

ESSAY: INVESTOR-STATE ARBITRATION AND INTELLECTUAL PROPERTY

By:

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My essay explores an area of law that has been recently called by Professors Michael Reisman and James Crawford one of the more remarkable developments in international law in the past 40 years. I am referring to the widespread pattern by which countries, through international investment treaties, have given their consent – in advance – to participate in international arbitration. This situation can arise when an investor from one of the contracting States to an international investment treaty brings a claim alleging that his rights under the treaty have been violated by the other contracting State where his foreign investment was actually made. Recently, there has been a surge in the number of disputes between investors and such host States. The focus in this brief paper is on a particular type of investor-State dispute involving investments comprised of intellectual property-based assets, protected by intellectual property (IP) rights. To date, there have been no publicly reported decisions concerning IP-centered investments. However, I predict that this may change. Following the long-honored tradition of predicting the path of the law,¹ I refer to a time, perhaps not far off, when the general economic shift to “ideational content” in the larger economy will be matched in foreign direct investment (FDI), and may result in an increasing number of international investment disputes in which IP rights are the focus. If these disputes arise, we can ask the following questions: how will enforcement of the IP rights take place, and how will existing standards in international investment agreements be applied in relation to IP rights?

The legal infrastructure is now in place that would enable a significant shift in the enforcement of both (i) private IP rights, and (ii) a public IP rights as viewed through a country’s implementation of international IP norms. This shift can take place through the mixed private-public model of investor-State arbitration. The World Trade Organization’s (WTO) 1995 Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS) established far-reaching international protection for IP, while IIAs accord investors direct “private attorney-general” rights to bring claims against Host States. Thus, while this IP enforcement shift has not yet begun to occur, the international legal infrastructure is in place. If you combine this legal framework with fundamental changes in the world economy that bring more focus to IP rights (explained below), this may result in more IP-based investor disputes. In order to explain this shift, let me first explain certain transformational changes in the economy and in FDI, and then address investor-State IP disputes and important changes brought about by IIAs.

FDI AND THE MOVE TOWARD A CONCEPTUAL ECONOMY

We live in a time in which foreign direct investment has been characterized as the “cutting edge of globalization.”² The rate of growth in FDI for the two decades prior to 2000 exceeded comparable growth rates for world economic output and trade over the same period. In 2006, global FDI flows approached historic highs.³ In academic and international policy-making circles, the importance of FDI is often considered in connection with develop country and technology

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¹ Oliver Wendell Holmes, Jr., *The Path of the Law*, 10 Harv. L. Rev. 457, 457-458 (1897).

² See Economic Intelligence Unit, *World Investment Prospects to 2010: Boom or Backlash*, at 22 (2006).

³ See UNCTAD, *World Investment Report 2007: Transnational Corporations, Extractive Industries and Development*, at xi (2007).

transfer issues.⁴ For businesses large and small, on the other hand, FDI represents a strategic option among alternatives (such as direct exports, distribution agreements or licensing) for expansion into foreign markets – to gain market share, out-source the manufacture of products or supply of certain services, or even locate new research and development (R&D) facilities.

While FDI continues to expand, another powerful trend is transforming a central part of many economies. Modern economies are becoming predominantly “conceptual,” reflecting the vital role of ideas in common and highly valued products and services, and shifting the emphasis in asset valuation from physical to intellectual property. Alan Greenspan, former chairman of the Federal Reserve Board, has spoken repeatedly about the irreversible and accelerating shift in the United States to a “conceptual economy,”⁵ observing that over the past half-century, “the increase in the value of raw materials has accounted for only a fraction of the overall growth of U.S. gross domestic product (GDP).” The rest of the growth in economic output, he explains, has become predominantly “conceptual,” reflecting the embodiment of ideas in the products and services that consumers value. Of course, the common expression for the legal property rights associated with such “ideas” is intellectual property.

