An Appellate Mechanism for Investor-State Dispute Settlement:  
A Perspective Based on the WTO Appellate Body Experience

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Discussions of the creation of an appellate mechanism for investor-State dispute settlement frequently take the World Trade Organization’s Appellate Body as a point of reference. This is not a coincidence. When the U.S. Congress, in 2002, identified the establishment of an investor-State appellate mechanism as an objective to be pursued in trade agreement negotiations, it clearly had the Appellate Body in mind.¹

The comparison is an attractive one. In investment disputes, as in trade disputes, claims of breaches of treaty obligations are heard in the first instance by ad hoc panels of experts. In trade disputes, the ability to appeal the legal conclusions of an ad hoc panel to a permanent Appellate Body serves two valuable functions. First, by acting as a check against legal error, it facilitates acceptance by the Members of the WTO of a dispute settlement regime under which a losing respondent’s failure to take remedial action may result in the imposition of legally authorized trade sanctions by the complainant. (This is in contrast to the pre-WTO dispute

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settlement regime under the *General Agreement on Tariffs and Trade 1947*, which lacked an appellate body, but which also allowed a losing respondent to block formal adoption of a panel’s findings.) Second, recourse to a permanent Appellate Body helps to ensure consistency of interpretation of treaty provisions from one dispute to the next. It thus enhances predictability as Members implement their WTO obligations.

Presumably, investment treaties also would benefit from an institution that strengthens confidence in the dispute settlement system, thus facilitating the acceptance of and compliance with adverse outcomes in particular cases. And, presumably investment treaties would benefit from an institution that helps ensure consistency of interpretation from one dispute to the next.

So, why not simply transpose the WTO Appellate Body, adapting it to the investment context? The answer, not surprisingly, is that while the Appellate Body may offer some useful lessons to the negotiators of an investment appellate mechanism, there are important differences between the WTO context and the investment treaty context. Some of those differences provide an interesting perspective from which to consider the challenges of designing an investment appellate mechanism.

I have been asked to address two aspects of the design of an investment appellate mechanism: (1) the effect of the mechanism’s decisions, and (2) the relationship of the mechanism’s review to current U.S. law. I will address each aspect by reference to corresponding aspects of the design of the WTO Appellate Body and U.S. law pertaining to decisions of the Appellate Body.
The Effect of an Appellate Mechanism’s Decisions

Turning first to the effect of the mechanism’s decisions, negotiators will need to consider at least three key questions: Will the appellate mechanism have the power to remand a case for further findings in light of its decisions? If it lacks the power to remand, will it have the power to fill gaps in a tribunal’s findings to allow final resolution of a dispute in the event that certain tribunal findings are reversed or modified? Will the mechanism’s decisions have the effect of precedent that is binding on future tribunals in their consideration of claims involving the same treaty provisions?

Analogous questions have been addressed in the design of the WTO Appellate Body.

Will an appellate mechanism have the power to remand or fill gaps?

The Appellate Body is authorized to uphold, modify, or reverse the legal findings and conclusions of a panel. It does not have the power to remand a case to the panel. In some cases, where the Appellate Body has modified or reversed a panel’s legal conclusions, it has taken the additional step of “completing the panel’s analysis” — that is, “examin[ing] and

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3 Several WTO Members have proposed creating a remand mechanism. See, e.g., Contribution of the European Communities and its Member States to the Improvement of the WTO Dispute Settlement Understanding, TN/DS/W/1 at p. 8 (Mar. 13, 2002) (“Recent experience makes clear that the DSU must contain a remand authority for the Appellate Body, as it is the task of panels to establish clearly and unequivocally issues of facts.”); Jordan’s Further Contribution Towards the Improvement and Clarification of the Dispute Settlement Understanding, TN/DS/W/56 (May 19, 2003) (proposing remand procedure). However, to date, there is no consensus on any of these proposals.
decid[ing] an issue that was not specifically addressed by the panel” in order to facilitate a final settlement of the dispute.⁴

However, it has been extremely cautious about doing so, declining to complete the analysis where it perceives a lack of sufficient factual findings or undisputed facts that would allow it to complete the analysis.⁵ The effect in such a case may be to leave the dispute unresolved.

