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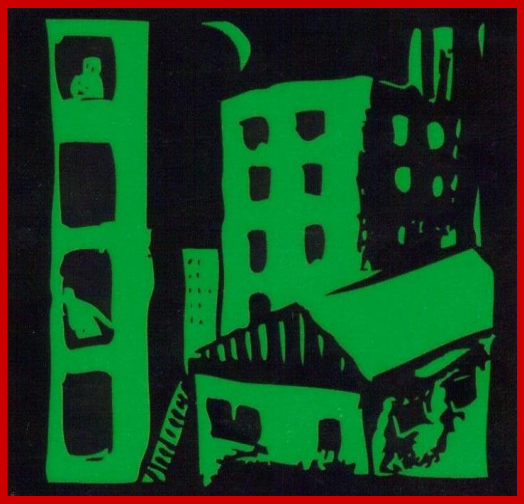

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The exhaustion of local judicial remedies in investor-state dispute settlement: a proposal for the African Continental Free Trade Agreement on Investment Protocol

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ABSTRACT

Over the past few years, the international Investor-State Dispute Settlement (ISDS) mechanisms have been confronted with an unprecedented level of scrutiny, and the system's legitimacy is being questioned by both developed and developing countries alike. This article presents a proposal for the adoption of the old customary international law rule of exhaustion of local remedies in the upcoming Investment Protocol of the African Continental Free Trade

Agreement (AfCFTA). It observes that the ISDS mechanism that will be developed under the AfCFTA framework is likely to be shaped by the legitimacy crisis in investment treaty arbitration and ongoing global debates about the reform of the ISDS mechanisms. In particular, the ISDS debate in the African region will continue to characterise and potentially derail the negotiations of the AfCFTA Protocol on Investment. The main contention is that adopting the exhaustion of local remedies under the AfCFTA Protocol on Investment before recourse is had to the ISDS is arguably the single reform with the greatest potential to foster a balanced investment dispute resolution mechanism and reduce political opposition to ISDS while still providing investors with access to ISDS when domestic remedies are inadequate. The article finally proposes a drafting suggestion for the adoption of the exhaustion of local remedies rule into the ISDS provision of the AfCFTA Protocol on Investment.

Keywords: Exhaustion of local remedies; African Continental Free Trade Area; Investment Protocol; ISDS; African courts.

1 INTRODUCTION

The ongoing phase II negotiations[1] for the African Continental Free Trade Area on Investment Protocol[2] present an opportunity for African countries to reconsider an old customary international law principle which requires foreign investors to exhaust local remedies before they can bring an investment claim under the International Investor-State Dispute Settlement (ISDS) mechanisms. Globally, the ISDS has been confronted with an unprecedented level of scrutiny and the system's legitimacy is being questioned by both developed and developing countries alike.[3] The controversies regarding the utility of ISDS mechanisms reached another level in July 2017 when Member States of the United Nations Commission on International Trade Law (UNCITRAL) entrusted its Working Group III with a broad mandate to work on the reform of ISDS. As can be observed from the discussions that have taken place so far in Working Group III, the legitimacy crisis faced by the ISDS has multiple facets and dimensions ranging from the perceived length and costs of investment arbitration, and the structural inadequacies of ad hoc adjudicatory bodies to ensure consistency in the interpretation of treaties, to the

[1] Phase II and Phase III negotiations-update available at https://www.tralac.org/blog/article/15090-afcfta-phase-ii-and-iii-negotiations-update.html (accessed 25 March 2021), Chidede says : "Phase II negotiations were initially scheduled to be concluded by December 2020 and Phase III negotiations to commence immediately after the conclusion of Phase II. This deadline was missed due to the coronavirus pandemic. The AU Assembly has set 31 December 2021 as the deadline for the conclusion of Phase II and III negotiations".

[2] Agreement Establishing the African Continental Free Trade Agreement available at https://au.int/sites/default/files/treaties/36437-treaty-consolidated_text_on_cfta_-_en.pdf (accessed 14 September 2020).

[3] United Nations Conference on Trade and Development, World Investment Report 2015-Reforming international investment Governance (June 2015) available online at http://unctad.org/en/PublicationsLibrary/wir2015en.pdf (accessed 15 September 2020).

perceived lack of impartiality and independence of investment arbitrators, so-called Third-Party Funding, while mass as well as class actions are considered extremely problematic developments in the ISDS system.[4]

As a result of the legitimacy crisis, both developed and emerging economies are currently re-evaluating their approaches to ISDS through various institutional reform approaches as well as international investment agreements (IIAs), including bilateral investment treaties (BITs) and the Investment Chapters of Free Trade Agreements.[5] Most prominently, the European Union (EU) has been advocating for the establishment of a multilateral investment court system where private investors retain standing to file claims directly against States. At its core, this "systemic" change would create a tribunal of first instance and an appellate body, with the judges having fixed terms, paid a regular salary, and selected on a random basis from a roster designated by States. These judges accordingly would be restricted from acting as counsel in other cases.[6] The EU has already concluded agreements containing such a system, designed for bilateral relations, but including flexibilities for multilateralization, with Canada,[7] Singapore,[8] Vietnam[9] and Mexico,[10] and indications are that more agreements with these features will follow.[11] As one of the world's largest sources and recipient of foreign direct investment and given that around half of all existing BITs involve EU members, the EU exercises considerable leverage in this reform process. [12]

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[4] United Nations Commission on International Trade Law Working Group III available at https://uncitral.un.org/en/working_groups/3/investor-state (accessed 13 September 2020).

[5] Porterfield MC "The exhaustion of local remedies in investor-state dispute: an idea whose time has come?" (2015) 41 *The Yale Journal of International Law* at 2.

[6] Multilateral Investment Court Overview of the reform proposals and prospects available online at https://www.europarl.europa.eu/RegData/etudes/BRIE/2020/646147/EPRS_BRI(2020)646147_EN.pdf (accessed 15 September 2020).

[7] Comprehensive Trade and Economic Agreement between Canada and European Union, https://investmentpolicy.unctad.org/international-investment-agreements/treaties/treaties-with-investment-provisions/3546/canada---eu-ceta-2016- (accessed 25 March 2021).

[8] EU-Singapore Trade and Investment Agreement http://trade.ec.europa.eu/doclib/press/index.cfm?id=961 (accessed 25 March 2021).

[9] EU-Veit Nam Investment Protection Agreement (signed 30 June 2019) available at https://investmentpolicy.unctad.org/international-investment-agreements/treaties/treaties-with-investment-provisions/3616/eu---viet-nam-investment-protection-agreement-2019- (accessed 25 March 2021).

[10] EU-Mexico Trade Agreement (not yet in force) available at https://ec.europa.eu/trade/policy/in-focus/eu-mexico-trade-agreement/ (accessed 25 March 2021).

[11] Zarra G "The relevance of state interests in recent ICSID practice" (2016) 26 *The Italian Yearbook of International Law* 487.

[12] Gaffney JP & Zeynep A "European bilateral approaches" in Bundenberg M, Griebel J, Hobe S & Rinisech A (eds) *International investment law: a handbook* Oxford : Hart Publishing (2015) 186.

While the African Union Member States have not yet concluded the African Continental Free Trade Agreement (AfCFTA) on Investment Protocol, some scholars such as, Rameau[13] and Madana[14], have argued that the Pan-African Investment Code (PAIC) is well suited to be used in the negotiation of the AfCFTA on Investment Protocol because it seeks to promote mutually beneficial investments for investors and host States and to harmonise intra-Africa trade. From the PAIC one can conclude that there is not yet a clear consensus on whether ISDS is desirable, and if not, the appropriateness of its alternatives continue to be controversial among African countries. In the South African Development Community (SADC) region, Annex I to the SADC Protocol on Finance and Investment,[15] which was finalised in August 2016, completely removes the provision on ISDS, but only provides for State-State dispute settlement. In addition to the Protocol, the SADC region has also adopted a Model Treaty (SADC Model BIT).[16] The new SADC Model BIT differs from its first edition by taking a stronger stand in excluding ISDS as it removes it from the actual treaty text. However, upon the request of some SADC members, an appropriate text on ISDS has been annexed to the reviewed model. The commentary to the SADC Model Treaty warns SADC countries about including ISDS in investment treaties.

Equally unhappy with the rulings of the International Centre for Settlement of International Disputes (ICSID), the South African government also resolved to move away from international investment arbitration. South Africa regards the ISDS as a system that jeopardises its national interests by subjecting it to an "unpredictable international arbitration that may constitute direct challenges to legitimate, constitutional and democratic policy making.[17] Furthermore, in August 2018, Tanzania tendered notice of its intention to terminate the Tanzania-The Netherlands BIT and the termination became effective in April 2019.[18] An ISDS provision is absent from some

[13] Rameau R "The Pan-African Investment Code as a model for negotiation on the Investment Protocol to the Agreement Establishing the African Continental Free Trade Area" (2021) *Transnation Dispute Management* 2 available at https://www.transnational-dispute-management.com/journal-advance-publication-article.asp?key=1874 (accessed 19 April 2021).

[14] Madana MK "The Pan-African Investment Code: A good step but more is needed" available online at https://academiccommons.columbia.edu/doi/10.7916/D8H14HXV (accessed 03 April 2021).

