

# Oil and Gas Investor-State Dispute Settlement: Is Mediation-Arbitration Considered a Mechanism for Common Interests?

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## ABSTRACT

International oil and gas investment disputes constitute an important part of investor-state dispute settlement (ISDS) system. Investment arbitration which is regarded as a prevalent dispute settlement mechanism in this area has come under severe criticism since it creates huge costs, lengthens the process, and devastates the parties' long-term investment relationship. In recent years, the possibility of applying alternative dispute resolution (ADR) and hybrid dispute settlement mechanisms has largely been discussed. Mediation-arbitration (Med-Arb) is one of the hybrid integrated dispute settlement mechanisms which embodies flexibility, nonjudicial, and negotiate-oriented benefits of mediation and the finality advantage of arbitration simultaneously in a single process. In this method, mediation is first attempted by the parties before arbitration could be started; if settlement is not reached during the mediation phase, the appointed neutral or mediator will then act as (an) independent arbitrator(s), will continue the case under the arbitration process, and will render a binding arbitration award. In this method, if parties reach an agreement during the first phase (mediation process), they will not incur huge costs of lengthy investment arbitration. In this method, even if the first stage (mediation process) fails, since it has further clarified and narrowed down the disputes, then the arbitration process will be less lengthy and proceed more efficiently. Moreover, both investors and host states in oil and gas investment area do have strong ambitions to maintain the investment relationships. These goals are achieved better via adopting Med-Arb proceedings. The most noted concerns in this method relates to the issue of the impartiality of the neutral (mediator in the first stage) who acts as an arbitrator at the next stage. In other words, it may be argued that the confidential information learned by the neutral from the parties in the mediation stage may seriously impact on his/her impartiality in the arbitration stage. This issue can be responded in light of respecting party autonomy principle which selects the Med-Arb clearly and correctly for dispute settlement. This approach is affirmed and proposed by the UNCITRAL model law on international commercial conciliation (2002) as well. Also, concerns regarding the enforcement of international agreements resulting from mediation have already been addressed in the United Nations Convention on International Settlement Agreements Resulting from Mediation (Singapore Convention on Mediation), which has attained international acceptance by 51 state members so far.

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## 1. Introduction

Oil and gas industry has played a major role in international foreign investment sector<sup>2</sup>. Consequently, disputes in this industry have also been considered as crucial in terms of economic, political, legal, and reputational consequences for host states and investors. The settlement of disputes between investors and host states has evolved into what nowadays regarded as a full-fledged arbitration. In other words, the expansion and changes of law in the field of foreign investment is the result of disputes being resolved through international arbitration (Crawford, 2005, p. 10). Also, in the context of oil and gas investment disputes, arbitration is the preferred way of settling disputes (T.W.Walde, *Managing International OGEMI-Investment Disputes* (Presentation), 2004). However, despite many unique features of this privatized system of justice, there is a growing concern regarding costs (sometimes more cumbersome than court litigations) and protracted process of investment arbitrations<sup>3</sup>. Moreover, considering the adversarial feature of arbitration, long-lasting investment projects are usually put in danger, which is not desirable neither for oil and gas producing host states, regarding oil and gas investments as the development mega projects in their country/economy on which the national budget mostly depends, nor for investors who spent huge costs and time for establishing the investment projects in the host countries.

Alongside with the aforementioned concerns, it should be noted that distinct features of oil and gas investment disputes also lead us to provide comprehensive insights in this context. The important elements of sovereign issues in host states, historic and social backgrounds, political international relations, being exposed to global markets, and high inherent risks in this industry make the context of oil and gas investment arbitration even more complex (Reid, 2012).

Meanwhile, in recent years, prevention mechanisms and alternatives to the current investor-state arbitration

system, such as mediation, have been extensively debated<sup>4</sup>. For instance, investor-state mediation is currently being considered as a tool which offers a relatively efficient alternative to arbitration (Ali Shahla F, 2018) and is very capable of assisting parties in order to find creative solutions which may lie outside of strict legal remedies (Ali Shahla F, 2018). It should be considered that although mediation contains many advantages to arbitration in terms of lower costs, a rapid and flexible process, and creating an opportunity for parties to restructure their relationships together with settling their disputes, some serious concerns exist in relation to the enforcement of such mediation decisions when made. However, luckily one of the good contemporary achievements which should be taken into account is that the United Nations has already legislated the special Convention on International Settlement Agreements Resulting from Mediation which enables mediation settlement agreements to be directly enforced. However, until this convention becomes universally accepted and makes the potential users abide by the mediation decision, the concern may still exist (CHUA, 2018) and may prevent parties from entering an efficient ADR process such as mediation.