For example, in one of the several WTO disputes between Canada and the United States over lumber trade, Canada challenged a determination by the U.S. International Trade Commission (“ITC”) that dumped and subsidized Canadian imports threatened the U.S. lumber industry with material injury. A WTO panel found that the ITC had not breached provisions of the Antidumping Agreement and the Subsidies Agreement in making that determination. However, the Appellate Body found that the panel had misapplied the relevant standard and reversed. The question then was whether the Appellate Body would take it upon itself to apply the standard correctly and reach its own conclusion as to whether the ITC determination

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breached the covered agreements. It declined to do so, effectively leaving the dispute unresolved. ⁶

Had Canada wanted to continue to pursue its claim through dispute settlement, it would have had to start from the beginning and ask that a new panel be convened, a step that might have prolonged the dispute by an additional year. (As it happened, Canada and the United States reached a settlement in the lumber dispute, which entered into force six months after the Appellate Body issued its report, resulting in the termination of the lumber-related WTO cases.)

A result like the one that confronted Canada in the lumber case is unsatisfying in the extreme to the complaining party. Given the WTO context, however, the features that can lead to such a result may not be design flaws.

While the WTO dispute settlement mechanism has many of the features of an adjudicative process, it is part of an essentially diplomatic institution oriented to achieving negotiated results. It is designed to help parties come to their own solution to a dispute. ⁷ A WTO panel does not render an “award” in which a complaining party may be found legally entitled to money damages to compensate for past harm. It issues a “report” in which it may “recommend” that a respondent “bring the measure [at issue] into conformity” with obligations

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⁷ See generally Robert E. Hudec, The New WTO Dispute Settlement Procedure: An Overview of the First Three Years, 8 Minn. J. Global Trade 1, 11 (1999) (discussing importance of political will to “achiev[ing] reasonable levels of compliance” even in the absence of “rigorously binding procedures”).
under a WTO agreement. The report is supposed to assist the disputing parties in determining for themselves how best to resolve their dispute.\footnote{See, e.g., DSU, art. 11, 33 I.L.M. at 1233 (“Panels should consult regularly with the parties to the dispute and give them adequate opportunity to develop a mutually satisfactory solution.”).}

In this context, an appellate proceeding that leaves a particular dispute unresolved due to a reversal coupled with an inability to remand or complete the panel’s analysis still may advance the objectives of the dispute settlement mechanism. The panel and Appellate Body reports contain findings of fact and conclusions of law that could aid the parties in successful settlement of their dispute notwithstanding the inconclusiveness of the formal proceeding.

Different objectives underlie investor-State dispute settlement. It is not a part of an institution that is essentially diplomatic and negotiation-oriented in character. Quite the contrary. When a host Party consents to allow an investor of another Party, rather than the other Party itself, to vindicate rights under the agreement it is consenting to removal of the dispute from the realm of diplomacy. The expectation of a claimant in submitting a claim to investor-State dispute settlement is that the proceeding will be conclusive and yield an award that is subject to recognition and enforcement in multiple jurisdictions.

In this context, features that could leave an investment dispute unresolved at the conclusion of an appeal could well be considered design flaws to be avoided in setting up an appellate mechanism. In this respect, at least, the negotiators of an investor-State appellate mechanism may want to deviate from the WTO model. They may want to consider options such
as remand or empowering the mechanism to fill gaps that result from a reversal or modification of a tribunal’s conclusions in order to promote finality.\(^9\)

**Will decisions of an appellate mechanism be binding precedent?**

In addressing the effect of decisions, negotiators also should consider whether a decision of the appellate mechanism will be binding on tribunals and the appellate mechanism itself in future disputes. In other words, will the mechanism’s decisions be treated as *stare decisis* and, if so, should this be expressly acknowledged in the text establishing the mechanism?

It has been stated frequently that the findings of the WTO Appellate Body are not binding precedent. They apply only in the dispute in which they are made.\(^{10}\) Were it otherwise, the Members of the WTO effectively would have ceded to the Appellate Body the power to say definitively what the covered agreements mean.\(^{11}\)

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\(^9\) Negotiators must be mindful, however, of the criticism that surrounded the first encounters with annulment of ICSID awards in the mid-1980s, which some saw as unduly prolonging the resolution of claims. *See generally* Christopher F. Dugan et al., *Investor-State Arbitration* at 631-633 (2008) (discussing annulment proceedings in *Klöckner v. Cameroon* and in *Amco v. Indonesia*).

