

UNDERSTANDING THE MOST-FAVORED-NATION CLAUSE IN THE INTERNATIONAL INVESTMENTS LAW*

ENTENDENDO A CLÁUSULA DE NAÇÃO MAIS FAVORECIDA NO DIREITO INTERNACIONAL DOS INVESTIMENTOS

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ABSTRACT: This writing seeks to understand the meaning and scope of most-favored-nation clause in international treaties on investment. This clause is frequently present in these international instruments, but its definition is uncertain, in part because of the difficulties of adopting a uniform definition for all situations, also by its own nature (minimum standard) or general clause. Thus, from a specific case we seek to understand how the arbitral tribunal of the International Centre for Settlement of Investment Disputes - ICSID, applied the clause in the arbitration proceedings proposed by the Siemens A.G., against the Argentina Republic (Case n. ARB/02/8). Finally, we present some boundaries for the matter without, however, achieving a definitive conceptualization of most-favored-nation clause.

Keywords: Investment international. Most-favored-nation clause. International arbitration. ICSID.

RESUMO: Nesse artigo busca-se compreender o significado e alcance da cláusula de nação mais favorecida nos tratados internacionais sobre investimentos. Essa cláusula é frequentemente presente nesses instrumentos internacionais, mas sua definição é incerta, em parte por causa das dificuldades de adotar uma definição uniforme para todas as situações, também pela sua própria natureza (padrão mínimo) ou cláusula geral. Assim, a partir de um caso específico busca-se compreender como o tribunal arbitral do Centro de Solução de Disputas de Investimento - ICSID (em língua inglesa), aplicou a causa em um processo arbitral proposto pela Siemens A.G., em face da República da Argentina (Caso n. ARB/02/8). Finalmente, apresenta-se alguns contornos para o assunto sem, entretanto, apresentar uma conceituação definitiva para a cláusula de nação mais favorecida.

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1. INTRODUCTION

In this writing, we seek to understand the meaning of most-favored-nation clause therefore; we divided this analysis into two parts, a mostly theoretical and other more pragmatic. As we know the clause frequently visit the international treaties and arbitration award, therefore, in this paper we present one different treatment of the subject.

We adopted as work methodology the bibliographical analysis and one decision in international arbitration involving a recent dispute in the arbitral tribunal of the International Centre for Settlement of Investment Disputes - ICSID, in the case Siemens A.G. v Argentina Republic (Case n. ARB/02/8). From there, we have established some assumptions for purposes of empirical verification.

Our assumption is that international investments are necessary instruments for promoting the development and ensure the maximum access to materials progress of humanity, diversity of ideas, cultures etc. However, arising conflicts in the field of international investments, we can understand that arbitration is the most appropriate means to resolve the various problems originating in the investment international treaties.

In terms of arbitration in international investment it is worth saying that it is a process highly specialized for the resolution of conflicts between host States and international investors. Thus, we comprehend the arbitration as a mechanism to ensure some fundamental rights and guarantees, for example the private property, due process, protection against arbitrary acts or discriminatory, protection of the legitimate expectation, transparency, proportionality etc.

Maybe for this, confirming its relevance and actuation, the 116th Annual Report, published on 23 March 2017, of the Permanent Court of Arbitration affirm that:

During 2016, the Permanent Court of Arbitration ("PCA") administered 148 cases, 40 of which were initiated that year, comprising: [i] investor-state arbitrations arising under bilateral/multilateral investment treaties or national investment laws; [up until] conciliation between a private party and a public entity [...]¹

However, how can we understand the most-favored-nation clause? Christoph Schreuer² wrote that "[the] provision on most-favored nation (MFN) treatment seeks to settle a contentious question. It gives an unmistakably negative answer to the question whether MFN clauses apply to dispute settlement."

In the face of this, in this research we present some contributions and foundations to understand better the meaning and scope of most-favored-nation clause, applied in international investment arbitration proceedings, in terms of foreign investment. Taking into account, the characteristics of host States and foreign investors seek an approximation conceptual framework reasonably inferred about the subject.

