

**The Remedies Stage of the Investment Treaty
Arbitration Process: A Public Interest
Perspective**

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Statement of Originality

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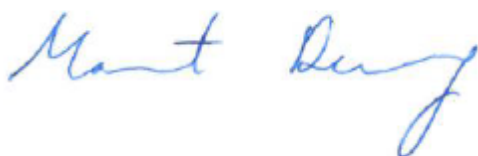
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Abstract

As the investment treaty arbitration regime matures, consensus is emerging as to the need for public interest considerations to be taken into account in resolving disputes under international investment agreements (IIAs). However, the question of how such considerations should be reflected remains contentious. This thesis proposes that the remedies stage of the process can, and should, play a role in taking account of public interest considerations and so in easing the tension between host state regulatory sovereignty and investment protection that lies at the heart of the investment treaty regime.

Thus, this thesis argues that, while, on the one hand, there is a need to introduce an element of reciprocity into the investment treaty arbitration process in order to ensure continuing state co-operation and to reflect the broader underlying purposes of IIAs, on the other, the primary object of the system remains the protection of foreign investors. These competing imperatives can lead to difficulties in taking account of public interest considerations at the merits stage of the arbitration process. Therefore, in order to reconcile these competing imperatives and to achieve an optimal balance between host state regulatory sovereignty and investment protection, this thesis proposes that public interest considerations should be recognised at the remedies stage where such considerations cannot be taken into account either sufficiently or at all at the merits stage and identifies a number of situations in which this approach would be appropriate. Potential doctrinal bases for implementation of this approach are also examined and the conclusion reached that, given the significant degree of discretion afforded to tribunals in applying the full reparation principle and the role that equity can permissibly play in quantifying damages, this approach can, save in the case of lawful expropriations, be implemented within the parameters of existing legal principles.

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Table of Contents

Statement of Originality	ii
Abstract.....	iii
Acknowledgments.....	iv
Abbreviations.....	viii
Chapter 1: Introduction and Thesis Overview.....	1
1.1 Introduction	1
1.2 Literature Review	13
1.3 Methodology and limitations	23
1.4 Definitions and key concepts	24
(a) International Investment Agreements (IIAs)	24
(b) The investment treaty arbitration system	28
(c) The substantive rights contained in IIAs.....	32
(d) The remedies stage.....	33
1.5 Conclusion.....	34
Chapter 2: Why should investment treaty arbitration tribunals take account of public interest considerations?.....	35
2.1 Introduction	35
2.2 The nature of international investment law and arbitration	35
2.3 The open ended nature of IIA rights.....	44
(a) The expropriation clause	45
(b) The FET standard	50
(c) The guarantee of full protection and security.....	56
(d) The non-discrimination standards	58
(e) Umbrella clauses	59
(f) Freedom of Transfer Guarantee	65
2.4 Reasons for taking account of public interest considerations.....	66

2.5	<i>Conclusion</i>	73
Chapter 3: The merits stage and public interest considerations: an uneasy balance.....75		
3.1	<i>Introduction</i>	75
3.2	<i>Proportionality analysis</i>	76
3.3	<i>Reliance on the state’s non-investment related international obligations</i>	90
3.4	<i>The defence of necessity and NPM clauses</i>	96
3.5	<i>Analysis of the effectiveness of methods of taking account of public interest considerations at the merits stage</i>	105
Chapter 4: The remedies stage as a platform for public interest considerations: an assessment.....108		
4.1	<i>An overview of the remedies stage</i>	108
	(a) <i>The full reparation principle</i>	109
	(b) <i>The IIA standard of compensation</i>	112
	(c) <i>Bases of valuation and customary valuation methods</i>	115
	(d) <i>Analysis of the approach taken by investment treaty arbitration tribunals to date at the remedies stage</i>	121
4.2	<i>An assessment of the remedies stage as a platform for public interest considerations</i>	126
	(a) <i>Normative arguments in favour of taking account of public interest considerations at the remedies stage</i>	130
4.3	<i>The ‘special case’ of lawful expropriations</i>	145
4.4	<i>Conclusion</i>	147
Chapter 5: From policy to implementation: taking account of public interest considerations at the remedies stage.....149		
5.1	<i>The doctrinal basis for taking account of public interest considerations under existing IIAs: the role of equity</i>	150
	(a) <i>The meaning of equity</i>	151
	(b) <i>The role of equity in international law</i>	157

(c)	<i>Equity in the international law of remedies</i>	162
(d)	<i>The influence of equity in international investment law</i>	166
(e)	<i>Equity and the full reparation principle</i>	170
(f)	<i>The ‘special case’ of lawful expropriations</i>	179
5.2	<i>New or renegotiated IIAs</i>	181
(a)	<i>Alternatives to the full reparation principle</i>	181
(b)	<i>Alternatives to the fair market value standard</i>	187
5.3	<i>Relationship between the remedies stage and reforms affecting earlier stages of the arbitration process</i>	192
5.4	<i>Conclusion</i>	197
	Chapter 6: Conclusions	199
	Bibliography	208
	<i>Books</i>	208
	<i>Journal Articles</i>	212
	<i>Contributions to edited books</i>	231
	<i>Publications by international organisations</i>	241
	<i>Working Papers</i>	245
	<i>Other Materials</i>	247
	<i>Cases and Arbitration Awards</i>	248
(a)	<i>ICJ/PCIJ Judgments</i>	248
(b)	<i>Investor-State Arbitration Awards</i>	249
(c)	<i>Other International Cases and Arbitration Awards</i>	255
(d)	<i>Domestic Case Law</i>	256
	<i>Treaties</i>	256

Abbreviations

ASEAN	Association of Southeast Asian Nations
BIT	Bilateral Investment Treaty
CCF	Capitalised Cash Flow
COMESA	Common Market for Eastern and Southern Africa
DCF	Discounted Cash Flow
Draft ILC Articles	Draft Articles on Responsibility of States for Internationally Wrongful Acts
EBIDTA	Earnings Before Interest, Taxes, Depreciation and Amortisation
FET	Fair and Equitable Treatment
FTA	Free Trade Agreement
ICC	International Chamber of Commerce
ICESCR	International Covenant on Economic, Social and Cultural Rights
ICJ	International Court of Justice
IIA	International Investment Agreement
IISD	International Institute for Sustainable Development
ICSID	International Centre for the Settlement of Investment Disputes
ICSID Convention	Convention on the Settlement of Investment Disputes between States and Nationals of Other States
IPFSD	Investment Policy Framework for Sustainable Development
MFN	Most Favoured Nation
NAFTA	North American Free Trade Agreement between Canada, The United States and Mexico
NPM	Non Precluded Measures
NIEO	New International Economic Order
OECD	Organisation for Economic Co-operation and Development
PCIJ	Permanent Court of International Justice
SADC	South African Development Community
UNCITRAL	United Nations Commission on International Trade Law
UNCTAD	United Nations Conference on Trade and Development
UNESCO	United Nations Educational, Scientific and Cultural Organisation
WTO	World Trade Organisation

Chapter 1: Introduction and Thesis Overview

1.1 Introduction

The allegorical personification of justice as a blindfolded woman holding a set of scales encapsulates the notion that, in law, as in life, balance is everything. In other words, the balancing of interests is an inherent feature of the law and achieving a balance between the competing interests at issue in a particular case is a central function of all adjudicative bodies. In particular, disputes between an individual and a state tend to throw into sharp relief the question of how an appropriate balance between individual interests and collective or state interests may be achieved. The field of investment treaty arbitration is no exception to this rule. Indeed, reconciliation of these competing interests has been described as the ‘core task’ of investment treaty arbitration.¹ This assertion is underpinned by the fact that international investment agreements (IIAs) afford private entities, both individual and corporate, the ability to bring claims against a state at an international level (generally without having to exhaust local remedies) and by the fact that such claims may challenge the regulatory acts of that host state (and thus potentially compromise its regulatory sovereignty). Of course, one of the primary functions of IIAs is to regulate the manner in which a state exercises its sovereign rights and the act of agreeing to such controls is, in itself, an ‘attribute of state sovereignty’.² Thus, as Álvarez memorably puts it, ‘[IIAs] are efforts by states to bind themselves to the mast to avoid the tempting sirens calling for breaches of investment contracts or nationalizations without compensation’.³ However, the fact that a state, by entering into IIAs, voluntarily cedes part of its regulatory sovereignty does not mean that host state sovereignty in the sense of the host state’s freedom to regulate its internal affairs is irrelevant to the application of IIAs. To the contrary, it is becoming increasingly widely acknowledged that, in resolving IIA disputes, a balance must be struck between investor interests and public interest

¹Campbell McLachlan, ‘Investment Treaty Arbitration: The Legal Framework’ in Albert Jan van den Berg (ed), *50 Years of the New York Convention: ICCA International Arbitration Conference* (Kluwer 2009) 101.

²*SS Wimbledon (United Kingdom v Japan)*, 1923 PCIJ (ser. A) No 1 (Aug 17) 25.

³José Álvarez, ‘The Return of the State’ (2011) 20 *Minn J Intl L* 223, 225.

considerations. However, the question of how, and at what stage of the arbitral process, public interest considerations should be reflected remains the subject of debate. It is upon this question that this thesis will focus.

Thus, the central argument of this thesis is that the remedies stage of the investment treaty arbitration process can, and should, play a role in taking account of public interest considerations and so in easing the tension between host state regulatory sovereignty and investment protection that lies at the heart of the investment treaty regime. While, in recent years, the remedies stage of the investment treaty arbitration process has received increasing attention in the academic literature and while the possibility of a balancing of public and private interests occurring as part of the damages quantification process has been alluded to, the question of whether, and in what circumstances, the remedies stage constitutes an appropriate platform for public interest considerations has not been comprehensively examined. In particular, the possible inter-relationship between the merits stage and the remedies stage in terms of taking account of such considerations has not been explored nor have the primary methods of taking account of public interest considerations at the merits stage been evaluated together with a view to determining the efficacy and appropriateness of balancing investor and public interests at the merits stage. Finally, the question of whether any doctrinal basis exists under the existing investment treaty regime for taking account of public interest considerations at the remedies stage of the arbitration process has not been explored in the academic literature nor has much attention been focussed on possible remedies-related provisions that could be included in new or renegotiated IIAs. This thesis aims to address these questions and, having examined the need for public interest considerations to be taken into account in investment treaty arbitration generally and assessed the efficacy of the various methods of taking account of such considerations at the merits stage, will argue that, in order to achieve an optimal balance between host state regulatory sovereignty and investment protection, the merits and remedies stages of the arbitral process should play complementary roles in taking account of public interest considerations.

However, before considering the bases for this proposition, the question of what is meant by the term ‘public interest considerations’ must be further explored. Although central to both politics and the law, defining what is meant by the term ‘public interest’ is notoriously difficult and gives rise to a range of questions

including the question of how individual expressions of interest can be translated into some form of common, public or general good and the question of how the boundaries of the ‘public’ should be delimited.⁴ This uncertainty has led to the concept of public interest being invoked in manifold (and sometimes contradictory) ways.⁵ In particular, in the context of international investment law, while the granting of rights to foreign investors under IIAs can be considered to be in the public interest (on the assumption that protecting foreign investors will lead to further foreign investment and economic development),⁶ on the other hand, it is frequently argued that the rights conferred on investors by IIAs should be curtailed so as to permit host state regulation in the public interest. The definition of the term ‘public interest considerations’ in this thesis cleaves towards the latter interpretation, while acknowledging the malleable nature of the concept of public interest (and the inherent tensions that arise in defining that concept in the sphere of international investment law).

Thus, the term ‘public interest considerations’ is used in this thesis to connote any legitimate regulatory interests that a state has a right or duty to pursue or to promote under either domestic (constitutional) law or international law.⁷ Regulation, in this context, is used to describe the deliberate influence of the state to control or influence industrial or social behaviour and, in particular, the establishment by the state of operational conditions for foreign investment in the interest of the public good.⁸ Regulation includes both the general legal and administrative framework of host countries as well as sector or industry-specific rules. It also entails effective implementation of rules, including the enforcement of rights.⁹ The interests which underlie host state regulation may pertain not only to domestic concerns but

⁴For an overview see Stephen M King, Bradley S Chilton and Gary E Roberts, ‘Reflections on Defining the Public Interest’ (2010) 41 *Administration & Society* 954.

⁵See generally Paul de Jersey, ‘Public Interest and Public Policy: Unruly Horses Alike?’ (2003) 6 *Legal Ethics* 16.

⁶See for example Nigel Blackaby, ‘Public Interest and Investment Treaty Arbitration’ in Albert Jan van den Berg (ed), *International Commercial Arbitration: Important Contemporary Questions: ICCA Congress Series 2002* (Kluwer 2003) 355.

⁷For the avoidance of doubt, the term ‘public interest considerations’ as used in this thesis does not encompass the collective interests of the claimant investor’s home state. Although the possibility that a particular investment dispute may have an impact on the interests of the investor’s home state cannot be excluded, generally where a dispute has arisen the interests of the home state are, to the extent that they are considered at all, seen to be best served by the maximisation of the private interests or expectations of the aggrieved investor in protecting its investment.

⁸Robert Baldwin and Martin Cave, *Understanding Regulation: Theory, Strategy and Practice* (OUP 1999) 1-2.

⁹UNCTAD, *Investment Policy Framework for Sustainable Development* (UNCTAD 2012) 12-13.

frequently also extend to the international level. Thus, the right of a state to regulate becomes a duty to protect where regulation becomes necessary in order to uphold a state's non-investment related treaty obligations such as its obligations under human rights or environmental treaties. For example, investments in natural resources may have severe environmental consequences and conflict with norms set out in international environmental treaties or in international human rights treaties, if the host state's population is negatively affected by the investment. The right to regulate is an essential aspect of state sovereignty while the duty to protect its population or the environment from harm arises out of both international and domestic legal instruments.¹⁰ The term 'legitimate regulatory interests' is therefore used to refer to a broad range of aims that regulation may pursue that would appear congruent with the welfare of society and the term 'taking into account public interest considerations' refers to the consideration of such legitimate regulatory interests in circumstances where the measures taken by the host state in pursuance of such interests are the subject of challenge under an IIA.

Having defined what is meant by the term 'public interest considerations', the question of whether, as a threshold matter, such considerations should be taken into account in investment treaty arbitration at all (whether at the jurisdiction, merits or remedies stage of the arbitral process) must be addressed. This will be the topic of the second chapter of this thesis, which will argue that public interest considerations should be taken into account when resolving disputes under current IIAs, regardless of whether the international investment treaty regime is viewed through a public law or private law lens. Thus, Chapter 2 will demonstrate that, although the two questions have, at times, been conflated, the question of whether public interest considerations should be taken into account in investment treaty arbitration can be separated from the question of whether international investment law constitutes a form of public law or, alternatively, whether each IIA constitutes a 'private', quasi-contractual bargain between the contracting states. Accordingly, the second chapter of this thesis will argue that investment treaty arbitration tribunals can permissibly take into account public interest considerations within the parameters of the principal substantive rights typically contained in IIAs as such rights are open-

¹⁰Suzanne A Spears, 'The quest for policy space in a new generation of international investment agreements' (2010) 13 J Intl Economic L 1037, 1038.

ended in nature, lack a well-defined normative basis and therefore confer an unusually broad margin of interpretative discretion on arbitrators.

Having demonstrated that investment treaty arbitration tribunals have the ability to take account of public interest considerations, Chapter 2 will then go onto argue that arbitrators should avail of this ability and interpret IIA rights in a manner sensitive to public interest considerations. It will be argued that this should occur as many IIA disputes relate to delicate policy issues which go to the ability of the host state to legislate in the public interest and the text of IIAs generally does not clarify the extent to which the host state's regulatory sovereignty has been ceded. In such circumstances, according the broadest possible scope to IIA rights could preclude elected authorities and administrative agencies from being able to alter policy in the public interest. Furthermore, given that IIAs may not necessarily reflect the democratic choices of states and that the longevity of IIAs may lead to the choices of one elected government binding a future government in a manner that fundamentally restricts its policy options, it will be argued that the need for public interest considerations to be taken into account by investment treaty arbitration tribunals is intensified. Finally (and perhaps most importantly), it will be argued that IIAs should not be interpreted in a manner that consistently disregards public interest considerations as this would likely lead to both traditional capital importing states and traditional capital exporting states exiting the investment treaty arbitration regime. Thus, Chapter 2 concludes by noting that the open-ended nature of IIA rights is such that the interpretation of the IIA text by each individual tribunal is crucial to maintaining a balance between investor protection and host state regulatory sovereignty and that this is a balance that tribunals should strive to achieve.