\(^{10}\) As one dispute settlement panel put it in declining to follow prior Appellate Body reasoning on a particular issue of interpretation of WTO rules on antidumping: “It is well established that panel and Appellate Body reports are not binding, except with respect to resolving the particular dispute between the parties to the dispute, but that such reports create ‘legitimate expectations’ among WTO Members and should therefore be taken into account where they are relevant to any dispute.” Panel Report, *United States – Measures Relating to Zeroing and Sunset Reviews*, WT/DS322/R, adopted 23 January 2007, as modified by Appellate Body Report WT/DS322/AB/R at para. 7.99 n.733; *see also* Appellate Body Report, *Japan – Taxes on Alcoholic Beverages*, WT/DS8/AB/R, WT/DS10/AB/R, WT/DS11/AB/R, adopted 1 November 1996, DSR 1996:I, 97 at p. 14 (prior panel reports “are not binding, except with respect to resolving the particular dispute between the parties to that dispute”).

\(^{11}\) *See* WTO Agreement, art. IX:2, 33 I.L.M. at 1148 (“The Ministerial Conference and the General Council shall have the exclusive authority to adopt interpretations of this Agreement and of the Multilateral Trade Agreements.”); Appellate Body Report, *United States – Continued Existence and Application of Zeroing Methodology*, WT/DS350/AB/R, adopted 19 February 2009 at para. 360 (summarizing U.S. argument that “treating prior reports as binding outside the scope of the original dispute would add to the obligations of WTO Members, inconsistently with Articles 3.2 and 19.1 of the DSU”); Dispute Settlement Body, Minutes of Meeting, WT/DSB/M/250 at paras. 50-55 (1 July 2008) (statement by United States on adoption of panel and Appellate Body reports in *United States –
Nevertheless, article 3.2 of the DSU states that “[t]he dispute settlement system of the WTO is a central element in providing security and predictability to the multilateral trading system.” Disputing parties, panels, and the Appellate Body itself have pointed to that statement in support of a strong presumption in favor of following precedent. How can there be “security and predictability” in the multilateral trading system if the Appellate Body may construe a given provision one way in one dispute while panels or even the Appellate Body itself construe the same provision a different way in a subsequent dispute? While they may avoid using the term “stare decisis,” panels and the Appellate Body typically analyze the legal questions before them in ways that suggest they believe the doctrine or something like it is operative.

I would expect the negotiators of an investor-State appellate mechanism to encounter a similar tension between striving for consistent interpretation of treaty text and avoiding ceding undue power to the new mechanism. The solution may be similar to the one that has emerged in the WTO – i.e., avoiding any explicit reference to stare decisis while invoking concepts like

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*Final anti-dumping measures on stainless steel from Mexico (DS344)* (criticizing Appellate Body report for “appear[ing] to transform the WTO dispute settlement system into a common law system”).

12 The Appellate Body articulated its position on this question quite clearly in its report earlier this year in one of several disputes involving the practice of the U.S. Department of Commerce known as “zeroing” in calculating antidumping duties. Appellate Body Report, *United States – Continued Existence and Application of Zeroing Methodology*, WT/DS350/AB/R, adopted 19 February 2009. There, the Appellate Body stated, “Following the Appellate Body's conclusions in earlier disputes is not only appropriate, it is what would be expected from panels, especially where the issues are the same.” *Id.* at para. 362. *See also id.* at paras. 362-365 (citing other dispute settlement reports standing for the same proposition).

“security and predictability” and “legitimate expectations” to suggest that some deference is owed to precedent.

In this respect, one important difference between the WTO context and the investor-State context is the relative ease of dealing with aberrant appellate decisions in the latter. It is extremely difficult for the WTO as an institution to decide that an Appellate Body legal conclusion is erroneous and should not be followed in future disputes. In theory, the WTO’s Dispute Settlement Body could decline to formally adopt the report containing the erroneous finding, but this would require unanimous consensus, including acquiescence by the Member that prevailed in the dispute and thus stands to benefit from the error.\textsuperscript{14} Other options may include the adoption of a clarifying interpretation of the agreement at issue\textsuperscript{15} or an amendment of that agreement.\textsuperscript{16} While the WTO Agreement contemplates the possibility of voting on proposed interpretations and amendments, the express norm and consistent practice has been “decision-making by consensus,”\textsuperscript{17} making the prospect of exercising either option extremely remote. Indeed, neither option has ever been exercised in response to a dispute settlement panel or Appellate Body report.

