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Arbitration Watch:
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1. Argentina liable for $217 Million in investment treaty arbitration with Siemens,
By Luke Eric Peterson

The Republic of Argentina has found itself on the losing end of another investment treaty arbitration at the DC-based International Centre for Settlement of Investment Disputes (ICSID).

In an award rendered on February 6th, 2007, an ICSID tribunal held Argentina liable for breaches of the Germany-Argentina bilateral investment treaty in relation to its treatment of an investment by German multinational Siemens. The tribunal awarded some $217 Million (US) in compensation to Siemens for its lost investment; however the tribunal rejected a bid by the German firm to collect a further $124 Million (US) for future lost profits.

The award is the fourth to go against Argentina over the course of the last 18 months.

However, the Siemens award also comes at an awkward time for the German firm which has been roiled by a flurry of corruption allegations and official investigations related to its international business operations.

The background to Siemens' arbitration with Argentina was an investment made by the German firm through a local subsidiary in the late-1990s. Siemens had made the successful bid for a contract to develop a national identification and immigration control

system for the Argentine Government. As part of the project, Siemens would oversee the production and distribution of national identity cards (DNIs) for Argentine residents.

The six-year contract – which was automatically renewable for two further three-year terms – went into effect on November 21, 1998.

According to the original plan agreed by Siemens and Argentina, production of DNIs was scheduled to begin in August of 1999. However, as demand for ID cards spiked in the months leading up to the October 1999 elections, the two sides agreed to postpone the roll-out of new ID cards until after the election.

Shortly after new Argentine President Fernando de La Rua came to power, government officials began to speak of the need to renegotiate the price of ID cards, and to increase the number of those cards which would be provided free-of-charge. Indeed, the cost of the ID cards – cards which every Argentine citizen was obliged to hold – was a matter of some public controversy.

When production was started in February of 2000, it very quickly was halted when the Government detected a problem with certain ID cards printed for foreigners. However, Siemens' subsidiary complained that the Government would not authorize it to rectify this mistake and resume production.

Instead, more than a year of negotiations would ensue as the two sides jousted over the contract which had been agreed by the previous Administration of President Carlos Menem.

In November of 2000, the Argentine Congress passed an Economic-Financial Emergency Law, as the country grappled with a growing public sector deficit problem. This Law empowered the President to renegotiate public sector contracts, and Siemens agreed to have its own contract with Argentina governed by this Law – thinking that this step would hasten renegotiation of the deal.

In May of 2001, the Argentine Government presented Siemens with new contract terms. According to the arbitral tribunal's account, when Siemens presented counter-proposals and requested copies of the exhibits accompanying Argentina's own proposal, Argentine officials informed the German company that the new terms were non-negotiable. On May 18th, 2001 the original contract was terminated pursuant to powers granted under Argentina's Emergency Law.

This contract-cancellation gave rise to the ICSID arbitration, as Siemens protested that it had invested (and lost) several hundred Million US Dollars on the project, not to mention that its expectation of future projects were now thwarted.

CORRUPTION ALLEGATIONS DOG SIEMENS, BUT NOT DISCUSSED IN ICSID ARBITRATION AWARD

When the De La Rua Administration cancelled Siemens' contract in May of 2001, the Financial Times newspaper reported that President De La Rua had complained of "the high price being charged by Siemens, and said there had been irregularities surrounding the contract, hinting at suspicions of bribery." ITN could find no further publicly-reported evidence to substantiate this charge.

However, in recent months, Siemens has been at the centre of a widening international corruption investigation by German authorities. Following a police raid in December, and the arrest of six senior Siemens employees, the Wall Street Journal reports that Siemens disclosed that it had uncovered some $540 Million (US) in suspicious transactions over a seven year period, leading the German firm to commission an external audit. Separate investigations have begun in Switzerland, Lichtenstein and the United States to probe the German conglomerate's international business activities.

Earlier this month, the Wall Street Journal reported that a former senior Siemens executive has stated to German investigators that the company paid bribes to Argentine Government officials in the late 1990s in an effort to win a different contract – this one for electronically scannable passports (a document distinct from National Identity Cards). Following a change in Government, the Wall Street Journal, reports that that contract was not awarded to the German firm. The Journal also reports that Siemens describes the Argentine bribery allegations as "false".