Nevertheless, the positive trend in applying the hybrid dispute settlement mechanism is growing up in order to respond to the abovementioned concerns and merge the advantages of judicial, semi-judicial, and nonjudicial dispute settlement mechanisms in a single and integrated nature, particularly by mixing arbitration and mediation. A mediation followed by arbitration (Med-Arb or same neutral Med-Arb) is one of the common hybrid methods to resolve the disputes. In this process, a neutral mediator tries to assist parties to reach a solution, and if the process fails, he/she then appears as an arbitrator in order to settle the disputes and issue the final binding arbitration award (CHUA, 2018). The main question in this paper is whether Med-Arb mechanism, in which a mediator tries to assist parties to solve their disputes through a mediation process and becomes a

<sup>2</sup> For instance, foreign investment in Egypt was skewed toward the oil and gas industry in the past years as significant discoveries of offshore gas reserves have attracted investments from Multi National Enterprises (MNEs). See: (UNCTAD, 2019).

<sup>3</sup> Average duration of investment arbitration length is four years, and the average cost per party is between USD 4-6 million. See: (ICSID, 2018)

<sup>4</sup> For example, UNCTAD has published a paper in 2011 including proceedings of the Washington and Lee University and UNCTAD Joint Symposium on International Investment and Alternative Dispute Resolution, held on 29 March 2010 in Lexington, Virginia, United States of America, which includes many notable scholars' and professionals' expression of views on the topic. This study demonstrates the status of the current system and the way forward. See: (UNCTAD, 2011).



member of the further arbitration panel, could be an efficient mechanism to be applied in the context of oil and gas investment disputes.

In order to propose an efficient and win-win potential mechanism from both investors and host states perspectives in petroleum industry, a multidisciplinary approach is taken into account in this paper. First, oil and gas investment features and disputes are identified. In the second part, the current practice in ISDS and its challenges in the oil and gas investment sector is analyzed. Finally, Med-Arb mechanism is introduced and the concerns and benefits of the disputants about using this tool is discussed in the context of oil and gas industry.

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## 2. Features of Oil and Gas Investments and Related Disputes

In this part, firstly oil and gas investment unique features is examined, and secondly the features of the oil and gas investment disputes is identified in order to evaluate dispute resolution mechanisms in this industry.

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### 2.1. Oil and Gas Investment Industry

Since the Industrial Revolution, the energy sector has always been a key factor in production all over the world (Stevens, 2018). The vital role of oil and gas resources as a crucial source of energy production is notable all over the world. In addition, the role of oil and gas in the economic development of the global economy and trade, the role of oil price in the macroeconomies, and the impact of the geopolitics of oil and gas corroborate the high importance and distinct features of this industry (Stevens, 2018).

Regarding high complexity and inherent risks in this industry, it is worth emphasizing that oil and gas extraction requires huge capital investments, and, in some territories, it requires very modern and nonconventional technologies to be utilized for exploitations to achieve production and profit, which is frequently a long-term investment. Another distinct feature of oil and gas investment industry is attributed to the players. It is worth clarifying that investors and states in this industry have special characteristics distinguishing them from other industries, which consequently leads scholars and practitioners concentrate on this industry more accurately, deeply, and comprehensively.

Investors in the oil and gas industry historically were traditionally international oil companies (IOCs) with huge financial, technical, and management sources and

capabilities. They have been executing mega oil and gas projects with financial, technical, political, commercial, legal, and environmental risks all over the world. On the other hand, there are national oil companies (NOCs) who act on behalf of states in investment contracts with private oil and gas investors. However, it should be mentioned that the role and balance-power of IOCs and NOCs have not been static in light of changes and developments in recent years. Some factors have caused significant changes in this context and changed the monopoly of oil and gas market by IOCs. For instance, capital technology and know-how, which have been the historical key motivations for NOCs-IOCs relationships, have changed due to the evolution of service companies which currently offer the capabilities that IOCs offered exclusively in previous decades (A.Xenofontos, 2018). On the other hand, NOCs have become more capable in many aspects of oil and gas investment projects and are currently less dependent on IOCs in comparison to the past decades. However, it should be considered that developing oil and gas producers still require the cooperation with oil and gas investors. The oil and gas investment projects are regarded as development projects in these countries. As a consequence, these countries do have serious concerns such as sovereignty and national resources challenges, accountability issues, dependence on the oil and gas investment revenues, environmental and social impact assessment requirements, oil and gas sale, and so on. As it is evident, both parties have legitimate concerns and expectations in oil and gas investment disputes, which is required to be included in their management strategies and plans for the definite investment projects (UNCTAD, Investor-State Disputes: Prevention and Alternatives to Arbitration, 2011). Therefore, seeking efficient dispute settlement mechanisms in this area has a pivotal importance for all beneficiaries.

