THE RELEVANCE OF MOST-FAVORED-NATION CLAUSES FOR THE
ESTABLISHMENT OF THE JURISDICTION OF INVESTMENT ARBITRATION TRIBUNALS

By Olha Hrynkiv

LL.M. SHORT THESIS
COURSE: Investments and Investment Disputes
PROFESSOR: Markus Petsche
Central European University
1051 Budapest, Nador utca 9
Hungary

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ABSTRACT

This thesis analyzes the scope of protection granted to investors through a most-favored-nation clause (*hereinafter MFN clause*). In a number of cases, claimants have sought to invoke MFN clauses in order to establish or to broaden the tribunal’s jurisdiction or to overcome certain procedural preconditions and gain direct access to arbitration. Analysis of this practice reveals underlying problems in the drafting and interpretation of bilateral investment treaties (*hereinafter BIT*) while also invoking certain public policy considerations.

This thesis proposes to extend the MFN clause to dispute settlement provisions in a limited number of cases: firstly, when it allows investors to overcome certain procedural obstacles and secondly, when there is a clear evidence of states’ will to arbitrate the dispute. Such a narrow interpretation of the clause is in line with the rules of treaty interpretation and prevailing practice, while at the same time minimizing the negative consequences of “a procedural bridge” between the BITs created by the MFN provision.
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<td>BIT</td>
<td>Bilateral Investment Treaty</td>
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<td>etc.</td>
<td>etcetera (others)</td>
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<td>GATT</td>
<td>General Agreement on Tariffs and Trade</td>
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<td>i.e.</td>
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<td>ICSID</td>
<td>International Centre for the Settlement of Investment Disputes</td>
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<td>MFN</td>
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Introduction

Bilateral investment treaties usually include a MFN clause which allows investors to benefit from the same treatment granted to the investors from a most-favored-state. The aim of this clause is to prevent competitive advantages for certain groups of investors in the economic sphere and therefore to ensure their equal treatment. In practice, however, it allows the investor to “cherry-pick” those benefits which could be extracted from the third-party bilateral investment treaty (hereinafter a third-party BIT) without considering the counterbalances to those benefits set forth in the treaty between its state and the host state (hereinafter a basic BIT).¹

Application of MFN clauses to procedural issues, rather than being limited to substantive issues, has brought a new dimension to the understanding of the problem. In particular, the question arises as to whether or not MFN clauses can be invoked by investors who want to replace the dispute settlement mechanism specifically negotiated for the basic BIT with the other, more permissive mechanism prescribed in the third-party BIT. Even if the answer is “yes” it remains difficult to apply an objective test to the issue of what mechanism is more favorable for investors.

This thesis examines how the MFN clause should be construed and interpreted to provide answers regarding how this interpretation can ensure the balance between investors’ and states’ interests. This thesis also determines whether the investor can only benefit from one aspect of the third-party BIT or, once invoked, whether the whole BIT will become available. Finally,

this thesis establishes under what circumstances the MFN clause entitles an investor to invoke the dispute settlement provisions from a third-party BIT.

The issue of the scope of the MFN clause and its application to jurisdictional matters has arisen in a number of cases, most of which were connected to one of the following jurisdictions: Argentina, Spain, Russia, Hungary, Bulgaria, and Jordan. Although this list is not exclusive, it demonstrates certain tendency: the parties involved in such disputes are usually either former communist or Latin-American states that had recently gone through serious economic crises.

While an in-depth discussion of the influence of states’ political and economic situation on the scope and limits of the BITs is outside the purview of this thesis, it examines the states’ drafting histories and their current conditions insofar as it reveals the intent of the parties at the moment of the conclusion of the treaty.

**Chapter 1** of this thesis introduces the general aspects of the MFN clause in international investment law. **Chapter 2** analyzes the decisions of tribunals regarding the application of the MFN clause to admissibility-related issues and jurisdictional issues, respectively. **Chapter 3** summarizes the reasons for and against applying the MFN clause to dispute settlement clauses. Finally, the thesis provides conclusions and recommendations in respect to the inclusion of MFN clauses in BITs and in the interpretation and application of MFN clauses by tribunals.

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Chapter 1 - MFN Clause and Dispute Settlement Mechanisms

The initial purpose of the MFN clause was to ensure equal treatment between the trade players from different countries. The MFN clause and the basic principles behind its application were first introduced into the General Agreement on Tariffs and Trade (hereinafter the GATT) which came into force on 1 January 1948. Having become a mechanism for ensuring adherence to the non-discrimination principles in a trade context, the MFN clause began to be applied in other fields and was eventually introduced into the BITs. The next subchapters define current role of MFN clauses in international investment law and their scope.

1.1. Role of the MFN Clause in the BIT

MFN clauses are efficient in the relationship of at least three States: **State A** (the State that provides the MFN clause in its BIT with State B); **State B**; and **State C** (any third State with whom State A has a BIT that provides for more beneficial treatment than the treatment included in the BIT between State A and State B).

BITs may contain different dispute settlement provisions. For example, they may provide a reference to domestic courts, UNCITRAL, or ICSID arbitration. Even assuming that all BITs include an arbitration clause, they may require the participating parties to negotiate in case of a dispute, to exhaust local remedies, or to bypass certain waiting periods prior to submission of their dispute to arbitration. In our scenario the dispute settlement clause in the BIT between

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State A and State B requires the exhaustion of local remedies prior to a submission of the dispute to ICSID arbitration. Meanwhile, the BIT between State A and State C allows the investors to immediately initiate arbitration proceedings. As a result, the application of the aforementioned precondition upon the investors from State B puts them in a less favorable position than the investors from State C that are not subject to such a limitation.

It is indisputable that jurisdictional matters ensure promotion of foreign investments and protection of foreign investors and are as important as substantive means of protection. The differences in treatment in regards to investors’ substantive or procedural protection may be equally disruptive. As explained by Prof. Schill, an investor who has recourse to arbitration has a competitive advantage over other investors, especially if the latter cannot fully benefit from access to domestic courts, which is often the case in developing countries. Such a situation imposes different preconditions for the enforcement of the provisions of the BIT and results in different costs for the transactions at stake.

