

CALVO'S GRANDCHILDREN: THE RETURN OF LOCAL REMEDIES IN INVESTMENT ARBITRATION*

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I. INTRODUCTION

One of the purposes of investor/State arbitration is to avoid the use of local courts. Litigation in the host State's domestic courts is often seen as lacking the objectivity that the investor desires. In addition, domestic courts are often bound to apply domestic law even if that law falls short of the standards provided by international law.

The traditional international remedy in investor/State disputes is diplomatic protection. But diplomatic protection is contingent upon the exhaustion of local remedies. It does not free the investor from going to the host State's courts. First going to the local courts of the host State meant delay and additional expense to the investor. But it also carried disadvantages for the host State.¹ Public proceedings in the domestic courts are likely to exacerbate the dispute and may affect the host State's investment climate. Once the host State's highest court has made a decision, it may be more difficult for the government to accept compromise or a contrary international judicial decision. The Preamble to the ICSID Convention states that "while such [investment] disputes would usually be subject to national legal processes, international methods of settlement may be appropriate in certain cases."

It is for these and other related reasons that international investment arbitration dispenses with the requirement to exhaust local remedies, at least in principle. Article 26 of the ICSID Convention specifically does away with this traditional requirement "unless otherwise stated".

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¹ The Report of the Executive Directors to the ICSID Convention states: "10. The Executive Directors recognize that investment disputes are as a rule settled through administrative, judicial or arbitral procedures available under the laws of the country in which the investment concerned is made. However, experience shows that disputes may arise which the parties wish to settle by other methods; and investment agreements entered into in recent years show that both States and investors frequently consider that it is in their mutual interest to agree to resort to international methods of settlement." 1 *ICSID Reports* 25.

It is open to a host State to insist on the exhaustion of local remedies when consenting to international arbitration. The ICSID Model Clauses contain a sample for a text to this effect for inclusion in an agreement between the host State and the investor.² Some bilateral investment treaties (BITs), providing for investment arbitration, make the exhaustion of local remedies a condition of consent. But clauses of this kind seem to be rare and are found mostly in BITs of older vintage.³ Two countries, Israel and Guatemala, have given notifications to ICSID that they will require local remedies to be exhausted. But Israel subsequently withdrew that notification.

Arbitral practice confirms that the exhaustion of local remedies is not required in contemporary investment arbitration. Both ICSID⁴ and non-ICSID tribunals⁵ have held that claimants were entitled to institute international arbitration directly without first trying their luck in the local courts.

This is not to say that proceedings in domestic courts will not play a role in investment arbitration. For instance, domestic courts can become active either to compel or to stay the arbitral proceedings.⁶ They may be competent to issue provisional measures.⁷ They can play a crucial role in the enforcement of awards. In non-ICSID arbitration domestic courts may have the power to set aside international arbitral awards.⁸ The activities of domestic courts may be the object of scrutiny by the international tribunal, especially where a denial of justice has been alleged.⁹ Most importantly, they may be in a position to clarify preliminary points of domestic law that are relevant to the case before the international tribunal: for instance if an

² ICSID Model Clauses, Clause 13, 4 *ICSID Reports* 365.

³ C. Schreuer, *The ICSID Convention: A Commentary*, p. 392 (2001).

⁴ *Lanco v. Argentina*, Decision on Jurisdiction, 8 December 1998, para. 39, 40 ILM 457, 469/70 (2001); *Generation Ukraine v. Ukraine*, Award, 16 September 2003, paras. 13.1–13.6.

⁵ *Yaung Chi Oo v. Myanmar*, Award, 31 March 2003, para. 40, 42 ILM 540, 547/48 (2003); *Loewen v. United States*, Award, 26 June 2003, paras. 142 et seq., 42 ILM 811 (2003).

⁶ *Attorney-General v. Mobil Oil NZ*, New Zealand High Court, 1 July 1987, 4 ICSID Reports 117; *SGS v. Pakistan*, Decision on Jurisdiction, 6 August 2003, paras. 35 et seq., 42 ILM 1290, 1297 (2003).

⁷ Schreuer, *Commentary*, pp. 376 et seq.

⁸ *Czech Republic v. CME*, Svea Court of Appeals, 15 May 2003, 42 ILM 919 (2003); *Mexico v. Metalclad*, Supreme Court of British Columbia, 2 May 2001, 5 *ICSID Reports* 236.

⁹ *Loewen v. United States*, Award, 26 June 2003, paras. 54 et seq., 42 ILM 811 (2003).

expropriation, or equivalent measure, is alleged by the investor, it may be useful for a domestic court to determine if and to what extent the property or contract rights in question existed in the first place.¹⁰

The old rule of the exhaustion of local remedies has been largely dispensed with in the context of investment arbitration but it keeps haunting us in other legal disguises. Or, to use another metaphor, Carlos Calvo is not alive but he has children and grandchildren that have an uncanny family resemblance to him.¹¹ Three members of the Calvo family in their contemporary appearance will be discussed below.