The imprecision or conceptual variation of the clause may compromise the legal security and, consequently, the realization of international investments. We seek, then, from a bibliographic survey preliminary understand its meaning ordinary. To define its scope we chose a qualitative sample from a specific case analyzed by the ICSID, the case n. ARB/02/8, arbitration procedure proposed by the Siemens A.G. (a Germany company), against the Argentina Republic. In this

¹ PCA. (2016). **116th Annual Report**, pp. 08.

² SCHREUER, C. (2016). **The development of International Law by ICSID Tribunals**. ICSID Review, Vol. 31, n. 3 (2016), pp. 737.

case, among other issues, the most-favored-nation clause was crucial for problem analysis between the host State and foreign investor by ICSID (Decision on jurisdiction).

2. FIRST PART: MEANING AND SCOPE OF MOST-FAVORED NATION CLAUSE

How do we know the most-favored-nation clause compose the international minimum standard. Certainly when interpreting an international treaty we are faced with a clause this, whose definition is imprecise. Of course, we know that the prevailing idea of equality on the international scene, that is why it is unacceptable for the different treatment among foreign investors who are in similar situations.

Especially when we think in terms of globalized economy marked by strong decentralization of economic capital, we understand the expressiveness and importance of foreign investments and especially of the mechanisms for resolving their conflicts. Everything indicates that Charles Oman, in this vision suggests:

The new term "new forms of investments" covers a broad and heterogeneous range of international corporate activities the all have a common denominator: a foreign company supplies goods (tangible or intangible) to an investment project or enterprise in a host country - goods that constitute assets for the investment project on enterprise - but local interests in the host country retain majority or whole ownership of the investment project enterprise.³

In addition, second the Organization for Economic Co-operation and Development - OECD (2006), the "Bilateral Investment Treaties constitute an

³ OMAN, C. (1989). OECD - **Development Centre Studies. New forms of investment in developing country industries: mining, petrochemicals, automobiles, textiles, food.** Paris: OECD, pp. 10.

important pillar of investment protection at the international level.”⁴ If the legal security is fundamental to perform any financial investment, speaking on international investments, we need even more.

With a view to avoiding, undue the discrimination improper between States, among other rules and principles, since 1778 was inserted the first most-favored-nation clause in the treaty between The United States and France. In 1974, the International Law Commission of the United Nations described the clause as:

1. Under an unconditional most-favoured-nation clause the beneficiary State acquires the right to treatment not less favourable than that accorded by the granting State to a third State, without the obligation to reciprocate the same treatment in kind to the granting State.⁵

In the fifth footnote, the Commission shows an illustrative example, which we transcribe them below part of it content:

For example, State X reduces its tariffs on oranges imported from State Y against the reduction by State Y of its tariff on textiles imported from X. If State X has made a most-favoured-nation pledge to State A, it has to concede the same reduced rate of tariffs on the oranges imported from that State as it has conceded to State Y, and it has no right to claim from State A a reduction of its tariffs on textiles or any other concession in turn.⁶

Still according to the OECD (2004), the most-favored-nation clause is, “[an] investor from a party to an agreement, or its investment, would be treated

⁴ OECD. (2006). **Policy brief: International Investment Agreements Concluded by MENA Countries**, Issue 3, pp. 10.

⁵ UNITED NATIONS. (1974). **International Law Commission. Yearbook of the 1974: documents of the twenty-sixth session: reports of special rapporteurs, other documents submitted by members of the Commission and report of the Commission to the General Assembly**. (Part one) Vol. II. pp. 118.

⁶ Cf. commentary to articles 6. Ibid., pp. 118.

by the other party 'no less favourably' with respect to a given subject-matter than an investor from any third country, or its investment."⁷

In another passage, a little later, the Organization (2006) clarifies that: "According to the MFN principle, once a country has accorded a given treatment to a foreign investor or a foreign investment of a particular state, it cannot grant less favourable treatment to any other investor or investment coming from a different state."⁸ Determining that, in similar circumstances, the member (States parties) of an agreement bilateral, regional or multilateral investment cannot get treatment less favorable, in relation to a third State.