Having argued in Chapter 2 that public interest considerations should be taken into account by investment treaty arbitration tribunals, the third chapter of this thesis will examine the extent to which public interest considerations have been taken into account at the merits stage of investment treaty arbitrations to date and will analyse the efficacy and appropriateness of the methods used. Three, inter-related, methods of introducing public interest considerations will be analysed for this purpose: first, the balancing of public interest considerations and investor interests in determining the content of substantive treaty obligations through the use of proportionality analysis; second, the interpretation of IIA rights in a manner consistent with a host

state's non-investment related international obligations and, third, reliance on the customary international law defence of necessity and/or on a non-precluded measures (NPM) clause. It will be argued that each of these methods does not constitute a wholly satisfactory means of taking account of public interest considerations.

Turning first to proportionality analysis, it will be argued that, although proportionality analysis potentially offers a methodologically robust structure for balancing competing interests, it is subject to certain limitations both generally and also in the specific context of investment treaty arbitration. First, proportionality analysis is not suitable for addressing conflicts between rules or rule-like provisions. Secondly, the manner in which proportionality testing has been applied in investment treaty arbitration to date has lacked analytical and procedural rigour. There has also been little consistency as to the standard of review applied by investment treaty arbitration tribunals (which is equally important to the method of review employed). However, while investment treaty arbitration tribunals could over time potentially introduce further rigour into their application of proportionality analysis and develop a more coherent standard of review, it will be argued that a more fundamental issue is the question of why the majority of tribunals have eschewed proportionality analysis to date. It will be suggested that tribunals' hesitancy in this regard may stem partly from the conceptualisation of certain IIA disputes by claimant investors or by tribunals themselves as involving rules rather than principles. A second reason which may underlie this hesitancy is that arbitrators may harbour doubts as to whether proportionality analysis should be applied in the field of investment treaty arbitration at all, given the hybrid nature of the investment treaty arbitration system and its focus on protecting the interests of a particular group of individuals. Finally and on a related note, the focus of investment treaty arbitration on the interests of foreign investors makes it difficult to argue that public interest considerations should be accorded equal weight to investor interests in the balancing exercise and, as alluded to above, leads to uncertainty as to how the 'public interest' in protecting foreign investors' rights should be reconciled with public interest considerations.

Chapter 3 will also examine the issues that arise in introducing a host state's non-investment related treaty obligations into an IIA dispute through the 'gateway' of Article 31(3) (c) of the Vienna Convention on the Law of Treaties. In particular, as

is the case with proportionality analysis, this interpretative technique cannot be used to resolve conflicts between rule-like provisions. In addition, the function and scope of application of Article 31(3)(c) rests entirely on the interpretation of its component parts (and, in particular, the terms ‘relevant rules’ and ‘applicable to the relations between the parties’). Furthermore, even assuming that these terms are interpreted in a manner that permits the obligations of the host state under, for example, a particular human rights treaty to be considered for interpretative purposes, the weight to be attributed to those obligations in determining whether an IIA breach has occurred is open to question. This gives rise to similar issues as those faced by investment treaty arbitration tribunals in attempting to balance investor interests and public interest considerations through proportionality analysis.

Finally, Chapter 3 will, by reference to a number of cases arising out of the Argentine economic crisis and sovereign default of 2000 to 2002, illustrate the difficulties associated with relying on the customary international law defence of necessity or on a NPM clause when the host state has acted to protect its essential interests in times of crisis. While the defence of necessity could conceivably be applied by future investment treaty arbitration tribunals in a manner which accords greater deference to the host state than has been accorded by some investment treaty arbitration tribunals to date, it will be argued that the defence will always have to be narrowly drawn. Similarly, given that NPM clauses are only included in a minority of IIAs and that they vary quite considerably in scope, Chapter 3 will argue that NPM clauses constitute a ‘patchy’ means of protecting states’ right to act to protect essential national interests in times of crisis.

Chapter 3 concludes by noting that the common thread underlying all of the methods used to take account of public interest considerations at the merits stage is that application of such methods can ultimately lead only to a black-or-white decision as to liability, which requires one set of interests to be prioritised in order to come to that determination and so may lead to either investor interests or host state interests not being optimised. This gives rise to the question of whether this ‘all or nothing’ approach to liability is appropriate or, alternatively, whether the remedies stage can play a role in taking account of public interest considerations, which is considered in Chapter 4.

Thus, having examined the legal standards applicable in quantifying damages for unlawful acts and compensation for lawful expropriations as well as the valuation methods customarily applied in quantifying such damages or compensation, Chapter 4 will proceed to argue that, although tribunals necessarily exercise a considerable degree of discretion in quantifying damages (and so conceivably may take account of public interest considerations in a clandestine manner), investment treaty arbitration tribunals have, to date, generally not explicitly referred to public interest considerations at the remedies stage or purported to adjust the compensation or damages payable by respondent host states on the basis of such considerations.

While the consideration of public interests in the formulation of remedies is a feature of other legal regimes (notably state liability law), Chapter 4 will argue that the approach taken to remedies under another legal regime cannot simply be transposed into the sphere of investment treaty arbitration and that justification reflecting the distinctive features of the investment treaty arbitration system is necessary to support the proposition that public interest considerations should be taken into account in quantifying the damages payable under IIAs. Thus, it will be argued that the primary justification for such a proposition is the need to introduce an element of reciprocity into the investment treaty arbitration process in order to ensure continuing state participation in the investment treaty system and to reflect the broader underlying purposes of IIAs. This is the case as the rights conferred on investors by IIAs are conferred on that particular societal grouping for broader public interest-related purposes (namely the promotion of investment and of further economic co-operation with the ultimate aim of promoting development in the state) rather than because investors have an inherent entitlement to such protection. However, given that the primary object of the system nonetheless remains the protection of foreign investors, a position that public interest considerations should inevitably take precedence over investor interests is untenable. Therefore, in order to reconcile the ‘asymmetric’ nature of IIAs and the need to introduce an element of reciprocity into the investment treaty arbitration process, a nuanced approach which takes account of both public interest considerations and investor interests to the greatest extent possible in each particular case is necessary. Given the difficulties associated with taking account of public interest considerations at the merits stage and the black-or-white decision as to liability that is required at that stage, it will be

argued that the merits and remedies stages should play complementary roles in this regard and that, in order to ensure that investor rights are not diluted, an approach that assesses the extent to which countervailing interests were considered at the merits stage in determining whether (and the extent to which) such interests need to be considered at the remedies stage is preferable to an approach that allows for countervailing interests considered insufficient to override investor rights at the merits stage to subsequently be considered *de novo* in quantifying damages.

Bearing these guiding principles in mind, Chapter 4 identifies and elaborates upon a number of specific situations in which recognition of public interest considerations at the remedies stage may be appropriate: first, where the impugned host state measure was taken in furtherance of the host state's obligations under a non-investment related treaty or in furtherance of the fundamental rights provisions contained in the host state's highest law; secondly, where the customary international law defence of necessity has been successfully invoked and, finally, in the case of certain breaches of a procedural nature. In each of these situations, there are specific policy reasons militating in favour of taking account of public interest considerations at the remedies stage. However, these specific reasons all centre on a common premise: namely that, in some cases, the fact that the host state acted in pursuance of a *bona fide* public purpose in introducing the measures challenged under an IIA may need to be considered at the remedies stage as this fact cannot be reflected either sufficiently or at all at the merits stage. This premise equally applies in respect of expropriations (and in particular lawful expropriations), notwithstanding the focus of the expropriation clause on the loss caused by governmental conduct rather than on the nature of that conduct. Indeed, it will be argued that the need to acknowledge host state regulatory sovereignty at the remedies stage is enhanced where lawful expropriations are concerned as, currently, the public function performed by the state is effectively disregarded given that the pronouncement that an expropriation is lawful in nature generally has little meaningful effect on the quantum of compensation payable.

Having outlined, in Chapter 4, a number of normative arguments as to why taking account of public interest considerations at the remedies stage is appropriate, the fifth chapter of this thesis will proceed to consider potential doctrinal bases for implementation of such an approach. It will be argued that tribunals are already afforded a significant degree of discretion in quantifying damages and that this

‘normal’ discretion, combined with the flexibility afforded to tribunals by causation principles, may already allow for recognition of certain public interest-related matters in applying the full reparation principle. However, having examined the role of equity in international law generally and in the international law of remedies in particular as well as the role that equity has played in investment treaty arbitration to date, it will be argued that increased reliance on equity could ‘enlighten’ the exercise of arbitral discretion and could reinforce the doctrinal basis for taking account of public interest considerations at the remedies stage.

However, given that investment treaty arbitration tribunals may be reluctant to acknowledge the influence of equity, Chapter 5 will go onto consider a number of possible alternatives to the full reparation principle that could be included in new or renegotiated IIAs. Having evaluated these provisions, it will be argued that, while amending the text of IIAs could potentially provide a more concrete doctrinal basis for reliance by tribunals on equity and/or for taking account of public interest considerations in quantifying the damages payable for unlawful acts, care would have to be taken to ensure that such wording is not overly prescriptive or, conversely, overly amorphous to provide sufficient guidance to arbitrators. Furthermore, it will be argued that a complete disaggregation of the amount of damages payable from the claimant’s loss would not accord with the nature and functions of the investment treaty arbitration system. Accordingly, Chapter 5 argues that treaty negotiators should be cautious in deviating from the current approach whereby IIAs are generally silent as to the approach to be taken to remedying unlawful acts.

Chapter 5 separately evaluates the question of whether the recognition of public interest considerations is possible in quantifying the compensation payable in respect of lawful expropriations, given the different standard of compensation applicable to lawful expropriations. It will be argued that the fair market value standard (which is the predominant valuation standard currently prescribed by IIAs) leaves little room for recognition of public interest considerations or for the application of equity and that, in order for such considerations to be meaningfully reflected, deviation from the fair market value standard is required. However, having evaluated a number of possible alternative provisions that could be included in new or renegotiated IIAs, it will be argued that, while given that public interest considerations cannot currently be taken into account within the parameters of the

fair market value standard, the need to consider alternatives to the fair market value standard is arguably greater than in respect of the full reparation principle, negotiators and drafters should nonetheless be cautious in completely disaggregating the compensation payable for lawful expropriations from the market value paradigm.

Finally, Chapter 5 examines how reforms that have been proposed as means of facilitating the consideration of certain public interests in investment treaty arbitration and which primarily affect the earlier stages of the arbitral process may relate to the taking into account public interest considerations at the remedies stage. It will be argued that, although it is impossible to predict how such provisions may affect the application or interpretation of substantive investor rights in future, there are grounds for suggesting that such provisions will not obviate the need for taking account of public interest considerations at the remedies stage.

Chapter 6 synthesises the conclusions reached in the thesis as a whole and concludes by noting that, while the proposals put forward in this thesis cannot, and do not purport to, constitute a complete solution to the problem of how to ease the tension between investment protection and host state regulatory sovereignty in investment treaty arbitration, they constitute a part of the answer.

Overall therefore, it is hoped that this thesis will make a contribution to the corpus of literature relating to the balancing of public and private interests in investment treaty arbitration and, more importantly, will cause academics, practitioners and arbitrators to examine (or re-examine) the possibilities of the remedies stage from a public interest perspective. Although, in one sense, this may seem an ambitious aim, the proposals contained in this thesis are avowedly ‘system-internal’ in nature (i.e. it is assumed that the procedural framework for investment treaty arbitration and the focus of IIAs on investor rights and freedom of investment will remain unchanged for the foreseeable future). Some commentators have argued that proposals of this nature, by assuming the survival of the investment treaty regime as it is currently configured are insufficient and that a complete overhaul or abolition of the current system is necessary.¹¹ In particular, commentators have criticised the effect of international investment law on host state regulatory sovereignty, particularly in the case of developing countries, and have claimed that many

¹¹See for example Howard Mann, ‘Reconceptualising International Investment: Its Role in Sustainable Development’ (2013) 17 *Lewis & Clark L Rev* 521.

developing countries enter into IIAs with more developed countries without knowledge of the implications and not wholly voluntarily due to inequality of bargaining power.¹² Furthermore, it has been argued that, even if foreign direct investment is encouraged by IIAs (a proposition which is hotly disputed), positive social and environmental results do not automatically result as foreign direct investment needs to be managed by the host state in order to encourage a developed domestic economy.¹³ Thus, it is claimed that the benefits flowing from IIAs are questionable and that IIAs may not in fact be necessary to resolve the problems of ‘obsolescing bargain’ and ‘credible commitment’ since investor-state contracts can perform such functions equally well (if not better).¹⁴ Finally, the unequal allocation of rights and obligations in IIAs has also been emphasised: foreign investors are granted much greater rights against host states than those available under customary international law while little to no obligations are placed on them *vis-à-vis* host states and host state citizens.¹⁵

While not detracting from the value of these arguments as compelling critiques of neoliberalism, it is submitted that the implementation of focussed, incremental, improvements within the parameters of the investment treaty arbitration system, which take account of the specific features of the system, is also of value.¹⁶ In this regard, the following comments of the late Thomas Wälde are particularly apt:

¹²Andrew T Guzman, ‘Why LDCs Sign Treaties that Hurt Them: Explaining the Popularity of Bilateral Investment Treaties’ (1997-1998) 38 *Va J Intl L* 640; Kevin P Gallagher and Lyuba Zarsky, ‘No Miracle Drug: Foreign Direct Investment and Sustainable Development’ in Lyuba Zarsky (ed), *International Investment for Sustainable Development: Balancing Rights and Rewards* (Earthscan Publishing 2005) 13-45; Surya P Subedi, *International Investment Law: Reconciling Policy and Principle* (Hart Publishing 2008) 85; M Sornarajah, *The International Law of Foreign Investment* (3rd edn, Cambridge University Press 2010) 177.

¹³For an overview of the literature on this subject see J Anthony VanDuzer, Penelope Simons and Graham Mayeda, *Integrating Sustainable Development into International Investment Agreements: A Guide for Developing Country Negotiators* (Commonwealth Secretariat 2013) 514-23.

¹⁴Public Statement on the International Investment Regime 31 August 2010 <<http://www.osgoode.yorku.ca/public-statement-international-investment-regime-31-august-2010>> accessed 19 March 2015. See also Jason Webb Jackee, ‘Do We Really Need BITs? Toward a Return to Contract in International Investment Law’ (2008) 3 *Asian Journal of WTO and Health Law* 121.

¹⁵Todd Weiler, ‘Balancing Human Rights and Investor Protection: A New Approach for a Different Legal Order’ (2004) 27 *BC Intl & Comp L Rev* 429; Adefolake Adeyeye, ‘Corporate Responsibility in International Law: Which Way to Go?’ (2007) 11 *Singapore Y B Intl L* 141, 143; Gus Van Harten, ‘Five Justifications for Investment Treaties: A Critical Discussion’ (2010) 2 *Trade, Law & Development* 1; Patrick Dumberry and Gabrielle Dumas-Aubin, ‘When and How Allegations of Human Rights Violations can be Raised in Investor-State Arbitration’ (2012) 13 *J World Investment & Trade* 349.

¹⁶Thomas Wälde, ‘Investment Arbitration and Sustainable Development: good intentions - or effective results?’ (2006) 6 *International Environmental Agreements: Politics, Law and Economics* 459, 460.

excessive focus only on moral sentiments – a kind of autistic moralism – may even be counterproductive. We need to understand how things work before we can try to change the world to make it somewhat better. The great risk is that the emotive animosity against investment arbitration leads to the opposite of what was...intended.¹⁷

Thus, although investment treaty arbitration may not be the perfect forum for resolving investor-state disputes and although the dominant paradigm underlying the regime should arguably be shifted to reflect sustainable development concerns, it is submitted that what one commentator dismissively refers to as ‘tinkering at the margins’¹⁸ within the parameters of the existing system is worthwhile if it operates to ease the tension between regulatory sovereignty and investment protection that characterises (and arguably plagues) the regime.¹⁹ This thesis aims to address such tension by examining the point of the arbitral process likely to be of most concern to both claimant investors and respondent host states from a practical perspective and arguably also, due to the fact that it is more comprehensible than the jurisdiction or merits stage, most likely to fuel backlash against the investment treaty arbitration process – the remedies stage.²⁰

Before embarking on this task however, the remainder of this introductory chapter will review the existing academic literature on the subject, outline the thesis methodology and its limitations and, finally, define key terms and concepts to be used throughout the thesis.

