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Possible Changes In Arbitrating Against The Chilean State: Lessons Learned from Bolivia

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After the October 2021's plebiscite, Chile began the process of drafting a new constitution, which was entrusted to a "*Convención Constituyente*". After a year of work, on July 4, 2022, the final proposal was delivered to the President of the Republic. The proposed constitution will be submitted to a ratifying plebiscite in September of this year, where the proposed text will be approved or rejected.

Article 331 of the new constitutional text proposes the creation of administrative courts to resolve lawsuits filed by or against the State. The idea of creating these courts is not new, it was also included in the current Chilean Constitution prior to its reform in 2005. However, these courts were never implemented. The difference with the new proposal is that it excludes arbitration from all those matters that fall under these new tribunals' jurisdiction (Article 331, number 4).

This prohibition has generated considerable debate in Chile, especially in the area of infrastructure projects and public works concessions. Notably, in the construction industry, it is usual to agree to submit disputes to arbitration, due to the specialization of arbitrators in the subject matter. If the new constitution were to be approved, disputes would need to be submitted to the new courts, with the uncertainty of the expertise of the judges and capabilities to effectively reach solutions and with the proper approach.

This proposal has also generated concerns about the position of Chile regarding foreign investors, given that arbitration clauses are generally agreed in international contracts. This could create an extra hurdle in negotiating and executing contracts with foreign parties, which are critical for the country's development.

Learning from the Bolivian experience

The limitation to the arbitrability of administrative contracts proposed by the *Convención Constituyente* is similar to Article 4 of Bolivia's Arbitration Act (*Ley de Conciliación y Arbitraje*), which prohibits disputes arising from administrative contracts to be submitted to arbitration, unless the contract has been entered into by a company with no domicile in the country (Article 6). Even though this rule is still recent (5 years old), its application in Bolivia has shown some problems for parties contracting with the State:

First, the competent forum for disputes emerging from administrative contracts would be either the Administrative Chamber of the Supreme Court (for contracts signed with national public entities) or the Administrative Chamber of the District Court (for contracts signed with regional public entities). Since the duration of the proceedings in these forums are usually three times longer than in arbitration, and these courts are not specialized in complex cases, their exclusive jurisdiction often times influences the decision of a contracting party to litigate or not against the State.

Second, most State-owned companies have abused this rule alleging that the public nature of their entities is equal to the State's administration, and therefore, avoid otherwise binding arbitration. In that regard, it is worth noticing that the similarities and differences between an administrative contract and a State-owned contract depend on many elements, for example, the contract's link to public use. However, State-owned companies have an open door to challenge the jurisdiction of an arbitral tribunal on this basis and delay the proceeding for many months. Moreover, these entities may use an alleged breach of contract to prosecute the counterparty and its representatives for criminal offences such as "damage to the State" or "breach of contract with the State", both considered corruption-related crimes.

Impact of the new constitutional text on ISDS

Chile's new constitution proposal also raises questions about the future of investor-state dispute settlement (ISDS), since article 228(12) establishes that "*when negotiating treaties or international investment instruments, he or she who holds the Presidency of the Republic position shall procure that the dispute resolution instances be impartial, independent, and* ***preferably permanent***" (emphasis added).

The last sentence has generated debate on whether "permanent" must be deemed a permanent center administrating the arbitration (e.g. ICSID), or a permanent court (e.g. CETA Investment Court System). The outcome is relevant since there is controversy on which system is better to resolve investor-state disputes.

Bolivia's experience with its Constitution is also similar on this point. Article 320 of the Bolivian Constitution sets forth a general rule that excludes the possibility of investment arbitration under international arbitration rules (with some exceptions, such as sunset clauses). Article 320 provides that: "*All foreign investment will be subject to Bolivian jurisdiction, laws, and authorities, and no one may invoke a situation of exception, or appeal to diplomatic claims to obtain more favorable treatment.*" In addition, Article 366 also prohibits international arbitration in the oil and gas industry: "*No foreign court or jurisdiction will be recognized in any case, and they may not invoke any exceptional situation of international arbitration, nor resort to diplomatic claims*".

As to permanent arbitration centers, Bolivia withdrew from the ICSID Convention in 2007 and has denounced all its BTIs since then, claiming it would renegotiate them to better protect the interests of the country. To date, no BIT has been renegotiated except for the Boliva-Peru BIT, that was extended for an additional six-month period, which has already expired.

Following the enactment of the Bolivian Constitution, the Bolivian Arbitration Act created a whole new regime for investment arbitration subject to Bolivia's local law, jurisdiction, and authorities (as mandated by Article 320 of the Bolivian Constitution). Both national and international arbitration claims related to investments in the country shall be solved according to Bolivian law

(procedural and substantive). The intention of the Bolivian government was to submit these controversies to the regulations and proceedings issued by an "*Investment dispute settlement center of an agency of which the Plurinational State of Bolivia is a party, within the framework of integration processes.*" This rule responded to a collective strategy designed by Argentina, Bolivia, Ecuador, and Venezuela to discredit the ICSID mechanism, to create a specialized forum at UNASUR (*Unión de Naciones Sur Americanas*), with a center to administer investment arbitrations. However, this regional mechanism has not been fully established and, thus, is not currently working. Chile's *Convención Constituyente* seems to follow this path when its proposal mentions a permanent instance.

Conclusion

If the new Chilean constitution proposal is finally ratified, article 228 (12) may become a critical provision in ISDS since the implementation of the new constitution is likely to generate changes in the Chilean economic order, and some international investors may decide to bring claims against Chile as a result of changes in the economic or legal framework.

The Bolivian case shows the likely path in relation to arbitration against the Chilean State if the constitution proposal is ratified. While such path may lead to protecting the Chilean State interests in the short term, it may also discourage foreign investors from investing in Chile in the long run.

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