ARGENTINA

Another set of ICSID claims against Argentina?

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On 20 November 2008, the Argentine Congress enacted a law eliminating private investment in the Argentine social security system. To complicate matters, foreign investors currently invested in the Argentine social security system will be adversely affected by the new law. The following article discusses the various protections granted to foreign investors under bilateral investment treaty (BIT) agreements, which may serve as the basis for a new set of claims against Argentina before the International Centre for Settlement of Investment Disputes (ICSID).

Social security administration in Argentina

In October 1993, the Argentine Republic enacted Law No 24,241, creating the Integrated System of Retirement and Pension Benefits (SIJP). The SIJP marked a substantial change from the previous loss producing, state-managed retirement system.
The most significant change introduced by the SIJP was the implementation of a mixed public and private system. The public regime, or *sistema de reparto*, existed prior to the enactment of the SIJP. The *sistema de reparto* was administered by the state through the Argentine Social Security Administration (ANSES) and depended on the direct distribution of monthly contributions made by all employed persons to retired persons. Under that framework, monies were not invested and there was no accumulation of interest.
The private regime, or *sistema de capitalización*, was tasked with receiving workers' contributions to their individual accounts and making investments to create the best possible yield on the workers' contributions.
Those investments were limited to options permitted by the government. The private regime was administered by the Retirement and Pension Funds Administrators (AFJPs).
On 20 November 2008, the Argentine Congress passed a law eliminating the private regime from the SIJP. The investment funds managed by the AFJPs and the monthly flow of new contributions were transferred to the control of ANSES, effectively replacing the private regime with the public. The work of the AFJPs, as well as its source of resources – commissions collected from workers' monthly contributions – will now be all but eliminated.
Section 13 of the new law governs the compensation AFJPs will receive following their elimination, indicating the serious damage the new law does to the AFJPs. The provision intends to limit the AFJPs' right to compensation by imposing quantitative limits on compensation from the state and limits on the form of payment the state will make. First, it limits the amount of compensation to the nominal value of the shares of capital stock, thereby rejecting any reference to the market value or proportional net asset value of the stock. Secondly, it provides that compensation will only be in the form of public bonds, subject to a minimum public bonds sale schedule. Moreover, section 15 of the new law further states that 'any real property, personal property and technical equipment necessary for the adequate operation' of the AFJPs will be transferred to the control of the ANSES.
Based on those provisions, the new law confiscates the AFJPs' assets and source of business, in violation of section 17 of the Argentine National Constitution.

International treaty standards

As of November 2008, four of the private AFJPs had foreign investment partners. BBVA Consolidar, HSBC Maxima AFJP, MET AFJP, and ORIGENES AFJP were all significantly invested in the private AFJPs.[1]
By eliminating the private AFJPs, the new law will negatively affect the rights of those foreign investors.
The foreign investment partners, therefore, may be able to invoke BIT protections to challenge the law or to recapture their investments. Ultimately, this may lead to a series of new lawsuits or arbitrations between foreign investors and ANSES.
The following discussion describes the different standards of protection under BITs that may serve as a basis for lawsuits or arbitrations brought by foreign investors.

Fair and equitable treatment

One standard included in most BITs is the fair and equitable treatment (FET) standard. FET protects foreign investors against damage to their legitimate expectations and requires states to act transparently and to conduct themselves in a foreseeable manner. The FET standard provides stability to the investment and legal frameworks and guarantees that a state's conduct will not be inconsistent, unreasonable, or discriminatory.

An investor's legitimate expectations are based on a state's applicable laws and regulations, as well as the express or implied guarantees that the state made to the investors. A change in the legal framework or a reversal of guarantees would violate the FET standard.[2] The FET standard is also violated when a foreign investor is treated differently than investors who are nationals of the state in which the investment was made. Even when a foreign investor would not be protected under a 'most favoured nation' agreement, the foreign investor may be protected from unfair or inequitable treatment by the FET standard.[3]

The FET standard is the most frequently invoked BIT clause in investment related disputes. Moreover, the majority of successful investment treaty arbitrations allege a violation of the FET standard. For example, in the 2005 case of *CMS v Argentina*, the court held that a substantial modification by the Argentine government of the legal framework for investments was unacceptable: 'The Treaty Preamble makes it clear, however, that one principal objective of the protection envisaged is that fair and equitable treatment is desirable "to maintain a stable framework for investments and maximum effective use of economic resources."… It is not a question of whether the legal framework might need to be frozen…but neither is it a question of whether the framework can be dispensed with altogether when specific commitments to the contrary have been made….'[4]

Applying the decision in *CMS v Argentina*, the court may find that the elimination of AFJPs is a violation of the duty to accord fair and equitable treatment.

Full protection and security

The full protection and security rule originally required that a state receiving foreign investments must guarantee those investments against physical violence, including, for example, the invasion of places where the investment was located. That protection was subsequently extended to include protecting investors' rights against the enactment of new laws and regulations by the receiving states.[5]

The expansion of the full protection and security rule has been upheld in recent arbitrations. In *CME v Czech Republic*, the arbitration panel held that '[t}he host State is obligated to ensure that neither by amendment of its laws nor by actions of its administrative bodies is the agreed and approved security and protection of the foreign investor's investment withdrawn or devaluated….'[6] Similar reasoning was applied in *Azurix v Argentina*[7] and in *Siemens v Argentina*,[8] where the courts held that the full protection and security standard may be violated even when there is no physical violence.