[15] See Agreement Amending Annex 1 (Cooperation on Investment) of the SADC Protocol on Finance and Investment, available at https://www.tralac.org/resources/by-region/sadc.html#FIP (accessed 15 September 2020).

[16] SADC "SADC Model Bilateral Investment Treaty Template with Commentary" (2012) available at www.iisd.org/itn/wpcontent/uploads/2012/10/sadc-model-bit-template-final.pdf (accessed 12 July 2019) (hereafter 'SADC Model BIT').

[17] Schlemmer E "An overview of South Africa's bilateral investment treaties and investment policy" (2016) 31(1) *ICSID Review - Foreign Investment Law Journal* 167 at 190.

[18] Legal Alert, Tanzania Terminates Bilateral Investment Treaty with Netherlands available at https://www.africalegalnetwork.com/tanzania/news/legal-alert-tanzania-terminates-bilateral-investment-treaty-netherlands/ (accessed 17 September 2020).

recent BITs involving African States, such as, the Brazil–Ethiopia BIT (2018)[19] and the Brazil–Malawi BIT (2015).[20] A "Special Note" to Article 23 of the 2016 East African Community (EAC) Model Investment Treaty shows a preference for a "no ISDS" framework. The Special Note reads : "the preferred option is not to include Investor-State dispute settlement. Several States are opting out or looking at opting out of Investor-State mechanisms, including Australia, South Africa and others."[21]Against this backdrop, the ISDS mechanism developed under the AfCFTA on Investment Protocol is likely to be shaped by the legitimacy crisis in investment treaty arbitration and ongoing global debates about the ISDS reform. In particular, the ISDS debate in the African region will continue to characterise and potentially derail the negotiations of the future AfCFTA on Investment Protocol.

This article contends that adopting the exhaustion of local remedies under the AfCFTA Investment Protocol before recourse is had to the ISDS through international arbitration is arguably the single reform with the greatest potential to foster a balanced investment dispute resolution mechanism and reduce political opposition to ISDS while still providing investors with access to ISDS when domestic remedies are inadequate. The next part of this article commences with a historical background to the rule on exhaustion of local remedies, and is followed by a discussion on the exhaustion of local remedies rule under international investment law. This is then followed by a discussion of the pros and cons of incorporating the exhaustion of local remedies and a drafting suggestion for the AfCFTA on Investment Protocol is proposed. Finally I provide some concluding remarks.

2 BACKGROUND TO THE RULE FOR EXHAUSTION OF LOCAL REMEDIES

Historically, the scholars of public international law, such as Chittharanjan Felix Amerasinghe, trace the exhaustion of local remedies rule to the old practices of authorized reprisals from as early as the 13th and 14th centuries, well before the rise of the modern system of international law.[22] Private individuals would be granted rights by their sovereign States to undertake reprisals against a foreign sovereign State that

[19] Agreement between the Federative Republic of Brazil and the Federal Democratic Republic of Ethiopia on Investment Cooperation and Facilitation available at https://investmentpolicy.unctad.org/international-investment-agreements/treaty-files/5717/download (accessed 17 September 2020).

[20] Investment Cooperation and facilitation agreement between the Federative Republic of Brazil and the Republic of Malawi available at https://investmentpolicy.unctad.org/international-investment-agreements/treaty-files/4715/download (accessed 17 September 2020).

[21] Article 23 of the 2016 East African Community (EAC) Model Investment Treaty (which was adopted in February 2016) available at https://www.eac.int/documents/category/investment-promotion-private-sector-development (accessed 16 September 2020).

[22] Amerasinghe CF *Local remedies in international law* New York: Cambridge University Press (2004) at 22.

had failed to do justice to them.[23] Reprisals were initially understood as private acts of revenge that were committed without the formal authorisation of sovereign States, but eventually they became public acts[24]. Doctrinally, reprisal rights are based on sovereign acts of a public nature, the authority to undertake reprisals was confined to recovery of private property in order to restore the property of a private individual to the status quo ante. Importantly, reprisal rights were exercised against the citizen of a foreign sovereign rather than the sovereign State itself.[25]

The rise of the principle of Statehood under public international law gave rise to the formation of centralised powers of governments. This was seen in that the granting of private letters of marque dwindled, and the grant of rights of reprisals by government ships on behalf of private individuals of a certain State. However, the private individuals on whose behalf those reprisal acts were taken were required first to exhaust local remedies before a sovereign State would intervene in respect of their claims. As discontent concerning the settlement of disputes through the use of force continued to grow, so did diplomatic espousal as a recognized practice under international law.[26] The requirement that a claimant should exhaust local remedies before a claim could be elevated to the international plane became part of the law of diplomatic protection. Indeed, the traditional international remedy in Investor-State disputes is diplomatic protection. But diplomatic protection is contingent upon the exhaustion of local remedies.[27]The unique feature of the local remedies rule is that it respects the sovereignty of a State by permitting that State to redress any wrong done to an alien in the State's territory before elevating the matter to an international plane and setting in motion the cumbersome process of espousal.[28] However , some exceptions to the rule have also been recognised under international law. For example, if the local remedies could be shown to be futile or non-existent, or if there had been a significant delay on

[23] See Porterfield (2015) at 2.

[24] Sohn LB "The new international law: protection of rights of individuals rather than states"(1982) 32 *American University Law Review* 3.

[25] Mummery DR "The content of the duty to exhaust local judicial remedies" (1964) 58 *American Journal of International Law* 389.

[26] Udombana N J "So far, so fair: the local remedies rule in the jurisprudence of the African Commission on Human and People's Rights" (2003) 94 *American Journal of International Law* 6.

[27] Heine LH "Impasse and accommodation: the protection of private direct foreign investment in the developing states" (1982) 14 *The Case Western Reserve Journal of International Law* 469.

[28] Article 15, International Law Commission (2006), Draft Articles on Diplomatic Protection, Official Records of the General Assembly, Sixty-first Session, Supplement No 10 UN Doc A/61/10 available at https://legal.un.org/ilc/texts/instruments/english/commentaries/9_8_2006.pdf (accessed 17 September 2020).

the part of the State in which local redress was being sought, a claimant was excused from having failed to exhaust local remedies.[29]

The International Law Commission (ILC) has suggested the codification of the exhaustion of the local remedies rule in the context of diplomatic protection. The exhaustion of local remedies rule requirement as a condition for the exercise of diplomatic protection is considered by the ILC as a "'principle of general international law' supported by judicial decisions, State practice, treaties and the writings of jurists".[30] Specifically, suggestions have been made by the ILC for the codification of the exhaustion of local remedies rule under Articles 14 and 15 of its Draft Articles on Diplomatic Protection. A State may only exercise diplomatic protection, or "present an international claim in respect of an injury to a national or other person", after the injured person has exhausted all local remedies. These are defined as the legal remedies available before administrative or judicial courts, whether ordinary or special, of the allegedly injuring State.[31] While the specific remedies available vary across States, the foreign national must appeal their case to the highest court of the allegedly injuring State, as far as domestic law permits. For the foreigner to satisfy the requirement, the arguments raised in the domestic proceedings must be the same as those intended to be raised in the international proceedings.

Article 15 of the ILC Articles on Diplomatic Protection provides five exceptions in terms of which local remedies need not be exhausted. Two of these exceptions that are relevant herein provide that local remedies need not be exhausted where (a) there are no reasonably available local remedies to provide effective redress, or the local remedies provide no reasonable possibility of such redress; or (b) there is undue delay in the remedial process that is attributable to the State alleged to be responsible. However, in exceptional circumstances, a foreigner does not need to exhaust local remedies. First, futility or ineffectiveness: local remedies need not be exhausted if they "are obviously futile", "offer no reasonable prospect of success", or "provide no reasonable possibility of effective redress". The foreigner must prove not only a low likelihood of success, but the inability of the domestic system to provide effective relief.[32] Secondly, undue delay caused by the allegedly responsible State in the conduct of domestic proceedings is another exception. No precise time limit can be abstractly determined, as this depends on circumstances, such as the volume of work required for the case to be thoroughly examined. Thirdly, the lack of a relevant connection between the foreigner and the allegedly responsible State is an exception that covers circumstances in which requiring the local remedies rule would be unreasonable or unfair, or cause great hardship. Lastly, there is the waiver of the requirement by the

[29] See Udombana (2003) at 8.

[30] Draft Articles on Diplomatic Protection with commentaries (2006) at 46.

[31] Draft Articles on Diplomatic Protection with commentaries (2006) at 47.