The difference in treatment between investors may be avoided through the reliance on the MFN clause provided by a basic BIT. Thus, in order to ensure equal treatment between the investors from State B and State C, the nationals of State B - subject to the BIT between State A and State B - can benefit from the treatment prescribed by the BIT between State A and State C, namely to submit their dispute directly to arbitration without fulfilling any additional preconditions.

Distinct from the other provisions in the BIT, the MFN clause does not only prescribe rights and obligations of the parties, it serves as the source of international obligations other than

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7 Without exhausting domestic remedies
those included in the basic BIT. In this regard the MFN clause itself “constitute[s] a sort of legal anomaly” since it creates rights and obligations for third states without their consent to it. At the same time, it prompts the participating states to adhere to their commitments and “creates a level playing field for the investors independent of their nationality.” Thereby, “apart from their impact on investor-state relations, and beyond the economic rationale, the MFN clauses also help to reorder inter-state relations.”

1.2. Scope of the MFN Clause: Different Approaches to its Interpretation

The relations between states arising out of foreign investments are mostly regulated by bilateral, not multilateral, treaties. States negotiate BITs on the basis of the specific goals and needs they wish to pursue. As a result, there is no standard wording of a MFN clause. Its scope vary from BIT to BIT. To clarify the nature of the MFN clause and the standard of its application, the Draft Articles on MFN clause were adopted in 1978 (hereinafter the Articles).

The Articles provide a general overview of the purpose of the MFN clause, the rights and obligations of the parties that have agreed upon it, as well as recommendations for drafting the clause and its suggested formulation. However, the Articles have no mandatory power. Therefore, they have not managed to achieve their intention of promoting uniformity in the application of the MFN clause within the context of foreign investments.

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A problem arises when a MFN clause is too general and does not provide a clear indication of parties’ intent to limit its scope. As found in the final report of the Study Group at its 3264th and 3277th meetings of the International Law Commission on 6 and 23 July 2015 respectively, the nature of the MFN clause did not change from the time of the Articles (1978), however, its scope of application expended. In the very beginning, MFN clauses were introduced to BITs solely with regard to substantive issues. Procedural matters initially entered into the scope of MFN clauses when analyzed in connection with GATT and international trade. Only recently has its application to jurisdictional provisions contained in BITs become an issue for discussion.

In light of the above, the following approaches to the scope of the MFN clause can be defined:

1. The scope of the MFN clause is limited to substantive issues.

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2. The scope of the MFN clause encompasses dispute settlement provisions to the extent that it does not preempt the intent of the parties in the BIT to submit disputes to a specific forum.\(^{19}\)

3. The scope of the MFN clause is interpreted as broadly as possible in order to ensure fulfilment of the commitments undertaken by states and the equal treatment of investors from different jurisdictions.\(^{20}\)

The states have a broad discretion to negotiate the scope of the MFN clause and its limits. They can expressly specify whether the MFN clause in their BIT covers procedural issues or not.\(^{21}\) In particular, most BITs concluded by the UK and by the US with other states expressly include the dispute settlement provisions within the scope of their MFN clauses.\(^{22}\)

The lack of a uniform practice with regard to interpretation of the MFN clauses by tribunals prompted some states to clarify the provisions of their BITs through the exchange of diplomatic notes. These notes may state the common intention of the parties to the BIT regarding the coverage of certain issues within the scope of the MFN clause. This is illustrated by Swiss BITs, which were interpreted as excluding any MFN clause application to their dispute settlement provisions.\(^{23}\) Likewise, after *Siemens A.G. v. Argentina*, Argentina and Panama exchanged diplomatic notes in order to ensure that the MFN clause did not extend to dispute

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settlement provisions. Nevertheless, when there is no explicit intention of the states to limit or otherwise delineate the scope of their MFN clauses, it is within the competence of tribunals to interpret these clauses on a case-by-case basis.

MFN clauses in BITs were invoked with regard to dispute settlement provisions in several ways, particularly in order to:

- invoke a dispute settlement mechanism not available under the basic BIT;
- broaden the scope of application of a dispute settlement clause to disputes which were not covered by the original clause contained in the basic BIT; and
- overcome some procedural preconditions where BITs prescribe negotiations between the investor and the host state, or require the expiration of waiting periods, or the exhaustion of local remedies prior to submitting the dispute to arbitration.

This thesis covers the approaches of the tribunals in each of the aforementioned situations by examining relevant cases insofar as the MFN clause is concerned.

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27 RosInvestCo UK Ltd. v. The Russian Federation, Final Award, http://www.italaw.com/cases/documents/925; (last visited March 30, 2016);
28 Emilio Agustín Maffezini v. The Kingdom of Spain, ICSID Case No. ARB/97/7, http://www.italaw.com/cases/641, (last visited March 30, 2016);
Chapter 2 – Problems with Application of the MFN Clause to Dispute Settlement Provisions

In order to determine whether the MFN clause covers the dispute settlement provisions prescribed by the third-party BIT it is essential to assess the stated intention of the parties upon the conclusion of each individual treaty.”

The issue of the scope of MFN clauses cannot be fully resolved given that it is impossible to foresee the contents of future BITs and future state practice at the moment of the conclusion of the treaty. Therefore, the general purpose of the MFN clause as well as public policy considerations must be also taken into account when looking at the applicability of MFN clauses to dispute settlement provisions.

2.1. Determining the Intentions of the Parties in the Dispute

The assessment of the parties’ intent to limit the scope of the MFN clauses has to be given on the basis of the rules of interpretation set forth in the Vienna Convention on the Law of Treaties 1969 (hereinafter the Vienna Convention). Accordingly, the treaty has to be “interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in

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their context and in the light of its object and purpose.” Interpretative techniques such as ejusdem generis rule may be also relied on by tribunals.

