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Mexico and the Settlement of Investment Disputes: ICSID as the Recommended Option

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The changes that have taken place in arbitration conditions, the greater fairness in the arbitration process, and the increasingly stringent qualifications to be met by arbitrators, as well as contemporary economic realities, have been instrumental in causing Mexico's about-face on its approach to arbitration.

In 1994, when the North America Free Trade Agreement ("NAFTA") came into effect, the doors were opened for the implementation by Mexico of various mechanisms to settle trade and investment disputes, and arbitration became the accepted dispute settlement formula.

This first political decision of the Mexican government was followed by the signing of a good deal of bilateral and multilateral treaties aimed at luring the flow of investment and trade to Mexico, relying on an arbitral process to handle potential differences between foreign investors and Mexico.

The signing of agreements of this kind has significantly increased Mexico's foreign trade, and enhanced the flow of foreign investment to Mexico. Between 1993 and 2003, Mexico's exports increased three-fold and its imports increased 160%.

Accumulated foreign investment jumped from 15 billion dollars in 1994 to 142 billion dollars in 2003. During the ten years preceding 1994, when NAFTA came into force, the flow of foreign direct investment ["FDI"] averaged 3.47 billion dollars each year; in the ten years following 1994, it averaged 12.6 billion dollars each year.

The benefit of the arbitration clause has its limits: as the number of countries that enter into agreements to promote FDI increases, so does the competition to lure FDI flow. For example, Mexico's share of the 235.5 billion dollar

1. With 158 votes in the U.N. General Assembly and 12 votes in the Security Council, Bernardo Sepúlveda Amor was elected as a judge on the International Court of Justice for a period of nine years beginning February 6, 2006. Bernardo Sepúlveda was the Secretary of Foreign Affairs from December 1982 to December 1988. He founded the Contadora Group that contributed to bringing peace to Central America. From January to November, 1982, he was Mexico's ambassador to the United States and from 1989 to 1993, ambassador to Great Britain and Ireland. In addition to his diplomatic career, he is a very prestigious international jurist. For the past nine years he has been a member of the United Nations Commission on International Law.

FDI worldwide in 1994 was 4.9%; in 2004, its share of the 612 billion dollar FDI worldwide flow was 2.9%.

In light of these figures, it is obvious that we're doing something wrong. If a second generation of fundamental structural reforms is not introduced, we're running the serious risk of suffering major setbacks in the field of competitiveness, technological progress, institutional development and governance, macroeconomic stability, and, even more serious, the well-being of a society still hindered by deep-rooted inequalities in the distribution of wealth.

In the past decades, Mexican corporations have become exporters of capital, and have achieved an outstanding presence in the United States and a good number of countries in Latin America, the European Union and Asia.

Twenty multinational Mexican companies combined earn 17 billion dollars in revenues from their foreign subsidiaries and have created fifty-five thousand direct jobs overseas. CEMEX is the one Mexican corporate group with operations in five continents. Other companies enjoying a high degree of internationalization are América Móvil, Grupo Maseca, Grupo Bimbo, Femsa, ICA, Grupo Posadas, Grupo Carso, Alfa, and Vitro.

The twenty major multinational Mexican companies, and others with a somewhat lower profile, do business in a variety of jurisdictions. In some of those jurisdictions there may be an investment treaty between Mexico and the corresponding country, and such treaty may include an arbitration clause. However, no such treaty exists in a large number of jurisdictions.

In some jurisdictions, Mexican investors could be subject to arbitrary or discriminatory government action that may, in an extreme case, lead to seizure of their property. It is also likely that domestic courts do not always provide the sufficient assurance that such investors' rights will be properly protected, especially if the adversary party in litigation is the host government. Such risks can be cut short if Mexican investors have access to an international arbitration mechanism that helps circumvent local gaps and legal voids.

However, when a dispute arises between a Mexican investor and the government of one of the 142 ICSID member states, such dispute cannot be settled based on the Convention, as Mexico is not a contracting party to ICSID. In the best scenario, the dispute may be settled through the ICSID Additional Facility Rules, but only if a contracting state and Mexico have agreed to submit to that jurisdiction in a bilateral investment treaty. This will not necessarily be the case in all circumstances.

What all this amounts to is the following: a Mexican investor that exports capital will find it most advantageous for Mexico to adhere to the ICSID Convention because, in the event of a dispute with the host state, an investor will have a greater assurance that the conciliation and arbitration proceedings afforded by ICSID are available.