In contrast to the over 150 Members of the WTO, free trade agreements and investment treaties tend to be limited to relatively small numbers of parties. Most of the free trade agreements and investment treaties to which the United States is a party have only one other

\textsuperscript{14} DSU, art. 17.14, 33 I.L.M. at 1237.
\textsuperscript{15} WTO Agreement, art. IX:2, 33 I.L.M. at 1148.
\textsuperscript{16} WTO Agreement, art. X, 33 I.L.M. at 1149.
\textsuperscript{17} WTO Agreement, art. IX:1, 33 I.L.M. at 1148.
party. Even the free trade agreement among the United States, the Dominican Republic and five Central American countries has only seven parties. Accordingly, a much smaller number of parties would need to agree to address an aberrant decision of an investor-State appellate mechanism. They could help ensure against similar errors being made in future cases either by amending the treaty or, in appropriate circumstances, providing an authoritative interpretation of the treaty. Indeed, the NAFTA Parties did just that in July 2001 in response to investor-State arbitral awards that appeared to construe NAFTA’s “minimum standard of treatment” article more expansively than they had intended. This greater flexibility in the Parties’ exercise of their autonomy in interpretation of an investment treaty as a result of smaller numbers may cause negotiators of an appellate mechanism to be less concerned about any suggestion that the decisions of the mechanism could be treated as binding precedent by future tribunals and the appellate mechanism itself.

The Relationship of Appellate Mechanism Review to U.S. Law

I will turn now to the matter of the relationship of an investor-State appellate mechanism’s review to current U.S. law. Here, the WTO perspective is illuminating in that it

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19 See CAFTA, art. 19.1.3(c) (authorizing Free Trade Commission, consisting of cabinet-level representatives of the Parties, to issue interpretations of the provisions of the Agreement) and art. 10.22.3 (requiring that awards of investor-State tribunals be consistent with interpretations adopted by Free Trade Commission).

calls attention to the difference I already have noted between a dispute settlement system that is an extension of a diplomatic institution and one that is an adjudicative system deliberately removed from the diplomatic realm.

U.S. law treats the action taken in response to adverse findings by the WTO dispute settlement mechanism as a political matter. Section 123(g) of the Uruguay Round Agreements Act (“URAA”) sets forth a detailed process to be followed after a WTO panel or the Appellate Body finds a U.S. regulation or practice to be inconsistent with a WTO obligation.21 The process involves consultations with Congress, private sector advisory committees, and the public. It also includes an opportunity for the congressional committees with jurisdiction over trade matters to adopt non-binding resolutions of agreement or disagreement with any proposed change to regulation or practice in response to adverse WTO findings. Section 129 of the URAA sets forth a variation on this process for antidumping duty and countervailing duty cases.22 The URAA does not set forth a process for revising legislation found to be inconsistent with a WTO obligation. Such revisions are subject to the numerous factors that affect all legislative decisions.

The consequence of not coming into compliance with adopted WTO panel and Appellate Body recommendations is that the complaining party may be authorized to suspend “concessions or other obligations” owed to the responding party.23 Most commonly, this action takes the form of increased tariffs on imports of the responding party’s goods. However, in certain cases it may

21 19 U.S.C. § 3533(g).
23 Another possibility is agreement between the complaining party and the responding party on “mutually acceptable compensation.” DSU, art. 22.2, 33 I.L.M. at 1239.
include suspension of other obligations too. The key point is that while “full implementation of a recommendation to bring a measure into conformity with the covered agreements” is the preferred option, the WTO provides other options to ensure that the balance of rights and obligations under the WTO Agreement is maintained.

By contrast, when it comes to an award favorable to the claimant, investor-State dispute settlement is concerned not with maintaining a balance of rights and obligations but with having the award recognized and enforced. Recognition and enforcement of foreign arbitral awards is provided for in U.S. law under the Federal Arbitration Act (“FAA”) (for non-ICSID Convention awards) and the Convention on the Settlement of Investment Disputes Act of 1966 (“ICSID Act”) (for ICSID Convention awards).

