

THE ARBITRATION REVIEW OF THE AMERICAS 2009

A Global Arbitration Review special report

Published by Global Arbitration Review
in association with

Sidley Austin LLP

GLOBAL ARBITRATION
REVIEW

THE INTERNATIONAL JOURNAL OF PUBLIC AND PRIVATE ARBITRATION

Making Investment Treaties Work for Latin America

Stanimir Alexandrov, Nicolás Lloreda, Patricio Grané and Meredith Moroney

Sidley Austin LLP

Latin American companies are emerging as global leaders, increasingly looking internationally for business and investment opportunities. Despite the growing prominence of Latin America as a source of international investment, Latin American investors have not yet taken advantage of the international agreements that are ready and available to protect their investments. International investment arbitrations have resulted in awards to investors from other regions in the hundreds of millions of dollars.¹ It is time that Latin American investors also take a closer look at the international agreements at their disposal to protect their investments.

The past decade has seen a tremendous growth in the flow of international investment worldwide. Between 1996 and 2006, the annual flow of worldwide foreign direct investment (FDI) nearly tripled, from US\$398 billion to US\$1.2 trillion.² As investors have increasingly looked abroad for investment opportunities, the protections afforded to such investments by international investment agreements (IIAs) such as bilateral investment treaties (BITs) and investments chapters in free trade agreements (FTAs) have become all the more important – particularly in times of market and political volatility. Foreign investors are invoking these investment treaties in disputes with host states, leading to what some commentators have called an ‘explosion’ in investment treaty arbitration.³ Latin American investors, however, are yet to take full advantage of IIAs to protect their investments abroad. Indeed, the number of international investment arbitrations brought by Latin American investors is exceedingly small.

To date, international investment agreements have been invoked most frequently by investors from the United States, Canada or Western Europe. Investors from these capital-exporting regions have relied on IIAs to protect their investments, and, when necessary, to bring claims against host states for measures that have harmed those investments. In contrast, Latin American countries have historically conceived of such agreements merely as a means of attracting investment into the region. Consistent with this conception of international investment agreements and the role of Latin America as a host to foreign investment, Latin American countries have more often found themselves as the respondents in such disputes. This fact is reflected in one recent study of investment arbitrations, which found that nearly half of all claims resulting in awards were brought by investors of the US and Canada, while Argentina and Mexico were named as respondents in almost one-third of the cases.⁴

The time has come for both Latin American investors and governments to rethink their approach to IIAs. The volume of foreign investment originating from Latin American countries is both substantial and growing, and Latin American investors should be paying attention to how these investments can be protected. In many Latin American countries, businesses and individuals with investments abroad have the benefit of extensive protections under international investment agreements – they need only to invoke them. International investment agreements create a ‘two-way street’, protecting Latin American investors abroad just as they do foreign investors who have invested in

Latin America. Investors from Latin American countries should follow the lead of their counterparts in other capital exporting regions and start taking full advantage of arbitration clauses in international investment agreements to protect their investments, both in Latin America and around the world.

Latin American investors are a significant and growing source of foreign investment

There is more than sufficient outbound investment from Latin American countries to justify the use of IIA protections by Latin American investors. Though the majority of Latin American states have historically been, and continue to be, net capital-importing countries, direct investment abroad by Latin American investors has grown substantially in recent years. According to the United Nations Conference on Trade and Development’s (UNCTAD) data on FDI, from 2001 to 2006 the outflow of foreign direct investment from South and Central America⁵ increased by over 700 per cent – from US\$5.2 billion in 2001 to US\$43.7 billion in 2006.⁶ While direct investment abroad has increased worldwide, FDI from Latin American countries has grown more rapidly in recent years, and thus now accounts for a greater proportion of worldwide investment flow abroad than the region did five years ago – over five times greater in 2006 than in 2001.⁷

While a significant proportion of the FDI volume can be attributed to outbound investment from Brazil, the growth in FDI is not limited to any one country. Over the same five-year period from 2001 to 2006, nine different Latin American countries saw at least triple-digit percentage growth in the outward flow of foreign direct investment: Argentina, Belize, Brazil, Colombia, Costa Rica, Honduras, Paraguay, Peru and Venezuela.⁸ Further, seven countries in the region invested more than US\$1 billion abroad in 2006:

- Brazil (US\$28.2 billion);
- Mexico (US\$5.8 billion);
- Chile (US\$2.9 billion);
- Venezuela (US\$2.1 billion);
- Argentina (US\$2 billion);
- Panama (US\$1.1 billion); and
- Colombia (US\$1.1 billion).

