

**USCIB Young Arbitrator's Forum
Panel Discussion**

Is there a System of Precedent in Investment Treaty Arbitration?
Tai-Heng Cheng

Date: October 22, 2006

Time: 6 p.m. –8 p.m.

Venue: Simpson Thacher & Bartlett LLP, New York

Remarks by Tai-Heng Cheng:

Good evening. It is an honor and pleasure to participate on such a distinguished panel of young arbitrators. I am grateful to Janet Whittaker and Rob Smit for inviting me to serve on this panel, and in particular to Janet, who has so kindly set the context of our topic, “Is there a system of precedent in investment treaty arbitration?”

In my view, the key issue is not whether there is strict adherence to a doctrine of *stare decisis*. It is, instead, whether there is some clear legal method by which awards are rendered that accounts for prior publicly-available publicly available decisions. Only with such accounting will international investment law – by which I mean principles and rules of public international law relevant to foreign investments – be stable. This stability is necessary to promote certainty in investment outcomes and to protect the legitimacy of international investment law in the eyes of investors and host states.

I propose to you that we do have a system of legal reasoning, in which prior decisions are accounted for, that is consistently applied to disputes. Over the next few minutes, I’d like to survey the relevant law and evidence as an aperitif to our discussions following this presentation.

Our first sip is of Article 38 of the ICJ Statute. Article 38 is widely regarded as codifying the customary law on sources of international law. It states that judicial decisions are merely “subsidiary means for the determination of rules of law.”¹ It lists instead as primary sources of law: customary law, treaties and general principles. On the face of Article 38, it appears to require arbitrators to apply customary law and treaties rather than the decisions of prior arbitrations. Prior arbitral awards, being subsidiary means of determining the law, do not

¹ Statute of the International Court of Justice 1945, Art. 38.

conclusively indicate the content of applicable international legal rules. In support of this formalistic argument, skeptics of investment treaty arbitration may point to apparent inconsistencies between arbitral awards in support of their view that there is an insufficient system of precedent.²

But the customary law that Article 38 codified in 1945 has evolved. Positivists Bruno Simma and Andreas Paulus have conceded that the “importance of [decisions of international tribunals] for the clarification of legal rules nowadays can hardly be overestimated.”³ At a minimum, prior well-reasoned arbitral awards are highly persuasive in arbitral disputes.

There are at least three practical reasons why awards are accounted for in arbitrations. First, arbitrators are eminent practitioners and scholars. They are steeped in the methods of legal reasoning in domestic law and can be expected to apply these methods with which they are most familiar.

Second, the domestic law methods are designed, *inter alia*, to promote the orderly exposition and development of domestic law. Arbitrators are acutely aware that international

² Compare *SGS Societe General de Surveillance S.A. v. Republic of Philippines*, ICSID Case No. ARB/02/6 (Jan. 29, 2004) (holding umbrella clause elevated contractual obligations to international law obligations) with *SGS Societe Generale de Surveillance S.A. v. Islamic Republic of Pakistan*, ICSID Case No. ARB/01/13, 42 I.L.M. 1290 (Aug. 6, 2003) (holding umbrella clause did not elevate contractual obligations to international law obligations).

³ Brunno Simma & Andreas Paulus, *The Responsibility of Individuals for Human Rights Abuses in Internal Conflicts: A Positivist View*, 93 AM. J. INT’L L. 302, 307 (1999).

law should also be developed in an orderly fashion, and thus would tend to apply the legal methods that promote such an order development of international law.

The third reason may be less noble. Arbitrators reap significant reputational benefits among fellow arbitrators, counsel and the college of international jurists if they render awards that are regarded as well-reasoned. In order to persuade their market of their eminence, and suitability for future arbitrations, arbitrators may use commonly-accepted legal methods.

In practice, what do arbitrators do? They tend to canvass prior decisions for guidance. They may then accept a prior decision as an accurate statement of law, reject it as no longer reflecting the law, reinterpret it, or distinguish it on its facts: just like judges in domestic cases.

For example, the content of the fair and equitable treatment standard is a hotly-contested area of law. Three awards in 2006 addressed this standard: *Saluka* on March 17;⁴ *Azurix* on July 14;⁵ and *LG&E Corporation* on October 3.⁶ Although these decisions did not cite each other, they did reach the same substantive conclusions. All three tribunals concluded that what was required under the fair and equitable treatment standard was highly fact-specific. The host state needed to provide measures that would ensure business and legal stability to attract foreign investments, and bad faith was not a necessary element for breach of the standard. The

⁴ *Saluka Invs. BV v. Czech Republic*, Partial Award, UNCITRAL (Oct. 3, 2006).

⁵ *Azurix c. Argentine Republic*, Award, ICSID Case No. ARB/01/12 (July 14, 2006).

⁶ *LG& E Corp. v. Argentine Republic*, Decision on Liability, ICSID Case No. ARB/02/1 (Oct. 3, 2006).

uniformity in the tribunal's substantive conclusions suggests a certain consistency of legal reasoning.

This hypothesis is supported by the fact that all three tribunals applied the same legal method. They all canvassed the awards that counsel brought to its attention. The arbitrators then followed numerous prior awards that found that this standard required the host state to create a stable legal and business environment for foreign investors.

In concluding that bad faith was not a requirement, none of the tribunals ignored the *Genin* award, which others had interpreted importing bad faith into the standard. The *LG&E* and *Saluka* tribunals interpreted *Genin* as holding that it interpreted *Genin* as holding that bad faith was merely one way in which the standard could be breached, but that bad faith was not a necessary requirement for breach. The *Azurix* tribunal took a different approach that was nonetheless familiar to domestic judges. It concluded that to the extent that *Genin* imposed a bad faith requirement for breach, this was a minority view, and the tribunal elected to follow the majority view that bad faith was not required.

Now we can debate whether the fair and equitable treatment standard should be drawn narrowly or broadly, and whether it should have bright-line standards or general principles. But these substantive debates do not necessarily suggest that there are unreasoned inconsistencies in arbitral awards. Quite to the contrary. Arbitral awards do acknowledge and address prior decisions in determining the fair and equitable treatment standard. Just as domestic judges have flexibility in elaborating developing areas of common law without exceeding the boundaries imposed by *stare decisis*, international arbitrators may explicate international investment law by applying, distinguishing or clarifying prior awards.

However, there is one key difference between *stare decisis* and decision-making in investment treaty arbitrations. When a lower court departs too far from *stare decisis*, a higher court can reverse the lower court's decision in order to reassert *stare decisis*. In international arbitrations, there is, generally speaking, no appellate review, only annulment on limited grounds. Thus, if a tribunal decided to ignore prior decisions, there are some, but not many, control mechanisms to insulate our system of precedent from damage that could result from that unreasoned award. In this century, as China's fortunes rise with its ambitions and more arbitrators emerge from Asia and other regions of the world, it will be interesting to observe if younger arbitrators trained in diverse legal traditions depart of our current system of precedent. If this occurs, how will the global community of arbitrators will respond?