II. THE REQUIREMENT TO USE DOMESTIC REMEDIES FOR A CERTAIN PERIOD OF TIME

The first such phenomenon is the requirement, contained in some BITs, that domestic remedies must be utilized for a certain period of time before international arbitration may be initiated. Of course this is not a requirement to exhaust local remedies. The claimant is free to turn to international arbitration once the time has elapsed.

An example is contained in Article 10 of the BIT between Argentina and Germany. It provides that if a dispute cannot be settled amicably it shall be submitted to the competent tribunals of the host State. The dispute may be submitted to international arbitration:

“(a) at the request of one of the parties to the dispute if no decision on the merits of the claim has been rendered after the expiration of a period of eighteen months from the date on which the court proceedings referred to in para. 2 of this Article have been initiated, or if such decision has been rendered, but the dispute between the parties persists.”

The time period foreseen in treaties for the attempt to settle the dispute in domestic courts varies between three months¹² and two years.¹³

¹⁰ See *Azinian v. Mexico*, Award, 1 November 1999, paras. 96–99, 39 ILM 537 (2000).

¹¹ The so-called Calvo doctrine is named after the Argentinean jurist Carlos Calvo and was first outlined in his book *Derecho Internacional Teórico y Práctico de Europa y América* (1868). See also D.R. Shea, *The Calvo Clause, A Problem of Inter-American and International Law and Diplomacy* (1955); W.D. Rogers, “Of Missionaries, Fanatics and Lawyers: Some Thoughts on Investment Disputes in the Americas”, 72 *American Journal of International Law* 1 (1978). Under this doctrine foreigners doing business in a country were to be treated in exactly the same way as local nationals. This meant that these foreigners were to be restricted to local means of dispute settlement, i.e. domestic courts.

¹² See e.g. the Egypt–United Kingdom BIT, Article 8 (1).

The shorter periods look quite unrealistic and make one wonder if the drafters seriously expected that a settlement might be achieved in this way. Even the longer periods are somewhat optimistic and look more like a cooling off period than a serious attempt to settle the dispute domestically.

In a way, the requirement to first try the domestic courts for a certain period of time is the opposite of a fork in the road clause.¹⁴ Rather than having to choose between domestic or international remedies, the investor is essentially forced to use both, one after the other.

In practice, the treaty requirement of taking the dispute to the host State's courts for a certain period of time before going to international arbitration has been honoured mainly through its non-application. Both in *Maffezini v. Spain*¹⁵ and in *Siemens v. Argentina*¹⁶ the claimants were able to rely on most-favoured-nation (MFN) clauses to avoid this requirement. Interestingly, the *Maffezini* Tribunal specifically stated that if the host State had conditioned its consent on the exhaustion of local remedies this requirement could not be bypassed by invoking an MFN clause.¹⁷ But it also found that the requirement to resort to domestic courts for 18 months differed from the exhaustion of local remedies¹⁸ and that, therefore, it could be overcome by way of the MFN clause. The *Siemens* Tribunal also distinguished the requirement to use domestic courts for 18 months from the exhaustion of local remedies rule, essentially, because there was no need to exhaust the possibilities offered by domestic courts.¹⁹

The requirement to attempt a settlement in the host State's domestic courts for a certain period of time looks like a half-hearted revival of the local remedies rule. But it does not seem to serve any useful purpose. The time periods foreseen for this purpose are usually too short to yield a meaningful result. This is particularly so if the domestic courts of the host State are notoriously slow. In the end, the investor retains the right to go to international arbitration, regardless of the outcome of the domestic proceedings. From the investor's perspective the enforced attempt to seek

¹³ See e.g. the France–Morocco BIT, Article 10.

¹⁴ On fork in the road clauses and practice thereto see C. Schreuer, "Travelling the BIT Route, Of Waiting Periods, Umbrella Clauses and Forks in the Road", 5 *The Journal of World Investment & Trade* 231, 239 (2004).

¹⁵ *Maffezini v. Spain*, Decision on Jurisdiction, 25 January 2000, paras. 38 et seq., 40 ILM 1129 (2001).

¹⁶ *Siemens v. Argentina*, Decision on Jurisdiction, 3 August 2004, paras. 82 et seq.

¹⁷ *Maffezini*, at para. 63.

¹⁸ *Maffezini*, at para. 28.

¹⁹ *Siemens*, at para. 104.

justice domestically will usually be no more than a costly ritual that serves no purpose except to delay arbitration.

III. DOMESTIC FORUM SELECTION CLAUSES IN CONTRACTS

By far the best known of Carlos Calvo's grandchildren is the domestic forum selection clause in investment contracts. Under these clauses disputes arising in the context of the contract are to be taken to national courts or tribunals. Not surprisingly, host States have argued that clauses of this kind deprived the international tribunals of their jurisdiction and were meant to restrict the investors to local remedies.