Several tribunals established a difference between the application of the MFN clause to jurisdictional issues and to the issues of admissibility of the claim in a particular forum. Accordingly, the general tendency among tribunals is that MFN clauses allow for the incorporation of parts of the dispute settlement clause through the MFN principle concerning the admissibility of a claim, but at the same time investors cannot establish jurisdiction of the tribunal on basis of the MFN clause. The tribunals came to such conclusions by referring to the ordinary meaning of the provisions of the BITs, to the context in which they were adopted, as well as to their object and purpose. Specific cases which illustrate the tribunals’ approach are discussed below.

2.1.1. MFN Clause as a Tool to Avoid Procedural Obstacles

Broad interpretation of the MFN clause has been adopted by the tribunals in the Maffezini v. Spain (2000) and Siemens A.G. v. Argentina (2004). In both cases the claimants sought to avoid submitting the dispute to local courts eighteen months before going to arbitration and in both cases they were allowed to bypass such a requirement by referring to the third-party treaties through the MFN clause.

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34 Vesel, Scott, Clearing a Path through a Tangled Jurisprudence: Most-Favored-Nation Clauses and Dispute Settlement Provisions in Bilateral Investment Treaties. Yale Journal of International Law 32 YJIL 125 (2007), p.120.
In *Maffezini v. Spain* the Agreement for the Reciprocal Promotion and Protection of Investments between the Kingdom of Spain and the Argentine Republic (*hereinafter the Argentine-Spain BIT*) included the MFN clause as follows:

“In all matters subject to this Agreement, this treatment shall not be less favorable than that extended by each Party to the investments made in its territory by investors of a third country.”

The tribunal had to define the meaning of the phrase “[i]n all matters subject to this Agreement…” and the word “treatment” as mentioned in the clause. In its analysis it took into account Article 31 of the Vienna Convention” and the maxim *ejusdem generis*. The latter is normally understood to mean that “the third party treaty must, in principle, regulate the same subject-matter as the basic treaty, otherwise the specific treatment standard would be taken out of its context and thus not be accorded in like circumstances or in like situations.” In other words, the tribunal’s ruling raised the question of whether, along with substantive issues, dispute settlement provisions could be invoked through the MFN clause.

The tribunal found that the Argentine-Spain BIT was the only one that mentioned “all matters subject to this Agreement.” The other BITs concluded by Spain had a narrower formulation of the MFN clause.

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40 *Ibid*, para.53, stating that “…in other treaties the most-favored-nation clause speaks of “all rights contained in the present Agreement…”*
Spain and Argentina had different approaches to the level of protection they granted to foreign investors at the moment of the conclusion of the treaty. At that point “Argentina had still sought to require some form of prior exhaustion of local remedies, while Spain supported the policy of a direct access to arbitration.”41

The wording of the dispute settlement clause included in the Spain-Argentina BIT was a kind of compromise to which the parties with their different approaches agreed to. This compromise consisted of the following: the investors had to refer to the local court prior to any arbitration proceedings, however, such a reference differed from the traditional approach of exhausting local remedies since the investors would not need to wait until the dispute was resolved in the domestic courts but only for a certain period of time. Upon the expiration of this period they could start arbitration proceedings without any other procedural obstacles. Nevertheless, after the conclusion of this BIT, Argentina changed its considerations and provided for direct access to arbitration in subsequent BITs.

Furthermore, since the raison d’être of the MFN clause is to provide most favorable “treatment” for an investor, the tribunal had to determine the scope of the word “treatment.”42

The tribunal acknowledged that “the scope of the clause might … be narrower than it appears at first sight.”43 However, it held that the word “treatment” mentioned in the MFN clause in the Argentine-Spain BIT included not only substantive protection of investors (e.g. national treatment, fair and equitable treatment, right against expropriation, etc.) but also protection

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41 Ibid, para.57.
through dispute settlement clauses since the latter also forms the standard of treatment for investors.\textsuperscript{44}

In another case, \textit{Siemens A.G. v. Argentina}, the respondent argued that: “it cannot be said that there is only one way to interpret the extent of the MFN clause, as this could change according to the provisions in which it is included.”\textsuperscript{45}

According to Article 3 of the Treaty between the Federal Republic of Germany and the Argentine Republic concerning the Reciprocal Encouragement and Protection of Investments (\textit{hereinafter the German-Argentina BIT}):

“All 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.”\textsuperscript{46}

The tribunal in this case also referred to Article 31 of the Vienna Convention and to the purpose of the BIT “as expressed in its title and preamble.”\textsuperscript{47} The intention of the parties was expressly stated in the preamble as the protection and promotion of investments so as to “stimulate private economic initiative and increase the well-being of the peoples of both countries.”\textsuperscript{48} The tribunal found that there was no need to exclude the protection in the form of dispute settlement provisions, from the list of the provisions fulfilling the aforementioned purpose.

\textsuperscript{44} \textit{Ibid}, para.63.


\textsuperscript{46} \textit{Ibid}, para.82.

\textsuperscript{47} \textit{Ibid}, para.81.

\textsuperscript{48} \textit{Ibid}, para.81.
The respondent in this case (Argentina) tried to differentiate the protection of investors, on the one hand, and the protection of investments, on the other hand, claiming that in the BIT as such, this distinction was necessary for the application of the MFN clause. Argentina argued that the following standards were applicable to the investment: fair and equal treatment; full protection and protection against discriminatory or arbitrary measures; MFN treatment; full protection and legal security. Meanwhile, it also held that the following standards were applicable to the investors: privileges granted under customs or economic unions or free trade areas; advantages granted under taxation agreements; national treatment; payments under guarantees; and dispute settlement. In other words, the MFN clause was not considered a part of the treatment guaranteed to the investors. However, the tribunal rejected this argument and ruled that when applying the MFN clause there was no need to differentiate between the treatment granted to the investor and the treatment granted to the investments.

