New Investment Arbitration Center in Latin America: UNASUR, A Hybrid Example of Success or Failure?

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Latin America is the region that has faced the largest number of investment treaty arbitration cases in the world, holding 30% of the total ICSID caseload (549 cases as of December 31, 2015). South America alone, comprised by twelve UNASUR members, has faced 131 ICSID cases with a number of adverse outcomes for the host states. As a result, during 2007-2012, Bolivia, Ecuador and Venezuela denounced the ICSID Convention, albeit with more political implications than legal effects, in a futile attempt to evade ICSID jurisdiction. (See, *Occidental v Ecuador* and *Pan American v Bolivia*).

Since 2010 the President of Ecuador, Rafael Correa, has advocated and led the works towards the creation of a new Arbitration Center under UNASUR, aimed at resolving international investment disputes among its members. The UNASUR is an international organization originally established in 2004 and formed by Argentina, Bolivia, Brazil, Colombia, Chile, Ecuador, Guyana, Paraguay, Peru, Suriname, Uruguay and Venezuela. UNASUR's main purpose is to promote economic, social and political integration in the region. The proposed mechanism is

said to aim boosting transparency, impartiality and control to ensure a fairer and more balanced outcome, while reducing time and costs for both states and foreign investors.

After 5 years of deliberations, the new Rules of the UNASUR Arbitration Centre (the **"Center"**) and a Code of Conduct of Arbitrators are almost ready and expected to be officially in place. These rules contemplate a number of hybrid rules, including: (1) facilitation and conciliation; (2) the exhaustion of local remedies, taken from diplomatic protection and ICSID Rules; (3) the exclusion of subject matter jurisdiction over specific sectors determined by each state at any time; and (4) an appeal mechanism to revert *errors in judicando* inspired in the WTO Appellate Body, which seems to aim to develop a system of precedent. As expected, the UNASUR Rules address most of the concerns raised over the ICSID regime while innovating in other fronts.

As to transparency, arbitral awards and conciliation agreements must be made public, except when there is confidential or protected information; or in case of information that, pursuant to the legislation of the host state, shall not be made public.

Some of the Center's key features are discussed below.

Exhaustion of local remedies

UNASUR states may compel the exhaustion of domestic remedies (administrative or judicial) as a precondition to their consent to arbitration or conciliation. This power may only be exercised at the time of the state's granting its consent to submit a dispute to UNASUR arbitration.

The origins of this requirement are found in the diplomatic protection mechanisms (supported by the ICJ in *Interhandel*, further clarified in *Diallo*). Nowadays, most BITs do not require the exhaustion of local remedies. However, some countries in Latin America have preserved this requirement influenced by the Calvo Doctrine. (See for example, the Argentina-UK BIT).

The necessity of exhaustion of local remedies has gradually been abandoned by customary international law, as illustrated in *BG Group Plc, v Republic of Argentina*, where initially the US Court of Appeals vacated the award for lack of jurisdiction, given that the arbitral tribunal disregarded the 18-month litigation requirement

foreseen in the BIT. However, the US Supreme Court reversed that decision by establishing that a local litigation condition "cannot be construed as an *absolute* impediment to arbitration"; and that the interpretation of a local litigation provision is primarily for arbitrators.

A perceived advantage of primary remedies is that host states can have the opportunity to resolve the dispute locally by reconsidering its decision through the judicial review process. However, UNASUR members need to make their domestic courts more efficient and arbitration-friendly should they wish to coupe with today's international adjudication standards of speediness, impartiality and technical specialisation.

Exclusion of jurisdiction over specific sectors

One of the most criticized features of ISDS is the limitation to the state's right to regulate. Therefore, modern investment treaties have aimed to modify the standards of protection for disputes involving regulations related to environmental or public health protections. (See for example, the relevant provisions of the CAFTA-DR, the TPP and the proposed text of the EU-Canada Comprehensive Economic and Trade Agreement). The very recent and sensitive cases relating to challenges of sovereigns' power to regulate in those fields have also raised concerns as to ISDS legitimacy. (See, *Vattenfall v Germany*, *Philip Morris v Australia* and *Philip Morris v Uruguay*).