Cases involving domestic forum selection clauses in contracts have been very prominent in recent years. But it is worth pointing out that the problem is not new. In fact, in the very first case before an ICSID tribunal, in a decision of 1974, the Tribunal was already confronted with this question.

In *Holiday Inns v. Morocco*,²⁰ the parties had concluded a "Basic Agreement" containing an ICSID clause. This agreement provided for the establishment and operation of hotels. The Basic Agreement also provided for financing by the Government. This financing was to be carried out by means of separate loan contracts. The loan contracts did not contain ICSID clauses but forum selection clauses in favour of the Moroccan courts.

After the ICSID Tribunal's decision, in which it found on the basis of the Basic Agreement that it had jurisdiction, the Moroccan Government objected to the jurisdiction of ICSID over the claims connected with the loan contracts. The Government contended that the Moroccan courts had sole jurisdiction to decide issues concerning the loan contracts and that such matters "should not be heard by the Arbitration Tribunal until [...] decided by the Moroccan courts at the suit of the interested parties."²¹

The ICSID Tribunal rejected these contentions and affirmed its jurisdiction over the entire claim. It based its reasoning on "the general unity of an investment operation" and the principle that "international proceedings in principle have primacy over purely internal proceedings".²² The Tribunal added that the Basic Agreement was the "charter of the investment", of which the loan contracts were "a measure of execution". The Tribunal added that certain aspects of the loan contracts could be isolated and considered outside the Basic Agreement. Therefore, questions "affecting the indirect or secondary aspects of the investment" could

²⁰ P. Lalive, "The First World Bank Arbitration (*Holiday Inns v. Morocco*) – Some Legal Problems", 51 *British Year Book of International Law* 123 (1980).

²¹ *Ibid.*, at p. 155.

²² *Ibid.*, at p. 159.

properly fall within the jurisdiction of the local courts. But with respect to the non-secondary aspects that were common to the “charter of the investment” and to the loan contracts, the ICSID Tribunal had priority.

The Tribunal also addressed the possibility that the domestic courts could be faced with questions which the ICSID Tribunal would also be called upon to decide. It said:

“In such a hypothetical situation the Moroccan tribunals should refrain from making decisions until the Arbitral Tribunal has decided these questions or, if the Tribunal had already decided them, the Moroccan tribunals should follow its opinion. Any other solution would, or might, put in issue the responsibility of the Moroccan State and would endanger the rule that international proceedings prevail over internal proceedings.”²³

Therefore, the ICSID Tribunal emphatically defended its competence. It did not uphold the forum selection clause pointing to the domestic courts. Rather, it emphasised the primacy of international over domestic proceedings and the principle of the general unity of the investment operation. These two principles led to the result that the entire claim had to be heard by the ICSID Tribunal.

The more recent cases all involved BITs as the basis of the jurisdiction of the international tribunals. Contracts with the host State or a government entity provided for adjudication of disputes arising from the contracts by domestic courts. When the investors instituted international arbitration on the basis of a BIT, the host States would object contending that the contractual forum selection clause, pointing to domestic litigation, constituted a waiver of international arbitration.²⁴

Tribunals at first tried to evade the issue by stating that the contract clauses directing claimants to domestic courts did not really constitute forum selection clauses: the domestic courts, thus selected, had jurisdiction anyway under domestic law and their jurisdiction was not subject to agreement or waiver.²⁵

²³ Ibid., at p. 160.

²⁴ See O. Spiermann, “Individual Rights, State Interests and the Power to Waive ICSID Jurisdiction under Bilateral Investment Treaties”, 20 *Arbitration International* 179 (2004).

²⁵ *Lanco v. Argentina*, Decision on Jurisdiction, 8 December 1998, paras. 39, 40, 40 ILM 457 (2001); *Salini Costruttori SpA et Italstrade SpA c/ Royaume du Maroc*, Decision on Jurisdiction, 23 July 2001, paras. 25–27, *Journal de Droit International* 196 (2002), 6 *ICSID Reports* 400, 42 ILM 609 (2003).

In *Vivendi v. Argentina*²⁶ the issue came to a head. The Tribunal distinguished between claims based on the Argentina/France BIT and claims based on the Concession Contract. It first found that the forum selection clause in the Concession Contract did not affect the Claimant's right to go to international arbitration to pursue violations of the BIT. But then it found that the two types of claims were closely linked. This is reminiscent of the idea of the general unity of the investment operation in *Holiday Inns*. But the *Vivendi* Tribunal drew the opposite conclusion and said that international arbitration would be available to the claimants only after they had asserted their rights in proceedings before the contractually designated domestic courts and had been denied their rights either procedurally or substantively.²⁷ The Tribunal said:

“[...] any claim against the Argentine Republic could arise only if Claimants were denied access to the courts of Tucumán to pursue their remedy under Article 16.4 or if the Claimants were treated unfairly in those courts (denial of procedural justice) or if the judgment of those courts were substantively unfair (denial of substantive justice) or otherwise denied rights guaranteed to French investors under the BIT by the Argentine Republic.”²⁸

The Tribunal immediately added that the obligation to pursue local remedies did not impose an exhaustion of local remedies requirement. Such a requirement would be incompatible with the BIT and with the ICSID Convention. Rather the requirement was imposed by the contractual forum selection clause and the impossibility to separate contract claims from BIT claims.²⁹

Despite the distinctions made by the *Vivendi* Tribunal, the effect of its decision would have been the same as in a situation that requires the exhaustion of local remedies.