It should also be noted that in order to prevent the oil and gas industry from incurring huge costs and suffering severe damages, a preventive mechanism and/or an amicable settlement should be initially approached by the parties through consideration and management of the

multiple elements of the TEFCEL<sup>5</sup> which is a model for strategic, dynamic, and consistent management of oil and gas disputes. This model is capable of managing the multiple risks of the petroleum project and presenting consistent and comprehensive solutions to settle the disputes for long-term oil and gas projects, thereby preserving contractual relationships.<sup>6</sup> TEFCEL was considered to be a comprehensive business model and consistent approach to problem-solving in upstream and downstream energy, in risk detection/analysis, in contractual negotiates and performance management, in contract allegation preventive management, in contract framework, and in conflict settlements. Arbitrators and mediators in oil and gas industry are the best qualified individuals who would be able to prevent and/or settle very complicated petroleum investment disputes as they should be acquainted and equipped with the knowledge and experience of nine elements of the TEFCEL model. Without any doubt, the execution and implementation of the TEFCEL model by the oil and gas industry mediators and arbitrators in the process of Med-Arb mechanism will be advantageous to settling the petroleum investment disputes comprehensively in an integrated multidisciplinary approach while maintaining the overall strategic relationship of the parties and preserving their long terms benefits and interests (Ebrahimi, 2011)

## 2.2. Identifying International Oil and Gas Investment Disputes

The fact that disputes arising from the extraction of crude petroleum and natural gas constitute a major share of international investment disputes<sup>7</sup> makes us have a

special focus on oil and gas investment disputes. In this context, it should also be kept in mind that few areas of international laws give rise to controversial opinions, and the law of foreign investment is one of the most notable examples in this regard. Many historical factors shaped and affected the system of foreign investment law<sup>8</sup>, and institutions involving in resolution of investment disputes such as ICSID, NAFTA, Iran-United States Claims Tribunal and a few decisions from the International Court of Justice (ICJ) and other ad hoc arbitral tribunals have had major roles in the evolution of this field (Crawford, 2005). It is worth remembering that judicial decisions are considered to be the subsidiary source of international law, and arbitral awards made on disputes arising from foreign investment transactions contribute to the subject (M.Sornarajah, 2010).

A foreign investment dispute is a disagreement between an investor from one country and a government which relates to an investment in the host country (Crawford, 2005). Company-versus-state disputes are often called investor-state or state-investment disputes (Martin, 2011) as well. Although this definition is simple, there are lots of complex issues which should be addressed in their own places. The role of states, multinational companies, and nongovernmental organizations (NGOs) and the interests of aboriginal groups should also be considered in developments and identifications in this field (M.Sornarajah, 2010).

Investment definition and investment dispute are a debatable issue in investment law area per se, so even if it is defined and reflected in international agreements

<sup>5</sup> TEFCEL stands for technical, technological, economic, financial, fiscal, commercial, contractual, environmental, and legal elements.

<sup>6</sup> The TEFCEL contract management model was first proposed by Dr. N. Ebrahimi in 2005 at oil and gas summit in London, and afterward it was elaborated and discussed in various workshops and master-classes in Johannesburg (South Africa), Kuala Lumpur (Malaysia), Ho Chi Minh City (Vietnam), and Dubai (UAE). The attendees of those workshops and master-classes have been the various experts from both IOCs and NOCs. This model not only works for professional negotiation, contract conclusion, contract management, and contract execution in oil and gas sectors, but also brings values for the prevention of disputes as well as disputes resolution.

<sup>7</sup> According to UNCTAD Investment Dispute Settlement Navigator on its website, the extraction of crude petroleum and natural gas sector has the highest share of treaty-based ISDS cases among primary industry sections. (UNCTAD, investment policy, 2019)

<sup>8</sup> Cold War, the Second World War and the Post Second World War backgrounds are historical milestones in which many changes have occurred (M.Sornarajah, 2010). Also, the notion of permanent sovereignty over natural resources which was affirmed by the General Assembly of the United Nations on 14 December 1962 shaped many future dramatic changes in the area of foreign investment law. This resolution provides that states and international organizations shall strictly and conscientiously respect the sovereignty of people and nations over their natural wealth and resources in accordance with the Charter of the United Nations and the principles contained in the resolution. These principles are set out in eight articles concerning, inter alia, the exploration, development and disposition of natural resources, nationalization and expropriation, foreign investment, the sharing of profits, and other related issues (Kilangi, 2019).



between the states, it is very probable that the parties have contradicting points of view regarding the investment definition which is one of the primary issues to be interpreted and decided in the context of investment dispute settlement. An investment which qualifies for investment treaty protection must include certain legal and economic characteristics (Douglas, 2009). In a similar vein, we have investor definition and different jurisprudences in this context too. Regardless of these elements and various jurisprudences on the definition of the mentioned terms, by contemplating investment arbitration disputes and awards, some major common disputes can be identified in oil and gas investment sectors. This methodology leads us to first identifying the main frequent investment disputes in this area and subsequently evaluating the proper hybrid dispute settlement mechanism according to the features of the disputes.

