IS NEER FAR FROM FAIR AND EQUITABLE?

Remarks of Judge Stephen M. Schwebel

International Arbitration Club, London

5 May 2011

In the wake of revolutionary and other tumultuous events over a period of years, Mexico in the 1920's concluded a number of conventions with States whose nationals were adversely affected. The Convention with the United States of America of 1923 resulted in a series of awards by a Claims Commission. The first award on the merits was in a case espoused by the United States on behalf of the widow and daughter of Paul Neer.

Neer, an American supervising a mining operation in Mexico, was riding in the evening to his home on horseback with his wife when they were stopped by a group of armed men, who murdered him. His wife escaped. It was alleged that on account of this killing, Mrs. Neer and her daughter sustained damages, for which the Mexican Government was liable, because "the Mexican authorities showed an unwarrantable lack of diligence or an unwarrantable lack of intelligent investigation in prosecuting the culprits..."

The Commission, in an award of less than three pages, held that the Mexican authorities "might have acted in a more vigorous and effective way than they did...", as indeed senior Mexican authorities had acknowledged. But the Commission held that there was "a long way" between so holding and concluding that "this record presents such a lack of diligence and intelligent investigation as constitutes an international delinquency..."

The Commission treated the allegations at issue as a claim of denial of justice. It referred to articles by John Bassett Moore and by De Lapradelle and Politis on denial of justice. It referred to no State practice whatsoever. The Commission held:

> "(first), that the propriety of governmental acts should be put to the test of international standards, and (second) that the treatment of an alien, in order to constitute an international delinquency, should amount to an outrage, to bad faith, to wilful neglect of duty, or to an insufficiency of governmental action so far short of international standards that every reasonable and impartial man would readily recognize its insufficiency."

The Commission's first holding – that the propriety of the acts of a government affecting aliens should be "put to the test of international standards" – was fundamental. It was hardly seminal. The essence of that holding was made in 1921 in the leading arbitral award in *Norwegian Shipowners Claims*. It was effectively made by the Permanent Court of

International Justice in 1925 in its judgment on *Certain German Interests in Upper Silesia*. The Neer award of 1926 cites neither of these authorities. But its holding, even if could be taken for granted in the industrialized democracies, could not be taken as universally accepted. Not only did Mexico deny it in the famous exchanges in the 1930's between its Foreign Minister and Secretary of State Hull in the dispute over compensation for oil nationalizations. As late as the 1970's, when Mexico took the lead in pressing for the United Nations to adopt the "Charter of Economic Rights and Duties of States," Mexico contended that an alien was entitled to no more than national treatment. Mexico, and the UN's Group of 77, supported in word and deed by the Communist bloc, contended that the minimum standard in international law did not exist. The Group of 77 supported not this holding of *Neer* but the doctrines of Calvo. Repeated resolutions of the UN General Assembly so demonstrate.

But in this regard the democratic governments of Mexico of recent years have made marked progress. With NAFTA, Mexico abandoned Calvo. In its submissions in NAFTA cases, Mexico has taken a relatively enlightened approach.

Whether the same can be said of the Governments of the United States and Canada is open to question. They appear to maintain that the quoted holding in *Neer* of 1926 in respect of the egregiousness of governmental acts today is an interpretive key to the meaning of Article 1105 of the North American Free Trade Agreement.

Article 1105, whose caption is "Minimum Standard of Treatment", provides in paragraph 1 that: "Each Party shall accord to investments of investors of another Party treatment in accordance with international law, including fair and equitable treatment and full protection and security."

Canada maintains that *Neer* provides the standard of interpretation of Article 1105.

Apparently it no longer contends that that standard is "frozen in amber"; it accepts that what may be seen in 2011 as egregious may differ from the perception of 1926.

In a recent case brought by a Canadian investor against the United States, *Glamis Gold*, the United States maintained that:

- Article 1105's duty to provide fair and equitable treatment in accordance with "international law" is solely a reference to the minimum standard of treatment required by "customary international law", as an authoritative interpretation of NAFTA of 2001 by its three Parties provides.

- Establishment of a rule of customary international law requires concordant State practice and *opinio juris*. Customary international law cannot be proven by decisions of international tribunals, as they do not constitute State practice.

- It is the burden of the claimant to establish that customary international law has changed. The Claimant had not borne that burden, had not shown that the standard of treatment had changed to require something less than "outrageous", "egregious" or "shocking" behaviour.