The Award was partly annulled.³⁰ The *ad hoc* Committee approved of the Tribunal's distinction between treaty claims and contract claims. But it

²⁶ *Compañía de Aguas del Aconquija, S.A. & Compagnie Générale des Eaux v. Argentine Republic*, Award, 21 November 2000, 16 *ICSID Review – FILJ* 643 (2001); 5 *ICSID Reports* 296; 40 *ILM* 426 (2001).

²⁷ *Ibid.*, paras. 77, 78.

²⁸ *Ibid.*, para. 80.

²⁹ *Ibid.*, para. 81.

³⁰ *Compañía de Aguas del Aconquija, S.A. & Vivendi Universal (formerly Compagnie Générale des Eaux) v. Argentine Republic*, Decision on Annulment, 3 July 2002, 6 *ICSID Reports* 340, 41 *ILM* 1135 (2002). After the partial

also found that the domestic forum selection clause in the contract, which related to contractual disputes, did not relieve the international tribunal of its duty to decide upon the claims under the BIT.

Subsequent tribunals have adopted the distinction between BIT claims and contract claims. They held consistently that the contractual clauses pointing to domestic courts did not deprive them of their jurisdiction to hear claims for violations of international law, especially BIT, claims.³¹

As it turned out, the distinction between treaty claims and contract claims is not always easy. For one thing, a particular course of action by the host State may well constitute a breach of contract and a violation of international law.³² The two categories are by no means mutually exclusive. Rather, two different standards have to be applied to determine whether one or the other or both have occurred.³³

In addition, many treaties providing for investment arbitration do not restrict the jurisdiction of tribunals to claims based on breaches of international law. They extend the tribunals' jurisdiction to "any dispute relating to investments".³⁴ On the basis of these wider definitions of arbitrable disputes, the majority of tribunals have found that jurisdiction is not restricted to claims asserting violations of the BITs' substantive provisions but includes contract claims.³⁵ In other words, under these wider

annulment, the case was resubmitted on 14 April 2004 to a new tribunal in accordance with Article 52 (6) of the ICSID Convention.

³¹ *Salini Costruttori SpA et Italstrade SpA c/ Royaume du Maroc*, Decision on Jurisdiction, 23 July 2001, *Journal de Droit International* 196 (2002), 6 *ICSID Reports* 400; *CMS v. Argentina*, Decision on Jurisdiction, 17 July 2003, paras. 70–76, 42 ILM 788 (2003); *SGS v. Pakistan*, Decision on Jurisdiction, 6 August 2003, paras. 146–174, 42 ILM 1289 (2003); *Azurix v. Argentina*, Decision on Jurisdiction, 8 December 2003, paras. 75–85, 43 ILM 262 (2004); *SGS v. Philippines*, Decision on Jurisdiction, 29 January 2004; *Enron v. Argentina*, Decision on Jurisdiction, 14 January 2004, paras. 89–94; *Siemens v. Argentina*, Decision on Jurisdiction, 3 August 2004, paras. 174–180.

³² See *SPP v. Egypt*, Award, 20 May 1992, paras. 164–167, 3 *ICSID Reports* 189, 228/229.

³³ *Azinian v. Mexico*, Award, 1 November 1998, para. 87, 5 *ICSID Reports* 269, 287/88; *Waste Management v. Mexico*, Award, 30 April 2004, paras. 163 et seq.; *Compañía de Aguas del Aconquija, S.A. & Compagnie Générale des Eaux v. Argentine Republic (Vivendi)*, Decision on Annulment, 3 July 2002, paras. 95, 96, 6 *ICSID Reports* 340, 365.

³⁴ See, for example, Article 8 (1) of the Argentina–France BIT; Article 9 (1) of the Italy–Jordan BIT; Article 8 (1) of the Egypt–United Kingdom BIT.

³⁵ See, for example, *Salini v. Morocco*, Decision on Jurisdiction, 23 July 2001, paras. 59–62, 6 *ICSID Reports* 398, 415; *Compañía de Aguas del Aconquija, S.A.*

jurisdictional provisions not only claims arising from international law but also contract claims are covered.