In addition, Peru was responsible for US\$428.1 million in FDI outflow in 2006, and Costa Rica, US\$98.1 million.⁹ By the end of 2006, US\$219 billion in foreign direct investment worldwide originated from Latin American countries.¹⁰

UNCTAD’s newly released 2008 World Investment Report provides further insight into developments in the region in 2007. The Report notes that after exceptional growth in 2006, FDI outflow from Latin American countries was not as high in 2007. Nevertheless, according to UNCTAD:

The fall in outward FDI was not caused by a slowdown in the internationalization efforts of Latin American companies; rather, it signified a return to more normal levels after the exceptional year of 2006. Latin American companies, mainly from Brazil and Mexico, are now competing for global

*leadership in such industries as oil and gas, metal mining, cement, steel, and food and beverages.*¹¹

The Report also notes that FDI data for 2007 ‘may underestimate the pace of internationalisation of Latin American companies’, due to significant cross-border acquisitions that are not registered as FDI outflows.¹² Examples include the Mexican company CEMEX’s US\$14.2 billion acquisition of an Australian company, and the US\$2.2 billion acquisition by Argentine company Tenaris of a US oil and gas company, both in 2007.¹³

There is no doubt that Latin American investors are looking internationally for investment opportunities, as the long-term growth and high volume of foreign investment from the region demonstrates. It is time Latin American investors also looked internationally to ensure that these global investments are protected.

International investment agreements provide important protections

Given the growth and volume of foreign direct investment by Latin American investors, it is critical that such investors consider how their investments may be protected. International investment agreements, such as BITs and investment chapters in FTAs, obligate host countries to provide certain protections for foreign investments. Most modern BITs, for example, contain certain standard substantive requirements concerning the treatment of foreign investors, such as prohibitions on expropriation without compensation, and guarantees of national treatment, most-favoured-nation treatment, fair and equitable treatment, and free transfer of funds. If a host government measure contravenes these standards and harms foreign investments, investors may be awarded monetary damages – sometimes hundreds of millions of dollars. As discussed below, these substantive protections afforded by IIAs are generally quite robust.

First, most international investment agreements prohibit host countries from expropriating foreign investment without compensation. This obligation covers various government measures that deprive the investor of the economic value of its investment. In addition, it is not limited to seizures of physical assets, or forced divestitures of assets or equity; it can also extend, for example, to revocations of licences or concession contracts, and, in some circumstances, excessively burdensome regulation.

Second, such agreements generally include national treatment provisions, which require governments to treat foreign investors no less favourably than they treat similarly situated domestic investors. They also often include most-favoured-nation treatment provisions, which extend the same protections afforded to foreign investors from one country to foreign investors from other countries. These two principles seek to ensure equality in the conditions of competition, and any measure that affects this equality could be a violation of an IIA. National treatment and most-favoured-nation provisions may, for example, constrain governments’ ability to place special restrictions on foreign investors through the use of capitalisation requirements or similar measures.

Third, investors are guaranteed ‘fair and equitable treatment’ and ‘full protection and security’ for investments. The fair and equitable treatment standard has been interpreted to require that a state protect investors’ ‘legitimate expectations’ (eg, honour written or even oral assurances made to an investor regarding its investment), provide due process to the investor through courts or administrative tribunals, act transparently and free from ambiguity, and refrain from unreasonable or arbitrary regulatory actions. In addition, pursuant to full protection and security provisions, governments may be required to take reasonable actions to protect investments from theft or harm by private parties.

Finally, international investment agreements often give foreign investors the right to transfer funds into and out of the host country without delay. The transfers typically protected by such provisions include transfers of interest, proceeds from liquidation, repatriated profits and infusions of additional financial resources after the initial investment has been made.

In addition to substantive protections, international investment agreements provide powerful dispute resolution mechanisms. In many IIAs, governments consent in advance to resolve disputes with foreign investors through binding international arbitration. Investors may be entitled to choose between multiple fora, such as arbitration at the World Bank-affiliated International Centre for Settlement of Investment Disputes (ICSID), or before an ad hoc arbitral tribunal organised under the United Nations Commission on International Trade Law (UNCITRAL) Arbitration Rules. Investors have obtained awards in the hundreds of millions of dollars in international arbitrations based on governments’ violations of international investment agreements.¹⁴ These agreements thus provide important protections against government mistreatment, mitigating some of the political risks associated with making investments in foreign countries.

