March 15, 2024

Proposed Guide on ISDS Management

by

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I. Introduction

1. This note has been prepared with the objective of providing UNCITRAL Working Group III with an experienced perspective, based on real policies and best practices, aimed at providing a Guide to help [respondent] States outline a general strategy towards Investor State Dispute Settlement (ISDS), enabling them to make better decisions about:

i) Early dispute prevention by rapidly resolving foreign investors' concerns;
ii) Efficient and prompt dispute settlement by entering into efficient and effective [settlement] transactions with foreign investors, and/or;
iii) Adequate defence of rights and interests before international tribunals, in case prevention or early settlement of disputes are not achievable.

2. In that sense, the proposed Guide is designed to assist States to build a system that, by creating a centralized coordination unit with specific competences and capabilities, should allow them to manage their disputes (and overall relations) with foreign investors, under a uniform and consistent perspective, avoiding contradictions and significantly reducing risks and costs, by building and strengthening the internal capacity of States, without altering or affecting their model, structure, and organization.

II. Assumptions

3. This document is prepared under the assumption that states are sovereign entities, with the supreme authority to govern their own territories, enact laws, and conduct their affairs without external interference. Having international legal personality, they are subjects of international law with rights and duties, with the capacity to defend their rights and interests against their peers and others; to issue binding statements; to enter into bilateral and multilateral treaties and to relate to other states in the manner they consider appropriate.

4. All States are equal under international law, enjoying equal sovereignty and legal standing. States can be held responsible for their actions under international law, including responsibility for violations of international law, for which they may be subject to corresponding legal consequences, including in the sensitive matter of ISDS.

5. Although there are existing similarities between governmental configurations, policies and practices, each State is different from any other, they are governed and administrated differently and have different concerns and their own particular objectives, in relation to Foreign Direct Investment (FDI) and Investor-State Dispute Settlement (ISDS)

6. Foreign investors are nationals typically protected by Bilateral Investment Treaties (BITs). While not legal persons under public international law, but an effect of said international treaties is to enable them to initiate claims against states in international fora, where States are most vulnerable.

7. Under Public International Law, States are indivisible entities, wholly responsible for the decisions and acts of all of their components and representatives, independent of their length of time in office or whether they are still in office or whether they served with small or large jurisdictions, authorities, and powers (whether in local governments without anticipating the international consequences of their actions).

III. ISDS Management Structure

8. The problems and apparent imbalances that ISDS poses to respondent States explains the existence of Working Group III. Dealing with the protection of FDI, has become the responsibility of investment recipient States, and ISDS is a new reality for the international community. The Working Group III and others will propose reforms in the system, investment courts may co-exist with ad hoc arbitration, codes of conduct and other reforms pursued. International organizations and others offer assistance to States, and there is much academic attention to the challenges they confront. Among the assistance to be offered is the proposed Advisory Center that Working Group is on the verge of adopting.

9. It is the author's view that, after all is said and done, that what States require is something else: a well-organized and efficient internal structure to fully take advantage of t the many aspects of such reforms. In other words, a well-designed ISDS Management structure with the proper capacities and competences should guarantee the state the best approach and best practices for preventing and managing ISDS cases and improving its relations with foreign investors and members of the international community.

10. For implementing an internal structure for the response and defense of a sovereign's international interests, a State may believe it would be preferrable for it to be created by a specific Law. In the author's view this is because foreign investment disputes are initiated under in public international law fora viz an international arbitration tribunal; therefore, states' representatives in this forum assume great responsibility. For this reason, State representatives may be better protected within the State if their competences and capabilities are clearly stated in such Law.

11. In addition, when reaching the international arbitration phase, investment disputes are often a matter of public and political discussion. For that reason, it is very important to efficiently react and respond to public and political criticism, so damage to the positions, strategies, statements, and actions of the State in such an international forum is avoided.

12. Once the Law has been established as the ruling source of the structure, its agency, and its procedures, it will be essential to provide it with brief, clear and sufficient powers, and functions, carefully drafted in order to prevent contradictions, aimed to protect the rights and interests of the state through preventing, mitigating, and solving investment disputes (assuming all three functions are housed inside the specific structure).