[32] Draft Articles on Diplomatic Protection with commentaries (2006) at 46.

allegedly responsible State: The waiver may appear in a pre-existing treaty, a contract between the State and the foreigner or an ad hoc arbitration agreement, or be implied or inferred from the State's conduct.[33]

In general, international investment agreements create special rules of international law, excluding or departing substantially from the rules on diplomatic protection. According to the ILC, "such treaties abandon or relax the conditions relating to the exercise of diplomatic protection, particularly the rules relating to local remedies rule". Therefore, the draft articles on diplomatic protection "do not apply to the extent they are inconsistent with special rules of international law, such as treaty provisions for the protection of investments".[34] The exhaustion of local remedies rule has also been recognised by the International Court of Justice (ICJ) in the *Interhandel* case as a "well established rule of customary international law"[35] and by a Chamber of the ICJ in *Elettronica Sicula SpA (ELSI)* (*ELSI* (1989)) as "an important principle of customary international law".[36] In the latter case the rule was described as requiring that "for an international claim to be admissible, it is sufficient if the essence of the claim has been brought before the competent tribunals and pursued as far as permitted by local law and procedures, and without success".[37] In the *Interhandel* case, the ICJ noted that the exhaustion of local remedies rule is a "well established principle of customary international law, generally applied in diplomatic protection claims, to give the state "where violation occurred….an opportunity to redress it by its own means within the framework of its domestic legal system, before resorting to international legal proceedings. The rule remains an important principle of customary international law and is applied both in diplomatic protection cases and in international human rights law.[38]

3 EXHAUSTION OF LOCAL REMEDIES UNDER INTERNATIONAL INVESTMENT LAW

In practice, international investment tribunals have been reluctant to require foreign investors to pursue local remedies.[39] As a result, foreign investors have been free to file treaty based arbitration claims in international tribunals without having to pursue, let

[33] Mollengarden Z "The utility of futility: local remedies rules in international investment law (2019) 58 *Virginia Journal of International Law* 412 at 413.

[34] Draft Articles on Diplomatic Protection with commentaries (2006) at 45.

[35] *Interhandel (Switz v US), Preliminary Objections*, 1959 ICJ Rep 6 at 27 (Mar 21) available online at http://www.icj-cij.org/docket/ files/34/2299.pdf (accessed 19 September 2020)

[36] *Elettronica Sicula SpA (ELSI) (Italy v US), Judgment* 1989 I.C.J. Rep. 15, 28 I.L.M. 1109 (July 20).

[37] *ELSI* : (1989) at para 91.

[38] Porterfield (2015) at 3.

[39] Porterfield (2015) at 4.

alone exhaust, the local remedies.[40] Unlike in the human rights law where the exhaustion of local remedies often applies in human rights treaties, very few international investment agreements require the exhaustion of local remedies. Investment tribunals, in both ICSID and non-ICSID cases, have generally held that, under the international investment law regime, the exhaustion of local remedies is waived unless expressly required.[41] The following parts explore the exhaustion of local remedies rule based on: the ICSID Convention, the non-ICSID Convention cases, and the IIAs.

3.1 Exhaustion of local remedies under the ICSID Convention

Pursuant to Article 6 of the ICSID Convention, the "consent of the parties to the international arbitration under the convention, shall unless stated otherwise, be deemed as a consent to the exclusion of any other remedy".[42] Under the same Article, "a contracting state may require the exhaustion of local administrative or judicial remedies as a condition of its consent to arbitration under the ICSID Convention".[43] Article 26 of the ICSID Convention alters or reverses the customary international law position by requiring the contracting parties to waive the requirement of exhaustion of local remedies unless otherwise stated.

The investors' waiver requires claimants to forego their local remedies once they have chosen the ICSID arbitration system. When interpreting Article 26 of the ICSID Convention, the tribunal in *Lanco International v Argentina (Lanco)*[44] held that the rule of exclusivity of forums in the first sentence of Article 26 "means that there is no need to exhaust domestic procedures before initiating ICSID arbitration, unless otherwise stipulated". Referring to earlier ICISD cases, the tribunal in *Lanco* concluded that the second sentence is precisely the waiver, by the contracting State Party, of the prior exhaustion of local remedies requirement, a requirement that a State may reserve to itself. Importantly, it indicated that States may require exhaustion as a condition for ICSID arbitration (i) in a bilateral treaty that offers submission to ICISD arbitration, (ii) in domestic legislation, or (iii) in a direct investment agreement that contains an ICISD clause.

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[40] Porterfield (2015) at 4.

[41] Kaufman & Potestà (2020) at 44.

[42] World Bank Group, CSID Convention, Regulations and Rules available at https://icsid.worldbank.org/sites/default/files/documents/ICSID%20Convention%20English.pdf (accessed 19 September 2020).

[43] Dolzer R & Schreuer C *Principles of international investment law* New York : Oxford University Press (2012) at 403.

[44] *Lanco International* Inc *v The Argentine Republic* ICSID Case No ARB/97/6.

Subsequent tribunals have followed the *Lanco* decision. In particular, in *Generation Ukraine v. Ukraine,*[45] the tribunal recalled the *Lanco* reasoning. Specifically, it held that, should a State wish to require exhaustion of the local remedies rule as a condition of consent to ICSID arbitration, the requirement "must be contained in the instrument in which such consent is expressed", in the case at hand, the investment treaty containing the arbitration clause. Moreover, the tribunal, in *Maffezzini vs Spain*,[46] confirmed the understanding that, under traditional international law, the exhaustion of local remedies rule is required unless expressly or implicitly waived. However, it read Article 26 of the ICISD Convention as making it clear that "unless a contracting state has conditioned its consent to ICSID arbitration on the prior exhaustion of local remedies, no such requirement will be applicable". Thus, reversing the customary international law rule.

Furthermore, the tribunal in *EDFI v Argentina*[47] held that recognising an implicit exhaustion requirement would be in conflict with the plain reading of Article 26, as well as invite States to mandate exhaustion of local requirement without giving fair warning of such stipulation to investors who enters a treaty expecting a clear path to arbitration. The reading of these cases therefore establishes a clear consolidated view that investment law cases under Article 26 of the ICSID Convention constitute an express waiver of the customary international law rule of local remedies in ICSID arbitrations. In some cases, tribunals have permitted investors to use most favoured nation (MFN) provisions to bypass local remedies requirements by invoking dispute settlement provisions in other IIAs that permit claims to be submitted directly to international arbitration.[48]

3.2 Exhaustion of local remedies in non-ICSID cases

In the NAFTA context, the *Waste Management II* tribunal affirmed that the NAFTA, "in common with almost all investment treaties", does not require the exhaustion of local remedies, which remain available until an international dispute is initiated under NAFTA Chapter 11.[49] The tribunal later clarified that Chapter 11, rather than requiring exhaustion of local remedies as a procedural condition for NAFTA arbitration, requires a waiver of any remaining remedies, including those before administrative and judicial courts of the host State. In a legal opinion prepared for the respondent in the *UNCITRAL case CME v Czech Republic (CME),* Christoph Schreuer and August Reinisch stated that, in order to take due account of Czech court decisions on matters of Czech law, the tribunal

[45] *Generation Ukraine* Inc *v Ukraine* ICSID Case No ARB/00/9. Award.

[46] *Emilio Agustín* Maffezini v *The Kingdom of* Spain ICSID Case No ARB/97/7.

[47] *EDF International SA, SAUR International SA and León Participaciones Argentinas SA v Argentine Republic*, ICSID Case No ARB/03/23.

[48] *Emilio Agustín Maffezini v The Kingdom of Spain* ICSID Case No ARB/97/7.

[49] *Waste Management Inc v United Mexican States* ICSID Case No ARB(AF)/00/3.

should await the final decision of pending proceedings in the Czech courts on the matters before the tribunal. Unpersuaded, the tribunal affirmed that doing so would amount to injecting into the applicable BIT an exhaustion of local remedies requirement, on which the BIT was silent. It further rejected the exhaustion of local remedies rule by expressing concerns about its policy implications: "Arbitration under a bilateral investment treaty would involve a high risk, always being threatened by the Damocles' sword of annulment on the basis that local remedies had not been exhausted."[50]

In *Mytilineos v Serbia and Montenegro*,[51] the UNCITRAL tribunal acknowledged the importance of the exhaustion of local remedies rule and recalled that many arbitral tribunals dispensed with it, both in ICSID arbitrations and in other contexts. It reasoned that the same interpretation should be adopted with regard to the Greece–Serbia and Montenegro BIT, whose fork-in-the-road clause resulted in a tacit waiver of the requirement, according to the tribunal. In conformity with the *CME* decision, it also indicated policy reasons why "BITs granting private investors direct access to international arbitration do not require local remedies to be exhausted": including such a requirement, in the tribunal's view, "would seriously undermine the effectiveness of this form of dispute settlement".

3.3 Exhaustion of local remedies in IIAs

In the African continent, the drafters of the PAIC decided to include the requirement for foreign investors to first exhaust local remedies in the Member States where their investment is located before a request for arbitration can be submitted.[52] This is done in a less detailed manner than will be suggested below. In this way, Investor-State arbitration becomes a remedy of last resort under the PAIC. For the inter-State arbitration, Article 28(4) of the SADC Model BIT requires the exhaustion of local remedies by an investor or investment before a State may initiate a claim on behalf of an investor. The 2016 Amending Annex 1 to the SADC Finance and Investment Protocol (FIP) does not provide for the exhaustion of local remedies rule or even the international resolution of ISDS.[53] Instead, Article 25 of the Amended Annex 1 of the

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[50] *CME Czech Republic BV v Czech Republic, UNCITRAL, Final Award* paras 412–413 (Mar 14 2003) available at http://www. italaw.com/documents/CME-2003-Final 001.pdf (accessed 17 September 2020).

[51] *Mytilineos* Holdings *SA v The State Union of Serbia* & *Montenegro and Republic of Serbia*, *Partial Award on Jurisdiction UNCITRAL*.

[52] Article 42(1)(c) the Pan African Investment Code available at https://au.int/en/documents/20161231/pan-african-investment-code-paic (accessed 15 September 2020).