While corruption allegations swirl around the German firm, there have been no further reports shedding light on the allegations alluded to by then Argentine President De La Rua in 2001, in relation to the separate contract to produce national identity cards.

What's more, the February 6th award rendered by an ICSID arbitration tribunal in the Siemens-Argentina arbitration is silent on the issue of alleged corruption. At Page 13 of the Award, the tribunal makes a veiled reference to an issue raised unsuccessfully by Argentina at a late stage of the proceeding – an issue which "had been known to the Respondent since 1998, and had not been previously raised" – but there is absolutely no indication as to the identity of this particular issue. Furthermore, the transcript of the arbitral proceedings and the documents filed by the parties in that proceeding are not a matter of public record.

ARBITRATORS FIND SEVERAL TREATY VIOLATIONS

For its part, Argentina characterized the dispute with Siemens as a contractual matter. The Argentine Government alleged that Siemens' local subsidiary had failed to meet certain of its obligations and that the contract needed to be renegotiated given the changing financial circumstances of the Argentine Republic and the need for both contractual parties to share the burden of such a renegotiation.

Argentina and Siemens differed as to whether Argentina was in a state of financial emergency around the time that the Government was urging a contractual renegotiation; the investor acknowledged that Argentina had declared a public deficit emergency in

2000, however Siemens stressed that this was not to be confused with the full-blown financial crisis which beset the country some months later.

Ultimately, the German investor would convince the ICSID tribunal that Argentina had committed several breaches of the Germany-Argentina bilateral investment treaty. In particular, the tribunal held Argentina to have expropriated Siemens' investments, and to have denied the claimants fair and equitable treatment, full protection and legal security, and freedom from arbitrary treatment. (See next item for more details).

The Siemens case was first brought to ICSID in 2002. For a period in 2004-2005, the proceeding was suspended while Argentina pursued an ultimately unsuccessful challenge to the Tribunal Chairman Dr. Andres Rigo Sureda. (See: "ICSID Rejects Challenge to lead arbitrator in Siemens case; Argentina rips decision", April 27, 2005, available on-line at: http://www.iisd.org/pdf/2005/investment_investsd_april27_2005.pdf)

Sources:

Siemens A.G. v. Argentine Republic (Case No. ARB/02/08), Award of February 6, 2007 and Siemens A.G. v. Argentine Republic, Separate Opinion of Prof. Domingo Bello Janeiro, February 6, 2007, both available on-line in the ITN Documents Centre: http://www.iisd.org/investment/itn/documents.asp

2. Analysis: Argentina liable for multiple treaty breaches in Siemens case,
By Luke Eric Peterson

In an arbitration award rendered this month in the ICSID case pitting Siemens against Argentina, the Republic of Argentina has been held liable for several distinct breaches of the Germany-Argentina bilateral investment treaty.

Perhaps most notable, the tribunal found Argentina to have expropriated investments of the German-based multinational Siemens. For its part, Argentina had plead that its treatment of Siemens' investments was a legitimate and proportionate response in the face of "disappointing and inadequate" contractual performance by Siemens' local subsidiary.

Indeed, Argentina invoked the "proportionality test", used by another tribunal in a recent BIT arbitration (Tecmed v. Mexico), in an effort to argue that states ought to be granted a certain degree of deference in determining what constitutes an important matter of public interest - and what sort of interference with foreign investments is warranted in light of the underlying public interest at stake.

Argentina invoked this proportionality approach in opposition to the so-called "effects test" urged by Siemens – an analysis which focuses exclusively upon the impact or effect of government measures upon a given investor, without considering the public interest or motive underlying those government measures.