1.2 Literature Review

The interaction between host state regulatory sovereignty and investor protection can be approached by focussing either on the potential for the rights conferred on foreign investors by IIAs to be interpreted in a manner that is likely to interfere with host state or public interests or, alternatively, by considering the actual interpretation of IIAs by investment treaty arbitration tribunals to date. In relation to

¹⁷ibid.

¹⁸Howard Mann, ‘Reconceptualising International Investment: Its Role in Sustainable Development’ (2013) 17 Lewis & Clark L Rev 521, 543.

¹⁹Julie A Maupin, ‘Public and Private in International Investment Law: An Integrated Systems Approach’ (2013-2014) 54 Va J Intl L 367, 430.

²⁰Thomas Wälde and Borzu Sabahi, ‘Compensation, Damages and Valuation’ in Peter Muchlinski, Federico Ortino and Christoph Schreuer (eds), *The Oxford Handbook of International Investment Law* (OUP 2008) 1053.

the former issue, there is extensive discussion in the academic literature of the potential for conflict between international investment law and other normative orders due to the broad-ranging nature of the investor rights generally contained in IIAs, particularly in circumstances where investors have challenged legislative or administrative measures that ordinarily would fall within the host state's regulatory sphere or which were introduced in order to implement the host state's obligations under a non-investment related treaty.²¹ A sub-set of this literature explores various mechanisms such as general exceptions clauses which have been included in more recent 'new generation' IIAs and which could be inserted into new or renegotiated IIAs in order to potentially remove some of this indeterminacy and to aid arbitral tribunals in taking into account public interests.²² The potential 'chilling effect' of this indeterminacy on host state regulation has also been emphasised in a portion of the literature.²³ Overall therefore, the literature on the potential for conflict between international investment law and other normative orders is quite comprehensive.

Turning to the issue of the actual interpretation of investor rights by investment treaty arbitration tribunals to date, the methods of review employed by tribunals in order to balance competing interests at the merits stage of the arbitral process have

²¹See for example Thomas Wälde and Abba Kolo, 'Environmental Regulation, Investment Protection and 'Regulatory Taking' in International Law' (2001) 50 ICLQ 811; Rudolf Dolzer, 'The Impact of International Investment Treaties on Domestic Administrative Law' (2006) 38 NYU J Intl L & Pol 953; Gus Van Harten, *Investment Treaty Arbitration and Public Law* (OUP 2007); James D Fry, 'International Human Rights Law in Investment Arbitration: Evidence of International Law's Unity' (2007) 18 Duke J Comp & Intl L 77; Surya P Subedi, *International Investment Law: Reconciling Policy and Principle* (Hart Publishing 2008); Pierre-Marie Dupuy, Ernst-Ulrich Petersmann and Francesco Francioni (eds), *Human Rights in International Investment Law and Arbitration* (OUP 2009); Stephan W Schill, *The Multilateralization of International Investment Law* (Cambridge University Press 2009); Marie-Claire Cordonier Segger, Markus W Gehring and Andrew Newcombe (eds), *Sustainable Development in World Investment Law* (Kluwer 2011).

²²See for example Aaron Cosbey, 'The Road to Hell? Investor Protections in NAFTA's Chapter 11' in Lyuba Zarsky (ed), *International Investment for Sustainable Development: Balancing Rights and Rewards* (Earthscan Publishing 2005); Andrew Newcombe, 'Sustainable Development and Investment Treaty Law' (2007) 8 J World Investment & Trade 357; Suzanne A Spears, 'The quest for policy space in a new generation of international investment agreements' (2010) 13 J Intl Economic L 1037; Andrew Newcombe, 'General Exceptions in International Investment Agreements' in Marie-Claire Cordonier Segger, Markus W Gehring and Andrew Newcombe (eds), *Sustainable Development in World Investment Law* (Kluwer 2011); Marie-Claire Cordonier Segger and Andrew Newcombe, 'An Integrated Agenda for Sustainable Development in International Investment Law' in Marie-Claire Cordonier Segger, Markus W Gehring and Andrew Newcombe (eds), *Sustainable Development in World Investment Law* (Kluwer 2011).

²³See for example Stuart Grass, 'Inordinate Chill: BITs, Non-NAFTA MITs and Host-State Regulatory Freedom - An Indonesian Case Study' (2003) 24 Mich J Intl L 893; Kyla Tienhaara, *The expropriation of environmental governance: protecting foreign investors at the expense of public policy* (Cambridge University Press 2009); Kyla Tienhaara, 'Regulatory Chill and the Threat of Arbitration: A View from Political Science' in Chester Brown and Kate Miles (eds), *Evolution in Investment Treaty Law and Arbitration* (Cambridge University Press 2011).

been analysed at length, the most prominent of such methods being proportionality analysis.²⁴ The problems associated with the current application by tribunals of proportionality analysis have also been explored in the literature²⁵ and the issue of the appropriate standard of review to be applied by tribunals has been considered.²⁶ The related question of whether it is appropriate to take into account the human rights and other non-investment related treaty obligations of the host state in interpreting IIA rights has also been extensively examined in the literature, particularly with regard to the potential use of the technique of systemic integration as embodied in Article 31(3) (c) of the Vienna Convention on the Law of Treaties.²⁷

²⁴See for example Ursula Kriebaum, 'Regulatory Takings: Balancing the Interests of the Investor and the State' (2007) 8 J World Investment & Trade 717; Han Xiuli, 'The Application of the Principle of Proportionality in Tecmed v Mexico' (2007) 6 Chinese J Intl L 633; Alec Stone Sweet and Jud Mathews, 'Proportionality Balancing and Global Constitutionalism' (2008) 47 Colum J Transnational L 73; Benedict Kingsbury and Stephan Schill, 'Investor-State Arbitration as Governance: Fair and Equitable Treatment, Proportionality and the Emerging Global Administrative Law' in Albert Jan van den Berg (ed), *50 Years of the New York Convention: ICCA International Arbitration Conference* (Kluwer 2009); Jasper Krommendijk and John Morijn, 'Proportional by What Measure(s)? Balancing Investor Interests and Human Rights by Way of Applying the Proportionality Principle in Investor-State Arbitration' in Pierre-Marie Dupuy, Ernst-Ulrich Petersmann and Francesco Francioni (eds), *Human Rights in International Investment Law and Arbitration* (OUP 2009); Benedict Kingsbury and Stephan W Schill, 'Public Law Concepts to Balance Investors' Rights with State Regulatory Actions in the Public Interest – The Concept of Proportionality' in Stephan W Schill (ed), *International Investment Law and Comparative Public Law* (OUP 2010); Alec Stone Sweet, 'Investor-State Arbitration: Proportionality's New Frontier' (2010) 4 Law & Ethics of Human Rights 47; Erlend M Leonhardsen, 'Looking for Legitimacy: Exploring Proportionality Analysis in Investment Treaty Arbitration' (2012) 3 J Intl Dispute Settlement 95; Benedikt Pirker, *Proportionality Analysis and Models of Judicial Review: A Theoretical and Comparative Study* (Europa Law Publishing 2013) ch 8.

²⁵ibid.

²⁶See for example William W Burke-White and Andreas Von Staden, 'Investment Protection in Extraordinary Times: The Interpretation and Application of Non-Precluded Measures Provisions in Bilateral Investment Treaties' (2007-2008) 48 Va J Intl L 307; William W Burke-White and Andreas Von Staden, 'Private Litigation in a Public Law Sphere: The Standard of Review in Investor-State Arbitrations' (2010) 35 Yale J Intl L 283; Anthea Roberts, 'The Next Battleground: Standards of Review in Investment Treaty Arbitration' (2011) 16 International Council for Commercial Arbitration Congress Series 170; Caroline Henckels, 'Indirect Expropriation and the Right to Regulate: Revisiting Proportionality Analysis and the Standard of Review in Investor-State Arbitration' (2012) 15 J Intl Economic L 223; Caroline E Foster, 'Adjudication, Arbitration and the Turn to Public Law "Standards of Review": Putting the Precautionary Principle in the Crucible' (2012) 3 J Intl Dispute Settlement 525; Stephan Schill, 'Deference in Investment Treaty Arbitration: Re-conceptualizing the Standard of Review' (2012) 3 J Intl Dispute Settlement 577; Caroline Henckels, 'Balancing Investment Protection and the Public Interest: The Role of the Standard of Review and the Importance of Deference in Investor-State Arbitration' (2013) 4 J Intl Dispute Settlement 197.

²⁷See for example Ursula Kriebaum, 'Privatizing Human Rights – The Interface Between International Investment Protection and Human Rights' in August Reinisch and Ursula Kriebaum (eds), *The Law of International Relations – Liber Amicorum Hanspeter Heuhold* (Eleven International Publishing 2007); James D Fry, 'International Human Rights Law in Investment Arbitration: Evidence of International Law's Unity' (2007) 18 Duke J Comp & Intl L 77; Campbell McLachlan, 'Investment Treaties and General International Law' (2008) 57 ICLQ 361; Bruno Simma and Theodore Kill, 'Harmonizing investment protection and international human rights: first steps towards a Methodology' in Christina Binder and others (eds), *International Investment Law for*

The current uncertainty as to the scope of the customary international law defence of necessity and as to the interaction of that defence with NPM clauses has also been the subject of a substantial body of literature.²⁸ However, while these issues all broadly relate to how investment treaty arbitration tribunals have balanced investor and public interests at the merits stage of the arbitral process and while the body of literature in relation to each of these issues is quite comprehensive, they have not been assessed together with a view to determining the efficacy and appropriateness of balancing investor and public interests at the merits stage. Furthermore, the advantages and disadvantages of balancing investor and public interests at the merits stage *vis-à-vis* the remedies stage have not yet been explored.

Indeed, up until comparatively recently, the remedies stage of the investment treaty arbitration process as a whole had not received much attention in the academic literature.²⁹ In the last number of years however, this deficit has quite rapidly been

the 21st Century: Essays in honour of Christoph Schreuer (OUP 2009); Jorge Daniel Taillant and Jonathan Bonnitcha, 'International Investment Law and Human Rights' in Marie-Claire Cordonier Segger, Markus W Gehring and Andrew Newcombe (eds), *Sustainable Development in World Investment Law* (Kluwer 2011); Emma Saunders-Hastings, 'The Asymmetrical Legalization of Investment Regimes in Africa: Lessons from Water Privatization' in Marie-Claire Cordonier Segger, Markus W Gehring and Andrew Newcombe (eds), *Sustainable Development in World Investment Law* (Kluwer 2011); Bruno Simma, 'Foreign investment arbitration: a place for human rights?' (2011) 60 ICLQ 573.

²⁸See for example Michael Waibel, 'Two Worlds of Necessity in ICSID Arbitration: CMS and LG&E' (2007) 20 Leiden J Intl L 637; Stephan W Schill, 'International Investment Law and the Host State's Power to Handle Economic Crises: Comment on the ICSID Decision in LG&E v Argentina' (2007) 24 J Intl Arbitration 265; William W Burke-White and Andreas Von Staden, 'Investment Protection in Extraordinary Times: The Interpretation and Application of Non-Precluded Measures Provisions in Bilateral Investment Treaties' (2007-2008) 48 Va J Intl L 307; José E Álvarez and Kathryn Khamsi, 'The Argentine Crisis and Foreign Investors: a Glimpse into the heart of the Investment Regime' in Karl P Sauvant (ed), *The Yearbook of International Investment Law and Policy 2008-2009* (OUP 2009); Christina Binder, 'Changed Circumstances in Investment Law: Interfaces between the Law of Treaties and the Law of State Responsibility with a special focus on the Argentine Crisis' in Christina Binder and others (eds), *International Investment Law for the 21st Century: Essays in honour of Christoph Schreuer* (OUP 2009); Asif H Qureshi, 'The Economic Emergency Defence in Bilateral Investment Treaties: A Development Perspective' in Christina Binder and others (eds), *International Investment Law for the 21st Century: Essays in honour of Christoph Schreuer* (OUP 2009); Alexis Martinez, 'Invoking State Defenses in Investment Treaty Arbitration' in Michael Waibel and others (eds), *The Backlash against Investment Arbitration: Perceptions and Reality* (Kluwer 2010); Jürgen Kurtz, 'Adjudging the Exceptional at International Law: Security, Public Order and Financial Crisis' (2010) 59 ICLQ 325; Christina Binder and August Reinisch, 'Economic Emergency Powers: a Comparative Law Perspective' in Stephan W Schill (ed), *International Investment Law and Comparative Public Law* (OUP 2010); José Álvarez and Tegan Brink, 'Revisiting the Necessity Defence: Continental Casualty v Argentina' in Karl P Sauvant (ed), *The Yearbook of International Investment Law and Policy 2010-2011* (OUP 2012).

²⁹This comment purposely excludes the quite extensive literature dealing with the question of whether compensation is due for expropriation in international law and the question of whether the amount of compensation should vary depending on whether the expropriation was lawful or unlawful in nature: see for example Oscar Schachter, 'Compensation for Expropriation' (1984) 78 AJIL 121; DW Bowett, 'State Contracts with Aliens: Contemporary Developments on

addressed and a substantial number of books and articles on the subject of remedies in investment treaty arbitration have appeared.³⁰ However, much of this substantial (and ever-growing) body of literature aims to describe the mechanics of the valuation methods that have customarily been applied by investment treaty arbitration tribunals in assessing damages and, thus, certain lacunae exist in the literature.³¹

Compensation for Termination or Breach' (1988) 59 British YB Intl L 49; William C Lieblich, 'Determinations by International Tribunals of the Economic Value of Expropriated Enterprises' (1990) 7 J Intl Arbitration 37; C F Amerasinghe, 'Issues of Compensation for the Taking of Alien Property in Light of Recent Cases and Practice' (1992) 41 ICLQ 22.

³⁰See for example Irmgard Marboe, 'Compensation and Damages in International Law and the Limits of "Fair Market Value"' (2006) 7 J World Investment & Trade 723; Brent C Kaczmarek, 'Compensation for Non-Expropriatory Treaty Violations: An Analytical Framework' (2006) 3 Transnational Dispute Management; MA Abdala and PT Spiller, 'Damage Valuation of Indirect Expropriation in International Arbitration Cases' (2007) 4 Transnational Dispute Management; T Senechal, 'Dealing with Uncertainty: Discounted Cash Flow (DCF) Versus Adjusted Present Value (APV)' (2007) 4 Transnational Dispute Management; Borzu Sabahi, 'Recent Developments in Awarding Damages in Investor-State Arbitrations' (2007) 4 Transnational Dispute Management; CN Brower and M Ottolenghi, 'Damages in Investor-State Arbitration' (2007) 4 Transnational Dispute Management; Sergey Ripinsky, 'State of Necessity: Effect on Compensation' (2007) 4 Transnational Dispute Management; K Hobér, 'Fair and Equitable Treatment - Determining Compensation' (2007) 4 Transnational Dispute Management; MJ Valasek, 'A "Simple Scheme": Exploring the Meaning of Chorzów Factory for the Valuation of Opportunistic Expropriation in the BIT Generation' (2007) 4 Transnational Dispute Management; John Y Gotanda, 'Assessing Damages in International Commercial Arbitration: A Comparison With Investment Treaty Disputes' (2007) 4 Transnational Dispute Management; WH Knull III, ST Jones, TJ Tyler and RD Deutsch, 'Accounting for Uncertainty in Discounted Cash Flow Valuation of Upstream Oil and Gas Investments' (2007) 4 Transnational Dispute Management; F Marrella and I Marboe, "'Efficient Breach" and Economic Analysis of International Investment Law' (2007) 4 Transnational Dispute Management; Ursula Kriebaum, 'Regulatory Takings: Balancing the Interests of the Investor and the State' (2007) 8 J World Investment & Trade 717; Sergey Ripinsky with Kevin Williams, *Damages in International Investment Law* (British Institute of International and Comparative Law 2008); Andrea K Bjorklund, Ian A Laird and Sergey Ripinsky (eds), *Investment treaty law: current issues. III, Remedies in international investment law emerging jurisprudence of international investment law* (British Institute of International and Comparative Law 2008) chs 1-7; Mark Kantor, *Valuation for Arbitration* (Kluwer 2008); Thomas Wälde and Borzu Sabahi, 'Compensation, Damages and Valuation' in Peter Muchlinski, Federico Ortino and Christoph Schreuer (eds), *The Oxford Handbook of International Investment Law* (OUP 2008); Irmgard Marboe, *Calculation of Compensation and Damages in International Investment Law* (OUP 2009); Kathryn Khamsi, 'Compensation for Non-Expropriatory Investment Treaty Breaches' in Michael Waibel and others (eds), *The Backlash against Investment Arbitration: Perceptions and Reality* (Kluwer 2010); Borzu Sabahi, *Compensation and Restitution in Investor-State Arbitration: Principles and Practice* (OUP 2011); Matthew T Parish, Annalise K Nelson and Charles B Rosenberg, 'Awarding Moral Damages to Respondent States in Investment Arbitration' (2011) 29 Berkeley J Int L 225; Diane Desierto, 'Calibrating Human Rights and Investment in Economic Emergencies: Prospects of Treaty and Valuation Defenses' (2012) 9 Manchester J Intl Economic L 162; Diane Desierto, 'ICESCR Minimum Core Obligations and Investment: Recasting the Non-Expropriation Compensation Model during Financial Crises' (2012) 44 Geo Wash Intl L Rev 473; Diane A Desierto and Desiree A Desierto, 'Investment Pricing and Social Protection: a proposal for an ICESCR-adjusted Capital Asset Pricing Model' (2013) 28 ICSID Rev 405.