In both writings, the OECD (2004; 2006), it presents as an example the text of the General Agreement on Tariffs and Trade - GATT (1986) that has on:

PART I Article I

General Most-Favoured-Nation Treatment

1. With respect to customs duties and charges of any kind imposed on or in connection with importation or exportation or imposed on the international transfer of payments for imports or exports, and with respect to the method of levying such duties and charges, and with respect to all rules and formalities in connection with importation and exportation, and with respect to all matters referred to in paragraphs 2 and 4 of Article III,* any advantage, favour, privilege or immunity granted by any contracting party to any product originating in or destined for any other country shall be accorded immediately and unconditionally to the like product originating in or destined for the territories of all other contracting parties.⁹

However, how we know, it is important to note that most-favored-nation clause is not the same in investment arbitration and in World Trade Organization - WTO system. In the first one, the application depends on the BIT

⁷ OECD. (2004). **Most-Favoured-Nation Treatment in International Investment Law**, Working Papers on International Investment, pp. 02.

⁸ Ibid., pp. 23.

⁹ GATT, 1986, pp. 02.

terms. In the second one, the application is immediately between the States members.

As rule, the WTO determines that if one of its members to grant certain advantage to another Member-State, it is established the extension to the other. Obviously, subject to the exceptions on the cooperation agreements and the common markets, for example, but remember: in investment, arbitration is different. That is to say, also, it is important to note that the application of most-favored-nation clause is not the same in investment arbitration and the WTO system.

Additionally, the clause was inserted in the Model BITs of Countries like Germany (1998) and Netherlands. Also in bilateral treaties between Albania and United Kingdom; US and Canadian; UK and Bolivia; Canada and Uruguay; in free trade treaties, as for example, US-Chile FTA, US-Singapore FTA, Canada-Chile FTA etc., in the Protocol for the Promotion and Reciprocal Protection of Investments in the MERCOSUR etc.

In general, the most common characteristics of these predictions are two: first, the treatment no less favorable and, second the accords in like circumstances. As indicated by OECD (2004), "Despite their prevalence in investment treaties, MFN clauses do not have a universal meaning. Indeed, the formulation and application of MFN clauses varies widely among investment treaties."¹⁰

Therefore, we ask what would be the limits of the most-favored-nation clause? It seems that this concern was already present since 1974, according to the seventh article of "Documents of the twenty-sixth session: reports of special rapporteurs da International Law Commission da United Nations", let us see:

¹⁰ Ibid., pp. 16.

Article 7. The scope of the most-favoured-nation clause regarding persons and things

1. The scope of the persons or things to whose most-favoured-nation treatment the right of the beneficiary State extends under a most-favoured-nation clause is confined to the class of persons or things expressly specified in the clause or in the treaty containing it or implicitly indicated by the agreed sphere of relations where the clause applies.¹¹

Still about the limits of the clause, Tony Colle (2012) says there is three limits, to know: "solely to more favorable treatment provided after the agreement is negotiated"; "favorability" and "not merely provide to the beneficiary any more favorable treatment provided to a third party". That is why the author¹² speaks in "instantaneous obligation", however, more forward clarifies that it is not rewrite the agreement originally entered into between the parties¹³, but to build the sense of this general clause.

The principle of non-discrimination, when applied in bilateral or multilateral relations, does not present a uniform solution. As we have said, the presupposition of most-favored-nation clause is the non-discrimination between two States, based on a bilateral treaty or multilateral with economic ends.

In fact, according to said Emmanuel Gaillard (2005), "[the] applicability of an MFN clause to dispute settlement arrangements is chiefly determined by the language of the clause."¹⁴ For this reason, beyond to the linguistic limitations

¹¹ UNITED NATIONS. (1974). International Law Commission. Yearbook of the 1974: documents of the twenty-sixth session: reports of special rapporteurs, other documents submitted by members of the Commission and report of the Commission to the General Assembly. (Part one) Vol. II. pp. 122.

¹² COLE, T. (2012). **The boundaries of most favored nation treatment in international investment law**, Michigan Journal of International Law, v 33, n. 537, pp. 570.

¹³ Ibid., pp. 572.