Then there are “umbrella clauses”. These clauses, contained in treaties guarantee the observance of obligations or commitments entered into vis-à-vis foreign investors. Therefore, they put contractual commitments under the treaties’ protective umbrella. The effect of such a clause is to make compliance with investment contracts and other undertakings by the host State a treaty obligation.³⁶

All of this shows that there is at least considerable overlap between the issues to be settled by the international tribunals and by the domestic courts. So where is the line to be drawn between international and local remedies?

The Tribunal in *SGS v. Pakistan* adopted the distinction between treaty claims and contract claims but then took a very narrow view of its jurisdiction over the latter. Despite a clause in the applicable BIT that referred quite generally to “disputes with respect to investments” and despite an umbrella clause, it held that it had no jurisdiction with respect to contract claims which did not also constitute breaches of the substantive standards of the BIT.³⁷

& Compagnie Générale des Eaux v. Argentine Republic (Vivendi), Decision on Annulment, 3 July 2002, para. 55, 6 *ICSID Reports* 340, 356; *SGS Société Générale de Surveillance S.A. v. The Republic of the Philippines*, Decision on Jurisdiction, 29 January 2004, paras. 130–135; *Tokios Tokelés v. Ukraine*, Decision on Jurisdiction, 29 April 2004, at FN 42 para. 52.

³⁶ P. Weil, *Problèmes relatifs aux contrats passés entre un Etat et un particulier*, 128 *Recueil des Cours* 130 (1969–III); F.A. Mann, “British Treaties for the Promotion and Protection of Investments”, 52 *British Year Book of International Law* 241, 246 (1981); R. Dolzer/M. Stevens, *Bilateral Investment Treaties*, pp. 81–82 (1995); I.F.I. Shihata, *Applicable Law in International Arbitration: Specific Aspects in the Case of the Involvement of State Parties*, in: *The World Bank in a Changing World*, Vol. II, p. 601 (1995); J. Karl, “The Promotion and Protection of German Foreign Investment Abroad”, 11 *ICSID Review – FILJ* 1, 23 (1996); K.J. Vandeveld, *United States Investment Treaties: Policy and Practice* (1992), at p. 78; C. Schreuer, “Travelling the BIT Route: Of Waiting Periods, Umbrella Clauses and Forks in the Road”, 5 *The Journal of World Investment & Trade* 231, 249 (2004); S.A. Alexandrov, “Breaches of Contract and Breaches of Treaty”, 5 *The Journal of World Investment & Trade* 555, 564–572 (2004). A. Sinclair, “The Origins of the Umbrella Clause in the International Law of Investment Protection”, 20 *Arbitration International* 411 (2004).

³⁷ *SGS v. Pakistan*, Decision on Jurisdiction, 6 August 2003, paras. 161, 165, 166, 42 ILM 1289 (2003). In *Joy Mining v. Egypt*, Award, 6 August 2004, the Claimant sought to rely on a BIT clause referring “any legal dispute [...] concerning an investment” to international arbitration. The Tribunal never

In *SGS v. Philippines* the Tribunal took the opposite position. It found that the dispute settlement clause in the applicable BIT referring generally to “disputes with respect to investments” and the umbrella clause in the BIT had the effect of giving it jurisdiction also over contract claims.³⁸ However, after finding that it had jurisdiction over contract claims as well as BIT claims, and after finding that some of SGS’s BIT claims were tenable,³⁹ the Tribunal still sent the parties to the domestic courts. It stayed the arbitral proceedings to allow the courts of the Philippines to determine the amount payable.

The main reason for this decision was that the provision on international arbitration in the BIT was the more general one which should yield to the more specific contractual clause referring disputes to the domestic courts.⁴⁰ The Tribunal’s reasoning ignores the fact that the dispute settlement clause in the BIT is merely a standing offer to investors. By accepting that offer an investor perfects a specific arbitration agreement.⁴¹ While the contract clause refers to any dispute arising from the contract, the ICSID arbitration agreement, as perfected through the institution of proceedings, applies only to the specific dispute. It follows that the ICSID arbitration agreement is the more specific one. Therefore, the principle *generalia specialibus non derogant*, that the Tribunal invoked,⁴² should work against the contractual forum selection clause and in favour of ICSID.

The Decision in *SGS v. Philippines* then introduced the concept of admissibility which it distinguished from jurisdiction. It held that a party should not be allowed to rely on a contract where the contract itself refers the claim exclusively to another forum.⁴³ This meant that SGS was bound by the terms of the exclusive jurisdiction clause in the contract to establish the quantum or content of the obligation that the Philippines was required

addressed the argument but seemed to reject it by declaring that it lacked jurisdiction in the absence of a treaty-based claim. At paras. 68–82. The *Joy Mining* Tribunal also essentially denied the effect of an umbrella clause at para. 81.

³⁸ *SGS v. Philippines*, Decision on Jurisdiction, 29 January 2004, paras. 131–135, 125–128.