13. The recommended elements such Law should contain, are:

i) General Definitions. Definition of investor-state dispute, foreign investor, and public entity, among others.
ii) Scope of application. Framework and limits of competences of any members of the internal response structure, in particular those of the Leading Agency.
iii) Description of the model to be used for the structure.
iv) Powers, capabilities, competences, limits, and responsibilities of the representatives of the State before investment disputes, as well as for entities, and public officials related to said disputes.
v) Managerial aspects related to budget and hiring mechanisms.
vi) Management of information related to disputes, confidentiality, publicity/transparency rules, and guidelines for the strict coordination of public statements.
vii) Mechanisms for the prevention of disputes and overall capacity building at all State levels.
viii) Rules aimed at establishing coherent and consistent state positions and defenses for future disputes, as well as standardizing dispute resolution provisions.

14. If a law is enacted, it will be important to regulate certain aspects of its content. These regulations should detail certain procedures to be followed in the event of the initiation of a dispute, as well as those aimed at preventing disputes. Likewise, it should detail the specific formalities and procedures for the operation of the Leading Agency, such as budgetary procedures, counsel, and expert hiring procedures, among others.

IV. The Lead Agency

15. The internal structure may be centralized and managed by a small, flexible but solid leading Agency designed to exercise consistent, comprehensive, and coordinated control of the state's response in the event of investment disputes, and its core mission will be to prevent, settle and defend the state when said disputes are initiated by investors or identified/acknowledged by state entities.

16. In the long term, the central Leading Agency should be designed to help the state to have better control of its overall decisions, actions, and statements with respect to the management of disputes, as well as of its relations with investors, and to master the evolution of investment protection treaties, practices, and dispute resolution mechanisms.

17. In our experience, a small but flexible, strong, well-equipped, and organized central Lead Agency[1] is the most efficient method for a state to achieve a timely, cohesive, and detailed approach to potential or initiated investor-state disputes, and; to identify and develop the most accurate and advantageous set of policies and best practices in relation with such sensitive concern.

18. A centralized Agency directing the internal structure for the state's ISDS response and case management has the advantage of maintaining a unique perspective of the state's decisions and activities under the light of their external/international consequences. Its position within the state, its unique competences and capacities allows the Agency to act as a "hinge" between the external forces and the internal situation in the State, and at the same time as a "lighthouse" offering the state the most comprehensive view of the ISDS phenomenon and, therefore the best opportunity to efficiently defend its interests in such forum.

[1] We were 3 lawyers: The author, chairing the Special Commission, a Technical Secretary, and a junior attorney.

19. Acting as a central axis, the Lead Agency is granted a clear vision of both the internal (national) and the external (international) domains the state commonly faces. This allows it to coordinate its responses in such a balanced manner that, when facing claims before international tribunals, avoids entering into contradictions that may affect its defenses.

20. As described below, if used properly a Law-based and well-established Lead Agency would be the best mechanism to prevent and/or settle potential investment disputes, in order to avoid ISDS, or if need be, to be better prepared to face it.

21. *ISDS prevention* usually relies on paying immediate attention to potential disputes. This is an important role for the Lead Agency. Timely action can be a decisive factor in whether a matter becomes an international dispute or not.

In our experience, the Lead Agency was alerted early of cases where, for instance, the parties were unable to reach a solution. In those cases, the Lead Agency immediately searched for consensus. The Agency prepared legal reports regarding the specific risks and costs ISDS will produce, recommended agreeable solutions for both parties, and drafted the proper transaction/settlement documents. These actions allowed the flexibility and protection state officials needed to settle disputes.

22. Capacity building is also key for ISDS prevention. The Lead Agency would prepare intensive and didactic courses, to be taught in a cross-cutting way to all public officials, both central government, regional and local governments, as well as state-owned companies. Courses would be designed to explain to public officials the international consequences of their actions and the responsibilities those actions entail. Likewise, they should include a summary of some of the best practices for anticipating and preventing disputes, as well as avoiding making contradictory statements.