Latin American investors can take advantage of international investment agreements to protect their investments

It is readily apparent that investors from Latin American countries have not taken advantage of the protections provided in international investment agreements to the same extent as investors from other regions. Countries around the world have negotiated over 2500 BITs and numerous FTAs to date. Latin American countries have over 300 BITs in force (in addition to FTAs). Despite the expansive IIA framework already in place for Latin American investors, historically it has been investors from other regions that have turned to international investment agreements to protect their foreign investments. A recent study of investment arbitrations found that of all claims resulting in awards, only three cases were brought by investors of Latin American nationality – just under 4 per cent.¹⁵

The relative scarcity of international investment arbitration claims brought by Latin American investors may in some instances be due to a dearth of investment protections in some countries. Brazil, for example, is one of the largest sources of outbound FDI from Latin America; at the end of 2006 Brazilian investment abroad had reached US\$87 billion.¹⁶ Brazil does not have any BITs in force, however.¹⁷ While the reluctance to ratify international investment agreements may help to limit Brazil’s own exposure to claims by foreign investors, it also puts Brazil’s outbound investors at risk. Given the recent swell in the outflow of Brazilian investment, perhaps it is time that Brazil reconsider its stance against BITs.

Colombian investors are in a similar position. Colombia has seen tremendous growth in outbound foreign investment in recent years, with more than US\$1 billion invested abroad in 2006 alone,¹⁸ and a total US\$10 billion invested abroad through the end of 2006.¹⁹ However, Colombia has BITs in force only with Peru, Spain and the UK.²⁰ Colombia did recently conclude an FTA with the US that incorporates investment protections for Colombian investments in the US, but that agreement is not yet in force.

Given the rate of outbound foreign investment by Brazilian and Colombian companies and individuals, investors might consider approaching their respective governments about the benefits and protections that additional international investment agreements could provide to homegrown investors as they expand abroad.

Importantly, Brazilian and Colombian investors do not have to wait for changes in government policy. Brazilian and Colombian investors (and other Latin American investors, for that matter) can seek to structure their investments so as to take advantage of the protections of BITs between other states. In many cases, an investor can establish a subsidiary in a country that has a BIT with the host state through which to channel its investments. Some BITs require only that the investor be established or incorporated in the home jurisdiction in order to acquire the protections of the BIT.²¹ When Bolivia took steps to nationalise the energy industry, Brazilian gas company Petrobras reportedly considered bringing investment claims against Bolivia for treaty violations by invoking the rights of its subsidiaries in Argentina and the Netherlands.²² Unlike Brazil, both Argentina and the Netherlands have BITs with Bolivia.

In contrast to Brazil and Colombia, the majority of Latin American countries do have a significant number of international investment agreements already in place. For example, Chile has nearly 40 BITs in force²³ and has invested over US\$26 billion abroad.²⁴ A Chilean investor made headlines in recent years when it invoked the Chile–Peru BIT to seek protection for its pasta factory in Peru, in the case of *Lucchetti v Peru*.²⁵ Although the investor ultimately did not prevail, the case focused attention on the use of BITs by Latin American investors even within Latin America.

Mexico is also a source of significant foreign direct investment, with over US\$35 billion in total foreign investment worldwide through the end of 2006.²⁶ FDI outflow from Mexico also rose by 43 per cent in 2007.²⁷ Mexico has 19 BITs in force,²⁸ and is also a party to the North American Free Trade Agreement (NAFTA). As yet, however, there are no reported cases brought by Mexican investors under NAFTA or Mexico's BITs. Notably, while no Mexican investor has arbitrated a NAFTA chapter 11 investment claim against the United States or Canada,²⁹ some 15 investors have filed notices of intent to bring NAFTA investment claims against Mexico.

Argentina has over 50 bilateral investment treaties in force with countries throughout the world.³⁰ While these international investment agreements have been the basis for claims against Argentina by foreign companies, the protections afforded by these international investment agreements extend to Argentine investors as well. These rights have been asserted by Argentine investors only in rare instances, however.³¹ The scarcity of claims by Argentine investors is all the more striking when one considers that by the end of 2006, foreign direct investment from Argentina abroad totalled US\$24 billion.³²

The Dominican Republic–Central America Free Trade Agreement (DR–CAFTA) between the US and the Central American countries of Costa Rica, El Salvador, Guatemala, Honduras and Nicaragua, as well as the Dominican Republic, provides additional investment protections, not only to US investors but also to investors from these Central American countries. Costa Rica, El Salvador, Guatemala, Honduras, and Nicaragua had invested a combined US\$1.2 billion abroad by the end of 2006.³³ As the growth of outward investment from these countries continues, DR–CAFTA will be an important source of investment protection for Central American investors.