The Tribunal accepted the U.S. contentions. It held that, because of the difficulty of proving a change in custom, this requirement "effectively freezes the protections provided for in this [NAFTA] provision at the 1926 conception of egregiousness". It agreed that arbitral awards "do not constitute State practice and thus cannot create or prove customary international law". It did acknowledge that "the *Neer* standard, when applied with current sentiments and to modern situations, may find shocking and egregious events not considered to have reached that level in the past." Yet it concluded that, "although situations may be more varied and complicated today than in the 1920s, the level of scrutiny is the same. The fundamentals of the *Neer* standard thus still apply today: to violate the customary international law standard minimum standard of treatment codified in Article 1105 of NAFTA, an act must be sufficiently egregious and shocking – a gross denial of justice, manifest arbitrariness, blatant unfairness, a complete lack of due process, evident discrimination, or a manifest lack of reasons – so as to fall below accepted international standards and to constitute a breach of Article 1105(1)...The standard for finding a breach of the customary international law minimum standard of treatment therefore remains as stringent as it was under *Neer*; it is entirely possible, however, that, as an international community, we may be shocked by State actions that did not offend us previously."

The award in *Glamis Gold* is substantial and well written. It was prepared by outstanding arbitrators. I have not studied the whole of this long award and do not have a view on much of it, nor have I reviewed the pleadings of the parties in the case.

But I am constrained to say that I question arguments of the United States as the award understood and accepted them.

The contention that the reference to "international law" in NAFTA Article 1105 means solely *customary* international law has support in the caption of that article and, apparently, in the intentions of the Parties, certainly as their 2001 interpretation portrays them. Yet the classic definition of international law is broader. Since 1920, the Statutes of the Permanent Court of International Justice and of the International Court of Justice have provided that the Court, in deciding disputes in accordance with international law, shall apply international conventions establishing rules expressly recognized by the contesting States, international custom as evidence of a general practice accepted as law, the general principles of law recognized by civilized nations, and judicial decisions and scholarly writings as subsidiary means for the determination of rules of law. There may be a measure of interplay between these sources and customary international law.

There is room to question as well the U.S. contention that the judgments of international tribunals cannot be a source of law. The United States, Canada and Mexico apparently rely on the award of the Claims Commission in *Neer* as setting a standard for the interpretation of NAFTA Article 1105. The Claims Commission was an international tribunal. Why should its terse, barely reasoned opinion – which examines no State practice at all – be the fount of customary international law as respects what is an international delinquency, while the judgments of contemporary international tribunals do not influence the content of customary international law in that regard? How is it that the governments of these States in their pleadings in the International Court of Justice invoke prior judgments of the Court, and, if my recollection is correct, awards of international arbitral tribunals, but hold them of no account in the evolution of customary international law in the NAFTA context?

It may indeed be asked why the *Neer* award is invoked at all. It had nothing to do with the treatment of foreign investors or investments. It did not address what is fair and equitable. Rather it only examined whether Mexico had committed a denial of justice in failing adequately to investigate and prosecute the murderers of an alien. It considered whether proper investigatory and judicial procedures were observed. It held that Mexico could not be held liable for sufficiently egregious failure to follow those procedures. What in another case may or may not be fair and equitable treatment by a State of foreign investment may involve procedural matters, or matters of substance, or both, far removed from the confines and criteria of a denial of justice.

While I was no longer an official of the U.S. Government when NAFTA was negotiated, in my earlier official days I was centrally concerned with the negotiations over the content of UN General Assembly resolution 1803 (XVII) on "Permanent Sovereignty over Natural Resources". That resolution subjects the treatment and taking of foreign investment not to customary international law but to international law. It provides that, "Foreign investment agreements freely entered into by, or between, sovereign States, shall be observed in good faith." To the best of my recollection, there was no whisper in the instructions which I wrote in Washington and executed in New York about the *Neer* criteria. Nor did the *Neer* criteria figure in the protracted negotiations over the Charter of Economic Rights and Duties of States. Nor, as far as I can remember, were they raised in the State Department's preparation of its first bilateral investment treaties.