³¹For a similar observation see Joshua B Simmons, 'Valuation in Investor-State Arbitration: Toward A More Exact Science' (2012) 30 Berkeley J Intl L 196, 199.

In particular, only a small sub-set of the literature on remedies makes even passing reference to taking into account public interest considerations or the host state's non-investment related treaty obligations at the remedies stage and an even smaller sub-set directly addresses the question of whether such considerations or obligations are, or should be, relevant to the assessment of damages. Thus, Liberti describes one arbitral award in which the host state's obligations under a non-investment related treaty appeared to be taken into account but does not purport to explore the normative arguments in favour of taking such obligations into account at the remedies stage. Nor does Liberti attempt to delineate any guidelines as to how public interest considerations could be taken into account by tribunals in future.³² Somewhat similarly, Kulick has argued that public interest considerations may have been introduced by investment treaty arbitration tribunals clandestinely by taking account of such interests at the remedies stage rather than at the merits stage.³³ However, apart from opining that taking account of public interest considerations at the remedies stage in a transparent manner is doctrinally preferable to the consideration of such interests at the merits stage and from touching upon some of the issues associated with taking into account public interest considerations at the merits stage,³⁴ Kulick does not examine the particular doctrinal basis for this conclusion or comprehensively examine the normative reasons supporting this approach. Finally, Gallus, in the context of discussing the FET standard, notes that some investment treaty arbitration tribunals have adjusted their damages awards to reflect the circumstances of the host state but does not discuss the benefits and drawbacks of this approach. He also explicitly leaves open the question of how this development affects or relates to the taking into account of the circumstances of the host state at the merits stage.³⁵

Admittedly, a small number of commentators have raised normative arguments in relation to the balancing of investor and public interests at the remedies stage. However, each of these falls short of a complete analysis. Thus, in his book 'Global

³²Lahra Liberti, 'The Relevance of Non-Treaty Investment Obligations in Assessing Compensation' in Pierre-Marie Dupuy, Ernst-Ulrich Petersmann and Francesco Francioni (eds), *Human Rights in International Investment Law and Arbitration* (OUP 2009).

³³Andreas Kulick, 'Sneaking Through the Backdoor – Reflections on Public Interest in International Investment Arbitration' (2013) 29 *Arbitration Intl* 435.

³⁴*ibid*, 447- 51.

³⁵Nick Gallus, 'The 'fair and equitable treatment' standard and the circumstances of the host state' in Chester Brown and Kate Miles (eds), *Evolution in Investment Treaty Law and Arbitration* (Cambridge University Press 2011).

Public Interest in International Investment Law’, Kulick, drawing on the German constitutional law principle of *praktische Konkordanz* whereby all competing rights have to be reconciled in a differentiated manner that aims at the optimal outcome for every such right, notes that the outcome of proportionality analysis at the merits stage ‘must find reflection in the amount of compensation and damages’ (i.e. the tribunal must determine whether a lower amount of damages is necessary, suitable and the least restrictive measure to address the public interest considerations underlying the host state measure).³⁶ However, while Kulick considers both possible doctrinal bases for proportionality analysis in international investment law and the normative reasons supporting its application, he does not focus upon the doctrinal basis for application of an overarching proportionality analysis affecting both the merits and the remedies stage nor on the particular normative reasons why an approach that envisages derogation from the full reparation principle may (or may not) be desirable.

Tudor, in discussing the FET standard, advocates the view that elements that may excuse, justify or which may have contributed to the behaviour of the host state such as its specific circumstances or the behaviour of the claimant investor should be taken into account exclusively at the remedies stage.³⁷ However, Tudor acknowledges that this approach is only appropriate to breaches of the FET standard which involve no expropriation-like effect, which, she admits, are quite rare.³⁸ In addition, Tudor acknowledges that the ‘general characteristics’ of the host state must still be taken into account at the merits stage in order to construct a standard against which the fairness and equitableness of the host state’s behaviour can be measured and to attach the state to a general category of similar states. Thus, Tudor’s approach is confined to a quite narrow category of breaches and, given the vagueness of the terms used, does not purport to adequately describe the inter-relationship between the merits and remedies stages in this regard. Furthermore, beyond the assertion that taking account of the claimant investor’s behaviour at the merits stage could impact on the decision of the tribunal as to the legality of the host state’s behaviour, which could deprive the fair and equitable treatment

³⁶Andreas Kulick, *Global Public Interest in International Investment Law* (Cambridge University Press 2012) 209-17. See also Andreas Kulick, ‘Sneaking Through the Backdoor – Reflections on Public Interest in International Investment Arbitration’ (2013) 29 *Arbitration Intl* 435, 451.

³⁷Ioana Tudor, *The Fair and Equitable Treatment Standard in the International Law of Foreign Investment* (OUP 2008) ch 7.

³⁸*ibid.*

standard of its *raison d'être* and result in an extension of the tribunal's competence beyond the scope of review conferred on the tribunal by the dispute resolution clause, Tudor does not consider the normative arguments supporting her suggested approach.

Similarly, Kriebaum, drawing on the case law of the European Court of Human Rights, argues that, in order to move away from the current 'all or nothing' approach to liability applicable in respect of lawful expropriations, proportionality analysis should be applied after an expropriation is deemed lawful in nature, which may serve to reduce the quantum of compensation payable. However, Kriebaum's analysis does not extend to unlawful acts and, in addition, does not consider how this approach would interact with the provisions on compensation for lawful expropriations contained in most current IIAs.³⁹

Finally, in a number of articles,⁴⁰ Desierto has discussed why (and how) certain non-investment related treaty obligations, namely the minimum core obligations of states under the International Covenant on Economic, Social and Cultural Rights (ICESCR), should be taken into account in quantifying damages where compliance with such obligations constituted the reason underlying the host state's IIA breach. While such host state obligations are clearly of crucial importance in protecting the most essential interests of its population and while the conflict between such obligations and IIA rights represents the archetypal example of a problematic restraint on host state sovereignty, nonetheless Desierto's analyses do not constitute (nor do they in any way purport to constitute) a complete analysis of whether public interest considerations generally should be taken into account in formulating remedies for IIA breaches. Overall therefore, while there has been some discussion of the issue of taking into account public interest considerations at the remedies stage, the analysis has not been comprehensive and, in particular, has not explored the inter-relationship between the merits and remedies stages in this regard.

³⁹Ursula Kriebaum, 'Regulatory Takings: Balancing the Interests of the Investor and the State' (2007) 8 J World Investment & Trade 717.

⁴⁰Diane Desierto, 'Calibrating Human Rights and Investment in Economic Emergencies: Prospects of Treaty and Valuation Defenses' (2012) 9 Manchester J Intl Economic L 162; Diane Desierto, 'ICESCR Minimum Core Obligations and Investment: Recasting the Non-Expropriation Compensation Model during Financial Crises' (2012) 44 Geo Wash Intl L Rev 473; Diane A Desierto and Desiree A Desierto, 'Investment Pricing and Social Protection: a proposal for an ICESCR-adjusted Capital Asset Pricing Model' (2013) 28 ICSID Rev 405.

However, on a related note, a number of commentators have suggested that public law concepts should be introduced at the remedies stage but have not elaborated substantially on how these concepts should be applied.⁴¹ For example, Wälde and Sabahi have proposed that, in the context of claims based on the FET standard, the concept of legitimate expectations ‘can not only be a concept to describe a subcategory of the fair and equitable treatment standard, but it can also be used to expand or delimit the scope for compensation’.⁴² However, the potential benefits and drawbacks of such a development are not explored by Wälde and Sabahi or by other commentators who have proposed (or have at least alluded to) the possible application of public law principles at the remedies stage.

Indeed, much of the literature which argues that public law principles should inform the approach of investment treaty arbitration tribunals towards remedies focuses on the fact that sovereign misconduct in public law has traditionally been addressed by non-pecuniary remedies (such as orders for specific performance, annulment or declaratory relief) rather than damages and argues that an award of damages does not sit easily with the nature of disputes dealt with by investment treaty arbitration tribunals.⁴³ Proposals have thus been made for the increased use of non-pecuniary measures in investment treaty arbitration, while acknowledging the significant difficulties associated with non-pecuniary relief.⁴⁴ Thus, from a theoretical

⁴¹See for example Thomas Wälde and Borzu Sabahi, ‘Compensation, Damages and Valuation’ in Peter Muchlinski, Federico Ortino and Christoph Schreuer (eds), *The Oxford Handbook of International Investment Law* (OUP 2008); Borzu Sabahi and Nicholas J Birch, ‘Comparative Compensation for Expropriation’ in Stephan W Schill (ed), *International Investment Law and Comparative Public Law* (OUP 2010); Irmgard Marboe, ‘State Responsibility and Comparative State Liability for Administrative and Legislative Harm to Economic Interests’ in Stephan W Schill (ed), *International Investment Law and Comparative Public Law* (OUP 2010); Anne van Aaken, ‘Primary and Secondary Remedies in International Investment Law and National State Liability: a Functional and Comparative View’ in Stephan W Schill (ed), *International Investment Law and Comparative Public Law* (OUP 2010).

⁴²ibid, 1089.

⁴³See for example Carole Malinvaud, ‘Non-pecuniary Remedies in Investment Treaty and Commercial Arbitration’ in Albert Jan van den Berg (ed), *50 Years of the New York Convention: ICCA International Arbitration Conference* (Kluwer 2009); Anne van Aaken, ‘Primary and Secondary Remedies in International Investment Law and National State Liability: a Functional and Comparative View’ in Stephan W Schill (ed), *International Investment Law and Comparative Public Law* (OUP 2010); Brooks E Allen, ‘The Use of Non-pecuniary remedies in WTO Dispute Settlement: Lessons for Arbitral Practitioners’ in Michael E Schneider and Joachim Knoll (eds), *Performance as a Remedy: Non-Monetary Relief in International Arbitration* (Juris Publishing 2011); Gisele Stephens-Chu, ‘Is it Always All About the Money? The Appropriateness of Non-Pecuniary Remedies in Investment Treaty Arbitration’ (2014) 30 *Arbitration Intl* 661.

⁴⁴See for example Christoph Schreuer, ‘Non-Pecuniary Remedies in ICSID Arbitration’ (2004) 20 *Arbitration Intl* 325; Martin Endicott, ‘Remedies in Investor-State Arbitration: Restitution, Specific Performance and Declaratory Awards’ in P Kahn and T W Wälde (eds), *New Aspects of International Investment Law* (Martinus Nijhoff 2007); Mavluda Sattorova, ‘Investment Treaty

perspective, the ordering of non-pecuniary relief by investment treaty arbitration tribunals is viewed by some as an undue interference with host state sovereignty as such reliefs compel the host state to act in a certain manner.⁴⁵ While the proposition that the granting of non-pecuniary relief necessarily or invariably interferes with host state sovereignty more than the granting of pecuniary relief has been questioned,⁴⁶ there remain, in any event, more practical problems associated with the granting of non-pecuniary relief. For example, the host state may be unwilling or unable to undo its actions (due to political, legal or constitutional constraints) or the relationship between the host state and the claimant investor may be irreparably damaged. Furthermore, investment treaty arbitration tribunals, given their *ad hoc* nature, have limited ability to supervise and enforce transfers of property or other restitutionary acts. These factors are likely to make restoration either impractical or futile and to cause the claimant investor to request pecuniary relief only, which, in turn, circumscribes the ability of the investment treaty arbitration tribunal to award alternative forms of relief. Lastly, the terms of the relevant IIA may preclude the granting of non-pecuniary remedies.⁴⁷ Given these difficulties and, accordingly, the limited circumstances in which non-pecuniary remedies are likely to be appropriate,⁴⁸ it is submitted that the literature on this topic is already quite comprehensive.

Finally, largely as a result of the investment treaty claims that arose out of the Argentine economic crisis and sovereign default of 2000 to 2002, a substantial body

Breach as Internationally Proscribed Conduct: Shifting Scope, Evolving Objectives, Recalibrated Remedies?’ (2012) 4 Trade L & Dev 315.

⁴⁵See *Amco Asia Corporation and others v Republic of Indonesia*, ICSID Case No ARB/81/1, Award 20 November 1984, 1 ICSID Rep 413, para 202. See also Zachary Douglas, *The International Law of Investment Claims* (2009) 100.

⁴⁶Thomas Wälde and Borzu Sabahi, ‘Compensation, Damages and Valuation’ in Peter Muchlinski, Federico Ortino and Christoph Schreuer (eds), *The Oxford Handbook of International Investment Law* (OUP 2008) 1060.

⁴⁷Christoph Schreuer, ‘Non-Pecuniary Remedies in ICSID Arbitration’ (2004) 20 *Arbitration Intl* 325; Martin Endicott, ‘Remedies in Investor-State Arbitration: Restitution, Specific Performance and Declaratory Awards’ in P Kahn and T W Wälde (eds), *New Aspects of International Investment Law* (Martinus Nijhoff 2007) 520; Campbell McLachlan, Laurence Shore and Matthew Weiniger, *Investment Treaty Arbitration: Substantive Principles* (OUP 2007) 341.

⁴⁸One suggestion for increased use of non-pecuniary remedies in investment treaty arbitration which avoids at least some of the difficulties associated with non-pecuniary remedies is for a tribunal in its final award to allow the host state to elect between a specific conduct remedy and a pecuniary remedy: see for example *Goetz and others v Burundi*, ICSID Case No ARB/95/3, Award 10 February 1999, 6 ICSID Rep 5. See also Brooks E Allen, ‘The Use of Non-pecuniary remedies in WTO Dispute Settlement: Lessons for Arbitral Practitioners’ in Michael E Schneider and Joachim Knoll (eds), *Performance as a Remedy: Non-Monetary Relief in International Arbitration* (Juris Publishing 2011).

of literature has developed in relation to the (uncertain) effect of successful invocation of the customary international law defence of necessity and/or of NPM clauses on the obligation to pay damages.⁴⁹ However, this analysis has not generally been connected to the wider question of whether taking into account public interest considerations at the remedies stage is desirable.

In conclusion, despite the growing body of literature relating to both the balancing of investor and public interests in investment treaty arbitration and on the remedies stage of the arbitral process, the question of whether, and in what circumstances, the remedies stage represents an appropriate platform for the taking into account of public interest considerations has not been comprehensively examined. This thesis aims to address this deficit.

