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Legitimacy in WTO law and investment arbitration: the role of the contracting parties

by
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International trade and investment law is characterized by two distinct models: the constitutional law model as found in the World Trade Organization (WTO),[1] where the remedy is "the bringing into conformity of the measure", and the tort law model, where international law standards establish the threshold for delictive behavior, to be remedied by damages.[2] Both models represent rules-based approaches to the peaceful settlement of disputes, replacing power diplomacy. They may be considered as the finest examples of the efficient application of rules of international law. Both sub-systems of international law are creations of treaties, which serve to control unreasonable political actors and positively affect regulatory governance even on a domestic level.

The development of the former GATT and present WTO law is driven and controlled by the contracting parties, through the adoption of panel reports based on rather precise behavioral rules, which leads to an "authentic" interpretation of such rules by its members.[3] In contrast, standards contained in international investment agreements (IIAs) are the result of a "dilatory formula compromise", i.e., a formal compromise without agreement on its precise content, due to historical reasons. They have been developed through interpretation by arbitral tribunals and scholarly writings in order to achieve a sufficient level of precision to provide for legal certainty and predictability. However, this occurs without further involvement of the contracting parties, which raises legitimacy issues.[4]

There is no evidence that states were aware, or should have been aware, of the potential widening of the scope of IIAs through the use of most-favored-nation (MFN) provisions, especially with regard to jurisdictional and procedural elements of such agreements. For example, IIAs do not contain criteria for the application of the fair and equitable treatment standard to regulatory measures, such as the intensity of the measures required to deem them illegal. Neither do IIAs provide further guidelines for the proper identification of comparators of discrimination for a finding of violation of the MFN and the national treatment standards. This has a direct impact on the amount of damages to be awarded.

Arbitral awards and scholarly writings have contributed to the development of international law standards in a mostly balanced and increasingly sophisticated manner. Arbitral awards, however, are at best a subsidiary means of demonstrating rules of international law[5] and limited to the parties of the arbitration.[6] Scholarly writings are only a subsidiary source of international law.[7] Both arbitral awards and scholarly writings provide content to international law standards used in investment arbitration, but not necessarily legitimacy, which may only be provided by the contracting parties. The absence of the contracting parties in the formulation of international law standards generates not only legitimacy concerns, but may also raise an impression of unfairness, which may lead to the impairment of this rather well-designed rules-based regime.

The NAFTA Commission has used authentic interpretation of international law standards to clarify the intent of its members. The exercise of treaty-making power to give precise content to the key international investment law standards and authentic interpretation is a core challenge for the future Transatlantic Trade and Investment Partnership between the European Union and the United States. This is a historic opportunity—and responsibility—to provide authoritative content to international investment law standards and to pave the way for a better-calibrated regime. We should hope that negotiators make the most of it and do not miss this opportunity.

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[1] Ernst-Ulrich Petersmann, *Constitutional Functions and Constitutional Problems of International Economic Law* (Fribourg: Fribourg University Press, 1988).

[2] Hersch Lauterpach, *Private Law Sources and Analogies of Law* (London: Longmans, 1927) 6; Borzu Sabahi, *Compensation and Restitution in Investor-State Arbitration* (Oxford: OUP, 2011), pp. 15-42; Zachary Douglas, "The enforcement of environmental norms", in Pierre-Marie Dupuy and Jorge E. Viñuales, *Harnessing Foreign Investment to Promote Environmental Protection* (Cambridge University Press 2013), pp. 422, 435, 437; Herfried Wöss, Adriana San Román Rivera, Pablo T. Spiller, and Santiago Dellepiane, *Damages in International Arbitration under Complex Long-term Contracts* (Oxford: OUP, 2014), pp. 13-6, 18-9, 223-233, 236-244.

[3] Wolfgang Benedek, *GATT from an International Law Perspective* (Berlin: Springer Verlag, 1990), p. 142.

[4] Santiago Montt, *State Liability in Investment Treaty Arbitration, Global Constitutional and Administrative Law in the BIT Generation* (Portland: Hart Publishing, 2012), pp. 146-154.

[5] Todd Weiler, *The Interpretation of International Investment Law, Equality, Discrimination and Minimum Standards of Treatment in Historical Context* (Leiden: Martinus Nijhoff, 2013), p. 53.

[6] Gilbert Guillaume, "The use of precedent by international judges and arbitrators", *Journal of International Dispute Settlement*, vol. 2 (2011), p. 16.

[7] Statute of the International Court of Justice, art. 38(1)(d).

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