The umbrella clause

The umbrella clause requires that both the investor and the state receiving the foreign investment fulfil their respective obligations. While some courts have interpreted the umbrella clause to provide broad protections on some occasions, other decisions have limited its scope.[9] For example, in the case of *Eureko v Poland*, the court held that the standard must be construed broadly, considering its ordinary meaning, the context of the clause, and its useful effect.[10] Similarly, in *Siemens v Argentina*,[11] the court rejected Argentina's position and held that '[a]ny agreement related to an nvestment that qualifies as such under the Treaty would be part of the obligations covered under the umbrella clause'.[12] Consequently, if one of the applicable BITs with foreign investors contains an umbrella clause, foreign investors may be able to claim a violation based on the abolition of the private regime, which eliminated the very purpose behind their investments.

Treaties and international law allow states to violate the provisions of BITs under certain special circumstances, including emergency, necessity, and force majeure. The new law abolishing private AFJPs, however, does not invoke any of these circumstances.

In this case, there is no alleged emergency – related to the Argentine social security system or otherwise – to support the elimination of the privately-managed retirement system. Consequently, Argentina cannot justify its change in law through those treaty principles.

Expropriation

Although a state's actions may violate provisions of BITs, a state may violate foreign investors' treaty rights if the action constitutes an expropriation.

Expropriations are generally accepted as valid, provided that the expropriation satisfies three basic requirements. First, the expropriation must be done to benefit the public interest. Secondly, an expropriation

must be followed by prompt, effective, and adequate compensation to the investors who have lost property.

Adequate compensation is generally understood to be the equivalent of the market value of the expropriated investment. Finally, the expropriation can neither be arbitrary nor discriminatory.

The type of expropriation – direct or indirect – is determined by whether the investor's legal title is affected by the state's actions. Direct, or formal, expropriation removes the investor's legal title.

Indirect expropriation leaves the investor's legal title untouched but deprives the investor of the ability to employ the investment in a useful manner.[13]

States typically aim to avoid direct expropriation.

Argentina's new law, however, constitutes a direct expropriation of foreign investment. By eliminating the private AFJPs, foreign investors will be deprived of the value of their shares and of the ability to use their investments in a useful manner.

The new law may also be classified as a 'creeping' expropriation. The term 'creeping' describes a series of successive acts that, when considered together, constitute an expropriation. Here, the series of measures previously adopted regarding the AFJPs could be validly considered a series of acts that, when considered jointly, led to the deterioration of the investor's business until its final expropriation.

Moreover, the new law does not satisfy the three requirements of a proper expropriation. The new law does not indicate its purpose is to benefit the public interest nor does the new law provide reasoning for the expropriation, thereby leaving the law open to challenges that it is both arbitrary and discriminatory.

The new law also does not contemplate a mechanism for prompt, adequate and effective compensation. In similar situations, arbitral decisions have recognised that the fair market value of the investment is an adequate compensation parameter, even when the occurrence of an expropriation has not been admitted: 'the Tribunal is convinced that… this case is more adequately addressed through the application of the fair market value standard. Although this standard has a main relation with expropriations, it does not exclude the possibility of it being appropriate for other non-conformities, if they are capable of generating considerable losses in the long-term… The Tribunal has concluded that the discounted cash flow method must be applied in this case.…'[14]

Conclusion

For the reasons stated above, a new set of lawsuits and/or arbitration claims against the Argentine National Government might be initiated, based on the elimination of the AFJPs. The AFJPs had legitimate expectations of developing long-term investments in Argentina that were terminated by the new law. Various BIT provisions may serve as the basis of the foreign investors' legal claims, and Argentina may not be able to justify their actions under the BIT.

Notes

1 See website of the AFJP's Union at **www.uafjp.org.ar**.
2 Rudolph Dolzer & Christoph Schreurer, Principles of International
Investment Law 133–34 (Oxford University Press 2008).
3 *Ibid.*
4 *CMS v Argentina*, Award dated 12 May 2005, paragraphs 274 and 277.
5 Dolzer & Schreurer, supra note ii, 149.
6 *CME v Czech Republic*, Partial Award, 13 September 2001, 9 ICSID
Reports 121, paragraph 613.
7 *Azurix Corp v The Argentine Republic*, Award dated 14 July 2006,
paragraph 406.
8 *Siemens v Argentina*, Award dated 6 February 2007.
9 For example, in the case of *SGS v Philippines* the tribunal viewed
its jurisdiction as defined by reference to the BIT and ICSID Convention. The tribunal also stated, however, that it should not
exercise its jurisdiction over a contractual claim when the parties
have already agreed on how such a claim is to be resolved and have
done so exclusively.
11 *Eureko v Poland*, Partial Award, 19 August 2005, 12 ICSID Reports 335.
Paragraphs 246 and 248.
12 *Siemens v Argentina*, Award dated 6 February 2007.
13 See *ibid.* at paragraph 206.
14 Dolzer & Schreurer, supra note ii, 92.
15 *CMS v Argentina*, Award dated 12 May 2005, paragraphs 410 and 411.