[53] Agreement Amending Annex 1(Cooperation on investment) of Protocol on Finance and Investment available at https://www.sadc.int/files/7114/9500/6315/Agreement Amending Annex 1 -

SADC FIP provides for ISDS via domestic courts, judicial or administrative tribunals of the host State.[54] The treaty only makes reference to the SADC Tribunal, whose legitimacy has also been a subject of much controversy, by requiring that "any dispute between state parties to this annex shall be resolved in the manner provided under the protocol on the tribunal". Article 18 of the Protocol on Tribunal grants the Tribunal an exclusive jurisdiction over all disputes referred to it by natural or legal persons.[55] A further problem is that the said Tribunal has not been established yet because the Protocol has not entered into force. This therefore means that inter-State investment dispute settlement is still not possible at the moment in the SADC region.

The EAC Model Investment Treaty, provides in Article 23(4) for the

> "… conditions for Submission of a Claim to Arbitration (i) An Investor may submit a claim to arbitration pursuant to this Treaty, provided that: the Investor or Investment, as appropriate, (i) has first submitted a claim before the domestic courts of the Host State for the purpose of pursuing local remedies, after the exhaustion of any administrative remedies, relating to the measure underlying the claim under this Treaty, and a resolution has not been reached within a reasonable period of time from its submission to a local court of the Host State"[56] .

At a domestic level, the South Africa government has rejected the ISDS international arbitration following the termination of its BITs with European countries.[57] However, the South African Protection of Investment Act,[58] although not a treaty or a Treaty Model, does provide for the exhaustion of local remedies rule as a condition for international arbitration relating to foreign investment. It provides that "the government may consent to international arbitration in respect of investments covered

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Cooperation on investment - on the Protocol on Finance Investment - English - 2016.pdf (accessed 17 September 2020).

[54] Article 25 Agreement Amending Annex 1 (Cooperation on investment) of Protocol on Finance and Investment available at https://www.sadc.int/files/7114/9500/6315/Agreement Amending Annex 1 - Cooperation on investment – on the Protocol on Finance Investment – English- 2016.pdf (accessed 17 September 2020).

[55] Protocol on Tribunal in the Southern African Development Community available at https://www.sadc.int/files/1413/5292/8369/Protocol_on_the_Tribunal_and_Rules_thereof2000.pdf (accessed 19 September 2020).

[56] In the East African Community, the EAC Model Investment Treaty, available at https://investmentpolicy.unctad.org/international-investment-agreements/groupings/23/eac-east-african-community (accessed 18 September 2020).

[57] Qumba MF "Safeguarding foreign direct investment in South Africa: does the Protection of Investment Act live up to its name?" (2018) 25 *South African Journal of International Affairs* 357.

[58] Protection of Investment Act 22 of 2015.

by this Act, subject to the exhaustion of domestic remedies".[59] More recently, the exhaustion rule has re-appeared in treaties of a few States. Notably, the exhaustion of local remedies rule also features in the recent 2016 Morocco-Nigeria BIT which provides : "If the dispute cannot be resolved within six months, the investor may, after exhaustion of domestic remedies, resort to international arbitration."[60]

Beyond Africa, the International Institute for Sustainable Development (IISD) Model International Agreement on Investment for Sustainable Development which was published in 2005, under its Article 45 on dispute settlement, provides that a dispute between an investor/investment and the host State may not be commenced until domestic remedies are exhausted. However, the Article also grants the investor the opportunity to raise an exception to the local remedies rule on the grounds that the remedies are unavailable, or on the basis of demonstrable lack of independence and timeliness in the administrative or judicial processes implicated in the matter under the jurisdiction of the host State.[61] The Albania-Lithuania BIT[62] also requires exhaustion of local remedies before a claimant can resort to international arbitration by providing that "if such a dispute cannot be settled amicably within six months from the date of written notification provided in paragraph 1, and domestic and administrative remedies have been exhausted, the contracting party or the investor shall be entitled to submit the dispute either to ICSID or Ad hoc UNCITRAL arbitration. Under the 1976 Germany-Israel BIT,[63] the local remedies rule is included as a condition for international arbitration. It relevantly provides : "Local judicial remedies shall be exhausted before any dispute shall be submitted to the arbitral tribunal." Also, the Romania-Sri Lanka BIT of 1981,[64] expressly requires the exhaustion of local remedies by employing similar language to that used in Article 26 of the ICSID Convention: however, each contracting

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[59] Art 13(5) of the Protection of Investment Act 22 of 2015.

[60] Reciprocal Investment Promotion and Protection Agreement between the Government of the Kingdom of Morocco and the Government of the Federal Republic of Nigeria available at https://investmentpolicy.unctad.org/international-investment-agreements/treaty-files/5409/download (accessed 19 September 2020).

[61] Mann H, Von Moltke K, Peterson LE, & Cosbey A "IISD Model International Agreement on Investment for Sustainable Development" (2005) 20 *ICSID Review - Foreign Investment Law Journal* 91.

[62] Agreement between the Council of Ministers of the Republic of Albania and the Government of the Republic of Lithuania on the Promotion and Protection of Investments available at https://investmentpolicy.unctad.org/international-investment-agreements/treaty-files/20/download (accessed 16 September 2020).

[63] Treaty between the Federal Republic of Germany and the State of Israel concerning the Encouragement and Reciprocal Protection of Investments available at https://investmentpolicy.unctad.org/international-investment-agreements/treaty-files/1344/download (accessed 18 September 2020).

[64] Romania and Sri Lanka Agreement on the mutual promotion and guarantee of investments. Signed at Bucharest on 9 February 1981 available at https://investmentpolicy.unctad.org/international-investment-agreements/treaty-files/2210/download (accessed 19 September 2020).

party requires exhaustion of local administrative or judicial remedies as a condition of its consent to conciliation or arbitration by the Centre.

The Indian Model BIT[65] introduces the rule of exhaustion of local remedies. A claim must first be submitted before a relevant domestic court or administrative body of the host State. The domestic court or administrative body has to be approached within one year from the date of knowledge of the measure in question. Interestingly, under the domestic law of India, the period for filing a claim before domestic courts is normally three years from the date of the cause of action. It is further clarified that "the investor shall not assert that the obligation to exhaust local remedies does not apply or has been met on the basis that the claim under this Treaty is by a different party or in respect of a different cause of action". The exhaustion of local remedies rule is inapplicable if the investor can show that no local remedies are available or that they are incapable of providing relief. The incapacity to provide relief can become a ground to argue that the relief, if obtained from the host State, may be after a long delay. In such cases, the exhaustion of local remedies rule would not apply.

The foreign investor cannot invoke arbitration unless five years have passed from the date when the investor first acquired knowledge about the measure. These provisions have the effect of giving the courts of the host State an opportunity to decide the case first, and if the courts hold in favour of the investor, then no arbitration would be required. If the host State courts fail to redress the concerns, only then can an investment tribunal look into State action. Certain IIAs require exhaustion of local remedies for breaches of some but not other substantive standards. For instance, the Australia-Hungary BIT[66] and the Australia-Poland BIT[67] specify that the investor need not exhaust local remedies before submitting claims of expropriation and nationalisation to international arbitration. However, for disputes in relation to other substantive standards of protection, local remedies must be exhausted first.

The North American Free Trade Agreement (NAFTA)[68] gives investors up to three years to trigger arbitration, and thus investors may pursue local remedies until that

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[65] Model Text for the Indian Bilateral Investment Treaty available at https://investmentpolicy.unctad.org/international-investment-agreements/treaty-files/3560/download (accessed 19 September 2020).

[66] Agreement between Australia and Republic of Hungary on the Reciprocal Promotion and Protection of Investments available at https://investmentpolicy.unctad.org/international-investment-agreements/treaty-files/153/download (accessed 20 September 2020).

[67] Agreement between Australia and the Republic of Poland on the Reciprocal Promotion and Protection of Investments available at https://investmentpolicy.unctad.org/international-investment-agreements/treaty-files/163/download (accessed 20 September 2020).

[68] North American Free Trade Agreement available at https://investmentpolicy.unctad.org/international-investment-agreements/treaty-files/2412/download (accessed 20 September 2020).

time. The EU-Canada Comprehensive Economic and Trade Agreement (CETA)[69] goes further. Like NAFTA, it establishes a three-year statute of limitations if no domestic remedies are pursued. However, if domestic remedies are pursued, then the investor has two years to commence arbitration after they are completed, subject to a maximum of ten years from the initial measure. In each case, once an investor initiates arbitration, they may no longer bring or continue its claims for damages before a domestic administrative tribunal or court. In this way, investors are granted time to resolve matters within domestic legal systems without pressure to trigger ISDS. There is some evidence that this mechanism may lead to more reliance on domestic courts than fork-in-the-road provisions under which an investor must exclusively use either local remedies or ISDS. The following part discusses the advantages and disadvantages of the exhaustion of local remedies rule.

4 THE ADVANTAGES OF EXHAUSTION OF LOCAL REMEDIES IN THE AFCFTA INVESTMENT PROTOCOL

4.1 Addressing the institutional deficiencies and promoting the rule of law

In Africa, there has always been mistrust and a perception of weakness that have long been raised regarding the quality of African courts to deal with commercial arbitration.[70] In particular, critical concerns have long been raised regarding the capacity of African countries to abide by the fundamental principles of the rule law. For example, the 2019 Ibrahim Index of African Governance Report points out that during the last decade overall governance on the continent has improved, but that there has been a "pronounced and concerning drop in safety and rule of law, for which 33 out of the 54 African countries, home to almost two-thirds of the continent's population, have experienced a decline since 2006, 15 of them quite substantially".[71] The study also pointed out that a lack of good governance also negatively affects the achievement of social and economic targets to which the continent committed in the context of the Sustainable Development Goals (SDGs) and African Union Agenda 2063.