³⁹ *Ibid.*, at paras. 160–163.

⁴⁰ *Ibid.*, at para. 141.

⁴¹ The Tribunal itself describes this process at para. 31 of its Decision.

⁴² *Ibid.*, at para. 142.

⁴³ *Ibid.*, at para. 154.

to observe. This was a matter of admissibility rather than jurisdiction and there was a degree of flexibility in the way it was applied.⁴⁴

Therefore, the *SGS v. Philippines* Tribunal first found that it had jurisdiction over the BIT claims and the contract claims. It then declined to proceed to the merits but referred the parties to the domestic courts for the determination of the amount due. This is strongly reminiscent of what the *Vivendi* Tribunal did. But the *SGS v. Philippines* Tribunal, unlike the *Vivendi* Tribunal, did not base its decision on the impossibility to separate BIT claims from contract claims. That would not have made sense since it had found that it was competent for both.

Technically, what the *SGS v. Philippines* Tribunal did was not to require the claimant to exhaust local remedies. The Tribunal did not reject the claim but merely stayed its proceeding. It emphasized repeatedly that it was staying the arbitration proceedings only until the domestic courts have determined the quantum of the claim and that it retained jurisdiction over the claim as such. But the practical difference to an exhaustion of local remedies is small. Presumably what the Tribunal has in mind is an adjudication of the claim by the domestic courts subject to the Tribunal's continuing supervision as to expediency of the proceedings, a possible denial of justice and actual payment of the amount thus adjudicated.

A better approach might be to abandon the idea of mutually exclusive competences. The jurisdictions of international tribunals and of domestic courts do not necessarily "override" or "replace" one another. This was the position taken by Arbitrator Antonio Crivellaro in his dissent appended to the Decision in *SGS v. Philippines*. He points out that where several dispute settlement clauses coexist, the claimant has the right to select amongst the alternative fora. The existence of the two clauses does not necessarily make them mutually exclusive. They can comfortably exist side by side.

This point was made clearly by the Tribunal in *Siemens v. Argentina*:

"As regards Article 26 of the [ICSID] Convention, the first sentence reads as follows: 'Consent of the parties to arbitration under this Convention shall, unless otherwise stated, be deemed consent to such arbitration to the exclusion of any other remedy.' This provision presumes exclusivity of the remedies under the Convention unless the parties had agreed otherwise. Article 26 does not provide that what may be agreed otherwise excludes the remedies under the Convention. In that case, the remedies under

⁴⁴ Ibid., at para. 170.

the Convention are not exclusive but neither are those otherwise agreed.”⁴⁵

Even the decisions by international tribunals that declare treaty claims within their jurisdiction and admissible but send the claimants to the domestic courts just for their contract claims are problematical. The idea that contract claims and BIT claims are conceptually separate and are subject to different standards is intellectually attractive. But whether it is practicable to assign them to different judicial processes is another matter. Despite the fact that the causes of action may differ, it seems uneconomical to employ parallel judicial processes, one domestic and one international to settle what is essentially two aspects of the same legal dispute. Once a dispute arises, it is usually not practical to dissect the relationship into different legal segments and to pursue remedies simultaneously in separate fora. If competing competences exist, it makes more sense to have the entire dispute heard by one forum, preferably the one with the most comprehensive jurisdiction. If the terms of reference in the BIT are broad enough to include contract claims in addition to treaty claims the international tribunal would be the one with the broadest jurisdiction.

Considerations of finality support this conclusion. Does it make sense that an international tribunal that has been seized and that has jurisdiction would remand part of the case to domestic courts? It is entirely possible that after protracted domestic litigation the investor remains dissatisfied and claims that the domestic courts have committed a denial of justice or have otherwise violated international obligations. That situation may well lead to further international proceedings.

The NAFTA has a straightforward solution to the problem of competing domestic and international proceedings. Article 1121 requires, as a condition for jurisdiction, that the Claimant submits a waiver of the right to initiate or continue before domestic judiciaries any proceedings with respect to the measures taken by the Respondent that are alleged to be in breach of the NAFTA.⁴⁶ The waiver does not relate to the dispute before

⁴⁵ *Siemens v. Argentina*, Decision on Jurisdiction, 3 August 2004, para. 181. See also at para. 107: “The BITs do not restrict the rights of investors or the State to pursue a dispute before the local courts. They provide an additional venue normally not open to investors.” See also *Lanco v. Argentina*, Decision on Jurisdiction, 8 December 1998, para. 38, 40 ILM 457, 469 (2001).

⁴⁶ Article 1121: Conditions Precedent to Submission of a Claim to Arbitration
1. A disputing investor may submit a claim under Article 1116 to arbitration only if:
[...]

the international tribunal but to “proceedings with respect to the measure” that is alleged to be in violation of the NAFTA. Therefore, it is disputable whether the distinction between treaty claims and claims based on domestic law apply.