1.3 Methodology and limitations

Doctrinal analysis of the primary sources of international investment law, namely IIAs and the awards of investment treaty arbitration tribunals, will be utilised throughout this thesis. This analysis, however, departs from the narrowest form of doctrinal analysis in that it seeks to break away from the idea of legal systems as self-contained systems and instead envisages a role for legal scholars in critiquing the law and in suggesting legal reforms.⁵⁰ Therefore, in the context of this thesis, doctrinal analysis refers to the analysis of legal sources in order to examine how investment treaty arbitration tribunals have decided cases of a given kind and how those tribunals ought to decide those cases in light of an underlying normative proposition (namely that public interest considerations should be taken into account in investment treaty arbitration).⁵¹

⁴⁹See for example Stephan W Schill, 'International Investment Law and the Host State's Power to Handle Economic Crises - Comment on the ICSID Decision in LG&E v Argentina' (2007) 24 J Intl Arbitration 265; Michael Waibel, 'Two Worlds of Necessity in ICSID Arbitration: CMS and LG&E' (2007) 20 Leiden J Intl L 637; Sergey Ripinsky, 'State of Necessity: Effect on Compensation' (2007) 4 Transnational Dispute Management; William W Burke-White and Andreas Von Staden 'Investment Protection in Extraordinary Times: The Interpretation and Application of Non-Precluded Measures Provisions in Bilateral Investment Treaties (2007-2008) 48 Va J Intl L 307; José E Álvarez and Kathryn Khamsi, 'The Argentine Crisis and Foreign Investors: a Glimpse into the heart of the Investment Regime' in Karl P Sauvant (ed), *The Yearbook of International Investment Law and Policy 2008-2009* (OUP 2009); José E Álvarez and Tegan Brink, 'Revisiting the necessity defense: Continental Casualty v. Argentina' in Karl P Sauvant (ed), *Yearbook of International Investment Law and Policy 2010-2011* (OUP 2012).

⁵⁰Joseph William Singer, 'Normative Methods for Lawyers' (2009) 56 UCLA L Rev 899.

⁵¹Chapter 2 establishes the bases for this normative proposition.

In conducting this analysis, the case for institutional and procedural reform of the investment treaty dispute resolution system will not be examined in detail. Rather the related issue of the need for public interest considerations to be taken into account in investment treaty arbitration and the means by which this has been, and could be, achieved will form the focus of the study. However, the efficacy of mechanisms such as general exceptions clauses which have been included in some ‘new generation’ IIAs will not be extensively evaluated except where such mechanisms have a potential impact on the remedies stage of the arbitral process. Furthermore, since the payment of damages has been the remedy awarded by the vast majority of investment treaty arbitration tribunals to date and given the significant difficulties associated with the use of non-pecuniary remedies in investment treaty arbitration, this thesis will focus on the remedy of damages. Finally, although interim or provisional remedies (which are increasingly being ordered by investment treaty arbitration tribunals)⁵² may significantly affect the parties’ incentives and may, in many cases, assist in reaching early settlement of the dispute (which may have an indirect effect on the public interest), this thesis deals only with the remedy of damages awarded at the final stage of the arbitral process.

1.4 Definitions and key concepts

(a) International Investment Agreements (IIAs)

Bilateral Investment Treaties (BITs) are the most common form of IIA.⁵³ As at the end of 2014, the IIA regime consisted of 3,268 IIAs, which included 2,923 BITs (of which approximately 2,223 remain in force) and 345 other IIAs, such as integration or cooperation agreements with an investment dimension (of which approximately 275 remain in force).⁵⁴ BITs place substantive obligations on each contracting state *vis-à-vis* investors from the other contracting state. While each IIA is, in theory, the

⁵²See Robert Volterra, ‘Provisional Measures (Interim Measures) and Investment Treaty Arbitration under ICSID and UNCITRAL: Developments and Trends’ in Andrea K Bjorklund, Ian A Laird and Sergey Ripinsky (eds), *Investment treaty law: current issues. III, Remedies in international investment law emerging jurisprudence of international investment law* (British Institute of International and Comparative Law 2008); Dan Sarooshi, ‘Provisional Measures and Investment Treaty Arbitration’ (2013) 29 *Arbitration Intl* 361.

⁵³In recent years however, there has been a move away from BITs towards other forms of IIA: see UNCTAD, *World Investment Report 2013: Global Value Chains: Investment and Trade for Development* (UNCTAD 2013) xix.

⁵⁴UNCTAD, *Recent Trends in IIAs and ISDS* (UNCTAD IIA Issues Note No 1 February 2015) 2. For statistics as to number of IIAs remaining in force see <<http://investmentpolicyhub.unctad.org/IIA>> accessed 19 March 2015.

product of its own negotiation, in practice the rights conferred by IIAs share many common features, although the exact meaning of each right or standard will depend on the wording of the individual treaty. This similarity can be explained in part by the history behind IIAs (and in particular BITs). The need for such investment treaties arose due to the inadequacies of relying on diplomatic means or, exceptionally, on inter-state adjudication as means of resolving investment disputes following the end of the age of European empire.⁵⁵ As there was no duty on the home state to grant a national diplomatic protection, states might decline to pursue a particular claim for political reasons.⁵⁶ Similarly, for inter-state adjudication to occur, the consent of both states was required. Such consent was generally preceded by bilateral negotiations, the outcome of which depended more on the relative strength of the parties than on the merits of the claim. In either circumstance therefore, investors were at the mercy of their governments.⁵⁷ In addition, even if compensation was recovered by the home state, there was no obligation on the home state to pass on the compensation to the investor who had suffered the damage.⁵⁸ In many cases, investors therefore had to absorb the cost of adverse government action by either doing nothing or by making a claim under their political risk insurance.⁵⁹

Therefore, business lobbies in the major Western states and Western states themselves began to push for a multilateral treaty which would protect foreign investors from expropriation and other interferences by host states. However, the many attempts to reach consensus on a multilateral investment code, such as the Draft Convention on the Treatment of Foreigners in 1929,⁶⁰ the Abs-Shawcross Draft Convention of 1959⁶¹ and the Multilateral Agreement on Investment of

⁵⁵On the background and history of IIAs generally see Andrew Newcombe and Lluís Paradell, *Law and Practice of Investment Treaties: Standards of Treatment* (Kluwer 2009) ch 1. See also Andrea K Bjorklund, 'Reconciling State Sovereignty and Investor Protection in Denial of Justice Claims' (2004-2005) 45 *Va J Intl L* 809, 820-30.

⁵⁶*ibid*, 822-23.

⁵⁷Andrew Newcombe and Lluís Paradell, *Law and Practice of Investment Treaties: Standards of Treatment* (Kluwer 2009) ch 1.

⁵⁸Stephan W Schill, *The Multilateralization of International Investment Law* (Cambridge University Press 2009).

⁵⁹Susan D Franck, 'Empirically Evaluating Claims about Investment Treaty Arbitration' (2007) 86 *N C L Rev* 1, 10.

⁶⁰The text of the 1929 Draft Convention is reproduced in International Conference on the Treatment of Foreigners, Preparatory Documents, LN Doc C.36.M. 21.1929.II.

⁶¹The text of the Abs-Shawcross Draft Convention is reproduced in UNCTAD, *International Investment Instruments: A Compendium* (UNCTAD 2000) vol V, 301.

1998,⁶² all ran aground. This deadlock occurred for several reasons, not least because certain developing states viewed these draft treaties as just another method of domination, which would hinder their attempts to gain more control over their own natural resources.⁶³ In accordance with this view, many developing countries, in particular those in Latin America and in the Soviet Bloc, subscribed to the so-called Calvo Doctrine (associated with Carlos Calvo, a nineteenth century Argentine diplomat and jurist) which essentially holds that the responsibility of a government toward foreigners cannot be greater than that which a government owes towards its own citizens.⁶⁴ Alternative proposals that affirmed this right of states to regulate foreign investors – primarily the Havana Charter⁶⁵ – were rejected by the US and by Western capital.⁶⁶

Due to this lack of consensus, states began to conclude bilateral, regional or sector-specific investment treaties instead.⁶⁷ Germany is credited with being the first state to sign a BIT: the Germany-Pakistan BIT of 1959.⁶⁸ However, although such treaties usually have a fixed lifespan and may be easier to renegotiate than multilateral agreements, they in fact adopt many of the protections put forward in

⁶²OECD, *The Multilateral Agreement on Investment: Draft Consolidated Text DAF/MAI(98)7/REV1*.

⁶³See for example the United Nations declarations associated with the New International Economic Order (NIEO): ‘General Assembly Resolution on Permanent Sovereignty over Natural Resources’, GA Res 3171, 17 December 1973 (1974) 13 ILM 238; Declaration on the Establishment of a New International Economic Order’ GA Res 3201, 1 May 1974 (1974) 13 ILM 715; ‘Charter of Economic Rights and Duties of States’ GA Res 3281, 12 December 1974 (1975) 14 ILM 251.

⁶⁴Charles Calvo, *Le Droit International Theorique et Practique: précédé d'un exposé historique des progrès de la science du droit des gens*, vol 6 (5th edn, A Rousseau 1896) 231. Montt notes that the doctrine was elucidated much earlier than the first writings of Calvo and appeared as early as 1832 in the first Latin American treatise of international law, Andrés Bello’s *Derecho de Jentes*: Santiago Montt, ‘What International Law and Latin America Can and Should Demand from each other: Updating the Bello/Calvo Doctrine in the BIT Generation’ (2007) 3 Res Publica Argentina 75, 79.

⁶⁵The Final Act and Related Documents of the United Nations Conference on Trade and Employment, Havana, Cuba, 21 November 1947-24 March 1948 (Final Act of the Havana Conference), included the draft Charter for the International Trade Organisation (ITO), UN Doc ICTO/1/4 (1948).

⁶⁶See generally Andrew Newcombe and Lluís Paradell, *Law and Practice of Investment Treaties: Standards of Treatment* (Kluwer 2009) ch 1.

⁶⁷The increasing emergence of pluri-lateral or regional investment protection treaties can be said to qualify somewhat the picture of the failure to reach multilateral agreement on the acceptable content of investors’ rights: see Campbell McLachan, ‘Investment Treaties and General International Law’ in Andrea K Bjorklund, Ian A Laird and Sergey Ripinsky (eds), *Investment treaty law: current issues. III, Remedies in international investment law emerging jurisprudence of international investment law* (British Institute of International and Comparative Law 2008) 113.

⁶⁸However, it appears that the first investment treaty to contain unqualified state consent to arbitration entered into force in 1969 between Italy and Chad and this, rather than the Germany-Pakistan BIT, can be considered to mark the true beginning of modern BIT practice: Andrew Newcombe and Lluís Paradell, *Law and Practice of Investment Treaties: Standards of Treatment* (Kluwer 2009) 42-45.

the failed multilateral treaties.⁶⁹ Thus, despite the lack of a multilateral investor code, a high level of protection for international investors has been achieved in practice⁷⁰ and this patchwork of treaties has become the dominant international vehicle through which investment is regulated.⁷¹

Adding to the historical factors which have encouraged convergence in investment treaty provisions, convergence is also stimulated by the inclusion in most investment treaties of most-favoured-nation (MFN) clauses, which encourage states to grant the same benefits to the nationals of each state they sign a treaty with. Finally, the ability of investors to forum-shop means that states have to assume that investors are covered by the highest investment protection standards.⁷² Thus, while in relation to peripheral issues, there is increasing variation among IIAs,⁷³ it is possible to generally describe the principal features of IIAs and this thesis proceeds on that basis. For example, it is possible to state that the definition of ‘investment’ in IIAs tends to asset based and therefore broad⁷⁴ and that the definition of ‘investor’ is generally also broad, although variation amongst IIAs exists, for example in relation to the basis on which the nationality of a juridical person is determined.⁷⁵ While the approximately 1,400 BITs entered into by EU Member States will be terminated in coming years following the conferral by the Treaty on the Functioning of the European Union of exclusive competence on the EU to conclude agreements covering all matters relating to foreign investment,⁷⁶ these BITs will, it seems, be progressively replaced by IIAs or investment chapters in FTAs concluded by the EU with third countries, the pillars of which should mirror

⁶⁹Surya P Subedi, *International Investment Law: Reconciling Policy and Principle* (Hart Publishing 2008) 103.

⁷⁰Stephan W Schill, *The Multilateralization of International Investment Law* (Cambridge University Press 2009) ch 1.

⁷¹Andrew T Guzman, ‘Why LDCs Sign Treaties that Hurt Them: Explaining the Popularity of Bilateral Investment Treaties’ (1997-1998) 38 Va J Intl L 640.

⁷²Gus Van Harten, *Investment Treaty Arbitration and Public Law* (OUP 2007) 113-17.

⁷³Lisa E Sachs and Karl P Sauvant, ‘BITs, DTTs, and FDI Flows: An Overview’ in Lisa E Sachs and Karl P Sauvant (eds), *The Effect of Treaties on Foreign Direct Investment: Bilateral Investment Treaties, Double Taxation Treaties and Investment Flows* (OUP 2009) 9.

⁷⁴Noah Rubins, ‘The Notion of “Investment” in International Investment Arbitration’ in Norbert Horn (ed), *Arbitrating Foreign Investment Disputes* (Kluwer 2004) 283-324.

⁷⁵Patrick Dumberry, ‘The Legal Standing of Shareholders before Arbitral Tribunals: Has Any Rule of Customary International Law Crystallised?’ (2010) 18 Mich J Intl L 353.

⁷⁶See Articles 63 and 207 of the Treaty on the Functioning of the European Union. See also Regulation (EU) No 1219/2012 of the European Parliament and of the Council of 12 December 2012 establishing transitional arrangements for bilateral investment agreements between Member States and third countries, 20 December 2012.

the investor rights included in existing Member States' IIAs.⁷⁷ Therefore, the commentary on existing IIAs is likely to retain much of its validity.

(b) *The investment treaty arbitration system*

Turning to the concept of investment treaty arbitration, this refers to a process used to resolve disputes between a foreign investor and a state under an IIA.⁷⁸ This is to be distinguished from other forms of prospective investment arbitration. Thus, a state can consent to arbitration of future investment disputes by contract, by domestic legislation or by treaty. Contract-based arbitration relies on the specific consents of private parties (or of the state acting in its private capacity) and the consent is typically regarded as being limited to a commercial relationship with another private party. While legislation-based arbitration is closer to treaty-based arbitration in that it involves the host state acting in its sovereign capacity in the regulatory sphere, the delegation of authority to arbitrators is subject to the direct control of the legislature or judiciary of the state in question.⁷⁹ Treaty-based arbitration, in contrast, removes investment disputes from the legal domain of the contracting states entirely as IIAs give investors from the other contracting state the right to bring claims directly against the host state without, in most cases, having to exhaust local remedies.⁸⁰ This by-passing of the requirement to exhaust local remedies is an anomaly in the general international law context.⁸¹ Furthermore, a

⁷⁷European Commission, *Towards a comprehensive European international investment policy*, 7 July 2010, COM (2010) 343 final; European Parliament, *Resolution on the future European international investment policy*, 6 April 2011, 2010/2203(INI). See also August Reinisch, 'The Future Shape of EU Investment Agreements' (2013) 28 ISCID Rev 179.

⁷⁸One OECD study found that 96 per cent of the sample treaties contained language on investor-state dispute settlement: see David Gaukrodger and Kathryn Gordon, *Investor-state dispute settlement: A scoping paper for the investment policy community*, OECD Working Papers on International Investment No 2012/3 (OECD 2012) 64.

⁷⁹Gus Van Harten, *Investment Treaty Arbitration and Public Law* (OUP 2007) 24-25. See also David D Caron, 'The Interpretation of National Foreign Investment Laws as Unilateral Acts under International Law' in Mahnoush H Arsanjani and others (eds), *Looking to the Future: Essays on International Law in Honor of W Michael Reisman* (Martinus Nijhoff 2010).

⁸⁰Article 26 of the ICSID Convention requires a State to make express provision if it wishes to insist on the exhaustion of local remedies and most modern IIAs dispense with the requirement. For example, in a study of 148 German BITs, 89 contained an explicit waiver of the local remedies rule, 48 were silent on the subject, 8 provided for a certain period of time to pass before investor-state arbitration could be resorted to and only 3 stated that local remedies 'shall be exhausted': International Law Association German Branch/Working Group, 'General Public International Law and International Investment Law – A Research Sketch on Selected Issues' 52 <<http://telc.jura.uni-halle.de/sites/default/files/BeitraegeTWR/Heft%20105.pdf>> accessed 19 March 2015.