(The “proper” approach to defining expropriation is a matter which has preoccupied multiple arbitration tribunals, leading to differing approaches in different cases. In a parallel move, certain governments, including Canada and the US have laid down clearer guidelines in some investment treaties so as to provide for greater certainty as to how tribunals will approach those disputes where government measures are challenged by foreign investors as a form of “expropriation”*)

For its part, the tribunal was unmoved by Argentina’s arguments in the Siemens case. A single measure – a Decree executed pursuant to the Emergency Law of 2000 – was held to have terminated the contractual rights of Siemens’ subsidiary. This, in itself, amounted to an expropriation of Siemens’ investments.

The tribunal expressed some doubts as to whether the expropriation had been carried out according to a “public purpose”, as required under the Germany-Argentina treaty. While the tribunal noted that the Emergency Law of 2000 was clearly designed to address Argentina’s gathering financial difficulties, the tribunal also expressed the view that the De La Rua Administration had long desired to lessen the burden of a contract which had been negotiated by Siemens with the previous Menem administration.

However, rather than make a clear statement as to whether Argentina’s actions were in pursuit of a “public purpose” in the sense of the treaty’s expropriation clause, the tribunal simply noted that the expropriation clearly violated another condition of the treaty: that the investor be compensated for the value of the expropriated investment.

Later in its award, the tribunal would turn to the question of appropriate compensation. First, however, other alleged treaty breaches were examined by the tribunal. Among these other breaches was the alleged failure of Argentina to provide fair and equitable treatment and full protection and legal security.

FAIR AND EQUITABLE TREATMENT

Siemens and Argentina differed in their understanding of the treaty obligation to provide “fair and equitable treatment”. For its part, Argentina insisted that it bore the responsibility to act in good faith and in a reasonable and consistent manner vis a vis foreign investors. Meanwhile, Siemens argued for an interpretation which placed greater obligations upon governments, including to meet the “legitimate expectations” of foreign investors.

The tribunal - in language noticeably similar to that used in another arbitration, Azurix v. Argentina, where Dr. Rigo chaired the tribunal – would hold that bad faith need not be shown in order for a state to be held in breach of the fair and equitable treatment standard. Moreover, the Siemens tribunal appears to concur with several other recent arbitration awards which held that the fair and equitable treatment standard protects the “legitimate expectations” of foreign investors.

Ultimately, the tribunal would go on to find that several actions of Argentina breached the fair and equitable treatment obligation owed to Siemens – including the failure by Argentina to conclude agreements with its provincial governments (as had been pledged to Siemens' local subsidiary). Indeed, the tribunal held this failure to amount to an absence of good faith, a clear breach of the fair and equitable treatment standard.

The tribunal identified further breaches by Argentina of the fair and equitable treatment obligations, for example by dint of Argentina's delay in paying compensation to Siemens, and by virtue of the Government's denial of Siemens' request for a copy of its administrative file – a file which the Investor sought in order to pursue an administrative challenge to the treatment of its investments in Argentina.

Added to these treaty breaches was a further breach of the treaty obligation to provide "full protection and legal security" by virtue of Argentina's pushing for contractual renegotiation "for the sole purpose of reducing its costs, unsupported by any declaration of public interest". The tribunal emphasized that the treaty referred to "legal security" – in contrast to many treaties which simply refer to "security" – and the forced contractual renegotiation clearly struck at the "legal security" of Siemens' investments.

Argentina was also held to have violated Article 2(3) of the Germany-Argentina treaty, thanks to certain "arbitrary measures" which were taken against Siemens' local subsidiary during the period when the contract was still in force, and which the tribunal held to have been not "based on reason".

Notably, the tribunal rejected an argument by Siemens that it had suffered discrimination at the hands of Argentine authorities. However, the tribunal did express the view that "intent" to discriminate need not be present in order to prove a breach of the non-discrimination rule (a question which has arisen in other investment treaty disputes, and one which remains has been the subject of much debate). In the tribunal's view, "the impact of the measure on the investment would be the determining factor to ascertain whether it had resulted in non discriminatory treatment."

On the facts of the Siemens case, the tribunal identified certain government actions which seemed discriminatory, however the tribunal ruled that the allegations of Siemens had not been fully substantiated. Given that other treaty breaches had been found, the tribunal deemed it "unnecessary to determine whether Argentina breached the non-discriminatory treatment obligation".