The conclusions arrived at in the Ibrahim Index of African Governance is largely supported by similar surveys, such as, Freedom House's Freedom in the World Survey; the World Justice Project Rule of Law Index; the World Bank's World Governance

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[69] Comprehensive Economic and Trade Agreement Between Canada, of the one Part and the European Union and its Member States, available at https://investmentpolicy.unctad.org/international-investment-agreements/treaty-files/3593/download (accessed 20 September 2020).

[70] Oduntan G "Africa before the international courts: the generational gap in international adjudication and arbitration" (2005) 5 *Journal of World Investment & Trade* 978.

[71] African Governments making progress: Ibrahim Index of African Countries available at https://www.dw.com/en/african-governance-making-progress-ibrahim-index-of-african-governance/a-55596399 (accessed 20 September 2020).

Indicators; and Transparency International's Corruption Perception Index.[72] In fact, in the Freedom in the World Survey 2019[73] , and by Freedom House[74], it was noted that of the11 countries in the world with the worst aggregate scores for political and civil liberties, six (Eritrea, South Sudan, Somalia, Sudan, Equatorial Guinea, and the Central African Republic) were from sub-Saharan Africa. In a poll jointly conducted by The New York Times and the Pew Global Attitudes Project in 2006, a majority of Africans polled in ten sub-Saharan African countries indicated that they had been better off five years prior to the survey.[75]

While the methodology of these rankings is not without controversy, these surveys portray a similar story: Africa is still lagging behind in the development of its legal institutions and in the protections accorded to foreign investors. These statistics can be a great cause of discomfort to foreign investors who have to accept that ISDS should be adjudicated in African courts instead of long-standing ICSID tribunals, UNCITRAL or other ad hoc tribunals. Therefore, there is no doubt that African legal systems need to be improved. In support of this, the United Nations Conference on Trade and Development (UNCTAD) has argued that the reform of the ISDS should not exclusively focus on arbitration but that domestic reforms aimed at fostering sound and well-working legal institutions in host States are important. This may ultimately help remedy some of the host State institutional deficiencies the ISDS system was designed to address.[76] Therefore, the exhaustion of local remedies rule, if adopted by the AfCFTA Investment Protocol, could help to both strengthen and integrate the domestic and international systems. It can also help to foster a well-functioning judicial institution in host States and may ultimately help to remedy some of the host State institutional deficiencies which investment arbitration was designed to address.[77] However, removing ISDS from the domestic courts discourages local courts from improving the

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[72] Fombad CM & Kibet E "The rule of law in sub-Saharan Africa: reflections on promises, progress, pitfalls and prospects" (2018) 18 *African Human Rights Law Journal* 206.

[73] Freedom in the World available at https://freedomhouse.org/report/freedom-world/2019/democracy-retreat (accessed 21 September 2020).

[74] Freedom House, Democratic Trends in Africa in Four Charts available at https://freedomhouse.org/article/democratic-trends-africa-four-charts (accessed 21 September 2020).

[75] See Shivute P 'The rule of law in sub-Saharan Africa: An overview' available at http://www.kas.de/upload/auslandshomepages/namibia/HumanRights/shivute2.pdf (accessed 20 September 2018).

[76] United Nations Conference on Trade and Development "Improving Investment Dispute Settlement: UNCTAD Policy Tools" available at https://unctad.org/system/files/official-document/diaepcb2017d8_en.pdf (accessed 21 September 2020).

[77] Brower C & Schill S "Is arbitration a threat or a boon to the legitimacy of international investment aw?" (2009) 9 *Chicago Journal of International Law* 473.

quality of domestic adjudication.[78] By resorting to international arbitration, ISDS substitutes the use of domestic legal institutions and can thereby entrench their weaknesses.

By contrast, when BITs provide investors with direct access to ISDS, they bypass domestic courts. As a result, they reduce courts' incentives to improve performance because they are deprived of the opportunity to improve the institutions.[79] Therefore, if the proposition that the AfCFTA Investment Protocol should adopt exhaustion of local remedies as a pre-condition to ISDS is accepted, African countries would have to make sure that foreign investors can be confident that the courts on the African continent will deal with their claims with sufficient independence and efficiency. Unfortunately, as the statistics assessing the quality of national judiciaries, good governance and the rule of law in African States show, African courts are perceived to perform badly. Therefore, there should be some concerted effort to improve this situation on the African continent through the use of the exhaustion of local remedies rule in the AfCFTA Investment Protocol.

4.2 Improve the quality of justice in the ISDS mechanisms

The scepticism surrounding the use of ISDS within the African continent continues to grow. Won Kidane, one of the leading opponents of the ISDS, has argued that the system is a tool invented by Western countries to impose their power on weaker or emerging economies and that African States have been required to play by the rules of international arbitral institutions. He points out that the African States have been required to understand a culture of legal proceedings that was totally external to their domestic legal cultures, and that their participation in the formation of ICSID, for instance, was limited to supporting the institutions when African States appear as respondents in ISDS cases.[80] African States have also raised concerns about the traditional ISDS system, including, lack of legitimacy and transparency, exorbitant costs of arbitration proceedings and arbitral awards, as well as inconsistent and flawed decisions. States have also complained that the system allows foreign investors to challenge legitimate public welfare measures of host States before international arbitration tribunals. Governments are concerned about their sovereignty or policy space as they are discouraged from adopting public welfare regulations, resulting in regulatory chill.[81]

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[78] Bronckers M "Is investor–state dispute settlement (ISDS) superior to litigation before domestic courts? An EU view on bilateral trade agreements" (2015) 18 *Journal of International Economic Law* 661.

[79] A Tzanakopoulos "Domestic courts in international law: the international judicial function of national courts" (2011) 34 *Loyola of Los Angeles International and Comparative Law Review* 133.

[80] Kidane W "The culture of investment arbitration: an African perspective" (2019) 34 *ICSID Review* 420.

[81] Mohamed H et al "Investment Treaty Arbitration and AfCFTA: Towards a New Horizon of Reshaping ISDS Regime" available at https://www.africaarbitrationacademy.org/wp-

The legitimacy crisis and ongoing debates concerning the integrity of the ISDS mechanisms prove the fact that international tribunals are not superior to domestic litigation, including those in Africa.[82] In particular, the troubling concerns are about the chilling effect of the international investment regime on the ability of sovereign States to exercise their authority over their inherent sovereign right to regulate.[83] The most prominent feature of the debates is the regulatory chill effect caused by ISDS which was mentioned as an aspect that warranted consideration by the UNCITRAL Working Group III review of the ISDS. The Working Group commented that the ISDS has discouraged States from undertaking measures aimed at regulating their economic activities and to protect economic, social and environmental rights within their domestic sphere. The costs associated with ISDS proceedings and the large amounts awarded as damages by tribunals are elements that could undermine the States' ability to regulate.[84]

Pro-investor rules, enforced through the ISDS mechanism, are seen to undermine State sovereignty and States' constitutional obligations, subordinate the State's responsibility to regulate in the public interest and the public good, and erode democratic electoral mandates, processes, and accountability.[85] However, if the exhaustion of local remedies rule would be adopted by African States under the AfCFTA Investment Protocol, the international investment tribunals would benefit from the domestic courts' characterisation of the relevant African domestic law, such as policies on health and environmental issues decided by the domestic courts of African States.[86] This would give the African courts the opportunity to fix the problems before they are brought to an international tribunal. The use of exhaustion of local remedies as a reform option has received international backing. Notably, the Report of Working Group III on ISDS Reform mentioned that requiring investors to exhaust local remedies

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content/uploads/2019/10/Investment-Treaty-Arbitration-and-AfCFTA_Mohamed-Negm-and-Francoise-Ingabire-1.pdf (accessed 03 April 2021). See also Chidede T, Investor-State Dispute Settlement in Africa and AfCFTA Investment Protocol, available at https://www.tralac.org/blog/article/13787-investor-state-dispute-settlement-in-africa-and-the-afcfta-investment-protocol.html (accessed 03 April 2021)

[82] Van Harten G "Investment arbitrators' evident lack of restraint" (2014) 5 *Journal of International Dispute Settlement* 4.

[83] United Nations Commission on International Trade Law "The Working Group III: Investor-State Dispute Settlement Reform" available at https://uncitral.un.org/en/working_groups/3/investor-state (accessed 19 September 2020).

[84] Giorgetti C "Reforming international investment arbitration: an introduction" (2019) 18 *The Law and Practice of International Courts and Tribunals* 309.

[85] Van Harten G, Kelsey J & Schneiderman D "Phase 2 of the UNCITRAL ISDS Review: Why 'Other Matters' Really Matter" available at https://digitalcommons.osgoode.yorku.ca/cgi/viewcontent.cgi?article=1335&context=all_papers (accessed 19 September 2020).