⁸¹The requirement to exhaust local remedies forms part of customary international law and has been recognised as such by the ICJ in, for example, the *Interhandel case (Switzerland v United States)*, Preliminary Objections Judgment 21 March 1959 (1959) ICJ Rep 6.

prior contractual relationship between the host state and a claimant investor is not required in order for an investor to bring a claim. Rather the state, by entering into the IIA, effectively gives a general consent to all nationals of the other contracting state to have recourse to arbitration.⁸² In these arbitration proceedings the claimant will almost always be an investor and the respondent will always be the host state.⁸³ This system differs from the WTO dispute settlement system, and from most other international adjudication systems, which rely on governments to file claims against one another. Indeed, due to this right of direct recourse for investors to binding arbitration, the numbers of investment disputes now vastly exceed those brought to the WTO's interstate dispute settlement system.⁸⁴

In 1966 a dedicated self-contained framework for the arbitration of investor-state disputes was put in place by the Convention on the Settlement of Investment Disputes between States and Nationals of other States (the ICSID Convention)⁸⁵ and an International Centre for the Settlement of Investment Disputes (ICSID), affiliated to the World Bank, was established. ICSID was granted jurisdiction over:

any legal dispute arising directly out of an investment between a Contracting State (or any constituent subdivision or agency of a Contracting State designated to the Centre by that State) and a national of another Contracting State, which the parties to the dispute consent to in writing to submit to the Centre.⁸⁶

However, ICSID's early case load was modest and was dominated by contract-based claims.⁸⁷ In 1987 the first investment arbitration under a BIT was registered⁸⁸ but it was not until the 1990s that investment treaty arbitration really came into its

⁸²Jan Paulsson, 'Arbitration without Privity' (1995) 10 ICSID Rev 232.

⁸³A state-to-state dispute resolution mechanism is also a feature of many IIAs. However, formal state-to-state disputes under IIAs are rare: Luke Eric Peterson, 'All Roads Lead out of Rome: Divergent Paths of Dispute Settlement in Bilateral Investment Treaties' in Lyuba Zarsky (ed), *International Investment for Sustainable Development: Balancing Rights and Rewards* (Earthscan Publishing 2005) 127.

⁸⁴José E Álvarez, 'Meador Lecture Series 2007-2008: Empire: Contemporary Foreign Investment Law: An "Empire of Law" or the "Law of Empire"?' (2009) 60 Ala L Rev 943, 959.

⁸⁵Convention on the Settlement of Investment Disputes between States and Nationals of Other States, 575 UNTS 159 (18 March 1965).

⁸⁶ibid, art 25(1).

⁸⁷See for example *Holiday Inns SA v Morocco*, ICSID Case No ARB/72/1 (an unpublished ICSID award discussed in Pierre Lalive, 'The First "World Bank" Arbitration (Holiday Inns v. Morocco) - Some Legal Problems' 1 ICSID Rep 645); *AGIP SpA v Congo*, ICSID Case No ARB/77/1, Award 30 November 1979, 1 ICSID Rep 306.

⁸⁸*Asian Agricultural Products Ltd v Sri Lanka*, ICSID Case No ARB/87/3, 4 ICSID Rep 245.

own.⁸⁹ Since then, ICSID has become the most popular forum for settlement of investor-state disputes due to the self-contained nature of the ICSID Convention system, although investors also bring a substantial minority of claims outside the ICSID framework. Under the ICSID Convention, each contracting state, whether or not a party to the dispute, is required to recognise an award as binding and to enforce the pecuniary obligations imposed by the award as if it were a final judgment of that state's courts.⁹⁰ Thus, ICSID awards are not subject to review by the local courts prior to enforcement and the only review available is that provided for under Articles 50 to 52 of the ICSID Convention.⁹¹ This annulment process deals with procedural error and so falls short of being a comprehensive review process.⁹²

Apart from the ICSID Arbitration Rules, other institutional arbitration rules applied in investor-state arbitrations include the ICC Arbitration Rules⁹³ and the Stockholm Chamber of Commerce Arbitration Rules.⁹⁴ In addition, the ICSID Additional Facility Rules,⁹⁵ which authorise ICSID to administer disputes involving non-signatory states and their investors, can be chosen.⁹⁶ However, the ICSID Additional Facility is not governed by the ICSID Convention and, as a result, an award under the ICSID Additional Facility does not fall within the ICSID enforcement system. In *ad hoc* arbitrations (where arbitration procedures are

⁸⁹Campbell McLachlan, Laurence Shore and Matthew Weiniger, *Investment Treaty Arbitration: Substantive Principles* (OUP 2007) 5.

⁹⁰SA Alexandrov, 'Enforcement of ICSID Awards: Article 53 and 54 of the ICSID Convention' (2009) 6 *Transnational Dispute Management*.

⁹¹Article 50 of the ICSID Convention allows a party to request an interpretation of an award in the event of a dispute between the parties as to its meaning. Article 51 allows a party to request revision of an award 'on the ground of discovery of some fact of such a nature as decisively to affect the award...'. Finally, Article 52 allows a party to request annulment of the award on certain limited grounds such as failure to state reasons for the award or corruption on the part of a member of the tribunal.

⁹²See generally David D Caron, 'Reputation and Reality in the ICSID Annulment Process: Understanding the Distinction Between Annulment and Appeal' (1992) 7 *ICSID Rev* 21.

⁹³Rules of Arbitration of the ICC in force as from 1 January 2012 <http://www.international-chamber.co.uk/images/ICC_Documents/icc_arbitration_and_adr_rules.pdf> accessed 19 March 2015.

⁹⁴Arbitration Rules of the Arbitration Institute of the Stockholm Chamber of Commerce adopted by the Stockholm Chamber of Commerce and in force as of 1 January 2010 <http://www.sccinstitute.com/media/40120/arbitrationrules_eng_webbversion.pdf> accessed 19 March 2015.

⁹⁵Rules governing the Additional Facility for the Administration of Proceedings by the Secretariat of the International Centre for Settlement of Investment Disputes <<https://icsid.worldbank.org/ICSID/StaticFiles/facility/partA-article.htm>> accessed 14 March 2015.

⁹⁶These rules can be chosen where either the host state or the investor's home state is not a party to the ICSID Convention. However, where neither the home state nor the host state is a party to the ICSID Convention, these rules cannot be used: *ibid*, art 2.

conducted without supervision by any administrative institution), the United Nations Commission on International Trade Law (UNCITRAL) Arbitration Rules⁹⁷ are most popular, although arbitrations can also be conducted in a classical *ad hoc* fashion, with no prescribed rules apart from the provisions of the relevant IIA.⁹⁸

Most IIAs provide the investor with a choice of dispute resolution options. For example, Article 10(5) of the Argentina-Netherlands BIT is quite typical in providing that the investor may submit the dispute either to ICSID or to an *ad hoc* arbitration tribunal established under the UNCITRAL Arbitration Rules.⁹⁹ However, other IIAs make the choice between ICSID arbitration and arbitration under the UNCITRAL Arbitration Rules subject to agreement by both the claimant investor and the host state and provide for arbitration under the UNCITRAL Arbitration Rules as a default where agreement cannot be reached.¹⁰⁰ Yet another group of treaties provide for the application of UNCITRAL Arbitration Rules only in circumstances where the ICSID Arbitration Rules and the ICSID Additional Facility Rules are unavailable.¹⁰¹ Finally, some IIAs provide that for arbitration under ICSID Arbitration Rules only¹⁰² and some provide for arbitration under the UNCITRAL Arbitration Rules only.¹⁰³

In non-ICSID arbitrations (including arbitrations under the ICSID Additional Facility rules), awards or their enforcement can be challenged under the commercial arbitration framework established by national law, the New York

⁹⁷ UNCITRAL Arbitration Rules as revised in 2010 (with new article 1, paragraph 4, as adopted in 2013) <<http://www.uncitral.org/pdf/english/texts/arbitration/arb-rules-2013/UNCITRAL-Arbitration-Rules-2013-e.pdf>> accessed 19 March 2015.

⁹⁸ However, the UNCITRAL Arbitration Rules can also be used in arbitrations administered by an institution such as ICSID, the ICC, the Stockholm Chamber of Commerce or the London Court of International Arbitration.

⁹⁹ Agreement on encouragement and reciprocal protection of investments between the Kingdom of the Netherlands and the Argentine Republic, signed 20 October 1992, entered into force 1 October 1994.

¹⁰⁰ See for example Agreement between the Government of the United Kingdom of Great Britain and Northern Ireland and the Government of the Republic of Argentina for the Promotion and Protection of Investments, signed 11 December 1990, entered into force 19 February 1993, art 8(3).

¹⁰¹ See for example Agreement between the Government of Canada and the Government of the Republic of Venezuela for the Promotion and Protection of Investments, signed 1 July 1996, entered into force 28 January 1998, art XII(4).

¹⁰² See for example Agreement between the Government of the United Kingdom of Great Britain and Northern Ireland and the Government of Malaysia for the Promotion and Protection of Investments, signed 21 May 1981, entered into force 21 October 1988, art 7.

¹⁰³ See for example Agreement between the Government of Hong Kong and the Government of Australia for the Promotion and Protection of Investment, signed 15 September 1993, entered into force 15 October 1993, art 10.

Convention¹⁰⁴ and other relevant treaties. Therefore, the national law at the place of arbitration controls the losing party's request to set aside the award, or as the case may be, to refuse enforcement.¹⁰⁵ Article V of the New York Convention allows a state to refuse recognition and enforcement of an arbitral award. However, the grounds for refusal are quite narrow. Thus, recognition and enforcement of the award may be refused if, *inter alia*, the subject matter of the dispute is non-arbitrable in the state in which recognition and enforcement is sought or if it is contrary to public policy in that State. However, this 'public policy' ground has generally been narrowly construed by domestic courts.¹⁰⁶ Article VII of the New York Convention further reduces the likelihood that an award will be refused enforcement as it enables courts hearing annulment actions to effectively disregard the grounds for recognition and enforcement under the New York Convention if local arbitration law contains grounds more favourable to the validity and enforceability of the award.¹⁰⁷ Thus, the system of supervision by domestic courts in the seat of commercial arbitration or enforcement (in the case of non-ICSID awards) or by an ICSID annulment committee remains essentially limited to jurisdictional errors, procedural improprieties and serious violations of *ordre public*, and the latter only in the case of non-ICSID awards. More deference is afforded to foreign arbitral awards than to domestic awards in many countries¹⁰⁸ and, in most cases, almost automatic recognition and enforcement of awards is likely in relation to non-ICSID awards.¹⁰⁹

(c) *The substantive rights contained in IIAs*

¹⁰⁴UNCITRAL, Convention on the Recognition and Enforcement of Foreign Arbitral Awards (1958).

¹⁰⁵ In one study it was found that the annulment ratio in the case of ICSID awards is significantly higher than the set-aside ratio for non-ICSID treaty awards: Gaëtan Verhoosel, 'Annulment and Enforcement Review of Treaty Awards: To ICSID or Not to ICSID' in Albert Jan van den Berg (ed), *50 Years of the New York Convention: ICCA International Arbitration Conference* (Kluwer 2009) 287.

¹⁰⁶See for example the leading US case of *Parsons & Whittemore Overseas Co. Inc. v Société Générale de l'Industrie du Papier RAKTA and Bank of America*, 508 F. 2d 969 (2nd Cir, 1974).

¹⁰⁷See for example Article 1520 of the French Code of Civil Procedure as an example of a provision that is more favourable to recognition and enforcement of foreign awards than the New York Convention and which therefore has led to the New York Convention playing a residual role in France: *Société Polish Ocean Line v Société Jolasry*, Cour de Cassation, Case Number 91-16.041.

¹⁰⁸Eloise Henderson Bouzari, 'The Public Policy Exception to Enforcement of International Arbitral Awards: Implications for Post-NAFTA Jurisprudence' (1995) 30 *Tex Intl L J* 205.

¹⁰⁹Gaëtan Verhoosel, 'Annulment and Enforcement Review of Treaty Awards: To ICSID or Not to ICSID' in Albert Jan van den Berg (ed), *50 Years of the New York Convention: ICCA International Arbitration Conference* (Kluwer 2009) 313.

Apart from the dispute settlement provisions contained in IIAs, which have been characterised by investment treaty arbitration tribunals as arrangements provided to better protect the rights of foreign investors rather than as mere procedural mechanisms,¹¹⁰ modern IIAs tend to include most of the following substantive rights, albeit with different formulations and qualifications: the fair and equitable treatment (FET) standard,¹¹¹ the guarantee of full protection and security, the contingent standards of national treatment and of MFN treatment and the duty to pay compensation in the event of an expropriation or nationalisation. Umbrella clauses are also an important feature of a sizeable minority of IIAs and most IIAs also contain a guarantee in relation to the repatriation of profits. Some IIAs also contain stipulations as to the conditions of admission of the investment and prohibitions on the imposition of performance requirements. The principal substantive rights typically contained in IIAs will be explored further in the following chapters.

(d) *The remedies stage*

As with other adversarial adjudicative processes, an investment treaty arbitration tribunal must first decide whether it has jurisdiction over a particular dispute (the jurisdiction stage), before moving on to consider whether the claimant investor's rights have been breached (the merits stage) and, if liability is established, to determining the remedy to be awarded to the claimant investor (the remedies stage). While some tribunals have rendered an award which deals with all three stages together (if such is necessary),¹¹² other arbitral tribunals have rendered a separate award in respect of each of the stages,¹¹³ while yet another group of arbitral tribunals have rendered an award covering two stages of the process while considering either the jurisdiction stage¹¹⁴ or the remedies stage separately.¹¹⁴ A separate award relating to remedies may be favoured due to the need for input from

¹¹⁰Campbell McLachlan, Laurence Shore and Matthew Weiniger, *Investment Treaty Arbitration: Substantive Principles* (OUP 2007) 45.

¹¹¹There is ongoing debate as to whether fair and equitable treatment should be conceptualised as a 'standard': see Roland Kläger, 'Fair and Equitable Treatment' in *International Investment Law* (Cambridge University Press 2011) pt II, ch 5 for a critique of such conceptualisation; cf José E. Álvarez, 'A BIT on Custom' (2010) 42 N Y Univ J Intl L & Pol 17, 77-78. For the purposes of consistency, the term will be used throughout this thesis.

¹¹²See for example *MTD Equity Sdn. Bhd. & MTD Chile S.A. v Chile*, ICSID Case No ARB/01/7.

¹¹³See for example *Chevron Corporation (USA) and Texaco Petroleum Company (USA) v Ecuador*, UNCITRAL, PCA Case No 34877.

¹¹⁴See for example *Continental Casualty Company v Argentina*, ICSID Case No ARB/03/9.

valuation experts at this stage of the process. However, even where the consideration of remedies is dealt with in the same award as the other stages of the arbitral process, it still clearly constitutes a distinct stage of the adjudication process.

1.5 Conclusion

This chapter has outlined the purpose of the thesis and the principal arguments that will be made in this thesis. The existing literature relating to the tension between investor interests and public interests in investment treaty arbitration and, in particular, the literature relating to the remedies stage of the investment treaty arbitration process has also been analysed and the conclusion reached that, despite the growing body of literature on both the balancing of investor interests and public interests in investment treaty arbitration and on the remedies stage of the arbitral process, the question of whether, and in what circumstances, the remedies stage represents an appropriate platform for the taking into account of public interest considerations has not been comprehensively examined. This thesis addresses this question. However, before focussing on the remedies stage, the issue of why public interest considerations need to be taken into account in resolving disputes under IIAs in the first place must be considered. Chapter 2 will examine this issue.

Chapter 2: Why should investment treaty arbitration tribunals take account of public interest considerations?

2.1 Introduction

This chapter will consider why public interest considerations should be taken into account by investment treaty arbitration tribunals (whether at the jurisdiction, merits or remedies stage of the arbitral process). It is necessary to consider this question as, while consensus is emerging as to the need for public interest considerations to be taken into account in the sphere of investment treaty arbitration *per se*, whether this can be accomplished only in the context of the introduction of ‘new generation’ national and international investment policies (including new or renegotiated IIAs), which would explicitly recognise the duty of host states to regulate in the public interest, is open to question. However, this chapter will present a number of reasons why public interest considerations should also be taken into account by investment treaty arbitration tribunals when resolving disputes under the majority of current IIAs that make little or no reference to such considerations. This question will be considered by reference to the nature of the investment treaty arbitration regime (and, in particular, the ‘public-private’ distinctions which underlie the regime) and to the principal substantive rights typically contained in IIAs.