The frequent disputes in oil and gas investment sectors mostly include the following issues and claims: interpretation of modern stabilization clauses (by renegotiation, rebalance, or equilibrium clauses), interpretation of using permitting power by host states or indirect expropriation claims, interpreting governmental (authorities or intervention) to sell oil and gas to state companies, interpretation of calculation formula (including or not including decommissioning expenses for example in production sharing agreements), fluctuations in the oil and gas price worldwide and its effects on parties' contractual relationship, breach (or alleged breach) by state monopoly of a long-term sales contract in the context of high regulatory/governmental density, alleged manipulative use of bankruptcy and tax law to drive an investor into bankruptcy, and the manipulative use of bankruptcy to channel assets to state company (T.W.Walde, *Managing International OGEMI-Investment Disputes* (Presentation), 2004). The abovementioned claims and disputes are just the most notable examples in this industry. The investor (an oil and gas company or a consortium of oil and gas companies) can base its claims on its investment contract (e.g. production sharing contract (PSC) or risk service agreement (RSA)), on an investment treaty, or possibly on both. Most treaty claims are made under bilateral investment treaties (BITs)<sup>9</sup>, which are negotiated and ratified by two sovereign states.

Although it may be argued that oil and gas investment disputes may not often happen to international oil companies (IOCs), when they do occur, they involve large sums of money and therefore have a significant impact on a company's bottom line (Martin, 2011). In the same vein, host states, particularly developing ones, also suffer from huge costs when these disputes arise in the investment environment of their countries (UNCTAD, *Investor-State Disputes: Prevention and Alternatives to Arbitration*, 2011).

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### **3. Current System of Dispute Resolution Between Investors and Host States**

In this section, different dispute settlement mechanisms applied to investor-state disputes are analyzed. Since arbitration is a prevalent mechanism in this area, the status of ADR mechanisms between host states and investors and hybrid mechanisms are evaluated. Finally, the opportunities and challenges of Med-Arb in the oil and gas ISDS are also examined.

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#### **3.1. Arbitration: a Prevalent but not Always an Efficient Mechanism for Investor-State Disputes**

The international investment arbitration is a special form of mixed dispute settlement mechanism between states and private parties. This feature of investment arbitration leads to many controversial issues. The availability of effective and proper dispute settlement mechanisms gives rise to the attraction of more investors and meets the development concerns of host-states (Muchlinski, 2008). Also, effective dispute settlement mechanisms assure host countries that their disputes shall be resolved in a fair and effective manner. From investor's perspective as well, the availability of an efficient dispute settlement mechanism is important as it assists them with saving costs, increasing profitability, and maintaining their investment projects in the host states.

Provisions regarding ISDS have been included in international investment agreements (IIAs) since the 1960s (Echandi, 2007). Instead of recourse to the national courts of the host countries which may not be considered effective for resolution of investor-state disputes, international investment arbitration has been widely accepted in IIAs and free trade agreements (FTAs) worldwide in the past decades. However, it

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<sup>9</sup> There are presently more than 3000 BITs involving some 180 countries in existence around the world (Martin, 2011).



should be noted that these provisions to institute arbitral proceedings were not used until 1987, when the first investor-state dispute based on a BIT<sup>10</sup> was registered in the arbitral proceedings of the World Bank's International Centre for Settlement of Investment Disputes (ICSID). Currently, international investment arbitration is considered as an internationalized approach to investor-state dispute settlements (Muchlinski, 2008).

The increased trend in investment arbitration—which still continues—is a sign of success for the investment arbitral system (Reinisch, 2012). Apart from multilateral treaties such as Energy Charter Treaty, there are more than 3000 BITs worldwide, and most of them include direct investor-state dispute resolution through arbitration. This is a meaningful sign which demonstrates the general acceptance of the investment arbitration system. In other words, the availability of investment arbitration and the enforcement of investment arbitral awards<sup>11</sup> are two major and apparent incentives being very crucial to investors although enforceability of the awards is important for host states as well as investors.

From the perspective of host states, this quid pro quo for investment arbitration may be considered as their interest in creating a positive investment attraction environment. Moreover, states also seek for a fair judicial arbitral dispute settlement procedure, and, in

many ICSID or non-ICSID procedures, states have won some cases. Moreover, when states are engaged in investment arbitration award, they are not required to justify the rendered decisions before their public authorities, public opinion, and other beneficiaries such as NGOs because they have been rendered by a third party. Further, the decisions taken and imposed by third parties per se make the justification of the rendered decisions before public opinion/other beneficiaries easier in comparison to “settlement solutions” in which the parties have direct responsibility. (Céline, 2013). In other words, from the managerial points of view, accepting the risks and responsibility of entering settlement processes such as mediation is a more complex issue than attributing the results of a case to a third party decision maker with a binding power such as arbitration (Céline, 2013).