Investment protection treaties deal with substantive rather than procedural limitations. In this regard, the UNASUR Rules, as a procedural instrument, are not capable of limiting the power of arbitrators to adjudicate disputes involving challenges to regulations in sensitive areas, such as above described, environmental and public health. Therefore, the Rules grant the member states the option to notify the Treaty Depositary of any sectors they refuse to consent to arbitration. However, the Rules establish that this notifications will not prevail against the express consent of the state to submit a dispute to arbitration, for instance in a current treaty.

Appellate mechanism

The main concern raised by Bolivia after denouncing ICSID was the lack of an appeals mechanism, preventing not only the formation of a coherent jurisprudence, but also the ability to remedy potential *errors in judicando.* Under

Article 52.1.b. of the ICSID Convention, erroneous legal findings by arbitral tribunals do not necessarily amount to annulment under the 'manifest excess of power' threshold. (See, *CMS v Argentina*).

UNASUR arbitration awards will be subject to an appeal mechanism, inspired in the Geneva-based Appellate Body of the WTO, which has reached an average rate of appeals of two-thirds according to the organization's statistics. Recourse to appeal would be available to either party claiming an error in the application or interpretation of the law applicable to the investment dispute, within a period of 120 days from the date of rendering of the award. The Appeal Commission would have the power of confirming, modifying or revoking the award. It is also under consideration that the Rules also include as a ground for appeal "an error of *fact* and transcendence" incurred in the evaluation of a determining piece of evidence in the award. The latter has been raised by some members during the negotiations, but is still pending final approval.

Similarly, Article 28 of the U.S. Model BIT (2012) envisions an appellate mechanism for reviewing awards rendered by investor-state tribunals, albeit subject to other institutional arrangements by the BIT members. Once the UNASUR Rules are approved, it will be interesting to see if they will follow the WTO model of a direct appeal, or the U.S. BIT model rule. The latter would require UNASUR members to reach a subsequent agreement establishing the appeals mechanism.

On the positive side, an appeal mechanism aims to improve the quality and 'correctness' of awards, while preventing gross mistakes committed by arbitral tribunals, without having to resort to domestic courts. However, it will inevitably increase the time for a final decision. As the stakes in investment disputes are high, for both investors and states, some are of the view that an additional scope of review may prove to be necessary and valuable to enhance the legitimacy of investment awards in the coming years.

Potential Obstacles

The Center's operation may be undermined by skepticism and distrust coming from investors and scholars. It should be noted that the initiative is rooted in the anti-arbitration view which derives from the multiple million-dollar awards rendered against several South American countries such as Argentina, Ecuador and Venezuela. Thus, investors may be concerned about the risk of political

interference with the decision-making process in favor of states.

It is the drafters' responsibility to assure to the international community that the Center will provide neutral and independent services, free of political pressure. For instance, the burden of a closed list of arbitrators pre-selected by the Center or UNASUR member states might raise a red flag as to the neutrality of the Center's adjudicative proceedings.

The main challenge for the Center will be competing with co-existing arbitral institutions provided for in treaties that are already in force as well as investment protection laws and investment agreements. In what circumstances will the new parties refer their disputes to the Center? The burden is on the member states to promote the Center's Rules, foresee them in local investment promotion laws and negotiate to add them to new treaties with other states or investment contracts with potential investors. We will have to wait to see how the member states' frame their foreign investment policy to give life to the UNASUR Rules.

Conclusion

UNASUR arbitration could provide a new alternative route of solving disputes to foreign investors doing business in Latin America. Such investors may be best served by a "hybrid" system that embraces both ICSID and regional standards and principles, what is proposed in the UNASUR model. In any event, its success will be subject to a correct implementation of the new rules by the member states, the impartiality of arbitrators, but above all, in the level of trust by investors in the coming years.