As this trend continues, one can observe that a similar change is occurring in FDI: foreign investments reflect an increasing concentration of intellectual capital invested in knowledge goods and realized through technology transfer protected by IP rights. While the historic focus of FDI has been on physical assets such as buildings, equipment, or large infrastructure projects (e.g., roads, energy or power), the subject matter of FDI today is highly diverse. It encompasses not only traditional assets, but also investments in sectors where IP forms a core basis for asset value, such as high technology, health care, pharmaceuticals, bio-technology, telecommunications, and the creative industries, as well as the corresponding trademarks and brand names and the R&D investments intended to spur innovation. While it is difficult to isolate the IP element in trade flows and FDI,⁶ there is no denying the increasing significance of IP in an increasingly globalized world in which science and technology, as well as creative works and international branding, are generating enormous economic value.⁷ As the shift toward a conceptual economy continues, FDI will more typically involve investments comprised of substantial IP-based assets.

INCREASE IN INVESTOR-STATE DISPUTES

The number of IIAs, primarily in the form of bilateral investment treaties (BITs), has grown remarkably since the early 1990s. As of the end of 2006, there were almost 5,500 assorted international investment agreements (“IIAs”), comprised of 2,573 bilateral investment treaties (“BITs”), 2,651 double taxation treaties, and 241 free trade agreements and economic cooperation arrangements containing investment provisions, between more than 175 countries. While IIAs, and in particular BITs, have generally reflected a North-South pattern between the countries entering into them, developing countries are becoming much more important participants in investment policy, partly reflecting growing South-South flows of FDI. By 2006, there were approximately 680 BITs concluded between developing countries, accounting for 26 percent of all BITs. This pattern contributes to the view that the proliferation of IIAs has profoundly transformed international investment law.

⁴ See John Barton, *New Trends in Technology Transfer: Implications for National and International Policy* (2002).

⁵ See Alan Greenspan, *Intellectual property rights*, Stanford Institute for Economic Policy Research Economic Summit (Feb. 27, 2004).

⁶ Daniel Gervais, *Intellectual Property, Trade and Development: State of Play*, 74 *Fordham L. Rev.* 505, 524 (2005).

⁷ Francis Gurry, *The Evolution Of Technology and Markets and the Management of Intellectual Property Rights*, 72 *Chi-Kent L. Rev.* 369, 370 (1996).

Many of these agreements contain dispute settlement provisions permitting investors to bring claims directly against contracting States to enforce the standards of protection guaranteed for their investments under these agreements. In particular, the agreements reflect a widespread pattern in which governments give their consent that, should an investment dispute arise with a qualifying private investor from another contracting country, they will submit to international arbitration.⁸ This form of “pre-consent” is a powerful mechanism which, working in tandem with the dramatic increase in the number of IIAs, has already produced a sharp rise in the number of disputes. With the increase in IIAs since the early 1990s, it is simple to appreciate that, as investors have more investments treaties they can rely on to bring claims against States, the number of disputes will increase. The substantial increase has resulted in more than 258 known investor-State arbitration cases as at the end of 2006, with the number of pending cases before the International Center for the Settlement of Investment Disputes (ICSID) reaching an all-time high of approximately 120.

Taken one step further, a confluence of powerful forces, including the growth in FDI, the proliferation in IIAs and related surge in investment disputes, and the shift to a conceptual economy, are all working together to increase the likelihood that investor-State disputes centered on IP issues will be on the rise. Until recently, there were no effective enforcement mechanisms in place to confront government conduct that may have a direct or indirect adverse effect on an investor’s IP-based investment. “[F]oreign investors had limited options for redressing international law violations.”⁹ The investor could attempt to bring a claim in the host State’s courts, possibly facing sovereign immunity objections, or it could petition its own government to render assistance through diplomatic protection. As regards the latter, the investor would rely on its own government to resolve the dispute, although the government’s motivation to do so would be subject to the vagaries of other pressure points in the relations between the two countries. Similarly, the investor could request that its government invoke WTO dispute settlement procedures, as long as the host State is a member of the WTO and the relevant allegations bear on that State’s obligations under TRIPS. Again, this approach would rely on the willingness of the investor’s government to take action. With the expanding network of IIA’s, however, there may be an investment treaty between the countries concerned: if a claim arises under the protective standards of the treaty, the investor may choose to act directly.