It should be discussed that in recent years, investment arbitration system has been criticized a lot in terms of huge expenses and a lengthy arbitration procedure<sup>12</sup>, confidentiality and transparency issues, and bias of this system in favor of investors in some situations. In certain cases, the backlash against the investment arbitration system has led to the denunciation of some countries such as Ecuador and Venezuela from ICSID in 2009<sup>13</sup>. In other reactions, some governments have revised their current BITs or BIT models<sup>14</sup>.

<sup>10</sup> It should also be considered that international investment disputes can also arise from contracts between investors and governments; a number of such disputes are (or have been) brought before ICSID, or submitted to other institutional arbitration systems or ad hoc arbitration (Echandi, 2007).

<sup>11</sup> Arbitration institutions and ad-hoc arbitral procedures are so well-defined and developed that the parties can easily rely on (Reinisch, 2012). Awards rendered pursuant to most of ad hoc investment arbitrations, as well as those administered by arbitration institutions such as ICC, LCIA, SCC, or the centers, are usually treated as foreign arbitral awards in the sense of the 1958 New York Convention and therefore are enforceable in domestic courts based on the convention's provisions. Article III of the convention reads as: Each contracting state shall recognize arbitral awards as binding and enforce them in accordance with the rules of the procedure of the territory where the award is relied upon, under the conditions laid down in the following articles. There shall not be more onerous conditions or higher fees or charges imposed substantially on the recognition or enforcement of the arbitral awards to which this convention applies than imposed on the recognition or enforcement of domestic arbitral awards.

<sup>12</sup> The increase in the use of ISDS over the last decade

has evidenced various shortcomings and challenges of the existing mechanisms (i.e. arbitration). One issue is related to time. Investment disputes are fact-intensive and may take years to be resolved. For both investors and states, such a lengthy process entails not only a high economic and political cost but also the possibility of irreparable damage to the parties' long-term working relationship. Another critical issue is the high cost of arbitration, which represents an important financial burden which governments have to face when defending a case (UNCTAD, Investor-State Disputes: Prevention and Alternatives to Arbitration, 2011).

<sup>13</sup>Denunciation of the ICSID convention and BITS can have lots of sophisticated legal consequences. According to one of UNCTAD publications in this regard, mechanisms to strengthen the legal capacity of host countries (e.g. through the creation of an advisory facility), fostering of dispute avoidance and preventive mechanisms (e.g. through the more frequent use of alternative dispute resolution (ADR) techniques such as conciliation and mediation), and efforts to improve the consistency, coherence, and development dimension of IIA interpretation can be possible options to address current concerns in the context of IIAs (Zhan, 2010).

<sup>14</sup> The 2004 model US BIT scaled back a number of foreign investor protections in favor of protecting the



The mentioned challenges raised the question of possibility in applying alternative or hybrid dispute resolution mechanisms in the contexts of ISDS so that more efficient options are offered in a manner that is in line with the interests of the states, investors, and other beneficiaries. Creating a balanced efficient dispute settlement in this field with a comprehensive win-win approach will definitely lead to more peaceful, profitable, and lasting relationships between the investors and governments at the global level

### **3.2. ADR Mechanisms in ISDS: Idealism or a Real Practice?**

While arbitration is a prevalent means for dispute resolution in ISDS, there is a growing trend in applying dispute prevention mechanisms and managing investor-state disputes in other efficient ways simultaneously (UNCTAD, *Investor-State Disputes: Prevention and Alternatives to Arbitration*, 2011). As elaborated in the previous section, the average length of arbitration process seems to be 4-7 years in investment disputes, which imposes huge costs (more than million dollars in certain investment disputes) on parties. Arbitration, which in its initial appearance was considered as political arbitration and had the feature of “settling” disputes between parties, nowadays, in a modern arbitration, has transformed to a semi-judicial process (T.W.Walde, *Pro-Active Mediation of International Business and Investment Disputes Involving Long-Term Contracts: From Zero-Sum Litigation to Efficient Dispute Management*, 2004). Using the judicial and semi-judicial mechanisms ruins the established investment relationship between parties which consequently leads to the loss of anticipated profits and expected goals of investors and host states. In the context of oil and gas investment industry, IOC’s recourse to arbitration may contain severe reputational impacts. As a consequence, applying alternative mechanisms, which have a collaborative feature in their nature but do not have the adversarial nature of arbitration or adjudicative means, can be more constructive for both investors and host countries (T.W.Walde, *Law, Contract and Reputation in International Business: What Works*, 2002).