Although in certain quarters doubts remain in Mexico as to the advantages of international arbitration, it would be ill advised to ignore a legal and political

reality. In signing treaties that include an arbitration clause, Mexico has assumed rights and obligations. Politically speaking, a border has already been crossed. In the face of this indisputable fact, the many benefits implicit in the legal commitments already assumed by Mexico in the field of arbitration would be strengthened by joining ICSID.

A critical issue is to determine whether the dispute resolution system afforded by ICSID is the legal framework that best serves the goals of Mexico, which encompass a variety of elements, such as legal certainty, preventing conflicts with other states, promoting international law, and strengthening international tribunals using the advantages provided by a global economic system, and luring a greater flow of trade, investment, financing and technology to help national development.

One preliminary matter in this assessment is related to ICSID's legal character. The Convention is a treaty signed by states that confers certain rights, imposes certain obligations, and sets a balance between the host state's and the investors' interests. Pundits consider the institution created by the Convention as "one of the most modern and sophisticated mechanisms in contemporary international arbitration."

The Center, created on the basis of the Convention, is an international organization under the auspices of the World Bank; its arbitration process is subject to international law. It is an autonomous institution with its own legal capacity and its own legal rules, independent of domestic courts, and provides for proceedings that allow, pursuant to certain previously established rules, challenges to arbitral awards through appeals.

Since the Convention is a treaty, any differences arising among contracting states regarding its interpretation or application may be submitted to the International Court of Justice.

The use of the Additional Facility Rules implies the exclusion of the Convention, since it expressly states that "none of the provisions of the Convention shall be applicable to the proceedings (to which the Additional Facility Rules refer), or to recommendations, awards, or reports which may be rendered therein." (Additional Facility Rules, Article 3). Being exempted from the application of the Convention may turn out to be a disadvantage, as Mexico or one of its investors will be prevented from resorting to the legal and institutional framework afforded by the ICSID.

This means, for example, that the Convention rules regarding the recognition and enforcement of arbitration awards will not apply to awards issued under the Additional Facility. In the context of the Additional Facility Rules, such recognition and enforcement must follow a different set of regulations, as we will see later on.

The Convention has created a legal and institutional framework whose usefulness has been proven, with a Center that becomes an arbitration facilitator. It has a roster of arbitrators, and a contracting state may appoint four persons to the panel of arbitrators, a power not granted by the Additional Facility Rules.

If Mexico joins the Convention as a contracting party, it will be represented in the Center's Board of Directors. As such, it will take part in the drafting of the guidelines for the Center's operation, which includes the determination of the rules applicable to arbitration. Some proposals are already on the floor to enhance the Center's operation, which address issues that are certainly of interest for Mexico.

The general rule is that the award is binding upon the parties and that it cannot be appealed or otherwise challenged, except in the cases provided for under the Convention. One of the consequences of this principle is that the award will not be subject to judicial review by the national courts, as will happen in the case of the Additional Facility Rules.

For Mexico it is more advisable to ground the award interpretation, revision and annulment motions, as well as award recognition and enforcement, in a single statute, all wrapped up in a single package. All of these proceedings will thus be deposited within the framework of an organized institutional system with established and proven rules - a system that has gained experience, become reliable, and staffed with highly qualified arbitrators well acquainted with ICSID standards and international law.

Submitting motions for review of an award to a domestic court, as prescribed in the Additional Facility rules, is risky. The local court might ignore or be unaware of the peculiarities of arbitration, the precedents existing in the ICSID and, still worse, be unfamiliar with an international legal system applicable to foreign investment.

One of the critical goals of the ICSID system is to avoid confrontations between states by depoliticizing investment-related disputes. Under the ICSID system, an investor can assume a certain dispute as his own without the state of which he is a national being involved or having to grant diplomatic protection. This reduces or removes potential frictions between states, by encapsulating the nature of the conflict and putting some distance between the two involved states so as not to damage the bilateral political relationship.

The Convention expressly forbids a contracting state from extending diplomatic protection to one of its investors or filing an international claim if the dispute is subject to arbitration pursuant to the ICSID Convention. This prohibition is not provided for in the Additional Facility Rules, which would mean, in an undesirable case, that it is possible to commence an arbitration proceeding against Mexico. At the same time, the state of which the investor is a national could also exert whatever action is available under the diplomatic protection principle, with all of the inherent negative effects.

Mexico is already bound by a good number of treaties that include an arbitration clause for the settlement of investment disputes. From a legal and political point of view, it seems advisable for Mexico to advance one step further and become a contracting party of ICSID, with the benefits and advantages that accrue from this system of rules.