Francis Gurry, Deputy Director General of the World Intellectual Property Organization (WIPO), has suggested that most international IP disputes can be classified as having either “a private-law or public law nature.”¹⁰ On the private side, if an IP dispute arises between two internationally diverse parties, they may not wish to submit to the jurisdiction of the courts of the opposing party. Instead, they can choose an arbitration procedure to be located in a neutral venue and decided by arbitrators who are expert in the field. The data suggest that the referral of private IP disputes to arbitration is increasing. For example, in 2007, 375 IP cases were filed with the American Arbitration Association, while the International Chamber of Commerce estimates that 10-15 percent of its annual caseload involves an IP element.¹¹ WIPO has received approximately 100 requests for arbitration and 70 requests for mediation since its establishment in 1994, along

⁸ See R. Doak Bishop, James Crawford & W. Michael Reisman, *FOREIGN INVESTMENT DISPUTES, CASES, MATERIALS AND COMMENTARY*, at 1 (2005) (“The field of foreign investment law is rapidly changing, with a veritable explosion of foreign investment disputes being resolved through international arbitration.”).

⁹ Susan D. Franck, *Integrating Investment Treaty Conflict and Dispute Systems Design*, 92 *Minn. L. Rev.* 161, 172-73 (2007); see also William S. Dodge, *Investor-State Dispute Settlement Between Developed Countries: Reflections on the Australia-United States Free Trade Agreement*, 39 *Vand. J. Transnat’l L.* 1, 5-14.

¹⁰ *Id.*, *supra* note 7, at 382.

¹¹ Sophie Lamb, Alejandro Garcia, *Arbitration of Intellectual Property Disputes*, *Global Arbitration Review: The European & Middle Eastern Arbitration Review* 2008, *Int’l J. of Public and Priv. Arb.*, at 1.

with some 10,000 international domain name disputes since 2000.¹²

On the public law side, an IP dispute may arise in response to a country's violation of international norms established by TRIPS. TRIPS secures Member countries' obligations to protect and enforce IP rights within their territories. Should a country fail to fulfill its obligations, the WTO Understanding on Rules and Procedures Governing the Settlement of Disputes (DSU) provides a mechanism for the resolution of disputes arising out of alleged non-compliance. As noted above, if a private actor is adversely affected by a WTO member's non-compliance, that party can petition its government to initiate dispute settlement proceedings before WTO. In the investment context, investors whose IP-based investments are harmed by such government conduct that has a direct or indirect adverse effect on the investment can be faced with a difficult set of choices:¹³

- consider withdrawing from the foreign market and thereby incur the losses;
- seek relief by litigating within the legal system of the host State, where the defense of sovereign immunity may be asserted;
- assert contract-based dispute settlement rights and procedures (e.g., arbitration) if the host State or one of its agencies is a party to the contract; or
- petition the investor's own government for assistance, requesting that WTO dispute settlement procedures be invoked if the host State is a member of the WTO and the relevant allegations bear on the host State's obligations under TRIPS. However, the private actor's government will nonetheless weigh "the diplomatic pros and cons of bringing any particular claim."¹⁴

All of these options may be considered unsatisfactory to investors whose IP-investment suffers a serious loss due to government conduct. However, with the machinery of investor-State arbitration, a third category of international IP dispute can be added to the dual classification of private and public law disputes: mixed private-public disputes arising by virtue of a host State's alleged violation of an investment treaty and thereby falling within the prerequisites of investor-State arbitration. Investment treaty arbitration has been characterized as a "mixed" system, one that "grafts a traditionally private dispute resolution system onto an international treaty between Sovereigns."¹⁵ Investment treaty arbitration arises as a result of a negotiation of rights between two Sovereigns often implicating "a number of public and governmental interests."¹⁶ This form of arbitration, by which a private party can bring a claim against the host State pursuant to rights under a treaty, is significantly different from international commercial arbitration founded on "freedom of contract" principles and involving private law issues.¹⁷ When an investor-State dispute arises involving IP rights, not only are governmental interests implicated under the investment treaty, but also in relation to the IP rights themselves. Fundamental to the IP ownership right is the right to exclude third-parties from use of a particular intellectual creation. In his book on IP disputes, David Plant emphasizes that "[t]he powerful exclusionary rights associated with intellectual property are often granted, administered or controlled by a government agency. They are considered to be matters of substantial public concern."¹⁸

¹² See WIPO Arbitration and Mediation Center website at <http://arbiter.wipo.int/amc/en/center/caseload.html>.