[86] See Porterfield (2015) at 7.

before bringing their claims to investment arbitration was a tool to be considered in reforming ISDS rather than a concern to be addressed.[87]

The rule may guide and inform the international tribunals on whether any property rights had vested in domestic law, instead of leaving such matters to the unfettered discretion and highly subjective inquiry of arbitral tribunals Similarly, judicial pronouncements on the relevant standards of protection for property rights could provide tribunals with evidence of relevant State practice for the purpose of defining standards of protection, such as, Fair and Equitable Treatment (FET) and indirect expropriation, that are intended to reflect customary international law.[88] Deferring an investor-State claim until after domestic courts have addressed a dispute would also promote compliance with the principle—espoused by the South African government—that IIAs should not provide investors with greater substantive rights than the comparable protection provided to citizens under domestic law.[89] A tribunal, for example, would presumably hesitate to find that the South African government had engaged in the indirect expropriation of an asset of a foreign investor if the South African Constitutional Court had determined that the relevant measure did not constitute a "regulatory taking" under section 25 of the South African Constitution.[90] The result is that ISDS legitimacy would improve by granting domestic courts an opportunity to decide on matters of public policy, such as, affirmative action, health issues, and environment, labour and human rights issues. Indeed, on 17 July 2019, the government of South Africa submitted its proposals for ISDS reform in preparation for the 38th Session of UNCITRAL Working Group III. Among others, the South African government argued that the local remedies must first be exhausted before an approach is made to the ISDS. According to the country's submission, this would ensure that domestic judicial institutions get a first shot at managing government conduct before a case can proceed to ISDS. This would also align investment law with customary international law and international human rights law, and would help to prevent incompatibility with national laws and regulations. Investment arbitrators are generally specialists in international investment law, and are not necessarily familiar with the intricacies of domestic legal systems.[91]

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[87] The United Nations Commission on International Trade Law, Working Group III: Investor-State Dispute Settlement Reform available at https://uncitral.un.org/en/working_groups/3/investor-state (accessed 21 September 2020).

[88] Barrera EB "The Case for Removing the Fair and Equitable Treatment Standard from NAFTA" available at https://papers.ssrn.com/sol3/Data_Integrity_Notice.cfm?abid=3012347 (accessed 19 September 2020).

[89] Preamble of the Protection of Investment Act 22 of 2015.

[90] Section 25 of the Constitution of the Republic of South Africa, 1996.

[91] United Nations Commission on International Trade Law, Working Group III "Possible reform of Investor-State dispute settlement (ISDS) Submission from the Government of South Africa" available at

Furthermore, scholars, such as, Chen,[92] Onyema,[93] and Portfield[94], agree that local courts are critical if not indispensable for the resolution of investor-State disputes. Secondly, the African Union (AU) vigorously supports the use and development of local courts. This is done at three levels. The African Charter mandates that human rights disputes must first be referred to domestic courts before they can be referred to the AU Commission. Furthermore, Agenda 2063 envisages that by 2023, seventy per cent of the populations of AU Member States must perceive their judiciaries to be independent, that they deliver judgments on a fair and timely basis, and that the rule of law is entrenched.[95] Finally, the AU proposes an AfCFTA dispute settlement architecture wherein natural and legal persons may refer disputes emanating from the AfCFTA to their local courts. The proposal states that local courts will assist in decentralising dispute resolution, and that such referral will work best if it is provided for in the AfCFTA Agreement.

4.3 Provide a review mechanism for African courts

Domestic judicial systems would reassume their roles as the primary fora for disputes involving claims by foreign investors, and investor State tribunals would provide an extra layer of protection against any deficiencies in domestic legal processes. The exhaustion of local remedies requirement would reduce the bypassing concern while still preserving the option of arbitration as a last resort.[96] Franck notes some additional advantages: presumably, if foreign investors were required to litigate disputes through domestic courts rather than directly taking their claims to international arbitration, this might build the capacity of local courts by the following: (1) providing domestic courts with an opportunity to articulate relevant principles of domestic law; (2) increasing the transparency of the system; and (3) giving notice to future investors of the relevant domestic legal standards and their application. Moreover, the local remedies rule would be compatible with the desire to harmonise the varying approaches taken by States to investor protection in IIAs, given that it would provide a consistent standard for

https://uncitral.un.org/sites/uncitral.un.org/files/176-e_submission_south_africa.pdf (accessed 22 September 2020).

92 See Chen R "Bilateral investment treaties and domestic institutional reform" (2017) 55 *Columbia Journal of Transnational Law* 567 at 570.

93 Onyema E "African participation in the ICSID system: appointment and disqualification of arbitrators" (2019) 34 *ICSID Review - Foreign Investment Law Journal* 376.

94 See Porterfield (2015) at 8.

95 Agenda 2063 "The Africa We Want" available at https://www.un.org/en/africa/osaa/pdf/au/agenda2063.pdf (accessed 27 September 2020).

96 Ginsburg T "International substitutes for domestic institutions: bilateral investment treaties and governance" (2005) 25 *International Review of Law and Economics* 119.

determining whether and when ISDS was appropriate in any dispute against a State, ie whether or not the investor has pursued all reasonably available domestic remedies.[97]

The jurisprudence from the African courts indicates that the activities of domestic courts may be the object of scrutiny by the international tribunal, especially where a denial of justice has been alleged. A typical form of interaction between international arbitral tribunals and domestic courts in investment law occurs when the national court proceedings become subject to review in investment arbitration. In the arbitral proceedings in *Jan de Nul NV* and *Dredging International NV v Arab Republic of Egypt* (*Jan de Nul* (2008)),[98] a judgment of an Egyptian lower court in the district came under scrutiny. The dispute arose out of a misunderstanding about the terms and conditions of a contract for dredging activities in the Suez Canal. The claimants alleged that the Suez Canal Authority (SCA) had misrepresented the size of the tasks. They contended to have encountered conditions during the performance of the dredging works that were not mentioned at the tender stage, namely, a lesser volume to be dredged, an imbalance between the deepening and widening operations, and a higher proportion of rock. Therefore, the claimants requested compensation for additional costs, which was denied by the SCA and thus led to two contract claims before Egyptian national courts. The first was an action to declare the dredging contract null and void due to error and fraud. With regard to the second action, the investor sought relief for a series of deductions made by the SCA from the amounts paid under the dredging contract.[99]

The Administrative Court of Ismaïlia rendered the decisions for the two contractual disputes. In substance, as regards the first contractual case, the Court declined to annul the contract for fraudulent misrepresentation or error and dismissed the claim for extra compensation, because the claimants "had failed to make the necessary investigations and had undertaken to perform at the price agreed regardless of the dredging conditions". Concerning the second contractual case, the Court awarded the claimants USD 1 087 997. 64 and LE 216 045, which constituted around one-third of the deductions claimed. Disagreeing with the outcome of the case, the claimants appealed the judgements in both cases to the High Administrative Court of Egypt. The SCA also appealed, but only against the second contractual claim for undue deductions. In addition, the claimants submitted a BIT claim to the ICSID. Throughout the arbitral proceeding the national appeal proceedings remained pending.

Before the investment tribunal, the claimants, relying on the fair and equitable treatment standard, claimed that a denial of justice had occurred through the "unfair" decision made by the Administrative Court of Ismaïlia. The claimants' concern with the

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[97] Frank SD "The legitimacy crisis in investment treaty arbitration: privatizing public international law through inconsistent decisions" (2005) 73 *Fordham Law Review* 1522.

[98] ICSID Case No ARB/04/13 (2008).

[99] *Jan de Nul* (2008) at para 33.

Egyptian judgment was its outcome, which did not recognise the fraudulent misrepresentation in the contract as the SCA had retained technical information as regards the size of the project. The arbitral tribunal did not accept the arguments of the claimants. First, the tribunal emphasised that the investors did not "complain of the failure of the Egyptian legal system as such, but merely of the conduct of the Ismaïlia Court. This is not sufficient to justify a claim for denial of justice, let it be through the fair and equitable claim". Moreover, the appellate proceedings were ongoing and did not appear to be "in any manner dysfunctional".[100]

As a result, the tribunal explicitly denied that "an unjust judgement of a lower court may per se constitute unfair and inequitable treatment and, therefore, denial of justice". Finally, all claims based on the BIT were dismissed by the ICSID tribunal. According to available information, the claimants have dropped both actions for appeal before the Egyptian national courts. The judgement in the appeal initiated by the SCA was rendered on 24 January 2017. The High Administrative Court of Egypt nullified the 2013 decision of the Administrative Court of Ismaïlia, which thus resulted in the nullification of any compensation for the claimants for the alleged undue deductions made by the SCA. *Jan de Nul* (2008) shows that investment tribunals are not easily satisfied with a denial of justice claim made by a claimant. On the contrary, the case highlights that investors are to make a reasonable attempt in domestic courts to obtain redress before a claim for the violation of the international protection standard can be filed against the host country. The *Jan de Nul* (2008) tribunal thus reserved the role of the Egyptian national courts to decide upon the contract claims that were submitted to it.[101]

The best example from within the African continent of where international tribunals had to exercise their review powers is the domestic forum selection clause in investment contracts. Under this clause disputes arising in the context of the contract are to be taken to national courts or tribunals. Not surprisingly, host States have argued that clauses of this kind deprived the international tribunals of their jurisdiction and were meant to restrict the investors to local remedies. Cases involving domestic forum selection clauses in contracts have been very prominent in recent years, but it is worth pointing out that the problem is not new. In fact, in the very first case before an ICSID tribunal, in a decision of 1974, the tribunal was already confronted with this question. *In Holiday Inns v Morocco,*[102] the parties had concluded a "Basic Agreement" containing an ICSID clause. This agreement provided for the establishment and operation of hotels. The Basic Agreement also provided for financing by the Government. This financing was

[100] Jan de Nul (2008) at para 34.

