

# Bilateral Treaties Mitigate Risk



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**As Latin American governments become more hostile to foreign investment, international disputes will increase. The proliferation of bilateral treaties can help mitigate risk.**

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For more than a century, Latin American nations have alternated between welcoming foreign investors and nationalizing their assets. The pendulum has swung back and forth every 30 years or so. One significant difference during the current phase of the cycle, however, is that there are important new sources of legal rights for investors. The last 20 years have witnessed an enormous proliferation of bilateral and multilateral treaties that provide safeguards against state expropriation and other impairment of foreign investment.

Many of these treaties offer formal dispute resolution mechanisms and the vindication of the rights they confer by means of binding arbitration against host states. Moreover, powerful mechanisms for the enforcement of treaty-based arbitral awards may provide for seizure of host state property located in any of more than 140 other states.

The development of arbitration based on bilateral treaties, known as BITs, is a new phenomenon. Prior to BITs, foreign investors had little protection against states unless they had a contract with the host government. Bilateral investment treaties sprang up in the 1960s and exploded during the 1990s. By 2005 there were almost 2,400 executed BITs, with more being negotiated.

Most BITs allow claims to be submitted to the World Bank's International Centre for Settlement of Investment Disputes (ICSID). A total of 143 countries are parties to the ICSID Convention, including most of Latin America. In the first 30 years of the existence of ICSID through 1996, it registered only 35 arbitrations. Since 1996, ICSID has seen the number of cases increase to almost 200, including 25 registered in 2005 alone.

There are essentially the same number of ICSID cases pending as had been previously filed in its 40-year existence. These total 103 cases against 37 states, more than half against the following Latin American countries: Argentina (35) Bolivia (1), Chile (3), Peru (2), Ecuador (5), Venezuela (3), Mexico (6) and El Salvador (1).

Most BITs provide for a broad definition of investment, typically including any kind of asset or service. ICSID tribunals have had little trouble finding that acts taken by investors at the direct or indirect urging of a state amount to an investment.

BITs provide various possible bases of claims: expropriation

without prompt, adequate and effective compensation; fair and equitable treatment; and other international wrongs such as discrimination and national treatment. It is the reasonable, investment-backed expectations of the foreign investor that BITs are intended to protect.

In addition to the traditional bases of claim, an increasing number of BITs incorporate what is known as an umbrella clause, which have in some cases allowed investors to assert claims against sovereigns based on breach of contract. A typical umbrella clause provides as follows: Each contracting party shall observe any obligation it may have entered into with regard to investments of investors of the other contracting party. Several tribunals have interpreted this clause as allowing investors to bring purely contractual claims under the BIT, thereby internationalizing the contract claim.

Interest in "treaty shopping" has grown along with the recognition by sophisticated foreign investors of the advantages BITs can confer. A treaty between an investor's home state and another contracting state provides direct protection over the investment. If there is no treaty between the investor's state and the host state, an investor may still secure protection by structuring its investment to include a company with the nationality of a country that does have a treaty with the host state. Although this is an area of some dispute, "investor" typically is defined broadly under a BIT and a claimant may need little more than to have entities in the investment chain with a certain nationality to bring international legal rights into play.

The expansion of arbitration under BITs and ICSID can help mitigate some of the uncertainty about how disputes can be resolved. It may also increase the effectiveness of enforcing arbitral awards in many circumstances. As such, these and other contractual or security devices may become more common to mitigate some of the political risks involved in cross-border investment in the Americas. It is hoped that these types of legal tools will offset, in all but the most challenging countries, some of the chilling effects that recent state actions have had on foreign investment. **LF**

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