¹³ See Susan D. Franck, *supra* note 9, at 190-191.

¹⁴ Outcome of the Summit of the Americas and Prospects for Free Trade in the Hemisphere, Before Subcomm. On Trade, H.R. Ways and Means Committee, 107th Cong. 1st Session., Serial 107-22, 93 (2001) (statement of Daniel M. Price, Member, U.S. Council for International Business).

¹⁵ Susan D. Franck, *The Nature and Enforcement of Investor Rights Under Investment Treaties: Do Investment Treaties Have a Bright Future*, 12 U. Cal. Davis L. Rev. 47, 69 (2005); Bernardo M. Cremades & David J.A. Cairns, *The Brave New World of Global Arbitration*, 2 J. World Inv. 173, 183-185 (2002).

¹⁶ Bart Legum, *Trends and Challenges in Investor-State Arbitration*, 19 Arb. Int'l 143, 144-45, 147 (2003).

¹⁷ Susan D. Franck, *supra* note 15, at 70-73.

¹⁸ David W. Plant, *RESOLVING INTELLECTUAL PROPERTY DISPUTES*, at 13 (1999).

CONCLUSION

An IP claim brought by a private investor against a host State under an investment treaty implicates public policies (e.g., investment, IP and other laws) that could be either complimentary or cross-cutting. The balance to be maintained between IP and other public policies is one that has recently received growing attention.¹⁹ Will the alignment of investment treaty obligations and IP laws create needed privately enforceable rights to facilitate a fair and efficient system of governance for IP-based FDI, or will it establish a bulwark of legal protections in favor of the investor, to the detriment of other important public policies?²⁰ At a time when countries such as Bolivia, Cuba, Ecuador, Nicaragua and Venezuela have recently demonstrated dissatisfaction with the international regime for the settlement of investment disputes,²¹ it may be considered controversial to identify IIAs as an untapped and potentially powerful new means of IP enforcement. Indeed, there has been a long-brewing debate about IP's role in the socio-economic development of developing countries, a debate which now embraces what some have called an anti-intellectual property movement in relation to IP's role in the modern economy.²² Despite the heightened attention and intensified tensions these issues may inspire, they are nonetheless of growing importance for the 21st century, to be ignored only at one's peril. Discussing IP in his recent book, Thomas Friedman put the issue in a larger context: "Who owns what?" is sure to emerge as one of the most contentious political and geopolitical questions in a flat world..."²³

¹⁹ See Francis Gurry, *Seeking Balance for Intellectual Property*, Presentation at Fédération Internationale des Conseils en Propriété Industrielle World Congress (May 23, 2006).

²⁰ See Carlos M. Correa, *Bilateral Investment Agreements: Agents of New Global Standards for the Protection of Intellectual Property Rights?*, at 2 (Aug. 2004).

²¹ Bolivia and Ecuador have formally notified ICSID of their intention respectively to withdraw or limit their acceptance of certain claims under the ICSID Convention. See ICSID, *Bolivia Submits a Notice under Article 71 of the ICSID Convention* (May 16, 2007); ICSID, *Ecuador's Notification under Article 25(4) of the ICSID Convention* (December 5, 2007); Michael D. Nolan and Frederic G. Sourgen, *A Preliminary Comment – The Interplay Between State Consent to ICSID Arbitration and Denunciation of the ICSID Convention: The (Possible) Venezuela Case Study*, *Transnational Dispute Management* (Sept. 2007).

²² See UK Commission on Intellectual Property Rights, *Integrating Intellectual Property Rights and Development Policy* (Sept. 2002); Geneva Declaration on the Future of WIPO (March 4, 2005).

²³ Thomas L. Friedman, *THE WORLD IS FLAT: A BRIEF HISTORY OF THE TWENTY-FIRST CENTURY*, 218 (2005).