UMBRELLA CLAUSE

Finally, in terms of alleged substantive breaches, the tribunal also rejected an argument by Siemens that Argentina had breached Article 7(2) of the treaty – which stipulates that treaty-parties "shall observe any obligation it has assumed with regard to investments by nationals or companies of the other Contracting Party in its territory."

The two parties disagreed as to whether this treaty clause served to elevate alleged

contractual breaches to the plane of international law – thereby obviating any need for the contract signatories to use the dispute settlement mechanism provided under the relevant contract (i.e. the local Argentine courts).

Although Argentina insisted that alleged breaches of contract needed to be handled in the Argentine courts - rather than in international arbitration - the tribunal would reject this contention, at least insofar as contractual breaches might give rise to knock-on breaches of the Germany-Argentina BIT.

However, given that Siemens was itself not party to a contract with Argentina (rather, the German firm's local subsidiary was the contract signatory) the tribunal went on to hold that Siemens could not claim breach by Argentina of Article 7(2) of the Germany-Argentina BIT.

By denying Siemens the ability to claim for treaty breach in cases of alleged breach of contractual undertakings owed to parties other than the foreign investor, the tribunal echoed the finding in another ICSID arbitration, Azurix v. Argentina, where Dr. Rigo Sureda had chaired the proceeding.

In contrast, an ICSID tribunal in a separate arbitration (CMS v. Argentina) had permitted the claimant in that proceeding, US-based CMS Gas Transmission Company, to claim successfully for breaches of an umbrella clause, due to Argentine breaches of a license agreement to which CMS was not a party – notwithstanding the fact that CMS was not itself a party to that license agreement.

(* On the differing approaches to expropriation by arbitration tribunals see for example: "Analysis: Tribunal distinguishes regulation from expropriation in latest Czech case", Investment Treaty News, March 29, 2006, available on-line at: http://www.iisd.org/pdf/2006/itn_mar29_2006.pdf)

3. Analysis: Tribunal rejects bid for reduced compensation on social policy grounds,
By Luke Eric Peterson

When it came time to assess the compensation owing to Siemens in the recent ICSID proceeding between the German firm and Argentina, lawyers for Argentina invoked international human rights law in an effort to argue that Governments ought to be entitled to pay less than "fair market value" for expropriated property where compelling social reasons lay behind a government's actions.

The tribunal summarized Argentina's argument as follows: "Argentina argues that the fair market value of an expropriated property as the measure of compensation for an expropriated investment is not always applicable when an expropriation becomes necessary for social policy reasons. If this would not be the case, it would be a serious limitation on State sovereignty, and no social or economic reforms could be

accomplished by poorer nations."

However, the tribunal would reject this argument by Argentina – holding, for example, that Argentina's invocation of an earlier ICSID award in Tecmed v. Mexico was not relevant to the question as to whether less compensation ought to be paid where an expropriation was motivated by some compelling social reason.

Rather, the Siemens Tribunal held that the earlier Tecmed tribunal had looked to the purpose of the expropriation and the proportionality of Mexico's actions in furtherance of that purpose, in the course of determining whether an expropriation had taken place – not at the later stage of assessing the compensation owed for any such expropriation.

Additionally, the Siemens tribunal went on to dismiss the relevance of Argentina's efforts to invoke the jurisprudence of the European Court of Human Rights – whose case law has permitted lesser compensation to be paid in some cases where property deprivations were motivated by compelling social reasons.

The Siemens tribunal remarked, without further elaboration, that the European Convention on Human Rights affords a "margin of appreciation" not found in customary international law or the Germany-Argentina bilateral investment treaty.

It is not clear from the publicly available record, whether Argentina had invoked the concept of "margin of appreciation" at the compensation phase of the Siemens arbitration, or whether the tribunal was referring to that concept of its own volition.

THE MARGIN OF APPRECIATION CONCEPT REARS ITS HEAD

The reference to the "margin of appreciation" is notable, as the concept – a particular staple of European human rights jurisprudence – has been used by certain international courts and tribunals to show some deference to governments when their actions are subjected to international review.