The majority in *Waste Management v. Mexico*⁴⁷ came to the conclusion that the distinction between treaty claims and claims under domestic law did not apply in this context. Article 1121 of the NAFTA requires the investor to waive any domestic proceedings in respect of the incriminated measure before gaining access to international arbitration.⁴⁸

IV. RESORT TO DOMESTIC COURTS AS A SUBSTANTIVE REQUIREMENT OF INTERNATIONAL STANDARDS

The third member of the extended Calvo family to be addressed here may not be a blood relative but just an adopted child. It becomes active not at the stage of jurisdiction or admissibility but when the tribunal looks at the merits.

Tribunals have at times indicated that a violation of treaty standards occurs only once some redress has been sought and denied through proceedings in domestic courts. The Tribunal in *Waste Management* has described this phenomenon in the following terms:

“[...] in this context the notion of exhaustion of local remedies is incorporated into the substantive standard and is not only a procedural prerequisite to an international claim.”⁴⁹

(b) the investor and, where the claim is for loss or damage to an interest in an enterprise of another party that is a juridical person that the investor owns or controls directly or indirectly, the enterprise, waive their right to initiate or continue before any administrative tribunal or court under the law of any Party, or other dispute settlement procedures, any proceedings with respect to the measure of the disputing Party that is alleged to be a breach referred to in Article 1116, except for proceedings for injunctive, declaratory or other extraordinary relief, not involving the payment of damages, before an administrative tribunal or court under the law of the disputing Party.

⁴⁷ *Waste Management, Inc. v. United Mexican States*, Award, 2 June 2000, 40 ILM 56 (2001), 5 ICSID Reports 443. See also *Metalclad Corp. v. United Mexican States*, Award, 30 August 2000, 5 ICSID Reports 209, 229 FN 4; *Mondev Intl. v. United States*, Award, 11 October 2002, para. 96, 42 ILM 85 (2003).

⁴⁸ On this point see especially the Dissenting Opinion by Arbitrator Keith Hight 5 ICSID Reports 462 et seq.

⁴⁹ *Waste Management v. Mexico*, Award, 30 April 2004, para. 97. Footnote omitted.

The idea that a violation of substantive international standards has occurred only after redress has been sought exhaustively through the local courts, is hardly surprising in the context of an alleged denial of justice. Denial of justice is committed typically by the judiciary and is completed only if the incriminated decision has been appealed unsuccessfully. As the Tribunal in *Loewen v. United States* said:

“[...] a court decision which can be challenged through the judicial process does not amount to a denial of justice at the international level [...]”⁵⁰

In *Generation Ukraine v. Ukraine*, the requirement to attempt domestic remedies came up in the context of an alleged indirect expropriation. The Tribunal said:

“In such instances, an international tribunal may deem that the failure to seek redress from national authorities disqualifies the international claim, not because there is a requirement of *exhaustion* of local remedies but because the very reality of conduct tantamount to expropriation is doubtful in the absence of a *reasonable* – not necessarily exhaustive – effort by the investor to obtain correction.”⁵¹

The Tribunal specified this broad statement in the following terms:

“In the circumstances of this case, the conduct cited by the Claimant was never challenged before the domestic courts of Ukraine. More precisely, the Claimant did not attempt to compel the Kyiv City State Administration to rectify the alleged omissions in its administrative management of the Parkview Project by instituting proceedings in the Ukrainian courts. There is, of course, no formal obligation upon the Claimant to exhaust local remedies before resorting to ICSID arbitration pursuant to the BIT. Nevertheless, in the absence of any *per se* violation of the BIT discernable from the relevant conduct of the Kyiv City State Administration, the only possibility in this case for the series of complaints relating to highly technical matters of Ukrainian planning law to be transformed into a BIT violation would have

⁵⁰ *The Loewen Group Inc. and Raymond Loewen v. United States of America*, Award, 26 June 2003, para. 153, 42 ILM 811, 836 (2003). Generally see paras. 142–171, 207–217.

⁵¹ *Generation Ukraine, Inc. v. Ukraine*, Award, 16 September 2003, para. 20.30. See also *Lauder v. Czech Republic*, Award, 3 September 2001, para. 204.

been for the Claimant to be denied justice before the Ukrainian courts in a *bona fide* attempt to resolve these technical matters.”⁵²

Therefore, what looks like a broad obligation to try – if not exhaust – local remedies was moderated by the Tribunal’s finding that the administrative authorities had not *per se* violated the BIT. To establish a BIT violation the Claimant would have had to demonstrate a denial of justice in a *bona fide* attempt to seek redress.