23. *On dispute settlement*, the Lead Agency should have the key capacity to settle the termination of disputes. This allows it to promote and guide dialogues between foreign investors and public entities, in situations where public entities have been unable to engage in productive negotiations by themselves[2].

24. The suggested settlement mechanism, is a fairly simple one:

[2] In the case of Peru, a Special Commission, chaired by the Ministry of Economy and Finance, has the express mandate to negotiate the solution of potential disputes in exclusive representation of the State.

i) The Agency should assume the exclusive representation of the state regarding the dispute, restricting additional channels of communication that may create potential contradictions for the state; consolidating and leading the State's position in relation to the dispute.
ii) Conduct written communication with the investor until a formal settlement mechanism is put in place.
iii) Invite the investors to presential meetings (as many as needed), in order to allow the investor to express its grievances, positions, and claims;
iv) Initiate a confidential settlement process, by signing a Settlement Protocol document, containing the basic rules of the mechanism (good faith, confidentiality, deadlines, and non-binding statements, etc.).
v) Obtain approval, from the Council of Ministers or other highest instance of government, of the transaction solution formula. This is crucial and should also include the mechanism by which a proposed settlement is formally approved by such an instance.
vi) In case of arriving to a solution, always include in the settlement agreement, the investor's express withdrawal of all of its claims.

25. A few advisable practices regarding this very simple mechanism may include:

i) Offer the investor the chance to involve its attorneys from the very beginning of the negotiation process, even if the Lead Agency has not yet involved its own.
ii) Offer the investor the time and tools it may need to present its grievances, claims, and case.
iii) Make all the questions considered pertinent but avoid revealing the state's positions, until it is clear that the parties will engage in a formal negotiation process, leading to a solution.
iv) Finally, always request the investor to sign the minutes of every meeting it attends during the settlement process, so there is evidence of the existence of the meetings.

26. This process has proved very useful for the state to be better equipped to make informed decisions and build an efficient and successful settlement strategy, for several reasons:

i) First, investors find an agency willing and prepared to listen to its grievances and claims, so they are effectively attended, at very low cost for the state.

ii) Second, allowing the investor's legal counsel to participate in the settlement meetings gives the investor peace of mind and allows the state to learn about the investor's legal team and their behavior, in case of arbitration.

iii) Third, as a result of the process, the Lead Agency has a much better idea about the origins, background, and substance of the dispute, about what the investor's real goals and intentions are and about its legal team, in case of arbitration.

27. If as a result of the procedure, the Lead Agency fails to identify common points to settle with the investor, and arbitration is initiated, the Leading Agency will be in a very good position to defend the state's interests before the tribunal.

i) The agency will know its case very well and will not be surprised by claims or arguments that it did not know in advance.

ii) The agency will have met the investor's legal team, so will not be intimidated during the arbitration and will be capable of retaining an equivalent legal team.

iii) Experts and witnesses will already be identified and approached during the negotiations.

iv) Management of the case will be much less costly and much more expeditious.

28. On occasions, investors may attempt to use threats of arbitration to obtain licenses or permits that the State has justifiably denied. Such situations call for a more assertive response from the Lead Agency, such as recommending the withdrawal of frivolous claims; failing which, the Lead Agency will reserve its right to initiate civil or criminal actions, according to its rights and to law. In our experience, this has always proven a highly effective response.

29. As we have seen, direct management of the negotiation phase is very important for the State, allowing it to clearly identify the investor, its attorneys, and the scope of the potential claims, in order to determine a sensible course of action. The State's failure to fully develop and take advantage of direct negotiations could lead to potential problems, weaknesses, and disruptions during the arbitration phase, such as claimant's failure to issue payment for costs among other.

30. If well implemented and used, this stage could be very useful for the State, since it may be the best time to collect, identify and organize documents, communications, experts, and witnesses, in preparation for a potential arbitration. If that happens, the State's position would be much stronger and solid.