Based on the outcome of Maffezini v. Spain and Siemens A.G. v. Argentina, it may be stated that investors are able to rely on MFN clauses in order to avoid procedural obstacles such as mandatory waiting periods or requirements to first attempt to reach an amicable settlement with the host state before submitting a dispute to arbitration. This conclusion has been subsequently reaffirmed in Gas Natural SDG v. Argentina (2005) and Suez SA v. Argentina (2006).

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49 Ibid., para.83.
50 See Final Report of the Study Group at its 3264th and 3277th meetings of the International Law Commission on 6 and 23 July 2015. International Law Commission, http://legal.un.org/file/guide/1_3_part_two.shtml (last visited March 30, 2016), para.114, stating that in any case “[t]here has to be evidence that the MFN provision was designed to apply to change the jurisdictional limitations on the tribunal because the host State’s consent was predicated on compliance with those limitations.
Yet, in *Wintershall Aktiengesellschaft v. Argentina* (2008) the claimant was not allowed to invoke the MFN clause despite the almost identical compared to *Maffezini v. Spain* circumstances of the case. The claimant had relied on the MFN clause in order to bypass the procedural requirement prescribed by the Argentina-Germany BIT to submit the dispute to local courts before going to arbitration. The tribunal, however, held that the MFN clause in the Argentina-Germany BIT did not extend to dispute settlement provisions and that the investor still had to comply with the requirements set forth in the basic BIT.

Contrary to Prof. Capaldo, this decision did not “erode the consensus of the tribunals on the extension of the scope of the MFN clause”\(^{53}\) to the procedural obstacles prescribed by dispute settlement provisions.

*Wintershall Aktiengesellschaft v. Argentina* differed from *Maffezini v. Spain* on a number of crucial grounds. Firstly, the MFN clause in the Argentina-Germany BIT expressly defined that:

> “Regarding the matters governed by this Article the nationals or companies of either Contracting Party shall be accorded in the territory of the other Contracting Party the treatment accorded to the most-favored-country.”\(^{54}\)

Distinct from *Maffezini v. Spain*, where the wording of the MFN clause referred “to all the matter regulated by the treaty,”\(^{55}\) the MFN clause at issue referred to only one article which should provide full protection and security of investments and investment related activities as


well as their expropriation and nationalization. According to the tribunal, the scope of the clause at hand was confined solely to these matters.

Secondly, the dispute settlement clause in the Argentina-Germany BIT provided for ICSID arbitration while the Argentina-US BIT invoked by the claimant provided for either ICSID or UNCITRAL (upon the claimant’s request).

With this in mind the tribunal came to the following conclusion:

“[D]ifferent dispute settlement provisions under another treaty, whether or not “alien” to the basic treaty, are sufficient to negate the submission that the most-favored-nation clause … applies to dispute settlement justifying abandoning the dispute settlement clause in the Argentine – Germany BIT and adopting Article VII of the Argentine – US BIT.”\(56\)

Consequently, the similar factual circumstances of the two cases are not sufficient in invoking the same application and interpretation of the MFN clause. Although the general rule derived from previous tribunals’ decisions allows for the avoidance of certain procedural preconditions to dispute settlement in arbitration, the purpose of the BIT and the wording of the MFN clause contained within remain decisive factors for the outcome of each particular case.

2.1.2. MFN Clause as a Tool to Establish Jurisdiction

In a number of cases investors tried to use the MFN clause not just to avoid certain burdensome requirements set forth in the basic BITs but also to establish the jurisdiction of the tribunal on the basis of the MFN clause, in particular in Salini v. Jordan, Plama v. Bulgaria, Telenor v. Wintershall Aktiengesellschaft v. Argentine Republic, ICSID Case No. ARB/04/14, http://www.italaw.com/cases/1171, (last visited March 31, 2016), para.190.

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\(56\)
Hungary and Berschader v. Russian Federation. However, in all those cases, the proposals were rejected.

In Salini v. Jordan the Italy-Jordan BIT allowed investors to submit treaty claims (but not contract claims) to ICSID arbitration. At the same time, the US-Jordan BIT had a broader dispute settlement provision which allowed to submit both treaty and contract claims to ICSID arbitration.57

In its analysis the tribunal referred to two types of MFN clauses: firstly, to the clauses in which the scope was expressly defined by the BITs to include or exclude dispute settlement issues and secondly, to the clauses – found in such cases as Maffezini v. Spain - which cover “all matters” subject to the treaty. The tribunal found that neither of these examples were relevant for the case before them.

In making this determination, the tribunal did not expressly disagree with the conclusions made in the Maffezini v. Spain but rather differentiated between the cases on several grounds. First of all, the wording of the MFN clause in the Italy-Jordan BIT was not as broad as the one in Maffezini v. Spain, nor was there any evidence of either party’s intention to apply the clause to dispute settlement issues. The tribunal expressed its concern that approving the jurisdiction of the tribunal under the circumstances brought forward by the claimant would increase the risk of future treaty-shopping and therefore rejected the claim.58

According to the tribunal in Plama v. Bulgaria, the prerequisite for arbitration is a clear and unambiguous agreement of the parties to arbitrate their dispute.59 In this case the Bulgaria-

Cyprus BIT limited arbitration to a determination of the quantum of damages under the UNCITRAL arbitration rules. The claimant attempted to invoke a broader dispute settlement provision, which allowed for arbitration of the other claims.

In coming to the decision on this case, the tribunal referred to the wording of the clause itself without relying on the object and purpose of the Bulgaria-Cyprus BIT. This BIT had been concluded at a time when Bulgaria had the policy of granting limited protection to foreign investors as well as limited dispute settlement provisions. Since then Bulgaria has changed this practice. “In the 1990s, after Bulgaria’s communist regime changed, it began concluding BITs with much more liberal dispute settlement provisions, including resort to ICSID arbitration.”

Nevertheless, subsequent negotiations between Bulgaria and Cyprus demonstrate that the states did not have any intent to extend the MFN clause to a broader dispute settlement procedure. While they renegotiated a number of issues contained in the BIT between themselves, however they deliberately did not cover the scope of the MFN clause, indicating their unwillingness to substitute the previous agreement on the category of claims that could be submitted to arbitration.