2.2 The nature of international investment law and arbitration

International investment law and arbitration can be considered to be a hybrid system as it can be viewed through either a public law or a private law lens and it contains characteristics of both public and private law.¹ Indeed, even within the domain of public law, commentators have different views as to how investment

¹Zachary Douglas, ‘The Hybrid Foundations of Investment Treaty Arbitration’ (2003) 74 *British YB Intl L* 151; Benedikt Pirker, *Proportionality Analysis and Models of Judicial Review: A Theoretical and Comparative Study* (Europa Law Publishing 2013) 342. See also Julie A Maupin, ‘Public and Private in International Investment Law: An Integrated Systems Approach’ (2013-2014) 54 *Va J Intl L* 367, 371-72 criticising the artificial public/private distinction and arguing that international investment law should be approached from an integrated systems perspective, which focusses on ‘figuring out how it works in real time and how it can be improved’.

treaty arbitration should be categorised and as to how it interacts with extant public law. Thus, some have argued that the investment treaty regime has an effect on general public international law and may constitute the ‘new’ custom in the field of investment protection such that even states that are not signatories to IIAs may be subject to some of the rules emerging from the regime.² Viewed through this lens, international investment law constitutes a set of rules applicable to all states which regulate the exercise of states’ sovereign powers and investment treaty arbitration constitutes a process of law-making.³ Other commentators have taken a different view, while still emphasising the public law nature of investment law. Thus, it has been argued that the relationship between the respondent host state and the claimant investor in investment treaty arbitration is analogous to the relationship between the citizen and the state in domestic state liability law as the essential issue in both cases is how to keep a government from abusing its role as sovereign and regulator.⁴

If one subscribes to either of these views (or, indeed, if investment treaty arbitration is conceived of as forming part of public law in any way), this opens the door to criticism of the current adjudication model used to resolve investor-state disputes, which has borrowed its main elements from the international commercial arbitration model and which therefore can be perceived to lack certain features of public law adjudication such as consistency, transparency and accountability.⁵ Thus, perhaps the principal criticism of the commercial arbitration model is that it

²Andreas F Lowenfeld, ‘Investment Agreements and International Law’ (2003) 42 Colum J Transnational L 123; José E Álvarez, ‘A BIT on Custom’ (2010) 42 N Y Univ J Intl L & Pol 17, 63. See also Campbell McLachlan, ‘Investment Treaties and General International Law’ (2008) 57 ICLQ 361, 392-93. This is argued to be the case although international investment law, given the relatively recent genesis of IIAs and IIA disputes, does not wholly accord with the usual definition of custom (i.e. a constant and uniform (though not necessarily unanimous) practice of states in their international relations and the belief that such practice is required by law).

³Alex Mills, ‘Antinomies of Public and Private at the Foundations of International Investment Law and Arbitration’ (2011) 14 J Intl Economic L 469.

⁴Gus Van Harten and Martin Loughlin, ‘Investment Treaty Arbitration as a Species of Global Administrative Law’ (2006) 17 Eur J Intl L 121; Daniel Kalderimis, ‘Investment Treaty Arbitration as Global Administrative Law: What this might mean in practice’ in Chester Brown and Kate Miles (eds), *Evolution in Investment Treaty Law and Arbitration* (Cambridge University Press 2011).

⁵Alec Stone Sweet and Florian Grisel, ‘Transnational Investment Arbitration: From Delegation to Constitutionalization?’ in Pierre-Marie Dupuy, Ernst-Ulrich Petersmann and Francesco Francioni (eds), *Human Rights in International Investment Law and Arbitration* (OUP 2009); Ernst-Ulrich Petersmann, ‘Constitutional Theories of International Economic Adjudication and Investor-State Arbitration’ in Pierre-Marie Dupuy, Ernst-Ulrich Petersmann and Francesco Francioni (eds), *Human Rights in International Investment Law and Arbitration* (OUP 2009); Cornel Marian, ‘Balancing Transparency: The Value of Administrative Law and Mathews-Balancing to Investment Treaty Arbitrations’ (2010) 10 Pepp Disp Resol L J 275.

fails to ensure arbitrator independence and accountability. In constituting investment treaty arbitration tribunals, each party to the dispute typically has the right to appoint one arbitrator to the panel of three arbitrators that will preside over the dispute. A third individual, the chair of the panel, will then be appointed through agreement of the two party-nominated arbitrators and ideally the parties as well.⁶ Thus, arbitrators receive appointments only if investors bring claims and they lack security of tenure. Furthermore, so-called ‘issue conflicts’ may arise if a person is at the same time an arbitrator in one case and counsel in another⁷ and this can give rise to the risk of real or perceived bias.⁸ While the presence of institutional safeguards could help to address this perception of bias, such safeguards would appear to be absent in investment treaty arbitration as arbitrators are not accountable to any higher judicial authority or elected public authority as there is no appellate body for investment treaty arbitrations apart from the ICSID annulment procedure which is limited to procedural error only. Moreover, as noted in Chapter 1, judicial supervision of arbitrators by domestic courts in either the seat of the arbitration or in the place of enforcement is limited.

Linked to the issue of arbitrator impartiality are the issues of the lack of a formal doctrine of precedent in investment treaty arbitration, the perceived lack of transparency surrounding the arbitral process and the question of *amicus curiae* participation in arbitral proceedings. In relation to the former issue, although a *de facto* doctrine of precedent is emerging in investment treaty arbitration,⁹ the lack of a formal doctrine of precedent adds an element of unpredictability to arbitral

⁶This method of constituting the tribunal is enshrined in the ICSID Convention (Article 37), the UNCITRAL Arbitration Rules (Article 9) and in the text of most IIAs.

⁷WR Park, ‘Arbitrator Integrity: The transient and the permanent’ (2009) 46 San Diego L Rev 692. See also Philippe Sands, ‘Conflict and conflicts in investment treaty arbitration: Ethical standards for counsel’ in Chester Brown and Kate Miles (eds), *Evolution in Investment Treaty Law and Arbitration* (Cambridge University Press 2011) for a review of the case-law on this issue.

⁸ibid. See also Symposium Co-Organised by ICSID, OECD and UNCTAD: ‘Making the Most of International Investment Agreements: a Common Agenda’ (12 December 2005): Opening Remarks by Roberto Dañino, Secretary-General, ICSID <<http://www.oecd.org/investment/internationalinvestmentagreements/36053800.pdf>> accessed 19 March 2015.

⁹See for example *Saipem SpA v Bangladesh*, ICSID Case No ARB/05/7, Award 20 June 2009, para 90. See also Jeffrey P Commission, ‘Precedent in Investment Treaty Arbitration: A Citation Analysis of a Developing Jurisprudence’ (2007) 24 J Intl Arbitration 129, 148-53; Andrea K Bjorklund, ‘Investment Treaty Arbitral Decisions as Jurisprudence Constante’ in Colin B Picker, Isabella D Bunn and Douglas W Arner (eds), *International Economic Law: The State and Future of the Discipline* (Hart Publishing 2008).

decisions¹⁰ and, it is argued, could potentially threaten governments' ability to regulate for social and environmental purposes given that states are given little guidance as to how possible future cases against them would be resolved.¹¹ In relation to the lack of transparency surrounding the investment treaty arbitration process and the lack of public participation, steps have been taken towards addressing these issues. For example, in investment disputes under ICSID it is now routine for the basic details of the arbitration to be in the public domain¹² and several recent arbitrations have conducted public hearings on closed circuit television or online¹³ or at least have provided access to transcripts of the hearings and to a range of documentation relating to the proceedings.¹⁴ In addition, some more recent IIAs allow for, or require, the publication of the award and other documents relating to the proceedings.¹⁵ Finally, UNCITRAL has issued a set of transparency rules which require disclosure of information submitted to, and issued by, arbitral tribunals throughout proceedings, mandate open hearings and expressly allow for participation by non-parties to a dispute.¹⁶ However, notwithstanding these developments, it is argued that there is still room for improvement in terms of transparency and public participation¹⁷ and, in particular, the fact that *amicus curiae*

¹⁰On the use of precedent in international law generally see Gilbert Guillaume, 'The Use of Precedent by International Judges and Arbitrators' (2011) 2 J Intl Dispute Settlement 5.

¹¹Susan D Franck, 'The Legitimacy Crisis in Investment Treaty Arbitration: Privatizing Public International Law Through Inconsistent Decisions' (2005) 73 Fordham L Rev 1521, 1529-47.

¹²In about 50 per cent of cases, ICSID obtains the consent of the parties to publish the award. Where one of the parties does not consent, the other party commonly releases it for publication in publications such as International Legal Materials or ICSID Reports. If the award is not published by another source, ICSID publishes excerpts from the legal holdings of the award, pursuant to ICSID Arbitration Rule 48(4): OECD, *Transparency and Third Party Participation in Investor-State Dispute Settlement Procedures*, OECD Working Papers on International Investment, 2005/01 (OECD 2005) para 10. See also Federico Ortino, 'External Transparency of Investment Awards', Society of International Economic Law (SIEL) Inaugural Conference 2008 Paper, 12 <<http://ssrn.com/abstract=1159899>> accessed 19 March 2015, noting that only 5% of all ICSID decisions rendered between 2003 and 2007 are not publicly available.

¹³See for example *Railroad Development Corporation v Guatemala*, ICSID Case No ARB/07/23; *Pac Rim Cayman LLC v El Salvador*, ICSID Case No ARB/09/12.

¹⁴For example, many of the pleadings, orders and hearings transcripts of NAFTA cases involving the United States as a defendant are on the US Department of State website.

¹⁵See for example US Model BIT (2012), art 29

<<http://www.state.gov/documents/organization/188371.pdf>> accessed 19 March 2015.

¹⁶UNCITRAL, *Rules on Transparency in Treaty-based Investor-State Arbitration* (effective date 1 April 2014). See also United Nations, *Convention on Transparency in Treaty-based Investor-State Arbitration*, adopted by resolution of the General Assembly on 10 December 2014 and opened for signature on 17 March 2015, which constitutes the instrument by which state parties to IIAs concluded before 1 April 2014 can express their consent to apply the UNCITRAL Rules on Transparency in Treaty-based Investor-State Arbitration.

¹⁷See for example Lise Johnson, 'The Transparency Rules and Transparency Convention: A good start and model for broader reform in investor-state arbitration' Columbia FDI Perspectives, No 126,

submissions have been allowed in only a small number of cases has been criticised as has the treatment of *amici* in those cases in which *amicus curiae* submissions were permitted.¹⁸

Overall therefore, it has been argued that investment treaty arbitration as it currently operates does not display the procedural features necessary for its normative production to count as law as, among other features, awards do not have enjoy the force of precedent and quite often go unpublished, because there is no effective device to avoid multiple proceedings in relation to the same dispute and because the manner of appointment of arbitrators brings with it an inherent perception of bias.¹⁹ This perception of pro-investor bias²⁰ in particular is troubling from a host state perspective and also may not be in the long-term interests of investors and, as a result, many commentators have argued that a new international investment court with tenured judges should be established or, alternatively, some form of supervision of arbitral tribunals, either by courts or by an appellate body, should be introduced.²¹

However, while these arguments are quite persuasive (and pervasive), it is important to recognise (and, indeed, it has been explicitly acknowledged)²² that these arguments are based on the premise that international investment law is a

21 July 2014 (noting certain gaps in the coverage of the UNCITRAL Rules on Transparency in Treaty-based Investor-State Arbitration and in the Convention on Transparency in Treaty-based Investor-State Arbitration).

¹⁸Christina Knahr, 'The new rules on participation of non-disputing parties in ICSID arbitration: Blessing or curse?' in Chester Brown and Kate Miles (eds), *Evolution in Investment Treaty Law and Arbitration* (Cambridge University Press, 2011).

¹⁹Thomas Schultz, 'The Concept of Law in Transnational Arbitral Legal Orders and some of its Consequences' (2011) 2 *J Intl Dispute Settlement* 59.

²⁰Generally the issue of bias, real or perceived, has been considered as a pro-investor bias. Given that the respondent host state also appoints one of the arbitrators however, this could conceivably give rise to a real or perceived risk of pro-state bias. However, as investors almost always act as claimant in investment treaty arbitrations and given that the protection of foreign investment is the purpose of the system, the question of pro-investor bias has (rightly or wrongly) been accorded more weight by commentators.

²¹Susan D Franck, 'The Legitimacy Crisis in Investment Arbitration: Privatizing Public International Law Through Inconsistent Decisions' (2005) 73 *Fordham L Rev* 1521, 1617-25; Gus Van Harten, *Investment Treaty Arbitration and Public Law* (OUP 2007); Tomer Broude, 'Principles of Normative Integration and the Allocation of International Authority: The WTO, the Vienna Convention on the Law of Treaties, and the Rio Declaration' (2008) 6 *Loy U Chi Intl L R* 173, 180-81; Jacques Werner, 'Limits of Commercial Investor-State Arbitration: The Need for Appellate Review' in Pierre-Marie Dupuy, Ernst-Ulrich Petersmann and Francesco Francioni (eds), *Human Rights in International Investment Law and Arbitration* (OUP 2009); Aristidis Tsatsos, 'ICSID Jurisprudence: Between Homogeneity and Heterogeneity: A Call for Appeal?' (2009) 6 *Transnational Dispute Management*.

²²See for example Gus Van Harten, *Investment Treaty Arbitration and Public Law* (OUP 2007) chs 3, 6 and 7.

form of public law. However, although this is a view that has become increasingly popular in recent years, the characterisation of international investment law as a form of public law is not universal.²³ Thus, international investment law can also be characterised as an aspect of the bilateral relationship between particular states. Taking this view, IIAs are seen as ‘private’, quasi-contractual, agreements between individual states, under which those states make specific commitments to each other in the hope of gaining a competitive advantage over other states in attracting and retaining foreign direct investment.²⁴ While some proponents of this view accept that IIAs may contribute to the consolidation of already existing rules of custom in international investment law and to the crystallisation of new rules of customary international law in the future, they reject the proposition that IIAs represent the ‘new’ customary international law of investment protection.²⁵ Thus, this view would hold that international investment law is a term used to describe the multitude of individual investment treaties entered into by states and that, in interpreting such treaties, the intentions of the particular state parties to each individual treaty should be paramount.²⁶ Thus, since these treaties are regarded as *quid pro quo* arrangements, the use of arbitration as an adjudication model is not as problematic and, viewed through this lens, provides a depoliticised, neutral forum for dispute resolution much preferable to the ‘gunboat diplomacy’ upon which foreign investors in the past were forced to rely.²⁷

In reality, both of these seemingly contradictory perspectives as to the characterisation of international investment law have some validity as, while on one hand, the particular procedural requirements of each IIA for the initiation of the investor-state dispute settlement process would seem to reflect a specific bargain

²³José Álvarez and Tegan Brink, ‘Revisiting the Necessity Defence: *Continental Casualty v Argentina*’ in Karl P Sauvart (ed), *Yearbook of International Investment Law and Policy 2010-2011* (OUP 2012) 357-58.

²⁴Bernard Kishoiyian, ‘The Utility of Bilateral Investment Treaties in the Formulation of Customary International Law’ (1994) 14 *Nw J Intl L & Bus* 327, 373; Andrew T Guzman, ‘Why LDCs Sign Treaties that Hurt Them: Explaining the Popularity of Bilateral Investment Treaties’ (1997-1998) 38 *Va J Intl L* 640; Patrick Dumberry, ‘Are BITs representing the “New” Customary International Law in International Investment Law?’ (2009) 28 *Penn St Intl L Rev* 675; Benedikt Pirker, *Proportionality Analysis and Models of Judicial Review* (Europa Law Publishing 2013) ch 8.

²⁵*ibid.*

²⁶Jeswald W Salacuse, ‘BIT by BIT’ (1990) 24 *Intl Lawyer* 655, 660; Surya P Subedi, *International Investment Law: Reconciling Policy and Principle* (Hart Publishing 2008) 103.

²⁷See *Banro American Resources, Inc and Société Aurifère du Kivu et du Maniema S.A.R.L. v Congo*, ICSID Case No ARB/98/7, Award 1 September 2000, para 15.

entered into by the contracting states,²⁸ on the other hand, the substantive rights conferred by many treaties explicitly or implicitly rely on general international law or affirm established principles of state responsibility to aliens,²⁹ while also mirroring concepts that appear in domestic administrative law.³⁰ In addition, the subject matter of investment treaty arbitrations range from disputes which touch on core public law concerns (such as the ability of the state to achieve legitimate policy objectives) to disputes which are closer to commercial disputes between private entities. Thus, Maupin describes international investment law as ‘at once neither and both of these things’ and notes that these opposing perspectives as to the characterisation of international investment law are ‘two sides of the same coin, and each shapes and defines the other’.³¹

The ‘public law’ perspective may be more attractive to commentators as it allows one to draw some general conclusions as to the interpretation of IIA provisions and to view international investment law as part of the development of a global administrative law (i.e. law that is concerned with the exercise of public authority by bodies outside the state or by states in ways that reach beyond the state and its law)³² or as part of customary international law.³³ This approach is supported by the fact that IIAs generally do not characterise the obligations which they establish as specific to that particular treaty.³⁴ Furthermore, for historical reasons and due to the inclusion of a MFN clause in most IIAs which encourages uniformity in treaty drafting, it is possible, as a matter of fact, to describe the principal investor protections contained in IIAs, despite increasing variation among investment

²⁸Patrick Dumberry, ‘Are BITs representing the “New” Customary International Law in International Investment Law?’ (2009) 28 Penn St Intl L Rev 675, 687.