¹⁴ GAILLARD, E. (2005). **Establishing jurisdiction through a most-favored-nation clause**. New York Law Journal (International Arbitration Law), Vol. 233, n. 105, Thursday, June 2, 2005.

that the clause text can present, we understand how other possible examples of limits the essential good faith and the objectives of the parties.

Colle also claims that the "Mere invocation of an MFN clause does not gain the beneficiary all more favorable treatment currently being provided to third states, as would a general non discrimination (*siç*) clause."¹⁵ On the contrary, of the simple allegation we need a bit more to sustain its applicability in the case, in other words, the existence of at least two bilateral or multilateral agreements; not be foreseen in the exceptions on the agreement itself; must be present in the agreement concluded at a later date, among other requirements.

To prohibit discriminatory treatment between the interlocutors economic, emerge an apparent contradiction, this is because in a first moment indicates a treatment most favored a particular foreign investors; but, if we look more closely, in fact, we know that it represents a special form of protection do not have different treatments, without due cause.

Summing up the arguments presented. In the past lines remained the fact that the most-favored-nation clause, regulating in a generic form various matters, the dilemma that presents itself is whether in the face of each clause analyzed what is your content and your reach. We build the answers to each case. Therefore, in order to facilitate the understanding we will illustrate with a concrete situation, now for your exam.

3. SECOND PART: UNDERSTANDING THE CONCEPT FROM A PRACTICAL CASE - A EMPIRICAL EVIDENCE

¹⁵ Ibid., pp. 562.

3.1. The context

We studied the lines passed the most-favored-nation clause delimited by from the particularities of the case and, is this the objective that we seek to materialize in this topic. The classic case about the clause was the Anglo-Iranian Oil Company (1952), since then, many other cases have arisen as the Maffezini v. Spain (2000), Salini v. Jordan (2004), Plama Consortium Limited v. Bulgaria (2005), Siemens v. Argentina (2007) etc.

As have said, now that we know the substance of the clause, for this purpose we are going to spend studying from the case Siemens v. Argentina¹⁶, will analyze the most-favored-nation clause, in the light of this recent example.

Therefore, let is talk about the event started on July 17, 2002, in the International Centre for Settlement of Investment Disputes - ICSID, installed in Washington, D.C., the arbitration procedure, with the arbitration rules of the ICSID itself. This case was proposed by the Siemens A.G. (Claimant), against the Argentina Republic (Respondent State), having as basis the treaty between Argentina - Germany BIT (1991).

With award (final decision) dated in 6 February 2007, by Tribunal composed by Andrés Rigo Sureda (Spanish), President; the arbitrator Charles N. Brower (U.S.); and the arbitrator Domingo Bello Janeiro (Spanish), that after regular processing of the arbitration procedure, was favorably decided upon for the of investor (Claimant). Let the facts.

3.2. The facts

¹⁶ ICSID case n. ARB/02/8, Siemens, AG v. Argentina, arbitration award of 06/02/2007.

According to decision on jurisdiction (03 August 2004), the controversy appreciated by the arbitral tribunal had origin in one informatics services contract for the implementation of the system of immigration control. This system has been installed by Siemens for the Argentina Republic in 1996, so-called Siemens Nixdorf Information's System AG (SNI), performed by the Siemens IT Services S.A. (SITS).

In 1988, the parties concluded a contract of six years renewable for the same period (two periods of three years each). The Respondent, alleged technical problems, in February 2000 suspended the payment of the contract; being ended definitively in November 2001, but on this occasion was alleged issued under emergency Law.

Explaining a bit about the political and economic situation of Argentina, during this period, the country faced a severe economic crisis, fact that led it to review many contracts assumed by the previous government. The situation was also marked by a problematic political scenario, which for reasons of space we will not delve into the motives. The fact is that when reviewing these commitments, the host State understood the end of the contract with the foreign investor.

The Claimant invoked "a breach of the Treaty between the Federal Republic of Germany and the Argentina Republic (1991), concerning the Reciprocal Encouragement and Protection of Investments".¹⁷ Furthermore, by cancellation of the contract, the Siemens understood that there was a misuse indirect expropriation.

¹⁷ ICSID case n. ARB/02/8, paragraph 27.

