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2023 PAW Recap: Affaires d'Etats Vol. 2 – Abusive Claims Against States and How to Fight Them

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As part of 2023 Paris Arbitration Week ("PAW"), Curtis hosted a webinar on "Affaires d'Etats: Abusive Claims Against States and How to Fight Them". This was the second edition in the "Affaires d'Etats" series initiated by Curtis last year during 2022 PAW.

This year's panel addressed the growing sentiment in some quarters, including in the context of UNCITRAL Working Group III on the reform of ISDS, that abusive claims and practices in international arbitrations against States are on the rise. Such claims are said to drive up the costs of proceedings, harm the reputation of host States, and generate regulatory chill. The panel, moderated by Simon Batifort, comprised Wolfgang Alschner, Marie-Claire Argac, Miriama Kiselyová and Suzy Nikièma. The panelists first examined the "problem", before addressing the "solutions" to tackle this phenomenon. This post encapsulates the key takeaways from the discussion.

Typology of Abusive Claims and Practices

Miriama Kiselyová opened the floor by describing three types of claims usually found to be abusive:

1. attempts at treaty shopping, as illustrated by *Phoenix v. Czech Republic* in which a newly created Israeli company bought Czech companies which were already in ongoing legal proceedings in Czech Republic, and then brought the dispute to arbitration alleging a breach of the Czech-Israeli BIT;
2. multiple, parallel and successive claims, as in *CME v. Czech Republic* and *Lauder v. Czech Republic*; two landmark cases related to the same dispute, with the former brought by the company, and the latter by the ultimate shareholder of CME; and
3. attempts to resort to remedies not provided for in international investment agreements ("IIAs"), such as in the *Achmea v. Slovak Republic (II)*, in which the investor resorted to arbitration to prevent the State from adopting a new regulation that would allegedly have constituted a BIT breach.

Marie-Claire Argac provided examples of abusive practices in relation to damages. She pointed out that claimants on average are awarded less than 40% of the amounts initially claimed,

suggesting a concerning tendency to vastly exaggerate damage claims. She emphasized the exponential increase in the amount of damages claimed in investor-State arbitration in the last two decades, explaining that one of the causes was the enhanced reliance on the discounted cash flow ("DCF") methodology – a methodology particularly prone to abuse and "anchoring" tactics as it requires the projection of multiple parameters into the future.

She pointed out that some claimants have been trying to take advantage of the absence of strict regulations regarding the appropriate approach towards damage calculations to push for the application of this method to project alleged future lost profits, regardless of the existence of sufficient certainty as to the existence of such lost profits and in the absence of a going concern with a proven record of profitability. Ms. Argac also noted that the increased recourse to third party funders (TPF) was associated with the proliferation of abusive claims, as noted by as noted by UNCITRAL Working Group III.

A Threat for Developing Countries

Suzy Nikièma then highlighted that frivolous claims are particularly problematic for developing countries.

First, such claims entail a waste of time and financial resources. This proves to be detrimental even if such frivolous claims are ultimately dismissed at a jurisdictional stage.

Second, such claims generate a so-called "chilling effect" on States, including developing countries, to regulate in the public interest, as famously illustrated by the *Philip Morris v. Australia* case.

Thirdly, the impact on States' reputation can also be significant because usually only the amounts claimed and the number of cases brought against the State are ultimately remembered, rather than the final outcome of the dispute. Thus, abusive claims can reinforce preconceptions about the governance of developing countries.

A Procedural but also a Substantive Problem

Wolfgang Alschner underscored that frivolous claims are not simply a procedural problem, but also a substantive one.

More specifically, he noted that claims manifestly without legal merit were difficult to identify substantively due to the vagueness of many IIAs as to standards of protection. The notions of fair and equitable treatment, legitimate expectations or police powers are often (if not systematically) left undefined, making it difficult for States, investors and funders to identify what characterizes a claim manifestly without legal merit. This is amplified by the multiplicity of interpretations of substantive norms in the ISDS world, with tribunals often adopting contrary interpretations of the same standards of protection.

New Provisions in Recent IIAs

Moving on to solutions, Ms. Kiselyová discussed new kinds of provisions that Slovakia, the European Union (EU), and other States, have included in their new IIAs to try to curb abusive practices. For example, some recent EU treaties such as the CETA, the EU-Singapore Investment Protection Agreement and the EU-Vietnam Investment Protection Agreement include "Submission of Claims" provisions. Under such provisions, claimants have to withdraw from pending proceedings and confirm the absence of resubmission of the dispute in the future either by the claimants or by entities they control. In addition, Article 33 of the CETA deals with claims manifestly without legal merit (inspired by ICSID Arbitration Rule 41) and claims unfounded as a matter of law. These provisions also appear in the Slovak-Iran BIT, which has already been ratified.

Need for a Holistic, Substantive and Multilateral Reform

Prof. Alschner questioned the actual impact of new mechanisms designed to weed out frivolous claims, echoing some of the conclusions published in his recent book. While acknowledging the procedural developments in some of the new treaties, Prof. Alschner expressed skepticism about the substantive treatment of the problem, including about the framing of a substantive distinction between meritorious claims and those that manifestly lack legal merit. He observed that because of the multiplicity of investment treaties, an investor bringing a frivolous claim rejected under one instrument would still have the opportunity of introducing a new claim under another more permissive instrument.

Furthermore, although some new treaties include "substantive safeguards", such as general public policy exceptions, in practice these mechanisms have failed to operate effectively as some arbitrators have denied their full effect. An example is found in the recent *Eco Oro v. Colombia* case, where the tribunal held that the investor was entitled to claim compensation even though the public policy exception expressly set forth in the treaty applied.

Prof. Alschner concluded that focusing only on procedural reforms was insufficient and that there was a need for a more holistic and multilateral reform on the substance of international investment law.

Existing and Potential Preventive Mechanisms

Ms. Nikièma emphasized the importance to supplement measures focused on halting frivolous claims at early stage with strategies that proactively deter the occurrence of such claims. She then addressed existing mechanisms that can be used to prevent frivolous claims from making their way into arbitration. A first option is the requirement of exhaustion of local remedies, to ensure that local laws and regulations, which sometimes place more stringent requirements on the legal and factual basis of a claim, are respected. A second, more substantive approach would be to adopt more circumscribed definitions of the concepts of investor and investment, as is the case in some recent African investment treaties that have adopted an enterprise-based definition of investment.

Ms. Argac listed some of the avenues being discussed to curb abusive practices in relation to

damages, including: (i) ordering the claimants to bear a higher fraction of the costs if the damages claimed exceed the actual amount awarded by a certain percentage, even if the claimant is successful on part of the claim; (ii) limiting damages to the amount actually invested or even capping the maximum damages that can be awarded; (iii) compensating moral or reputational damages to States, although this would have to be balanced against the general prohibition of punitive damages; and (iv) reshaping the normative framework governing TPF and security for costs.

Ms. Argac also emphasized the need to select counsel, arbitrators and experts who have a thorough understanding of these issues as soon as possible in the proceedings and stressed the role of arbitrators in curbing these abusive practices by rejecting these types of claims outright but also by calling them out and holding claimants accountable.

Conclusion

In closing, the proliferation of abusive claims and practices is a topic of serious concern calling for both procedural and substantive reform of international investment law. It remains to be seen whether ongoing efforts at UNCITRAL Working Group III and other fora will achieve significant improvements on this front.

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