The tribunal also placed an emphasis upon the fact that:

“[D]ispute resolution provisions in a specific treaty have been negotiated with a view to resolving disputes under that treaty. Contracting states cannot be presumed to have agreed that those provisions can be enlarged by incorporating dispute settlement provisions from other treaties negotiated in an entirely different context.”

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60 Ibid, para.195.
61 Ibid, para.198.
62 Ibid, para.198.
63 Ibid, para.207.
This approach was reaffirmed in *Berschader v. Russia* (2006) and *Telenor v. Hungary* (2006). In both cases the basic BITs limited the jurisdiction of the tribunal to the adjudication of expropriation claims while the third-parties’ BITs provided for arbitration of any disputes relating to an investment.

In *Berschader v. Russia* the MFN clause reads as follows:

> “Each Contracting Party guarantees that the most-favored-nation clause shall be applied to investors of the other Contracting Party in all matters covered by the present Treaty…”  

64 The tribunal agreed that the ordinary meaning of “all matters covered by the present Treaty” was clear. However, the phrase must be seen in its broad context, particularly in relation to the concept of the MFN clause. The Protocol to the Treaty provided that “the Soviet Union would accord, in its territory, to Belgian investors treatment at least equivalent to that accorded to investors from countries that were members of the OECD on the date when the Protocol was signed.”  

65 According to the tribunal, this language appears to indicate that what the parties had in view was the material rights accorded to investors within the territory of the Contracting States.

The question that arose was whether the tribunal had to follow the practice of the previous decisions and allow the MFN clause to encompass not only material but also procedural standards of protection for investors. Contrary to *Maffezini v. Spain* and *Siemens A.G. v. Argentina*, the tribunal stated that:

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65 Ibid, para.185.
“The problem with these arguments [given by the tribunals in the previous cases] is that they are of a general nature. They offer strong support for the conclusion that a MFN provision is generally capable of incorporating by reference a dispute settlement clause and that such incorporation would typically advance the purpose of BITs. However, these arguments offer little or no guidance as to whether, in a specific case, the contracting parties to a treaty … actually intended the arbitration clause to be extended in the future to other kinds of disputes.”66

Finally, the tribunal held that the phrase “all matters covered by the present treaty” in this particular case should not have been read literally and did not encompass dispute settlement provisions.

Similarly, in *Telenor v. Hungary* the Hungary-Norway BIT limited the jurisdiction of the tribunal to specific claims while all the other Hungarian BITs provided for the arbitration of any disputes. In order to clarify the intention of the parties behind the basic BIT the respondent pointed out that out of the 15 Norwegian BITs publicly available, the BIT with Hungary was the only one that specified the categories of disputes referable to ICSID arbitration, whereas the 14 other BITs provide for “all” or “any” disputes.67 The tribunal in its rejection of the claim noted that a broader interpretation of the MFN clause would allow creating jurisdiction where none had existed before, contrary to the plain meaning of the BIT’s wording.68

The aforementioned cases demonstrate that the general tendency is to reject attempts to use a MFN clause is such a way that it establishes the jurisdiction of the tribunal on matters not

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covered by the basic BIT. So far there is only one exception to this tendency: the decision of the tribunal in *RosInvestCo v. Russia* (2007).

In this case the tribunal found that the UK-Russian BIT did not grant the tribunal the power to decide the dispute at hand relating to the issue of expropriation. However, the tribunal allowed the claimant to rely on the MFN clause in the basic BIT in order to incorporate a broader dispute settlement provision found in the Denmark-Russia BIT.

Article 3 of the UK-Soviet BIT states that:

“Neither Contracting Party shall in its territory subject investments or returns of investors of the other Contracting Party to treatment less favorable than that which it accords to investments or returns of investors of any third State.”

Similar to *Maffezini v. Spain*, the tribunal based its finding on an analysis of the plain meaning of the provision and the word “treatment.” It came to the conclusion that “if it applies to substantive protection, then it should apply even more to procedural protection.”

Although the tribunal acknowledged that there were a number of decisions where the expansion of the scope of the MFN clause under similar circumstances was not allowed, it noted that “the wording in Article 3 and 7 of the UK-Soviet BIT is not identical to that in any of such other treaties considered in these other decisions.” Accordingly, every clause had been specifically drafted for the purposes outlined in the relevant BIT and has to be interpreted in its own light. Thus, the tribunal simply disregarded the previous practice.

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70 Ibid, para.131.
71 Ibid, para.137.
To confirm its finding the tribunal referred to the arbitration clauses in BITs concluded by the UK, the Soviet Union, Russia, and other states. In all those BITs the issues connected with expropriation were under the jurisdiction of arbitral tribunal. As such, the tribunal found that there was no reason to prohibit a broad interpretation of the MFN clause in that case and not to expand the tribunal’s jurisdiction in that area.\footnote{Ibid, para.159.}

Consequently, the practice of establishing jurisdiction on the basis of MFN clauses is anything but uniform. Applying the same rules of treaty interpretation in accordance with the Vienna Convention, the tribunals still came to different conclusions as to the scope of MFN clauses.

### 2.2. Determining the Contents of “More Favorable”

As for the application of MFN clauses, the question arises as to in what way can the tribunal rely on the dispute settlement provision from a third-party BIT. It can mean either that the dispute settlement clause from one BIT is incorporated into another or that investors are entitled to rely on only that part of the clause which is more favorable to them. It is also debatable which dispute settlement mechanism provides a better treatment and whether the need to establish equality between investors requires the applicability of the same dispute settlement mechanism to all of them.\footnote{Vesel, Scott, Clearing a Path through a Tangled Jurisprudence: Most-Favored-Nation Clauses and Dispute Settlement Provisions in Bilateral Investment Treaties. Yale Journal of International Law 32 YJIL 125 (2007): p.125; Douglas, Zachary, The MFN Clause in Investment Arbitration: Treaty Interpretation off the Rails, 2 J INT. Disp. Settlement 97 (2011), p.111.}

The question of applicability of the MFN clause was brought forward in Siemens A.G. v. Argentina and RosInvestCo v. Russia. In Siemens A.G. v. Argentina the tribunal found an answer when considering the main purpose of the MFN clause – to treat German investors in a way that was not less favorable than the treatment granted to investors from the most-favored-
state (Chile). The tribunal held that only those provisions of the Chile-Argentina BIT that guaranteed a more beneficial treatment to the investor could be invoked by the MFN clause. As such, this approach did not place Siemens in a better position than Argentina’s Chilean investors.74 This is because “[t]he MFN clause works both ways…,”75 since investors from Chile will be able to claim similar benefits under the German-Argentine BIT.