V. Autonomy of the Lead Agency and exclusivity of its representation functions.

31. Autonomy is essential for the purposes of preventing and managing investment disputes, and for the correct functioning of the State's internal response structure and the Leading Agency that manages it.

32. The structure/agency implemented by the state will be responsible for safeguarding the rights and interests of the state when in opposition to those of investors. It is important to be clear that the structure and its agency are not meant to provide foreign investors with a special mechanism to attend to their grievances (that function, if it exists, may be housed elsewhere in the government), but to defend the interests of the state when disputes arise. If in the interest of the State, it appears that the most efficient and least costly solution is solving the investor's grievances, then that solution will be applied.

33. As ISDS is a dispute settlement mechanism under international law, the state acts as a whole legal person. In the international arena, the whole state responds for all of the acts of all of its representatives. The Lead Agency will need to always bear in mind that it is defending the rights and interests of "its country", not of any particular administration or local government, or any single ministry. For that reason, it is very important to detach the Lead Agency from the control or influence of government authorities and politicians looking to protect their positions and/or businesses, instead of defending the interests of the state.

34. In that same line, autonomy must be accompanied by exclusivity. When a foreign investor expresses its intention to initiate an international dispute, it may be doing so under the protection of a treaty, or otherwise bringing international law into application, where. states are bound by their statements. For that reason, it is of utmost importance for states to avoid entering into contradictions when involved in an investment dispute. The Lead Agency must be the exclusive voice of the state in relation to every investment dispute. It is key to prevent other state officials from making offers to the foreign investor, not in accordance with the interests of the state, and that the investor will bring before an international tribunal.

VI. Basic Capabilities of the Lead Agency

35. In order to achieve the goal of balancing the internal (local) and external (international) realities of a state, the Lead Agency should need to be invested with certain key competences, such as:

i) capacity to determine its own competence (autonomy);
ii) exclusivity of representation of the interests of the state (including determining responsibility of those unwilling to cooperate);
iii) ability to engage a professional team, including outside counsel (and the necessary budget)

36. The decision about the design of the internal structure depends on the needs and preferences of the state. A variety of flexible models can be designed, be it a collegiate organ, a centralized organ, or an arm of the Attorney General office; in fact, the internal structure, and its exact location within the organization of the state are not as relevant as the fact that it will need to be invested with certain unalterable and exclusive capabilities of its own.

37. Let us repeat the fundamental capabilities (among others) we recommend are:

i) Ability to elaborate and sustain the State's official position regarding a dispute and any facts and/or allegations related to it.
ii) Exclusivity in the representation of the State. Once the representation has been assumed and in order to avoid contradictions, all other public entities must refrain from making statements or rulings regarding the facts in dispute, without previous coordination with the Unit.
iii) Control in the handling of public and press releases issued by the State in relation to the dispute.
iv) Ability to negotiate on behalf of the State.
v) Ability to demand information and collaboration from all public entities and officials.

38. If the Lead Agency is collegiate, the terms of its sessions and the decision-making process shall be governed by its own rules. Its decisions shall be made by agreements, except for decisions which by their nature (e.g., out-of-court settlement or payment of international obligations arising from an arbitral award) must be made by the relevant authorities, such as certain ministers or the cabinet of ministers, according to law.

VII. Results

39. By implementing an internal structure such as that hereby proposed, in the short term the state will be able to observe, a substantial reduction of:

(i) the risks attendant on receiving dispute initiation notices;
(ii) adverse arbitral awards;
(iii) amounts ordered to be paid by tribunals, and;
(iv) legal fees.

40. Also, the state will experience a rapid enhancement of the state's

(i) capacity to prevent disputes;
(ii) confidence in its own public entities and in dispute resolution mechanisms, in general, and;
(iii) control of its responses and public statements.

41. The practices, measures, and policies, detailed in this document are not exclusive and are not intended to preclude others; they are designed to be implemented in coordination and conjunction with any other, measures that States consider necessary and/or useful to implement, so long as they do not dilute the necessary Basic Capabilities.

42. In case clarification or amplification is needed, delegations can write to cjvalderrama@idec.org.pe , or to cjvalderrama@outlook.com