3.3. The problem

Many were the issues considered by tribunal arbitral, but we will concentrate here on the controversies surrounding the most-favored-nation clause. Therefore, in this first moment, the parties disagreed on the interpretation of the treaty, basically, on the following points:

- a) General or specific character of the MFN clauses in Article 3;
- b) If the MFN clauses in Article 3 are considered general clauses, rationale of the MFN clause in Article 4;
- c) Effect of reference to national treatment on the scope of the MFN clause;
- d) Effect on the scope of the MFN clause of the right of the State to bring the dispute to its courts;
- e) Claim of a benefit under a treaty by the operation of an MFN clause as triggering application of all the provisions of that treaty.¹⁸

To we understand the significance of the demand, transcribe the article in question, let us see:

Article 3(1): None of the Contracting Parties shall accord in its territory to the investments of nationals or companies of the other Contracting Party or to investments in which they hold shares, a less favorable treatment than the treatment granted to the investments of its own nationals or companies or to the investments of nationals or companies of third States.

Article 3(2): None of the Contracting Parties shall accord in its territory to nationals or companies of the other Contracting Party a less favorable treatment of activities related to investments than granted to its own nationals and companies or to the nationals and companies of third States.¹⁹

3.4. Divergent points of view with the same basis

¹⁸ Ibid., para. 79.

¹⁹ Ibid., para. 82.

The Claimant support, essentially, the violation factual and temporal of the bilateral treaty, contesting its restrictive interpretation. "Siemens considers that 'the existence of treaties with diverse provisions is not an argument against the application of an MFNC but a necessary precondition for its application.'"²⁰

In turn, the Respondent maintains in its defense the most-favored-nation clause present in the treaty between "Argentina and Chile concerning the Reciprocal Encouragement and Protection of Investments of October 2, 1991"²¹, that ensures the local jurisdiction (domestic jurisdiction) with a period of eighteen months to reply the parties. Soon, if we understand this way the consequence will not appreciation of the demand by arbitral tribunal (ICSID).

Support also that the concept of investment is large enough to cover the issue of contract with the immigration system. "As a final point, Argentina finds that the Tribunal should not consider as purely temporal the requisite that investors bring an investment dispute before a local court."²² We understand, therefore, that both sides invoked the most-favored-nation clause, in opposite directions and with results quite different.

3.5. The decision

In the decision on jurisdiction (2004), the ICSID understood that "It is a treaty 'to protect' and 'to promote' investments."²³, and as such should be interpreted in this sense. About the scope of the word "activity" contained in third article:

²⁰ Ibid., para. 71.

²¹ Ibid., para. 32.

²² Ibid., para. 59.

²³ Ibid., para. 81.

Treatment in Article 3 refers to treatment under the Treaty in general and not only under that article. For these reasons, the Tribunal finds that a plain and contextual reading of Article 3(1) and (2) does not limit the treatment to transactions of a commercial and economic nature in relation to exploitation and management of investments as alleged by Argentina.²⁴

Putting an end to the controversy "The Tribunal concurs that the formulation is narrower but, as concluded above, it considers that the term 'treatment' and the phrase 'activities related to the investments' are sufficiently wide to include settlement of disputes."²⁵

However, there is no reason to "[the] exhaustion of local remedies rule and that that rule may not be tacitly waived."²⁶, second alleged by the Respondent in his defense. In this way "As already indicated, the Tribunal considers that the public policy considerations adduced by the Respondent are not applicable."²⁷

Thus, as stated in the first part of this writing, the arbitral tribunal, in this arbitration procedure, establish that: "Each treaty may carry advantages and disadvantages, and the MFN clause 'implies the right to select those aspects of provisions in different treaties that favor the MFNC's beneficiary most.'"²⁸ More specifically, "Even if the MFN clause is of a general nature, its application will be related only to the benefits that the treaty of reference may grant and to the extent that benefits are perceived to be such."²⁹

In summary, the arbitral tribunal considers that "Therefore, a literal reading of the Treaty does not support the allegation that the definition of investment excludes indirect investments."³⁰ Therefore, in this stretch of the

²⁴ Ibid., paras. 85-86.

²⁵ Ibid., para. 103.