The efficient management of investor-state disputes includes various mechanisms such as facilitated negotiation (conciliation or mediation), fact-finding,

sovereign prerogatives of the state hosting the foreign investment. While the 2004 model and more recent 2012 model include robust ISDS provisions, these provisions have been more thoroughly refined, and many of the substantive provisions have been revised, which has

early neutral evaluation (ENE), dispute resolution board (DRB), ombudsman services, or other similar mechanisms with the function of assisting disputants in resolving their claims and disputes in a peaceful, constructive, and efficient manner. These nonadjudicative mechanisms differ from judicial ways in which (a) third party(s) render(s) binding decisions. These ADR mechanisms are not exclusive at all as enumerated above and are in line with parties’ autonomy (UNCTAD, *Investor-State Disputes: Prevention and Alternatives to Arbitration*, 2011). However, mediation is the frequent applied ADR form.

Mediation involves an independent third-party (or the mediation team) who does not make a legally binding determination of the dispute matters, and instead works with parties to move them toward an agreed settlement which both consider as proper and better than protracted, costly and relationship-destroying judicial and semi-judicial procedures (T.W.Walde, *Pro-Active Mediation of International Business and Investment Disputes Involving Long-Term Contracts: From Zero-Sum Litigation to Efficient Dispute Management*, 2004). In mediation, the process of information collecting or (information learning) is less biased than the adversarial mechanisms of litigation or semi-litigation procedures. This process is not formal but includes (or must include) many aspects like cultural, organizational behavior, coordination, and many other relevant factors in a professional efficient mediation (T.W.Walde, *Managing International OGEMI-Investment Disputes (Presentation)*, 2004).

While there is no exact statistics on the investor-state cases settled by arbitration, the facts demonstrate that many of these cases are settled through alternative dispute resolution mechanism (UNCTAD, *Investor-State Disputes: Prevention and Alternatives to Arbitration*, 2011). For instance, ICSID reports affirm that about 40% of registered cases, which are mostly treaty-based claims, have settled without binding arbitration award. However, regarding the process in which parties settled, our information is little mostly due to confidential concerns and not publishing the process of reaching settlements by institutions such as ICSID. For instance, it is not known whether these cases have

reduced the level of foreign investor protection. Overall, the models seek to recalibrate the balance between the rights of the investors and the nations to regulate the public interest (Malcolm Langford, 2018).

been settled via direct negotiation, mediation, or any other alternative mechanisms (Céline, 2013).

### 3.3. Hybrid Dispute Settlement Mechanisms and Med-Arb Status in ISDS

As the international trade, investment, and globalization expand, dispute settlement mechanisms grow as well. Thus, the role of arbitrators, mediators, governments, and all beneficiaries in this development is undeniable (E.Mason, 2011). In the combined data gathered from the Global Pound Conference series from 2016 to 2017, 52% of respondents indicated that the most effective commercial dispute resolution processes usually involve combining adjudicative and nonadjudicative processes. When asked which tools or processes should be prioritized to improve the future of commercial dispute resolution, 45% of the respondents indicated that combining adjudicative and nonadjudicative processes should be prioritized (CHUA, 2018). The abovementioned information illustrates that combining processes, particularly mediation and arbitration in dispute resolution, is popular in the context of international commercial dispute resolution system. Mixing modes of arbitration and mediation may appear in myriad forms such as Arb-Med, Med-Arb, Arb-Med-Arb, mediation window, and other ways with their own distinct functions and natures. Consequently, most of the dispute settlement centers around the world endeavor to offer hybrid clauses<sup>15</sup> and procedures to parties<sup>16</sup>.

Med-Arb is one of the most popular mode of combined dispute settlement procedures (Limbury, 2009). The phrase is used to refer to a process in which

mediation is first attempted by parties before arbitration is started. If a settlement achieved after the mediation phase, obviously there is no need for initiating the arbitration stage<sup>17</sup>. If no settlement agreement is achieved, the appointed arbitrator (who is the previous mediator) will proceed to hear the case and render a binding arbitration decision. Where the mediator and arbitrator are the same person, the phrase “same neutral Med-Arb” should be used to avoid doubt (CHUA, 2018). Considering the opportunities, limitations, and challenges of this mixing mode of dispute settlement, the question is that to what extent the hybrid processes—particularly Med-Arb tool as defined—are, or in practice used, in the contexts of ISDS. In a similar vein, can this hybrid method provide both oil and gas investors and oil and gas producing host states with more benefits than other adjudicative, or nonadjudicative processes?

## 4. Med-Arb Opportunities and Challenges in Oil and Gas ISDS

The most distinctive opportunities and challenges regarding applying Med-Arb mechanism from the perspectives of both investors and host states are evaluated in order to provide a clear picture in which parties can manage the challenges and decide about an efficient dispute settlement mechanism for their investment disputes.

### 4.1. Med-Arb Opportunities in Oil and Gas ISDS

As defined earlier in this article, Med-Arb in one of its common forms, refers to a situation in which a neutral

<sup>15</sup> Hybrid dispute settlement mechanisms are different from multi-tiered dispute settlement clauses/agreements which comprise different steps that begin with various alternative dispute resolution (ADR) techniques, and arbitration is designed as the last step if the dispute cannot be resolved by preliminary ADR efforts (Kayali, 2010). Contrary to hybrid dispute settlement mechanisms, in multi-tiered dispute settlement techniques, the steps are different and distinct.