In *Waste Management v. Mexico*, the issue of the prior use of local remedies arose in the context of the host State’s obligation to guarantee fair and equitable treatment and full protection and security. The Tribunal said:

“It is true that in a general sense the exhaustion of local remedies is a procedural prerequisite for the bringing of an international claim, one which is dispensed with by NAFTA Chapter 11. But the availability of local remedies to an investor faced with contractual breaches is nonetheless relevant to the question whether a standard such as Article 1105(1) has been complied with by the State.”⁵³

The Tribunal proceeded to look at legal proceedings that had taken place in Mexico reaching the conclusion that there had not been a denial of justice which would have constituted a violation of NAFTA Article 1105(1). The Tribunal does not distinguish clearly between the use of local remedies as a general prerequisite for the invocation of the fair and equitable standard and a denial of justice which is part of the broader issues covered by fair and equitable treatment.

It would be an exaggeration to say that these decisions indicate that tribunals have developed a general principle that requires that domestic remedies must be reasonably attempted, if not exhausted, before an international remedy may be sought for a claim of expropriation or a violation of the fair and equitable standard. But it is not difficult to see that the rationale in these cases can be developed into something that reintroduces the local remedies rule through the back door.

Once it is accepted that the investor should make an attempt at local remedies it is only a small step to require that the attempt should not stop at the level of the lowest court. Once we require that reasonable appeals be taken we are close to demanding that these be exhaustive.

⁵² *Ibid.*, at para. 20.33.

⁵³ *Waste Management, Inc. v. United Mexican States*, Award, 30 April 2004, para. 116.

It is not inherently unreasonable to require that the investor make some efforts domestically to obtain redress before seizing an international tribunal. But then neither is the domestic remedies rule inherently unreasonable. The decision to do away with it in investor-State investment arbitration was made consciously and for good reasons. Therefore, we should think twice before making the use of local remedies a constitutive element or substantive requirement of a violation of international standards.

Further problems are likely to arise if it becomes generally accepted that local remedies must be attempted before international arbitration becomes available. For instance, it is unclear how such a requirement can be combined with a fork in the road provision in an applicable BIT. Under such a provision, the claimant has an irreversible choice between domestic courts and international arbitration. Therefore, any step by the claimant to take the dispute to the national courts would rule out subsequent access to the international forum.

V. CONCLUSIONS

The exhaustion of local remedies is not a requirement of modern investment arbitration. This is one of several advantages it has over the traditional remedy of diplomatic protection. But the requirement to use domestic courts, before going to international arbitration, is reappearing in a number of ways.⁵⁴ We should be wary of these tendencies. Perhaps the members of the Calvo clan should not all be banished outright. But they should be kept under close surveillance.

VI. SUMMARY

1. International investment arbitration typically dispenses with the requirement to exhaust local remedies. It is possible for host States to insist on the exhaustion of local remedies but this is rarely done.
2. Nevertheless, the requirement to resort to domestic remedies – not necessarily to exhaust them – is a recurrent feature in contemporary investment arbitration.
3. Some bilateral investment treaties (BITs) require that local remedies be utilized for a certain period of time before international arbitration may

⁵⁴ It is worth mentioning that international courts have displayed a tendency to restrict the application of the local remedies rule. See *The M/V "Saiga" (No. 2) Case*, International Tribunal for the Law of the Sea, 1 July 1999, paras. 89–102, 38 ILM 1323 (1999); *Avena and other Mexican Nationals (Mexico v. United States of America)*, International Court of Justice, 31 March 2004, paras. 38–40.

be initiated. So far, claimants have been able to avoid this requirement by relying on most-favoured-nation clauses in these BITs.

4. Domestic forum selection clauses in contracts have been invoked by host States to challenge the jurisdiction of international tribunals. Tribunals established under BITs have defended their competence by distinguishing between claims based on the contract and claims based on the treaty.

5. The distinction between contract claims and treaty claims has not always been easy: a particular course of action may well constitute a breach of contract and a violation of international law; some BITs extend the jurisdiction of international tribunals beyond breaches of the treaty to investment disputes in general; umbrella clauses in treaties guarantee the observance of contractual commitments made by host States vis-à-vis foreign investors.

6. Some tribunals have held that they have jurisdiction but have still referred the claimants to the domestic courts. In *Vivendi* the Award was partially annulled for that reason. In *SGS v. Philippines* the Tribunal merely stayed the proceedings until the domestic courts have determined the quantum of the claim.

7. The jurisdiction of domestic courts and arbitral tribunals is not necessarily mutually exclusive. Where several provisions on dispute settlement coexist the claimant may have a right to select among the alternative fora.

8. If the international tribunal has jurisdiction over treaty claims and contract claims the more economical approach is to have the entire dispute decided by the tribunal.

9. In several recent decisions Tribunals have indicated that a violation of treaty standards occurs only once some redress has been sought and denied through proceedings in domestic courts. Under this theory the need to resort to local remedies is incorporated into the substantive standard and is not a procedural requirement that determines admissibility.

10. The requirement to try local remedies before going to international arbitration may well develop into something that resembles the old exhaustion of local remedies rule.