Unlike the URAA, which provides a political process for the implementation of WTO recommendations, the FAA and the ICSID Act provide a judicial process for the recognition and enforcement of foreign arbitral awards. The FAA requires a U.S. district court to confirm a foreign arbitral award, unless a ground for refusal of recognition and enforcement exists under either the Convention on Recognition and Enforcement of Foreign Arbitral Awards (“New York

24 See, e.g., Decision by the Arbitrator, United States – Subsidies on Upland Cotton – Recourse to Arbitration by the United States Under Article 22.6 of the DSU and Article 4.11 of the SCM Agreement, WT/DS267/ARB/1, 31 August 2009, at para. 5.230 (finding that under specified circumstances Brazil will be authorized to suspend obligations owed to the United States under the Agreement on Trade-Related Aspects of Intellectual Property Rights and the General Agreement on Trade in Services).
25 DSU, art. 22.1, 33 I.L.M. at 1239.
Convention”))\(^{28}\) or the Inter-American Convention on International Commercial Arbitration ("Panama Convention"),\(^{29}\) whichever is applicable.\(^{30}\) Both the New York Convention and the Panama Convention identify grounds on which recognition and enforcement may be refused, including the existence of certain procedural defects in the underlying arbitration, as well as the subject matter of the dispute being incapable of settlement through arbitration under the law of the country where recognition and enforcement is sought or recognition and enforcement being contrary to the public policy of that country. The possibility of refusing recognition or enforcement on any of these grounds creates the prospect of a U.S. district court engaging in some review of an award and/or the process that led to rendering of the award.

The ICSID Act simply states that “[t]he pecuniary obligations imposed by . . . an [ICSID] award shall be enforced and shall be given the same full faith and credit as if the award were a final judgment of a court of general jurisdiction of one of the several States.”\(^{31}\) This implements the obligation of the United States under Article 54 of the ICSID Convention.\(^{32}\) Unlike the New York Convention and the Panama Convention, the ICSID Convention does not provide any bases on which a court could refuse recognition and enforcement of an ICSID Convention award. Any

\(^{28}\) Convention on the Recognition and Enforcement of Foreign Arbitral Awards, 10 June 1958, 330 UNTS 3 ("New York Convention").

\(^{29}\) Inter-American Convention on International Commercial Arbitration, 30 January 1975, 14 I.L.M. 336 ("Panama Convention").


\(^{31}\) 22 U.S.C. 1650a(a).

\(^{32}\) Convention on the Settlement of Investment Disputes Between States and Nationals of Other States, 18 March 1965, art. 54, 575 UNTS 159 ("ICSID Convention").
challenge to an ICSID Convention award would have to be made through the special annulment process within ICSID.\(^{33}\)

The question, then, is what amendments may have to be made to the FAA and the ICSID Act to accommodate the establishment of an appellate mechanism. For non-ICSID Convention awards, the availability of an appeal probably renders somewhat redundant the opportunity to ask a U.S. court to refuse recognition and enforcement under the grounds provided in New York Convention or Inter-American Convention. Not only would such U.S. court review prolong the dispute settlement process, it also could undermine the very rationales for creating an appellate mechanism in the first place. To the extent a court is empowered to review an arbitral award for consistency with public policy, it could be drawn into second-guessing the appellate mechanism’s interpretation of key legal provisions, which could lead to fragmented rather than consistent interpretation of those provisions, undermining both confidence in the dispute settlement system and consistency of interpretation.

Accordingly, in establishing an appellate mechanism, the United States should consider amending the FAA to eliminate the possibility of a U.S. court’s refusing recognition and enforcement of an arbitral award where appellate review is available. Such an amendment would make the FAA look more like the ICSID Act.

Additionally, to the extent that review by the appellate mechanism would replace the annulment process for review of ICSID awards, the United States may need to amend the ICSID

\(^{33}\) See ICSID Convention, art. 52, 575 UNTS 159.
Act. That act pertains to “[a]n award of an arbitral tribunal rendered pursuant to chapter IV of the [ICSID] Convention.” Given that review by a newly created appellate mechanism would fall outside of chapter IV of the ICSID Convention, it may be desirable to clarify that an ICSID award that has been subject to review by the mechanism still qualifies as “[a]n award of an arbitral tribunal rendered pursuant to chapter IV of the [ICSID] Convention.”

Conclusion

In conclusion, it is useful for the negotiators of an investor-State appellate mechanism to consider the example of the WTO Appellate Body. In certain respects, the Appellate Body is an important and relevant precedent that may provide negotiators with valuable insights. At the same time, it must be recognized that the context in which the Appellate Body operates is different in key respects from the context in which an investor-State appellate mechanism would operate. Those differences should be borne in mind in building the essential aspects of an investor-State appellate mechanism.