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Negotiation Clauses in BITs – Empty Words?

Claudia Ludwig (Herbert Smith Freehills LLP) · Tuesday, May 24th, 2011 · Herbert Smith Freehills

In the recent investment treaty case Alps Finance Trade AG v Slovak Republic, an UNCITRAL tribunal had to consider whether Alps had satisfied the obligation contained in Article 9 of the Switzerland-Slovakia BIT which requires that "consultations will take place" and that they "do not result in a solution within six months" before the matter can be referred to arbitration. Slovakia argued that this was a condition precedent to arbitration which had not been met by Alps and that Slovakia's consent to arbitration was therefore missing and the Tribunal lacked jurisdiction to hear the case. Alps responded that it had actively attempted to consult with the Slovak Government but that the Slovak Government had not shown any interest in addressing or pursuing Alps' proposals.

The Tribunal held that the negotiation clause in the BIT was not an obstacle to its jurisdiction as all that was required was that "consultations be at least attempted" and that six months had elapsed without any resulting solution. Any deficiencies in Alps' notice to the State of the outbreak of the dispute and attempt at pre-arbitral settlement did not render the State's consent to arbitral jurisdiction ineffective. In reaching its decision, the Tribunal followed a purposive approach to the interpretation of the negotiation clause, holding that the rationale of the clause was to avoid "that a State be brought before an international investment tribunal all of a sudden, without being given the opportunity to discuss the matter with the other party".

The Tribunal's decision in Alps v Slovakia is consistent with the non-formalistic approach to negotiation clauses taken by previous investment treaty tribunals which had viewed negotiation clauses as imposing procedural rather than jurisdictional requirements on the parties concerned – see, for example, Ethyl v Canada, Salini v Morocco, Lauder v Czech Republic, SGS v Pakistan, Bayindir v Pakistan, Occidental v Ecuador and, most recently, Paushok v Mongolia. A similarly non-formalistic approach has also been favoured by the ICJ – see, for example, Libya v United States of America (Lockerbie), Nicaragua v United States of America and South West Africa. When a majority of the ICJ deviated from this approach in its recent decision in Georgia v Russian Federation, advocating a very formalistic interpretation of Georgia's obligation to negotiate before commencing proceedings, this was strongly criticised in several dissenting opinions. The general view is that, where the claimant has taken reasonable steps to bring the dispute to the State's attention and resolve the matter

amicably or where negotiations are bound to be futile, no purpose would be served by suspending the arbitration and, even less so, by forcing the claimant to re-start the proceedings. The reasons given by the various tribunals for not forcing the parties to adhere strictly to the terms of the negotiation clause include that it is not cost-effective and could potentially allow a State party who does not really wish to negotiate to obstruct and delay arbitration proceedings.

Accordingly, the only cases where tribunals have enforced the negotiation clause were where the claimant did not give the State any notice at all, or only very short notice, of its claim prior to commencement of the arbitration. In Burlington v Ecuador, where the claimant had only informed the State of the dispute by submission of its request for arbitration, the ICSID Tribunal found that the claimant had deprived the State of the "opportunity to redress the problem before the investor submits the dispute to arbitration" and that, as a result, the Tribunal lacked jurisdiction over the claimant's claim (therefore holding that the duty to give proper notice of the claim was not just a procedural but a jurisdictional requirement). Similarly in the recent case of Murphy v Ecuador, the ICSID Tribunal rejected the claimant's argument that the six-month "cooling-off" period provided for in the BIT was a mere procedural formality. It held that the "cooling-off" period was "a fundamental requirement" of the BIT with which the claimant had not complied with by filing its request for arbitration with ICSID on the first business day after giving notice to the State that it had a claim against it. However, in his partially dissenting opinion, Dr. Horacio A. Grigera Naón criticised this decision as not marrying well "with the concept of a reasonably fast and efficient access to the arbitral instances provided for in the BIT and seriously impair[ing] [the claimant's] right to access arbitral justice". It seems, however, that tribunals are not consistent in their decisions. In SGS v Pakistan the negotiation clause in the BIT provided for a 12-month consultation period and SGS had notified Pakistan of its belief that a dispute within the ambit of the BIT existed only two days before it submitted its request for ICSID arbitration. Two days are clearly not sufficient for a State to consider the claims made against it, but the ICSID Tribunal found that it was not "consistent with the need for orderly and cost-effective procedure to halt this arbitration at this juncture and require the Claimant first to consult with the Respondent before re-submitting the Claimant's BIT claims to this Tribunal".

When negotiating its BITs it is usually in the State's interest to push for a relatively long notice period prior to a claimant being able to commence proceedings. Unlike the claimant who is of necessity familiar with the facts and may have been preparing its claim for several months, the State may hear of the matter for the very first time with submission of the dispute to ICSID arbitration or upon receipt of the notice of arbitration. Accordingly, it is difficult for a Sate to consider and engage in any meaningful settlement negotiations unless it is given sufficient time to establish the facts. In addition, while negotiations and a settlement obviously remain possible while the arbitration proceedings are pending, the fact that the commencement of the proceedings, at least in the event of an ICSID arbitration, is publicised and that costs have started to be incurred, will likely make them more difficult. The claimant, on the other hand, has an interest in being able to pursue its legitimate rights in an efficient arbitration process without being unduly subjected to a State's delaying tactics. However, whichever position one takes, it is submitted that the current situation, where considerable delay is caused and costs are incurred because of disputes over

whether the negotiation stage was fulfilled, which are generally, unless in extreme circumstances, decided in favour of the claimant, is unsatisfactory and not in the interest of either party.

In Alps v Slovakia, the Tribunal made the point that the negotiation clause in the Switzerland-Slovakia BIT (which was, in the relevant parts, identical to the negotiation clause in the Switzerland-Pakistan BIT relied on by Pakistan in the SGS v Pakistan case), only required that "consultations will take place" and did not impose "specific formalities for the consultations". Similarly, in Salini v Morocco, the Tribunal highlighted the fact that the negotiation clause "does not set out any procedure to be followed in relation to reaching an amicable settlement". This suggests that the tribunals' decisions in these cases might have been different if the relevant BITs had imposed specific formalities for the consultations such as a formal "Letter before Action" setting out the claims made, a specific number of negotiation meetings and specified participants. Giving the tribunal clear benchmarks against which to measure the parties' conduct by setting out clear procedural steps which the parties have to meet in the BIT may therefore be a way to resolve the current ambiguities surrounding the interpretation of negotiation clauses.

Alternatively, BITs could be re-negotiated to make the jurisdictional nature of the "cooling-off" period clear by, for example, expressly stating that consent to arbitration is only given once a six-month period has expired. In the meantime, given that renegotiation of BITs is a long-term project, the parties to a dispute may want to try to agree to dispense with a negotiation clause completely and, instead, make provisions in their procedural timetable for additional time for negotiations, notwithstanding the additional impediments to settlement once a claim has been formalised and publicised.

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