Looking ahead

It is critical that Latin American investors consider how their investments may be protected – after years of growth, foreign direct investment from Latin American countries has reached over US\$200 billion worldwide,³⁴ and UNCTAD predicts that FDI outflows from Latin American countries will increase in

2008.³⁵ International investment agreements are not just a tool for investors from traditional capital-exporting regions to assert rights against Latin American host states – they can also be an important tool for Latin American investors. Latin America is no longer just a host for foreign investment; Latin American companies are increasingly emerging as global leaders, expanding the region's investments abroad, and these investors should take full advantage of the international investment agreements at their disposal to ensure that their investments are protected.

Notes

- 1 For example, *France Telecom v Lebanon*, in which the investor was awarded US\$266 million for violations by Lebanon of the France–Lebanon BIT; *Azurix Corp v Argentina*, in which the investor was awarded US\$165 million for violations by Argentina of the US–Argentina BIT; and *Rumeli Telekom AS and Telsim Mobil Telekomunikasyon Hizmetleri AS v Kazakhstan*, in which the investor was awarded US\$125 million for violations by Kazakhstan of the Turkey–Kazakhstan BIT.
- 2 See UNCTAD, *World Investment Report 2007: Transnational Corporations, Extractive Industries and Development – 'Major FDI Indicators' Direct Investment Abroad (FDI Outward) Flow*, <http://stats.unctad.org/FDI> (UNCTAD 2007 FDI Outward Flow).
- 3 See, for example, Susan D Franck, 'Empirically Evaluating Claims About Investment Treaty Arbitration', 86 *North Carolina Law Review* 1, 4 (2007).
- 4 See *id.* at 86 app 1.
- 5 Consistent with UNCTAD's FDI statistics, South America is defined herein to include Argentina, Bolivia, Brazil, Chile, Colombia, Ecuador, Falkland Islands (Islas Malvinas), French Guiana, Guyana, Paraguay, Peru, Suriname, Uruguay and Venezuela; Central America is defined herein to include Belize, Costa Rica, El Salvador, Guatemala, Honduras, Mexico, Nicaragua and Panama. Latin America is used herein to encompass both regions.
- 6 See UNCTAD 2007 FDI Outward Flow, *supra* note 2.
- 7 See *id.*
- 8 See *id.*
- 9 See *id.*
- 10 See UNCTAD, *World Investment Report 2007: Transnational Corporations, Extractive Industries and Development – 'Major FDI Indicators' Direct Investment Abroad (FDI Outward) Stock*, <http://stats.unctad.org/FDI> (UNCTAD 2007 FDI Outward Stock).
- 11 UNCTAD, *World Investment Report 2008: Transnational Corporations and the Infrastructure Challenge*, p60, available at www.unctad.org/Templates/webflyer.asp?docid=10502&intItemID=2068&lang=1 (UNCTAD World Investment Report 2008).
- 12 *Id.*
- 13 See *id.* at p81, n77 (explaining that the acquisition by CEMEX is not reflected in Mexican outward FDI because it was financed through CEMEX's foreign affiliates, while the acquisition by Tenaris is not reflected in Argentinean outward FDI because the company is headquartered in Italy).
- 14 See *supra* note 1.
- 15 See *supra* note 3.
- 16 See UNCTAD 2007 FDI Outward Stock, *supra* note 10.
- 17 See UNCTAD, *Total Number of Bilateral Investment Agreements Concluded*, 1 June 2007 – Brazil, available at www.unctad.org/Templates/Page.asp?intItemID=2344&lang=1.
- 18 See UNCTAD 2007 FDI Outward Flow, *supra* note 2.
- 19 See UNCTAD 2007 FDI Outward Stock, *supra* note 10.
- 20 See SICE: Foreign Trade Information System, *Colombia: Bilateral Investment Treaties*, www.sice.oas.org/ctyindex/COL/COLBITs_e.asp (last visited September 26, 2008).