<sup>16</sup> For instance, American Arbitration Association (AAA) Commercial Arbitration Rules provide Arb-Med-Arb services, and Singapore International Arbitration Center offers concurrent mediation-arbitration. Also, it is worth noting that in civilian system jurisdictions such as China, Germany, Switzerland, and Iran, it is predicted in their domestic arbitration rules that arbitrators may facilitate the settlement between the parties before the arbitration hearing.

<sup>17</sup> In Med-Arb, If the parties reach settlement during the mediation stage, they may appoint an arbitrator to record

their “settlement agreement” as a “consent arbitral award.” However, it should be emphasized that while some national jurisdictions such as China allow that the settlement agreements in this sense be considered as consent arbitral award, in the context of “international” commercial arbitration, this issue may give rise to enforcement challenges. It is inferred from Article 1 of the 1958 New York Convention, that settlement agreements which have been achieved prior to the commencement of arbitration are not protected under the New York Convention (Davydenko, 2015). Therefore, it appears that until the United Nations Convention on International Settlement Agreements Resulting from Mediation (the Singapore Convention on Mediation) or UNCITRAL Model Law on International Commercial Mediation accepts this type of agreement universally, the awards issued after the mediation phase based on the parties’ agreement and when the arbitration process has not yet started may be challenged at international level (CHUA, 2018).





(mediator) assists parties to reach a solution for their disputes, and if this process fails, he/she acts as an arbitrator, and the process is transformed to arbitration followed by rendering a binding decision accordingly. Without any doubt, it is more favorable for the parties that they voluntarily agree on a proper solution in a peaceful and nonadversarial process such as mediation. Frequently, settlement agreements reflect both parties' benefits and are thus more favorable than the decisions made by third parties such as arbitrators or judges. More importantly, Med-Arb provides disputants with a unique advantage of control and flexibility in the process. In other words, parties are entitled and assured that if the mediation phase becomes inefficient, they can switch to a binding process of arbitration with less costs and time being spent on appointing arbitrator or other challenges at any stage of the mediation. Having control and flexibility in the process may not be considered so important. However, when assessing international complex disputes particularly in the energy sector, this feature becomes more noticeable (T.W.Walde, *Efficient Management of Transnational Disputes: Case Study of a Successful Interconnector Dispute Resolution*, 2006). When the disputes being referred to arbitration with its own sophisticated and specific culture, the parties have no control on the process and management of the dispute settlement process anymore. While it is probable that both host states and oil and gas investors reach a settlement during the mediation phase, it should be emphasized that an efficient mediation aims not only at ending disputes, but also at creating additional values by restructuring the relationship, so it becomes as profitable for both parties as possible—a nonzero sum objective (T.W.Walde, *Efficient Management of Transnational Disputes: Case Study of a Successful Interconnector Dispute Resolution*, 2006).

Another advantage of Med-Arb mechanism refers to reducing costs in this process. The costs and duration of oil and gas investment arbitration process has been seriously criticized, which undermines the efficiency of the investment arbitration system (UNCTAD, *Investor-State Disputes: Prevention and Alternatives to Arbitration*, 2011). Therefore, Med-Arb can be regarded as an alternative offering more flexible and efficient, albeit less costly, advantages to the disputants. Even if

mediation fails partially or totally at the first stage of the Med-Arb process, it is worth noting that the neutral, who previously acted as the mediator and currently appears as the arbitrator, has a better understanding of the disputes, and this fact, per se, facilitates the arbitration process in terms of reviewing evidence, sophisticated documents of the parties, and so on. In addition, the disputes have become narrower in this case, which makes the arbitration process more efficient and rapider. (Pappas, 2015).

It should be kept in mind that by adopting adversarial dispute settlement mechanisms, the continuation of commercial/investment relationship will be at risk. Oil and gas investment projects are based on long-term contracts, very costly detailed due-diligence studies, and the huge time and financial investments of both parties. By adopting Med-Arb, since mediation is applied at the first stage before the initiation of adversarial arbitration procedure, disputants have the opportunity of preserving and even enhancing their relationships (CHUA, 2018). Since oil and gas investors (IOCs) require a stable investment and long-term contracts so as to be able to secure new reserves, increase their competitiveness capability and reputation, and recoup their investments and other concerns, it is of vital importance that they plan to choose proper dispute settlement systems (A.Xenofontos, 2018). On the other hand, oil and gas producing countries, among which developing countries play a significant role in the world oil and gas production<sup>18</sup>, seek for long-lasting investment projects to realize their development goals. Therefore, from both sides, it is vitally important to design proper dispute settlement mechanisms which offer flexibility, finality, and efficient features simultaneously.