The same finding was made in RosInvestCo v. Russia. The respondent at hand (Russia) contested tribunal’s decision on jurisdiction, claiming that because of the limitations set forth in the Denmark-Russia BIT (related to taxation) RosInvest’s claims would not have been satisfied if it had been based on the dispute settlement clause prescribed by this treaty.76 The tribunal held that:

“While indeed the application of the MFN clause widens the scope of dispute settlement provision and thus is in conflict to its limitation, this is a normal result of the application of MFN clauses, the very character and intention of which is that protection not accepted in one treaty is widened by transferring the protection accorded in another treaty.”77

In Siemens A.G. v. Argentina the respondent (Argentina) also contested that allowing investors to choose which provisions of the third-party BIT they wanted to invoke would lead to “provision-shopping.” In its view, a better approach would be to allow the investor by invoking

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75 Ibid, para.108.
77 Ibid, para.131.
the third-party BIT, to invoke the entire dispute settlement clause contained in the treaty (not only its more favorable part). Such an approach was supported by Prof. Vesel.

However, to allow transposition of an entire dispute settlement clause into the basic BIT would instead lead to a different kind of anomaly – “treaty-shopping.” Furthermore, the tribunal in *Siemens A.G. v. Argentina* affirmed that it would be contrary to the functions of the MFN clause to provide these investors with the most favorable treatment in certain aspects but with less favorable treatment in other aspects.

The notion of a more favorable treatment depends on the circumstances of each case. In order to establish whether the dispute settlement mechanism was a part of the treatment guaranteed to investors the tribunal in *Maffezini v. Spain*, for instance, first had to find whether the possibility of initiating arbitration proceedings without prior reference to the court was an advantage to Brazil investors. Today it is widely recognized that arbitration is the preferred method of dispute resolution as it is a private mechanism and is therefore not connected to the state and its domestic policy. In this respect the tribunal in *Maffezini v. Spain* referred to the ICSID reports and stated that:

> “Traders and investors, like their states of nationality, have traditionally felt that their rights and interests are better protected by recourse to international arbitration than by submission of disputes to domestic courts, while the host governments have traditionally felt that the protection of domestic courts is to be preferred.”

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Another example is *Plama v. Bulgaria* where the claimant argued that it was more favorable for the investor “to have a choice among different dispute settlement mechanisms” and “to have the entire dispute resolved by arbitration as provided in the Bulgaria-Finland BIT, than to be confined to … arbitration limited to the quantum of compensation for expropriation.”

The question remains which mechanism is more favorable if one BIT provides for UNCITRAL arbitration and another one provides for ICSID arbitration. One arbitration institution may be more favorable for an investor than the other in particular because it produces more easily recognizable awards.

In any case, the definition of the MFN clause itself indicates that the clause attracts only favorable treatment and not disadvantages. As such an investor can only benefit from the more favorable aspects of a treaty and cannot replace the entire dispute settlement clause in the basic BIT by referring to the third-party BIT. Otherwise, many treaties would lose their relevance. At the same time, whether or not the treatment provided for investors is more favorable should be defined on a case-by-case basis.

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2.3. Determining the Relevance of Public Policy Considerations

Public policy, as it is generally understood, reflects the fundamental legal, moral, political, religious, social, and economic standards of the state. Therefore, the threshold for invoking public policy considerations is extremely high.

Prof. Schill compares the term “public policy consideration,” as used in the context of the MFN clause with the public policy exceptions to enforcement of arbitration agreements in commercial arbitration.

In commercial arbitration, public policy considerations exist to ensure the specific interests of the state “in preventing private parties from settling disputes outside the … state’s court system.” However, in investment arbitration, this cannot be applied to the states as they are the parties to dispute settlement clause and therefore do not have to be protected against the enforcement of their obligations under international law. Otherwise, they would be able to unilaterally invoke public policy considerations, or in some cases to create considerations, whenever it was beneficial for them. That would make the MFN clause inoperative and would allow states to escape their commitments.

This controversy caused a concern in those cases where application of the MFN clause to dispute settlement mechanisms was eventually allowed. In Maffezini v. Spain the tribunal indicated that the possibility of benefiting from the better treatment prescribed by the third-party BIT should not contradict existing public policy considerations. The tribunal failed to

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87 Emilio Agustín Maffezini v. The Kingdom of Spain, ICSID Case No. ARB/97/7,
provide any criteria for defining such considerations but rather explained that the application of the MFN clause should not override fundamental conditions for the acceptance of the agreement by the parties in question. The tribunal provided the following examples of such conditions:

- the exhaustion of local remedies;
- fork-in-the-road provision (once the choice between the institutions is made, it becomes final and cannot be bypassed by invoking a MFN clause);
- the choice of a particular system of arbitration; and
- the choice of a highly institutionalized system of arbitration and specified rules of procedure (these specific provisions reflect a clear will of the parties to arbitrate).\(^{88}\)

None of these public policy exceptions were adopted in \textit{Maffezini v. Spain} or \textit{Siemens A.G. v. Argentina}. In the latter case, the tribunal simply stated that the limitations mentioned in \textit{Maffezzini v. Spain} were not applicable as the procedural requirement (submission of a dispute to local courts eighteen months before going to arbitration) did not reflect a fundamental public policy question. Such a vague explanation has only given rise to a greater degree of confusion and difficulty in subsequent cases.\(^ {89}\)

In \textit{Salini v. Jordan} the tribunal expressed concern about the approach adopted in \textit{Maffizini v. Spain}, stating that the exceptions based on public policy considerations might be difficult to apply and would increase the risk of forum-shopping by claimants.\(^ {90}\)

\(^{88}\) Ibid, para.63.