- 21 The BIT between Lithuania and the Ukraine, for example, defines an investor to be 'any entity established in the territory of the [contracting state] in conformity with its laws and regulations', requiring only that an investor be legally organised or incorporated in the home state in order to acquire the protections of the BIT.
- 22 See Luke E Peterson, 'Analysis: Foreign Investors Still in the Dark as to Terms of Bolivian Nationalisation', *Investment Treaty News*, May 16, 2006.
- 23 See UNCTAD, Total Number of Bilateral Investment Agreements Concluded, 1 June 2007 – Chile, available at www.unctad.org/Templates/Page.asp?intItemID=2344&lang=1.
- 24 See UNCTAD 2007 FDI Outward Stock, supra note 10.
- 25 See *Lucchetti v Peru*, ICSID Case No. ARB/03/4.
- 26 See UNCTAD 2007 FDI Outward Stock, supra note 10.
- 27 See UNCTAD World Investment Report 2008, supra note 11, at p60.
- 28 See UNCTAD, Total Number of Bilateral Investment Agreements Concluded, 1 June 2007 – Mexico, available at www.unctad.org/Templates/Page.asp?intItemID=2344&lang=1.
- 29 Mexican company Signa SA filed a notice of intent to bring a NAFTA Chapter 11 claim against Canada in 1996, but arbitration was never commenced and Signa later withdrew the notice.
- 30 See UNCTAD, Total Number of Bilateral Investment Agreements Concluded, 1 June 2007 – Argentina, available at www.unctad.org/Templates/Page.asp?intItemID=2344&lang=1.
- 31 See, for example, *Maffezini v Spain*, ICSID Case No. ARB/97/7, Award of November 9, 2000 (concerning an Argentine investor's claim against Spain under the Argentina–Spain BIT).
- 32 See UNCTAD 2007 FDI Outward Stock, supra note 10.
- 33 See id.
- 34 See id.
- 35 See UNCTAD World Investment Report 2008, supra note 11, at p66.



1501 K Street, NW
Washington, DC 20005
United States
Tel: +1 202 736 8000
Fax: +1 202 736 8711

Stanimir Alexandrov
salexandrov@sidley.com

Nicolás Lloreda
nlloreda@sidley.com

Patricio Grané
pgrane@sidley.com

Meredith Moroney
mimoroney@sidley.com

www.sidley.com

Sidley Austin LLP's international arbitration practice is comprehensive and truly global in reach, with experience in arbitral fora ranging from London to Washington to Hong Kong. In addition to a full international commercial arbitration practice, Sidley is particularly known for its substantial practice in the high-profile field of investor-state (investment treaty) arbitration.

Sidley represents multinational companies as claimants, and sovereign governments as respondents, in disputes over government actions that allegedly injure foreign investments. Sidley lawyers also serve as arbitrators in investor-state cases, and Sidley has one of the largest dockets of any firm of ICSID and UNCITRAL cases.

In tandem with its investor-state arbitration practice, the international arbitration team advises Sidley's corporate clients on structuring multinational transactions to take advantage of the protections and arbitration options that investment treaties have to offer.

Sidley's investment treaty team includes lawyers who have served in government negotiating, and overseeing negotiations of and disputes under, bilateral and multilateral investment treaties. Sidley lawyers have served as arbitrators in investor-state disputes, have been appointed by governments to serve on standing rosters of arbitrators, and have taught courses and seminars in investment treaty arbitration.

About the Authors



Stanimir Alexandrov
Sidley Austin LLP

Stanimir Alexandrov is the head of the international arbitration practice at Sidley. Mr Alexandrov focuses his practice on international dispute resolution, including investor-state arbitration, international commercial arbitration, and resolution of trade disputes before the World Trade Organization (WTO). He has represented private parties and governments in arbitration before the International Centre for Settlement of Investment Disputes (ICSID), as well as in ICC, UNCITRAL and AAA international arbitrations. He has also represented governments in WTO disputes. Mr Alexandrov has been appointed to ICSID's panel of arbitrators and panel of conciliators and serves as an arbitrator in a number of cases under the arbitration rules of ICSID, the London Court of International Arbitration and UNCITRAL.



Meredith Moroney
Sidley Austin LLP

Meredith Moroney is an associate at Sidley. She focuses her practice on international trade and dispute resolution. Prior to joining Sidley, Ms Moroney graduated from the University of Virginia School of Law, where she served as editor-in-chief of the *Virginia Journal of International Law*.



Patricio Grané
Sidley Austin LLP

Patricio Grané is an international lawyer at Sidley. He focuses his practice in the area of international dispute resolution, with particular emphasis on international arbitration under investment treaties and matters regarding the World Trade Organization (WTO). He advises sovereign clients and private parties in trade and investment disputes. His experience in international arbitration under investment treaties includes work on behalf of both multinationals and foreign governments. He has also represented developed and developing countries in dispute settlement proceedings under the WTO, where he has argued before panels and the Appellate Body.



Nicolás Lloreda
Sidley Austin LLP

Nicolás Lloreda is an international lawyer at Sidley. His practice focuses on international business transactions, trade and investment policy, and international dispute resolution, with experience in international arbitration, intellectual property matters and trade negotiations. Mr Lloreda previously served as director general of the Andean Community. His trade negotiations experience includes leading the legal team for the preferential trade talks with Brazil and Argentina, as well as participating in the negotiations for the Free Trade Area of the Americas (FTAA). In 2006, Mr Lloreda was appointed by the government of Colombia as a mediator before ICSID.