional and global investment environment. This paper argues for a reassessment of the 2011 Policy Statement in light of these national, regional and global considerations.