## 4.2. Med-arb Challenges in Oil and Gas ISDS

One of the most evident criticisms of Med-Arb mechanism refers to the impartiality, confidentiality, and enforcement issues<sup>19</sup>. One may argue that functions of the mediator and arbitrator are so distinct that it should not be allowed that the same neutral acts in both capacities. For instance, if mediation fails and the neutral will act as the arbitrator, it may be argued that

<sup>18</sup> According to current estimates, 79.4 % of the world's proven oil reserves are located in Organization of the Petroleum Exporting Countries (OPEC) member countries, with the bulk of OPEC oil reserves in the Middle East, amounting to 64.5% of the OPEC total. See:

[https://www.opec.org/opec\\_web/en/data\\_graphs/330.htm](https://www.opec.org/opec_web/en/data_graphs/330.htm), last visited, August, 10, 2019.

<sup>19</sup> For review of comprehensive opportunities and challenges of applying Med-Arb, see: (Javadpour, Oloumiyazdi, & Ebrahimi, 2019)

confidential information he/she learned in the caucus<sup>20</sup> between the mediator and parties may affect his/her impartiality in the arbitration phase which requires rendering a binding decision. However, in the absence of clear applicable rules in this context, it should be noted that if the parties agree that the mentioned procedure should be applicable, the party autonomy principle should be considered, and their choice shall be respected in light of party autonomy principle. This approach and respecting the clear agreement of the parties lead to the consequence of “waiving challenging the arbitrator” based on violation of impartiality. This approach has been approved by UNCITRAL Model Law in International Commercial Conciliation under Article 12<sup>21</sup>, in which the agreement of the parties on conciliator acting as the arbitrator is respected. Also, it should be mentioned that in some jurisdictions such as Hong Kong and Singapore, it is predicted in the related rules that the same neutral shall disclose the learned confidential information if mediation fails, and the mediator changes his/her capacity to an arbitrator accordingly (CHUA, 2018).

Concerns regarding the enforcement of mediation agreements in international contexts may also affect the efficiency of Med-Arb. However, it should be considered that the concern for the enforcement of international agreements resulting from mediation is addressed in the United Nations Convention on International Settlement Agreements Resulting from Mediation and is attaining the good attention of the international community with 51 state members having joined this convention so far.

Another managerial challenge in relation to adopting Med-Arb mechanism in oil and gas investor-state disputes refers to decision-making problems in host countries, particularly developing ones. Recourse to settlement and mediation procedure require having enough authorities within governments, which is not achieved easily sometimes due to the involvement of many entities and organizations. Moreover, from both sides, especially host states, engaging into the settlement process (herein the mediation phase) may be considered to be “compromise of national interests” and may have adverse social, political effects on the governments. It is

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<sup>20</sup> Separate confidential meetings between mediator and parties referred as caucuses in the dispute resolution terminology. See: <https://iccwbo.org/content/uploads/sites/3/2017/07/icc-2017-international-commercial-mediation-competition-rules.pdf>. Last visited: 9/22/2019.

<sup>21</sup> Article 12 of the UNCITRAL Model Law in International Commercial Conciliation (2002) states that

more favorable for the states to attribute the responsibility of the achieved results to a binding decision of the third party (i.e. the arbitration award) and preserving their own reputation in public opinion (UNCTAD, *Investor-State Disputes: Prevention and Alternatives to Arbitration*, 2011). Tackling this issue requires comprehensive knowledge and studying costs and benefits of various options and current experiences in the area of investor-state dispute settlement.

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## 5. Conclusions

Selecting and proposing an efficient dispute settlement mechanism which serves the concerns of both oil and gas investors and host states in a win-win perspective have a vital importance in today’s international investment industry from economic, social, reputational, and development aspects. Investment arbitration, which has largely evolved in the area of international investment law, is not currently considered as efficient as it should be. Consequently, other nonjudicial and hybrid mechanisms, which combine both nonjudicial and judicial advantages, are nowadays emerging in this field. Med-Arb is one of the evolving methods to not only settle international commercial disputes but also resolve the oil and gas investment disputes. Hence, by using Med-Arb mechanism, oil and gas investors and host states prefer to choose an efficient dispute settlement mechanism for their highly sophisticated investment disputes such as expropriation, nationalization, oil and gas price disputes, etc. arising from their long-term contracts in this industry. The advantage of applying Med-Arb mechanism is that both oil and gas investors and host states preserve their confidentiality, save their credit and reputation, reduce their costs, and protect the investment relationship in the process of dispute settlement.

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unless otherwise agreed by the parties, the conciliator shall not act as an arbitrator in respect of a dispute that was or is the subject of the conciliation proceedings or in respect of another dispute that has arisen from the same contract or legal relationship or any related contract or legal relationship.



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