Likewise, in *Plama v. Bulgaria* the tribunal agreed with that observation, providing that the principle of multiple exceptions found in *Maffezini v. Spain* should instead be replaced by “a different principle with a single exception: that an MFN clause does not incorporate by reference dispute settlement provisions from another treaty unless it leaves no doubt that this is the will of the contracting parties.”

As such the public policy considerations have not been used as the ground for a refusal to apply the MFN clause to jurisdictional issues. According to Prof. Schill, “the only defensible basis for the tribunal’s public policy considerations can be the consent of the states to a BIT,” addressed in subchapter 3.2 of this thesis.

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Chapter 3 – Consequences of a Procedural Bridge between the BITs

Investors and states consider dispute settlement clauses and MFN clauses from different perspectives. For investors, “treatment guarantees are of limited significance unless they are subject to a dispute settlement system and, ultimately, to enforcement;”\(^93\) while for host states, “consenting to arbitration is a concession, a waiver of the state’s sovereign prerogative not to be hauled before an international court without its consent.”\(^94\) The consequences of this clash of interests between investors and states is demonstrated below.

3.1. Future of Multilateralism

The tribunal in \textit{Maffezini v. Spain} referred to “the fact that the application of the most-favored-nation clause to dispute settlement arrangements in the context of investment treaties might result in the harmonization and enlargement of the scope of such arrangements.”\(^95\) However, this statement was subsequently criticized by the tribunal in \textit{Plama v. Bulgaria} that failed to see how harmonization of the dispute settlement provisions could be achieved through reliance on the MFN clause.\(^96\)

Some scholars do indeed support the view that a broad understanding of the MFN clause and the extension of its scope leads to the development of common standards in international investment law.\(^97\) The scope of the MFN clause and its limits depend on the understanding of

\(^{94}\text{Ibid, p.125.}
\(^{95}\text{Emilio Agustin Maffezini v. The Kingdom of Spain, ICSID Case No. ARB/97/7, http://www.italaw.com/cases/641, (last visited March 30, 2016), para.62.}

international investment relations. A broad interpretation of the MFN clause illustrates their multilateralization in that two states cannot define the scope of their relations disregarding the tendencies that are taking place at international level. Coming back to our hypothetical example, every preferential treatment provided by State A to State C has an influence on the commitments of State A to State B. Yet, to the contrary, the restrictive approach actually employed towards the interpretation of MFN clauses reflects the bilateral elements in international relations and regards the BITs “as expressions of *quid pro quo* bargains rather than as elements of an emerging international economic order.”

Consequently, the tribunals’ understanding of the scope of the MFN clause reflects a dichotomy between bilateralism of international investment relations, on the one hand, and their multilateralism, on the other hand. Such a dichotomy should be taken into account when answering the question, “to what extent may the MFN clause allow the application of provisions of the third-party BIT?”

### 3.2. Threats of “Cherry-picking”

Ambiguity in the application of MFN clauses to dispute settlement provisions may benefit states to the detriment of foreign investors. States may intentionally refuse to specify the scope of the MFN clause in their BITs in order to empower themselves to allow or prevent its invocation on a case-by-case basis. In this respect favoring a broad interpretation of MFN clauses can help to settle disputes and force states to comply with their treaty obligations. Yet

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98 The investors from State B are in a less favorable position than the investors from State C since the BIT between State A and state C grants to investors a more favorable dispute resolution mechanism, as mentioned in subchapter 1.1.

at the same time, a groundless extension of investors’ rights may lead to abuse of their rights and forum-shopping.

In Maffezini v. Spain as well as in Siemens A.G. v. Argentina the tribunals relied on the award of the Commission of Arbitration established for the Ambatielos decision in which it accepted the extension of the MFN clause to questions concerning the “administration of justice.” However, the tribunals did not provide their understanding of the term “administration of justice” which was highly criticized in subsequent decisions on the matter.\textsuperscript{100} It should be noted that “[t]here is a fundamental difference between the administration of justice and access to courts as substantive protection on the one hand, and interpretation of treaty provisions and settlement of treaty disputes as procedural mechanisms on the other.”\textsuperscript{101} Therefore, the argument of claimants based on the necessity to allow for the “administration of justice” should not be a decisive argument for tribunals in defining the scope of MFN clauses.\textsuperscript{102}

The tribunal in Telenor v. Hungary stated that those who advocated for a broad interpretation of the MFN clause had always examined the issue from the perspective of investors, yet “what has to be applied is not some abstract principle of investment protection in favor of a putative investor who is not a party to the BIT and who at the time of its conclusion is not even known, but the intention of the states who are the contracting parties.”\textsuperscript{103}

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According to Prof. Thulasidhass, a broad interpretation of the MFN clause causes a situation in which the consent of the contracting parties is replaced by the interests of private investors.\textsuperscript{104} This may lead to a greater anomaly resulting in a disregard for the domestic dispute settlement institutions, replacing the intended dispute settlement mechanism or the applicable rules agreed upon in the basic BIT; or establishing a jurisdiction where there was no primary intent of the parties to do so.\textsuperscript{105}

As a result of this slippery slope, so far no tribunal has allowed investors to replace the dispute settlement mechanism under the basic BIT with the dispute settlement mechanism contained in another BIT through operation of the MFN clause. According to the tribunal in \textit{Plama v. Bulgaria}, “the lack of precedent is not surprising.”\textsuperscript{106} When entering the BIT with specific dispute settlement mechanism, states cannot be expected to replace them with different dispute settlement mechanism in future, unless they have explicitly agreed thereto.