[101] Mbengue M & Schacherer S "International investment law in African courts" in Ruiz Fabri H & Stoppioni E (eds) *International investment law: an analysis of major decisions* Oxford : Hart Publishing 4. (forthcoming)

[102] *Holiday Inns* SA and others *v Morocco* ICSID Case No ARB/72/1.

to be carried out by means of separate loan contracts. The loan contracts did not contain ICSID clauses but forum selection clauses in favour of the Moroccan courts.

After the ICSID Tribunal's decision, in which it found on the basis of the Basic Agreement that it had jurisdiction, the Moroccan Government objected to the jurisdiction of ICSID over the claims connected with the loan contracts. The Government contended that the Moroccan courts had sole jurisdiction to decide issues concerning the loan contracts and that such matters "should not be heard by the Arbitration Tribunal until [...]decided by the Moroccan courts at the suit of the interested parties". The ICSID Tribunal rejected these contentions and affirmed its jurisdiction over the entire claim. It based its reasoning on "the general unity of an investment operation" and the principle that "international proceedings in principle have primacy over purely internal proceedings". The Tribunal added that the Basic Agreement was the "charter of the investment", of which the loan contracts were "a measure of execution". The Tribunal added that certain aspects of the loan contracts could be isolated and considered outside the Basic Agreement. Therefore, questions "affecting the indirect or secondary aspects of the investment" could.

One option involving complementarity is to provide for domestic decision-making up to a certain stage, subject to review by an international adjudicatory body. The NAFTA review of anti-dumping and countervailing duty decisions by national administrative bodies provides an example. Chapter 19 of the trade agreement provides that the State of nationality of the foreign exporter may, or upon the exporter's request shall, request the establishment of a binational panel to review the final determination issued by the relevant authority of the NAFTA party. The binational panel, composed of five members from the two countries involved, can affirm, overrule, or remand agency determinations. The decisions are binding within the domestic jurisdiction and cannot be appealed to domestic courts. The process is complemented by an extraordinary challenge procedure where a NAFTA party can challenge a binational panel ruling on limited grounds, such as for manifestly exceeding its powers.[103]

Under NAFTA Chapter 19, each party applies its domestic law, which it is free to amend at any time provided that its domestic law complies with WTO rules. WTO law, in turn, is enforced through interstate dispute settlement, which helps to clarify the meaning of the provisions. The binational panel's determination focusses exclusively on the correct application of the law by the domestic authority conducting the investigation, creating an international check on the domestic decision-making process. As a result, binational panels replace judicial review of national administrative decisions by domestic courts. In theory, parties could adapt this process to provide for first-level judicial review by a national court, subject to appeal to an international

[103] North American Free Trade Agreement available at https://investmentpolicy.unctad.org/international-investment-agreements/treaty-files/2412/download (accessed 20 September 2020).

tribunal. The ability to appeal judicial decisions to an international panel can check bias in national decision-making, but it also raises sovereignty concerns. Indeed, the current United States administration wants to terminate NAFTA Chapter 19, and others in the United States have questioned Chapter 19's constitutionality.[104] Similarly, Belgium asked the Court of Justice of the European Union (CJEU) to issue an opinion on the compatibility of the investment court system under CETA with EU law, and the CJEU held in March 2018 that the provisions for ISDS in a BIT between EU Member States are incompatible with EU law.[105] The sovereignty concerns would become even more salient were an international body to overrule a domestic court's application of domestic law. Reflecting this concern, India's new model BIT provides that arbitral tribunals shall not have jurisdiction "to re-examine any legal issue which has been finally settled by any judicial authority of the Host State".[106]

5 DISADVANTAGES OF THE EXHAUSTION OF LOCAL REMEDIES

The Preamble to the ICSID Convention states that "while such investment disputes would usually be subject to national legal processes, international methods of settlement may be appropriate in certain cases".[107] The Report of the Executive Directors to the ICSID Convention states: The Executive Directors recognize that investment disputes are as a rule settled through administrative, judicial or arbitral procedures available under the laws of the country in which the investment concerned is made. However, experience shows that disputes may arise which the parties wish to settle by other methods; and investment agreements entered into in recent years show that both States and investors frequently consider that it is in their mutual interest to agree to resort to international methods of settlement.[108]

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[104] North American Free Trade Agreement available at https://investmentpolicy.unctad.org/international-investment-agreements/treaty-files/2412/download (accessed 20 September 2020).

[105] Croisant G " Opinion 1/17- the CJEU confirms the CETA investment court system is incompatible with the EU law" available at http://arbitrationblog.kluwerarbitration.com/2019/04/30/opinion-117-the-cjeu-confirms-that-cetas-investment-court-system-is-compatible-with-eu-law/ (accessed 17 September 2020).

[106] Art 14 Model Text for the Indian Bilateral Investment Treaty available at http://www.jurisafrica.org/html/pdf_indian-bilateral-investment-treaty.pdf (accessed 19 September 2020).

[107] ICSID Convention, Regulations and Rules available at https://icsid.worldbank.org/sites/default/files/ICSID%20Convention%20English.pdf (accessed 19 September 2020).

[108] Report of the executive directors on the ICSID convention available at https://icsid.worldbank.org/resources/rules-and-regulations/convention/report-of-the-executive-director (Accessed 19 September 2020).

Requiring investors to pursue domestic remedies has been criticised for causing delay and increasing costs, especially since in many States it can take several years and layers of judicial review to reach a final judgment. According to some, insisting on exhaustion of local remedies would also carry disadvantages for the host State, as "public proceedings in the domestic courts are likely to exacerbate the dispute and may affect the host State's investment climate". Furthermore, "once the host State's highest court has made a decision, it may be more difficult for the government to accept a compromise or a contrary international judicial decision".[109] The very idea that an investment tribunal has authority to review the decision of the host State's highest court may not be acceptable for a number of States.[110] The challenges to local courts are, first, that a host State may not have an efficient and independent judicial system. Secondly, local litigation may take long to conclude, due to high caseloads, thus resulting in costly litigation. Thirdly, local courts may lack the expertise to deal with complex international law principles applicable to investment transactions.

Various studies confirm the existence of the above challenges for the judiciaries of some African States, such as, lack of resources, poor rule of law, lack of judicial independence, high litigation costs, and the long delays in concluding cases. Weak institutions can increase costs and create inefficiencies for businesses in general, whether foreign or domestic. Moreover, because their investments often result in sunk costs, foreign firms are "especially vulnerable to any form of uncertainty, including uncertainty stemming from poor government efficiency, policy reversals, graft or weak enforcement of property rights and of the legal system in general".[111] Thus, the quality of a State's institutions would be expected to affect the level of foreign direct investment (FDI) at least at the margins, and the evidence supports such a relationship. Foreign investors value a transparent and rational policymaking process. Undoubtedly the actual substance of a host State's laws is important, as investors will be drawn to environments that offer favourable tax laws and financial regulations. However, there is independent value in a well- functioning process. Rules in general are likely to be more effective when affected parties have a voice in shaping them, and business rules, in particular, likely benefit from the input of firms, including foreign owned ones. Moreover, foreign investors, worried about sunk costs, are particularly sensitive to policy instability and uncertainty. While even rational rulemaking institutions are liable to change course sometimes, they are at least less likely to veer off in an arbitrary direction.[112]

[109] Kaufmann-Kohler & Potesta' (2020) at 140.

[110] Dagbanja DN "Constitutionalism and local remedies rule as limitations on investor-state arbitration: perspectives from Ghana" (2017) 17 *Oxford University Commonwealth Law Journal* 121.

[111] Chen (2017) .

[112] See Chen (2017) at 570.

Foreign investors value an efficient bureaucracy. Apart from the institutions that create laws and regulations, businesses must be concerned about the range of government officials who implement and administer them. Excessive red tape interferes with the efficient conduct of business. Corruption similarly produces bottlenecks, heightens uncertainty, and raises costs, with the added concern of forcing investors to choose between forgoing an opportunity entirely and paying a bribe that could lead to criminal liability. By contrast, an efficient bureaucracy allows firms to reduce costs and minimise distractions as they focus on their actual value-creating business activity. More importantly, foreign investors value an independent judiciary capable of enforcing contract and property rights. Scholars have long noted the connection between a strong judiciary and a hospitable environment for investment, emphasising that even the "best" substantive law will be of little value in the absence of effective court enforcement. Foreign investors, like all commercial actors, depend on the presence of efficient and impartial courts to ensure that their contract and property rights will be protected. Backlogged courts with slow processing times, or judges who are subject to bribery or government influence, interfere with business activity by negating that expectation.[113]

6 DRAFTING THE EXHAUSTION OF LOCAL REMEDIES RULE UNDER THE AFCFTA INVESTMENT PROTOCOL

Investment tribunals, under the ICSID Convention as well as in other contexts, have consistently implied waiver from investment treaties that are silent on the applicability of the exhaustion of local remedies rule, reversing the customary international law presumption that it should apply unless clearly waived. Accordingly, States that wish the exhaustion of local remedies rule to apply to the ISDS mechanism in an investment agreement should expressly and unequivocally indicate that, for example, by stating that the investor “shall” or “must” exhaust local remedies before initiating international arbitration. This is the case with the recent models, such as, the SADC[114] and Indian models[115], which, in response to interpretations by investment tribunals, include an exhaustion of local remedies requirement. Accordingly, it is proposed that the AU in its drafting of the AfCFTA Investment Protocol should provide for a clause that reinstates the exhaustion requirement so that foreign investors' first recourse would be to domestic courts and administrative tribunals, within the foreign investment regulatory framework of the AfCFTA. Ideally, the exhaustion of local remedies rule should be

[113] See Chen (2017) at 571.