The European Court of Human Rights has been known to accord governments a certain margin of discretion when it comes to choosing the measures which are designed to achieve a particular objective. In other words, some measure of judicial restraint or deference is shown to states, particularly when states must act under the shadow of potentially vague or open-ended international norms.

While the concept looms large in some branches of international human rights law, in the investment treaty arbitration context, the concept has rarely been discussed by arbitral tribunals.

To date, only a handful of tribunals have spoken explicitly of related concepts such as "deference" or "restraint", and their relevance to an international review of alleged investment treaty breaches.

In the NAFTA Chapter 11 investment arbitration, SD Myers v. Canada, the arbitral tribunal held, in the course of analyzing NAFTA Article 1105, that international law ought to accord a “high degree of deference” to the right of domestic authorities to regulate matters within their own borders.

This reference to a “high degree of deference” has been interpreted by at least one legal scholar as a grant of a certain “margin of appreciation” to governments when it comes to determining how they will live up to their investment treaty obligations.**

Further, the reference by the SD Myers tribunal to a “high degree of deference” was later quoted approvingly by another arbitral tribunal in the Saluka v. Czech Republic arbitration pursuant to the Netherlands-Czech Republic bilateral investment treaty.

In the Saluka case, the tribunal, quoted the SD Myers language in support of the view that governments enjoy some leeway to regulate their “domestic matters in the public interest”, while, at the same, time taking into account the “legitimate expectations” of foreign investors.

Meanwhile, in another case, Tecmed v. Mexico, the tribunal in that case spoke of the “due deference” owed to states when they are assessing the issues that affect its public policy or its society as a whole - and the actions taken to protect those latter values.

At the same time, the Tecmed tribunal noted that it would review those government actions, nonetheless, to see if they are reasonable and proportional in light of the goals pursued and the impact on the foreign investor in question.

Notwithstanding occasional references to what might be classified as a “margin of appreciation”, the concept has not been much discussed – at least in explicit terms - in the preponderance of investment treaty arbitrations.

The Siemens award is notable for referencing the concept by name, even if the tribunal expressed the view that the doctrine was not applicable to the dispute (and specifically to the question of assessing compensation in the Siemens case).

Future disputes may see further discussion of this concept – and what bearing and relevance it has to arbitral review of alleged investment treaty breaches by governments.

TRIBUNAL MEMBERS SPLIT OVER COSTS AND VALUATION

In the Siemens case, the tribunal, in a majority decision, calculated that some $208 Million (US) reflected the fair market book-value of the expropriated investment. The tribunal also awarded Siemens some $9 Million (US) in consequential damages for having to maintain a skeletal support staff in Argentina after the contract-termination. As part of its award, the tribunal also ordered Argentina to return a $20 Million (US) contract performance bond which continued to be held by Argentina.

However, the tribunal rejected Siemens' claim for a further $124 Million (US) in "lost profits", dismissing this claim on the basis that such profits were "very unlikely to have ever materialized" for a multitude of reasons.

Notably, the tribunal members parted ways on the valuation of compensation in the Siemens arbitration. Arbitrator Domingo Bello Janeiro, a nominee of Argentina, argued in a dissenting opinion that the tribunal ought to have appointed an independent financial valuation expert, as requested by Argentina, so as to ascertain the appropriate compensation owed to Siemens. The remaining two arbitrators, Judge Charles Brower and Dr. Andres Rigo Sureda had rejected a request by Argentina to have an independent expert make such a valuation assessment.

Prof. Bello Janeiro also disagreed with the majority's approach to apportioning the costs of the proceedings. Whereas the majority decreed that Argentina would bear 75% of the costs of the arbitration (including arbitrators' fees), Prof. Bello Janeiro contended that it would be more appropriate, in line with arbitral practice, for each side to bear half of the cost of the proceedings.

Each side was ordered by the tribunal to bear the costs of its own legal representation in the arbitration.

(** See Yuval Shany, "Toward a General Margin of Appreciation Doctrine in International Law?", 16 European Journal of International Law, No. 5, 907-940, at 930)

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