Arbitration requires the explicit consent of the participating parties.\textsuperscript{107} The scope of the MFN clause should be limited only to the subject matter regulated by the basic BIT. If it does not provide for arbitration, meaning that this matter is outside of its scope, then the MFN clause should solely encompass substantive protection of investors.

The situation is different if the basic BIT provides for arbitration but only in a limited number of cases and under specific conditions. This demonstrates that the parties in principle recognize

\textsuperscript{105} \textit{Ibid}, p.8.
the possibility of arbitrating the dispute. As it was already analyzed in subchapter 2.1 of this thesis, tribunals usually allow for the avoidance of certain procedural preconditions to dispute settlement in arbitration through the MFN clause. The question is more difficult if the arbitration agreement encompasses an exclusive list of possible claims. That was the case in Salini v. Jordan, Plama v. Bulgaria, Telenor v. Hungary, Berschader v. Russian Federation and RosInvestCo v. Russia. Only in the latter did the tribunal allow extending of its jurisdiction.

According to Prof. Vesel, “[a] state’s consent is both forum-specific and party-specific, so that consent to arbitration under UNCITRAL rules does not constitute consent to ICSID arbitration, nor does consent to ICSID arbitration of disputes with Finnish nationals constitute consent to arbitration with nationals of Cyprus.”

This can be explained by the following: the limits of the scope of the MFN clause are established by the parties. In the absence of a clear consent to arbitrate the dispute, the tribunal has no power to impose on the parties to the BIT the commitments which they did not intend to undertake. In this respect Prof. Schill relied on the finding of the tribunal in Mondev v. United States which held that matters of jurisdiction should be interpreted neither extensively nor restrictively but objectively according to the accepted rules of treaty interpretation.

It can be stated that because of its specific nature and purpose the MFN clause will inevitably lead to treaty-shopping either when the substantive or procedural protection of investors is at stake. This makes the refusal to expand the scope of the clause to jurisdictional issues on this basis groundless.

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To be more specific, such a broad interpretation of the MFN clause with regard to jurisdictional issues will allow investors to “cherry-pick” those institutions, rules, and preconditions to dispute settlement which are most beneficial to them. This will subsequently cause uncertainty as to the exact nature of the commitments of the states - parties to the treaties - and may disregard their intent to submit disputes to a specific forum. Even assuming that in majority of cases this “cherry-picking” will not reach a high enough threshold for public policy violation, it may result in such a high level of ambiguity in relations between the states that it ultimately undermines the original purpose of the BIT per se.
Conclusion

A bilateral investment treaty is negotiated as one complete, balanced package of commitments that ensure a level playing field to investors. The MFN clause included in the basic BIT allows investors to rely on more favorable provisions contained in the third-party BIT. Two questions have arisen regarding the MFN clause: firstly, whether or not the same usage of the MFN clause is relevant for dispute settlement provisions; and secondly, whether the MFN clause can substitute state’s consent to arbitration or to a different arbitral forum which was set forth in the third-party BIT.

While acknowledging that no uniformity in resolving these issues is possible, this thesis argues against interpreting the MFN clause in an unjustifiably broad manner.

The scope of the MFN clause should be defined on the basis of parties’ intent through the ordinary meaning of the text of the treaty in light of its object and purpose. Therefore, the clause should be drafted as clearly as possible. The parties may avoid the abovementioned issues if they specifically determine in the treaty the scope of the MFN clause and whether it encompasses dispute settlement provisions.

Even if the parties have chosen to draft the MFN clause broadly, they can communicate their intent to each other to prevent any kind of uncertainty in future. That would enable investors to predict the level of protection granted to them under the treaty and would ensure a more efficient way of resolving disputes.

Even if the determination of parties’ intent is left to tribunals, recent cases have demonstrated a shift towards reliance on the text of the treaty rather than on its broader object and purpose. While defining the scope of the MFN clause tribunals came to different conclusions. However, it does not reveal the contradictions in the existing practice but rather demonstrates that
tribunals have made their decisions on a case-by-case basis taking into account the text of the treaties and factual circumstances of each particular case.

Likewise, public policy considerations should derive from the wording of the treaty itself. Any references to general exceptions without textual grounds would be either inoperative (no case would reach the necessary threshold) or would lead to the abuse of process by the states (they would be able to invoke such exceptions in any case when it is beneficial to them).

In order to avoid a conflict of interest between investors and states, the MFN clause has to ensure that investors enjoy the level of protection they want, and states have the level of flexibility they need.

Investors’ expectations to have equal access to dispute settlement mechanisms agreed upon under the treaties are legitimate and justifiable. Therefore, in principle nothing should prevent investors from relying on the MFN clause in order to bypass certain procedural obstacles to achieve a more expedient mode of dispute resolving.

However, the situation is different when investors rely on the MFN clause in order to choose a dispute settlement mechanism which is not agreed upon in the basic treaty, arbitration in particular. Arbitration without consent is like swimming without water; the existence of the arbitration clause in the third-party treaty cannot replace the intent of the parties to a basic treaty and cannot enable dispute settlement in arbitration without their explicit consent. Therefore, investors should not be allowed to establish the jurisdiction of the tribunal through the MFN clause.
The same argument is applicable to investors attempting “to mix and match dispute settlement provisions”\textsuperscript{110} prescribed by different treaties in order to come up with the most favorable configuration of dispute settlement mechanisms (especially as the states have never consented to such).

To presume the contrary would lead to forum-shopping and would make an unfair imposition on the parties to the treaty the results that could not have been intended by them. Although the protection of foreign investors is the cornerstone of bilateral investment treaties, it should not threaten the predictability and stability of the legal system.

The aforementioned conclusions are in compliance with the findings of the tribunals analyzed in this thesis and should be considered as the indicators of modern tendencies in the development of investment law. Nevertheless, the MFN clause is aimed at harmonizing bilateral state relations and its scope can be retroactively changed in light of a broader division between multilateralism and bilateralism, a subject in need of further research.

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