The NAFTA Tribunal in *Mondev International v. United States* expressed conclusions that may be more persuasive to the contemporary critic than those in *Glamis Gold*. In answer to the question, "What is the content of customary international law providing for fair and equitable treatment and full protection and security in investment treaties?", it began by recalling Canada's position respecting *Neer*. It continued:

> "...the *Neer* case...concerned not the treatment of foreign investments as such but the physical security of an alien. Moreover the specific issue in *Neer* was that of Mexico's responsibility for failure to carry

> out an effective police investigation into the killing of a United States citizen by a number of armed men who were not even alleged to be acting under the control or at the instigation of Mexico. In general, the State is not responsible for the acts of private parties, and only in special circumstances will it become internationally responsible for a failure in the conduct of subsequent investigations. Thus there is insufficient cause for assuming that provisions of bilateral investment treaties, and of NAFTA...are confined to the *Neer* standard of outrageous treatment where the issue is the treatment of foreign investment by the State itself.
>
> "Secondly, *Neer* and like arbitral awards were decided in the 1920's, when the status of the individual in international law, and the international protection of foreign investments, were far less developed than they have since come to be. In particular, both the substantive and procedural rights of the individual in international law have undergone considerable development. In the light of these developments it is unconvincing to confine the meaning of 'fair and equitable treatment' and 'full protection and security' of foreign investments to what those terms – had they been current at the time – might have meant in the 1920's when applied to the physical security of the alien. To the modern eye, what is unfair and inequitable need not equate with the outrageous or the egregious. In particular, a State may treat foreign investments unfairly and inequitably without necessarily acting in bad faith.
>
> "Thirdly, the vast number of bilateral and regional investment treaties...almost uniformly provide for fair and equitable treatment of foreign investments...In the Tribunal's view, such a body of concordant practice will necessarily have influenced the content of rules governing the treatment of foreign investment in current international law. It would be surprising if this practice and the vast number of provisions it reflects were to be interpreted as meaning no more than the *Neer* Tribunal (in a very different context) meant in 1927."

The *Mondev* Tribunal further held that, "A reasonable evolutionary interpretation of Article 1105(1) is consistent both with the *travaux*, with normal principles of interpretation and with the fact that...the terms 'fair and equitable treatment' and 'full protection and security' had their origin in bilateral treaties in the post-war period. In these circumstances the content of the minimum standard today cannot be limited to the content of customary international law as recognized in the arbitral decisions of the 1920's." Moreover, "the term 'customary international law' refers to customary international law as it stood no earlier than the time when NAFTA came into force. It is not limited to the international law of the 19th century or even of the first half of the 20th century...In holding that Article 1101(1) refers to customary international law, the FTC interpretations incorporate current international law whose content is shaped by the conclusion of more than two thousand bilateral investment treaties..."

I find these holdings of the *Mondev* Tribunal persuasive (not least because I was a member of it) – as did the Tribunal in the *ADF* case.

Finally, permit me to draw your wearied attention to the 2010 holdings of the Tribunal in *Merrill & Ring Forestry v. Canada*.

As to the meaning of NAFTA Article 1105(1), the Tribunal held that the reference in it to international law "can only be understood today with reference to...the Statute of the International Court of Justice, where the sources of international law are identified..." The reference in Article 1105(1) "must be understood as a reference to the sources of this legal order as a whole, not just one of them." It continued, "...customary international law has not been frozen in time...it continues to evolve in accordance with the realities of the international community. No legal system could endure in stagnation." The minimum standard has become obsolescent in the context of human rights. It was "scarcely mentioned" in the principal works concerning the codification of the law of State responsibility, notably the International Law Commission's Articles on State Responsibility. "State practice was even less supportive of the standard referred to in the *Neer* case. And in the absence of a widespread and consistent state practice in support of a rule of customary international law there is no *opinio juris* either. No general rule of customary international law can thus be found which applies the *Neer* standard, beyond the strict confines of personal safety, denial of justice and due process...State practice...shows that the restrictive *Neer* standard has not been endorsed or has been much qualified...A requirement that aliens be treated fairly and equitably in relation to business, trade and investment is the outcome of this changing reality...it is reflected today in customary international law as *opinio juris* the Tribunal is satisfied that fair and equitable treatment has become part of customary law."

The *Ring and Merrill* Tribunal further observed that if the minimum standard were interpreted to require "outrageous conduct", then "consistency would demand that the same standard be followed in respect of such claims made by NAFTA States in respect of the conduct of other countries...Yet this is not the case...Customary international law cannot be tailor made to fit different claimants in different ways. To do so would be to countenance an unacceptable double standard...the Tribunal finds today that...except for cases of safety and due process, today's minimum standard is broader than that defined in the *Neer* case and its progeny. Specifically this standard provides for fair and equitable treatment of alien investors within the confines of reasonableness."

My conclusion is that *Neer* is far from what is fair and equitable.