[114] SADC Model Bilateral Investment Treaty Template with Commentary available at https://www.iisd.org/itn/wp-content/uploads/2012/10/sadc-model-bit-template-final.pdf (accessed 16 September 2020).

[115] Model Text for the Indian Bilateral Investment Treaty available at http://www.jurisafrica.org/html/pdf indian-bilateral-investment-treaty.pdf (accessed 19 September 2020).

incorporated into the AfCFTA Investment Protocol's dispute resolution provisions. The rule regarding local remedies should thus be drafted so as to indicate its functions and facilitate its performance. I suggest, subject to improvements by those more skilled in drafting, a formulation of the exhaustion of local remedies rule in the AfCFTA Investment Protocol along the following lines:

> "1. In respect of the claim that the African Host State has breached any provisions of the AfCFTA Investment Protocol, subject to the provisions of paragraph 4 of this Article, a disputing investor must first exhaust local remedies before the relevant domestic court or administrative tribunal for purposes of seeking redress in respect of the same measure or similar factual matters for which a breach of this Treaty is claimed, before an investor's claim is brought to an international tribunal.
>
> 2. The international responsibility of the African Host State for an injury to a disputing investor may not be invoked in the form of an international arbitration so long as local remedies, available to the disputing investor under the domestic law of the African Host State and providing an effective, sufficient and timely means of redress, have not been exhausted. Such claim before the relevant domestic courts or administrative tribunals of the African Host State must be submitted within one (1) year from the date on which the disputing investor first acquired, or should have first acquired, knowledge of the measure in question and knowledge that the investment, or the investor with respect to its investment, had incurred loss or damage as a result of actions attributable to the African Host State.
>
> 3. Resort to local remedies is required prior to the presentation of an international claim in order to determine whether or not an injury to a disputing investor has in fact occurred; whether or not an act or omission is, in the circumstances, attributable to the African Host State; whether or not such an act or omission is incompatible with international law; and, in the event of an affirmative finding on these points, whether that State is prepared to discharge its international responsibility by appropriate means. For greater certainty, in demonstrating compliance with the obligation to exhaust local remedies, the investor shall not assert that the obligation to exhaust local remedies does not apply or has been met on the basis that the claim under this Treaty is by a different party or in respect of a different cause of action.
>
> 4. Should a dispute arise as to whether available local remedies have been exhausted or as to whether available local remedies in African domestic courts or administrative tribunals are effective, sufficient and timely, an international claim may be brought in order to permit the determination of this preliminary question; and the exhaustion of local remedies as a condition of the receivability of such an international claim may be waived by any international tribunal having jurisdiction over the parties and before which the claim is brought. If the disputing investor can demonstrate that there are no available domestic legal remedies capable of reasonably providing any relief in respect of the same measure or similar factual matters for which a breach of this Treaty is claimed by the investor, the requirement to exhaust local remedies shall not be applicable.

> 5. Where applicable, if, after exhausting all judicial and administrative remedies relating to the measure underlying the claim for at least a period of five years from the date on which the investor first acquired knowledge of the measure in question, no resolution has been reached satisfactory to the investor, the investor may commence a proceeding under this chapter by transmitting a notice of dispute to the African Host State."

Paragraph 1 of this proposal assumes that international responsibility may exist prior to a resort to local remedies, but, whether it exists or is merely alleged to exist, it may not be invoked in the form of an international claim prior to the exhaustion of local remedies in an African court or administrative tribunal. Paragraph 2 of the proposal prohibits a disputing investor from invoking international responsibility in the form of international arbitration until the claim has been submitted to the domestic tribunals or domestic courts within one (1) year from the date on which the disputing investor first acquired knowledge that the investment incurred loss or damage as a result of actions attributable to the African Host State. This provision in the proposed exhaustion requirement clause of the AfCFTA Investment Protocol gives effect to the "futility exception" in the event that the African Host State domestic tribunals or domestic courts fail to provide an effective, sufficient and timely means of redress under the doctrine of exhaustion of local remedies. In this sense, the burden to show that there is no reasonably available relief falls on the foreign investor.

Paragraph 3 explains two critical functions of the exhaustion of local remedies rule: : (1) the preliminary determination by African courts and administrative tribunals on whether international responsibility exists on the part of the African Host State; and (2) in the event of an affirmative finding, an opportunity for the responsible African State to discharge its duty. The attempts to discharge this international responsibility will not be final in the sense of being conclusive as regards the disputing investor. The latter, after exhaustion of local remedies in African courts or administrative tribunals, may challenge the findings or may deny that responsibility has been adequately discharged, and may then present its case in the form of an international claim. The proposed clause of the AfCFTA has another clarification attached to paragraph 4 which, on the one hand, restricts the foreign investors from asserting that the "obligation to exhaust local remedies does not apply to them," and, on the other hand, precludes the investors from claiming that they have complied with the exhaustion requirement on the basis that the claim under this treaty is by a different party or in respect of a different cause of action. This clarification is probably an attempt to water down the effect of the "triple test" adopted by several tribunals when discussing the fork in the road provisions.

Most significantly, an important qualification to African countries' consent to ISDS, as provided by paragraph 5 of this proposal, is that a disputing investor first should exhaust local remedies for a period of five years before the commencement of the international proceedings. These five years are to be counted from the date when the foreign investor first acquired knowledge of the measure in question and the resulting

loss or damage to the investment, or when the investor should have first acquired such knowledge. Under paragraph 4, the requirement to exhaust local remedies shall not be applicable if the investor can demonstrate that there are no available domestic legal remedies in the African courts or tribunals that are capable of reasonably providing any relief in respect of the same measure for which a breach of the Treaty is claimed.

7 CONCLUSION

This article, by tracing the historical development and the subsequent codification of the requirement to exhaust local remedies into treaty law, has demonstrated that the exhaustion of local remedies requirement is an old customary international law rule which has been widely recognised and accepted by State practice way before modern investment arbitration. As seen from the above discussion, the vast majority of international investment agreements are silent on whether the foreign investor must first exhaust local remedies in the Host State before they could institute international arbitration proceedings. For decades, in respect of both the investment tribunals under the ICSID Convention and in non-ICSID context, there has been an implied waiver of the exhaustion of local remedies rule in international investment agreements that are silent on the applicability of the exhaustion of local remedies rule, reversing the well-established principle of customary international law that presumes that the rule should apply unless expressly waived by treaties. Consequently, as seen from the proposed drafting suggestion, African States that wish to apply the requirement to exhaust local remedies in the AfCFTA Investment Protocol should unequivocally and expressly indicate that, for instance, by providing that the foreign investor "must" or "shall" exhaust local remedies before initiating international proceedings for any international arbitration On the other hand, African States should also adopt laws and regulations aimed at ensuring that their domestic legal systems provide foreign investors with reasonably available remedies that are capable of providing effective redress within a reasonable period of time. Those measures would be useful in preventing investors from bypassing the requirement by invoking the futility exception with regard to the exhaustion of local remedies rule.

The suggested local remedies clause in the AfCFTA Investment Protocol would need to meet certain criteria for the African States to derive the benefits of the rule as discussed above. First, the exhaustion of local remedies rule should be made an explicit condition of consent to ISDS mechanisms in order to counter the tendency of arbitrators to bypass the exhaustion of local remedies rule through the use of MFN provisions when invoking more favourable dispute settlement procedures. Secondly, an exhaustion of local remedies requirement should not be subject to an unrealistically short time limit, such as the eighteen months' period provided for in some IIAs. If a time limit is specified, it should not be shorter than the four-year period that reflects the average duration of investor-State proceedings, and the investor should be barred from instituting the investor-State claim prior to the expiration of that period. The suggested

period is five years in terms of paragraph 5 of the proposed clause. As seen in paragraph 4 of the proposed provision, the exceptions to the rule of local remedies should be narrowly drafted to cover only those circumstances when the pursuit of local remedies requirement would be futile. If one proceeds from the premise that neither ISDS nor litigation is inherently better than the other, as shown in the preceding discussion, then there is a case to be made for the retention of both mechanisms through the application of the exhaustion of local remedies rule. Reforms that do not address the displacement of domestic courts as the primary fora for disputes involving foreign investment are unlikely to resolve the debate over the investment provisions in the AfCFTA Investment Protocol or the broader legitimacy crisis facing ISDS. Incorporation of the exhaustion of local remedies rule in the AfCFTA Investment Protocol, in contrast, could provide a balanced mechanism to both the proponents of ISDS and those against it. Rather than functioning essentially as courts of first instance for investment disputes, investment tribunals would provide an additional layer of protection that would be available to foreign investors to address any deficiencies in African domestic legal systems.

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