²⁶ Ibid., para. 104.

²⁷ Ibid., para. 109.

²⁸ Ibid., para. 116.

²⁹ Ibid., para. 120.

³⁰ Ibid., para. 137.

decision is possible to affirm that the appropriate interpretation was to remove the argument of prior knowledge by the domestic jurisdiction and analyze the potential violations of the treaty between the Federal Republic of Germany and the Argentina Republic (1991), thus, assured the extension of a condition most favorable.

Commenting on the case analyzed, Gaillard³¹ explains how the Tribunal recognize the application of the clause, let us see:

This principle was similarly adopted by the Siemens v. Argentina Tribunal, which had to decide whether the investor could initiate an arbitration after the six-month negotiation phase as provided for in the Chile Argentine BIT rather than after exhausting the local remedies during an 18-month period as provided for by the applicable Germany-Argentina BIT [...]

Because of this decision, that allowed the continuity of the arbitration proceedings, and the decision on award of Tribunal in 2007 (decision of merit). According to which, the Argentina argued in its favor the most-favored-nation clause, requested the privilege or right that should firstly submit it to the local courts after six months its notification. Supporting as a precedent cases *Plama Consortium Ltd. v. Republic of Bulgaria* and *Salini Construttori, S.p.A. & Italstrade, S.p.A. v. Hashemite Kingdom of Jordan* on the application of the most-favored-nation clause.

However, "The Tribunal will limit itself to observe that the cases adduced by the Respondent deal with the application of the MFN clause to situations not akin to the instant case.",³² is a different extension of the case analyzed. Consequently the need to understand the meaning of the clause from each concrete situation.

³¹ GAILLARD, E. (2005). **Establishing jurisdiction through a most-favored-nation clause.** New York Law Journal (International Arbitration Law), Vol. 233, n. 105, Thursday, June 2, 2005.

³² Ibid., para. 68.

Although of the Tribunal already decided this point, the Respondent persist in the need for the submission prior to the domestic jurisdiction. "For that reason, Argentina's argument that simple acts of maladministration by low-level officials should be pursued in the local courts lacks validity in the circumstances of the instant case."³³ However, again without reason.

On another occasion, the theme of most-favored-nation clause is resumes. This time, about the compensation, more especially on the value of the compensation of the investment, obtained with the support of "experts to calculate". Therefore, the reach of the clause refers to the issues interpretative, and the Tribunal "Having reached this conclusion, it is unnecessary for the Tribunal to discuss the argument advanced by the Claimant that it is entitled to the fair market value of its investment on the basis of the MFN clause in the Treaty."³⁴

Finally, the Tribunal unanimously decided "1. that the Respondent breached Article 4(2) of the Treaty by expropriating Claimant's investment without complying with its terms;"³⁵, condemning the Argentina Republic the payment of approximately de amount of US\$ 460 million and "[...] shall be paid in dollars."³⁶

4. FINAL CONSIDERATIONS

Assuming that we have discussed throughout this writing, present as a conclusion to the existence of difficulties to define the expiration the meaning

³³ Ibid., para. 272.

³⁴ Ibid., para. 353.

³⁵ Ibid., para. 403.

³⁶ Ibid., para. 361.

of the most-favored-nation clause. Although, his generic formula is able to cover different situations, needs to be materialized in each situation analyzed. Fact that *per se* not mean the complete casuistry.

Thus, when we seek the meaning and scope of the hermeneutic activity should make use of principles of International Law, as is the case of fair and equitable treatment (good faith). It is worth saying, however, that the most-favored-nation clause not is a principle of International Law, even because, we can only apply the clause if it is provided for in the treaty as an obligation of States-Parties.

In the light of the principle of non-discrimination, we can remove different interpretations with different impacts on application; thus, require a tailored solution, always depending on the particular characteristics of the concrete situation. Especially when it comes to bilateral treaties on investments, the rules feature dimensions of two natures, one general and one particular, as we can see.

Finished, the most-favored-nation clause is one of the main substantive rights that investors have based on the principle of equality (non-discrimination). Summarize, the provisions may even be similar, but in practice should be interpreted in different ways depending on the facts of each case.

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