²⁹José E Álvarez, ‘A BIT on Custom?’ (2010) 42 N Y Univ J Intl L & Pol 17, 31.

³⁰RH Kreindler, ‘Fair and Equitable Treatment: a Comparative International Law Approach’ (2006) 3 Transnational Dispute Management.

³¹Julie A Maupin, ‘Public and Private in International Investment Law: An Integrated Systems Approach’ (2013-2014) 54 Va J Intl L 367, 435.

³²Benedict Kingsbury and Stephan Schill, ‘Investor-State Arbitration as Governance: Fair and Equitable Treatment, Proportionality and the Emerging Global Administrative Law’ in Albert Jan van den Berg (ed), *50 Years of the New York Convention: ICCA International Arbitration Conference* (Kluwer 2009); Armin von Bogdandy, ‘General Principles of International Public Authority: Sketching a Research Field’ (2008) 9 German L J 1909; Santiago Montt, *State Liability in Investment Treaty Arbitration – Global Constitutional and Administrative Law in the BIT Generation* (OUP 2009); Benedict Kingsbury, ‘“The Concept of Law” in Global Administrative Law’ (2009) 20 Eur J Intl L 23.

³³Andreas F Lowenfeld, ‘Investment Agreements and International Law’ (2003) 42 Colum J Transnational L 123.

³⁴For example, Article 5 of the US Model BIT (2012) (along with many other IIAs) links the FET standard and the full protection and security standard to the customary international law minimum standard of treatment of aliens.

treaties on peripheral issues. The presence of a MFN clause in most IIAs also means that investment treaty arbitration tribunals may have to substitute the substantive rights in the relevant IIA for more favourable provisions from the investor's perspective.³⁵ For example, in *Rumeli v Kazakhstan*³⁶ the FET standard was not present in the applicable BIT between Turkey and Kazakhstan. However, the tribunal used the MFN clause to import the FET standard from the Kazakhstan-UK BIT.³⁷ The presence of a clause that essentially facilitates the importation of rights from one IIA into another somewhat undermines the argument that each investment treaty constitutes an individual quasi-contractual bargain. Overall therefore, one can say that international investment law, as a matter of fact rather than theory, contains some systemic elements in that the majority of IIAs contain broadly similar investor protections. However, beyond this rather limited proposition, the characterisation of international investment law remains a question of perspective.³⁸

Crucially however, although the balancing of public and investor interests in interpreting IIA rights also creates a 'public-private' distinction, this distinction is not necessarily connected to the question of whether international investment law constitutes a system of public law or a set of 'private' agreements between sovereign states, although some commentators have linked the two questions by arguing that the use of proportionality analysis in balancing investor and public interests may contribute to the 'constitutionalisation' and 'judicialisation' of investment law (i.e. may contribute to making it more 'public law' in nature).³⁹ Accordingly, while balancing investor and public interests may seem (and perhaps is) more consonant with the characterisation of international investment law as a

³⁵Yannick Radi, 'The Application of the Most-Favoured-National Clause to the Dispute Settlement Provisions of Bilateral Investment Treaties: Domesticating the 'Trojan Horse'' (2007) 18 Eur J Intl L 757, 773-74.

³⁶ICSID Case No ARB/05/16, Award 29 July 2008.

³⁷ibid, para 575.

³⁸Julie A Maupin, 'Public and Private in International Investment Law: An Integrated Systems Approach' (2013-2014) 54 Va J Intl L 367, 416.

³⁹See for example Ernst-Ulrich Petersmann, 'Constitutional Theories of International Economic Adjudication and Investor-State Arbitration' in Pierre-Marie Dupuy, Ernst-Ulrich Petersmann and Francesco Francioni (eds), *Human Rights in International Investment Law and Arbitration* (OUP 2009); Alec Stone Sweet, 'Investor-State Arbitration: Proportionality's New Frontier' (2010) 4 Law & Ethics of Human Rights 47; Benedict Kingsbury and Stephan W Schill, 'Public Law Concepts to Balance Investors' Rights with State Regulatory Actions in the Public Interest – The Concept of Proportionality' in Stephan W Schill (ed), *International Investment Law and Comparative Public Law* (OUP 2010).

public law system, in fact, different participants in international investment law and arbitration may adopt different combination of perspectives in different situations. Thus, in contentious situations, Mills notes that respondent states are likely to argue in favour of a ‘public-public’ perspective whereas a claimant investor is likely to argue in favour of a ‘private-private’ analysis.⁴⁰ A ‘public-public’ perspective would hold that investment treaty arbitration should be conceived of as part of public law and should be interpreted in a manner that takes account of (public) state regulatory interests whereas a ‘private-private’ analysis would hold that the obligations imposed by IIAs are quasi-contractual in nature and that they should be interpreted in a manner that emphasises the protection of the (private) rights of the investor.⁴¹ This proposition is borne out by examining investment treaty arbitration awards. For example, in *Azurix v Argentina*⁴² Argentina argued that the FET standard should be construed in accordance with the minimum international standard of treatment under customary international law rather than in accordance with the provisions of the relevant BIT which provided that, ‘investment shall at all times be accorded fair and equitable treatment, ...and shall in no case be accorded treatment less than required by international law’⁴³ and further argued that the BIT should be interpreted with due deference to the right of the state to act in the public interest.⁴⁴ In contrast, the claimant investor pointed to the precise text of the FET provision and argued that the comma separating the phrase ‘fair and equitable treatment’ from the phrase ‘treatment required by international law’ suggested that the latter was intended to be a self-contained standard, independent of the former.⁴⁵ The claimant investor further argued, by reference to the treaty’s preamble, that the contracting states to the BIT had entered into the treaty with the aim of stimulating investment and that the tribunal should be mindful of this objective in interpreting the treaty, thereby urging the tribunal to interpret the investor’s rights in an expansive manner.⁴⁶

⁴⁰Alex Mills, ‘Antinomies of Public and Private at the Foundations of International Investment Law and Arbitration’ (2011) 14 J Intl Economic L 469, 499-500.

⁴¹*ibid.*

⁴²ICSID Case No ARB/01/12, Award 14 July 2006.

⁴³*ibid.*, paras 324-40.

⁴⁴*ibid.*, para 291.

⁴⁵*ibid.*, para 326.

⁴⁶*ibid.*, para 307.

However, ‘public-private’ and ‘private-public’ perspectives have also manifested themselves in academic commentary and in investment treaty arbitration awards, although such perspectives can be considered more likely to come into play when an IIA is being analysed outside the context of a dispute.⁴⁷ Thus, a ‘public-private’ perspective would hold that international investment law should be viewed as an emerging system of public law but that it should consist of strong standards of protection, in order to protect investors’ interests and to liberate investors from state regulatory control. This view is consonant with the belief that foreign investment is likely to lead to economic growth and to improvements in host state governance and so should be robustly protected.⁴⁸ On the other hand, those who are more concerned with the ability of states to regulate in the public interest and to act freely are more likely to adopt a ‘private–public’ perspective. Thus, the ‘private’ nature of individually negotiated treaties is emphasised to demonstrate that, in accordance with state sovereignty, investment standards should only be applicable where a state has specifically given its consent to such a standard. However, advocates of this perspective would simultaneously argue that standards of protection should allow states the ability to regulate in the public interest, in circumstances where the extent to which a state has ceded regulatory sovereignty is unclear.⁴⁹

Thus, the aim of the remainder of this chapter is to argue that, regardless of whether one characterises international investment law as a form of public law or whether one views each IIA as a ‘private’, quasi-contractual arrangement between sovereign states, investment treaty arbitration tribunals should, in either case, take account of public interest considerations in appropriate circumstances. In accordance with the above analysis, the answer reached will be a matter of perspective. However, the aim is to explain the reasons why this perspective is a valid one.

2.3 *The open ended nature of IIA rights*

⁴⁷Alex Mills, ‘Antinomies of Public and Private at the Foundations of International Investment Law and Arbitration’ (2011) 14 J Intl Economic L 469, 500-503.

⁴⁸*International Thunderbird Gaming Corporation v Mexico*, UNCITRAL, Separate Opinion of Thomas Wälde December 2005, paras 4-16; Charles H Brower II, ‘Corporations as Plaintiffs Under International Law: The Quest for Narratives about Investment Treaties’ (2011) 9 Santa Clara J Intl L 179.

⁴⁹*SGS v Pakistan*, ICSID Case No ARB/01/13, Decision of the Tribunal on Objections to Jurisdiction 6 August 2003, paras 167-172.

Before considering the reasons why investment treaty arbitration tribunals should take account of public interest considerations, the question of whether such tribunals have the ability to take account of such considerations must be examined. In this regard, the merits stage is the first point at which the interaction between investor interests and public interests can directly and explicitly be considered as, while the manner in which ‘investment’ and ‘investor’ are defined and the approach of investment treaty arbitration tribunals towards the question of jurisdiction are important from a public interest perspective,⁵⁰ these issues do not directly go to the key concern of interference with the ability of sovereign states to regulate.⁵¹ Turning therefore to the merits stage of the arbitral process, much has been written about the potential for the principal substantive rights conferred by IIAs to be interpreted in a broad and investor-friendly manner.⁵² However, the fact that such rights are generally open-ended in nature may conversely also provide investment treaty arbitration tribunals with the opportunity and ability to take account of public interest considerations. The principal substantive rights conferred by IIAs will now be examined in order to demonstrate their open-ended nature and the wide-ranging interpretative discretion accorded to investment treaty arbitration tribunals as a result.⁵³

(a) *The expropriation clause*

Expropriation clauses prohibit the expropriation or nationalisation of the foreign investor’s investment without the payment of compensation. Thus, the notion of expropriation is not primarily concerned with proscribing governmental behaviour but rather with ensuring that compensation is provided. Beyond this basic concept

⁵⁰Marek Jeżewski, ‘Development Considerations in Defining Investment’ in Marie-Claire Cordonier Segger, Markus W Gehring and Andrew Newcombe (eds), *Sustainable Development in World Investment Law* (Kluwer 2011); Filip Balcerzak, ‘Jurisdiction of Tribunals in Investor-State Arbitration and the Issue of Human Rights’ (2014) 29 ICSID Rev 216.

⁵¹*ibid*, 233-34.

⁵²See for example Rudolf Dolzer, ‘The Impact of International Investment Treaties on Domestic Administrative Law’ (2006) 38 NYU J Intl L & Pol 953.

⁵³For this purpose, prohibitions on performance requirements such as those contained in Article 1106(1) of NAFTA will not be considered as they do not confer a positive right on investors. Similarly, admission clauses which extend certain substantive treaty rights such as MFN commitments to the pre-establishment stage are not considered as the same interpretative issues apply in respect of the pre-establishment stage and, as yet, there have been no published instances of disputes arising under the minority of IIAs based on the ‘pre-establishment’ model: see Zachary Douglas, *The International Law of Investment Claims* (Cambridge University Press 2009) 141. See also Gus Van Harten, *Investment Treaty Arbitration and Public Law* (OUP 2007) 84.

however there are many uncertainties associated with expropriation clauses as the term ‘expropriation’ is generally not defined in IIAs. First, most expropriation clauses cover both direct and indirect expropriation. Terminology such as ‘measures tantamount to nationalisation or expropriation’⁵⁴ or ‘measures having an effect equivalent to expropriation’⁵⁵ is also frequently used, meaning that measures which have the same effect as a physical expropriation but which accomplish this in a less direct manner are also caught by the prohibition. While it is clear that a direct expropriation occurs where an investment is nationalised or otherwise expropriated through formal transfer of title or outright physical seizure, this type of expropriation is no longer as common and the meaning of indirect expropriation or of related concepts such as ‘measures tantamount to expropriation’ is less straightforward. The indirect expropriation concept is intended to apply where the state interferes in the use of property or with the enjoyment of the benefits associated with property even where the property is not seized and the legal title to the property is not affected.

Thus, examples of acts, which on their own or in combination with other acts, could amount to indirect expropriation include denial of judicial access,⁵⁶ substantial interference with the management or control of a business enterprise,⁵⁷ the imposition of taxes that are confiscatory in magnitude,⁵⁸ government-organised boycotts or the creation by the government of a monopoly for itself or another supplier, thereby forcing the foreign investor’s company out of business. Contractual rights can also be expropriated by host states, where the measure is taken in exercise of that state’s sovereign powers.⁵⁹ Even if one activity on its own is not enough to constitute expropriation, a cumulative series of regulatory acts or omissions, which may be interspersed with lawful state regulatory actions, may be

⁵⁴See for example Agreement between the People's Republic of China and the Federal Republic of Germany on the Encouragement and Reciprocal Protection of Investments, signed 1 December 2003, entered into force 11 November 2005, art 4.

⁵⁵See for example Agreement between the Government of Canada and the Government of the Republic of Costa Rica for the Promotion and Protection of Investments, signed 18 March 1998, entered into force 29 September 1999, art VIII.

⁵⁶*Waste Management, Inc. v Mexico*, ICSID Case No ARB/(AF)/00/3, Dissenting Opinion of Keith Hight 2 June 2000, paras 17-18.

⁵⁷*Benvenuti & Bonfant v Congo*, ICSID Case No ARB/77/2, Final Award 8 August 1980.

⁵⁸Thomas Wälde and Abba Kolo, ‘Confiscatory Taxation under Customary International Law and Modern Investment Treaties’ (1999) 4 CEPMLP Internet J 17.

⁵⁹*SPP v Egypt*, ICSID Case No ARB/84/3, Award on Merits 20 May 1992, paras 164-65; *Saipem SpA v Bangladesh*, ICSID Case No. ARB/05/07, Award 20 June 2009, para 129.

held to meet the threshold, thereby constituting a creeping expropriation.⁶⁰ For example, a creeping expropriation could occur if the host state government first blocked employee access to the foreign investor's plant, then took over a key supplier of the foreign investor's company and subsequently refused to supply it.⁶¹ The most controversial aspect of the indirect expropriation concept is that regulatory measures which adversely affect the investment could potentially also be held to constitute indirect expropriation. The reasoning behind this may be that many policies requiring what used to be a clear-cut taking of tangible property are now being operated by 'regulation' and so should be caught by the expropriation clause.⁶² However, it may be difficult to distinguish between an indirect expropriation and a legitimate and non-compensable regulatory measure taken by the host state in furtherance of social or environmental goals.⁶³ This is potentially problematic as a state's right to regulate is the closest approximation of the obligation to protect and promote human rights and if host state regulation is covered by the indirect expropriation concept, the state's ability to fulfil its human rights obligation could be undermined. For example, if the government introduced price freezes in relation to the provision of water by private enterprises based on its citizens' right to water, this could be challenged as constituting an indirect expropriation.⁶⁴ In fact, quite a number of investment treaty arbitrations have centred on disputes relating to the provision of essential services such as water, gas or electricity supply or waste management services by private entities.⁶⁵ Similarly,

⁶⁰*Generation Ukraine Inc. v Ukraine*, ICSID Case No ARB/00/9, Award 16 September 2003, para 20.22.

⁶¹V R Koven, 'Expropriation and the "Jurisprudence" of OPIC' (1981) 22 Harv Intl L J 269, 291.

⁶²Thomas Wälde and Abba Kolo, 'Environmental Regulation, Investment Protection and 'Regulatory Taking' in International Law' (2001) 50 ICLQ 811, 813.

⁶³The Dominican Republic-Central America-United States Free Trade Agreement is unusual in providing some criteria for determining whether government action constitutes indirect expropriation. Annex 10-C(4)(a) provides that the determination 'requires a case-by-case, fact-based inquiry' in which the tribunal must consider: (i) the economic impact of the government action, although the fact that an action or series of actions by a Party has an adverse effect on the economic value of an investment, standing alone, does not establish that an indirect expropriation has occurred; (ii) the extent to which the government action interferes with distinct, reasonable investment-backed expectations; and (iii) the character of the government action. Finally, the text makes an explicit exception for government regulatory actions 'designed and applied to protect legitimate public welfare objectives, such as public health, safety and the environment': see Dominican Republic-Central America-United States Free Trade Agreement, signed 28 November 1998, entered into force 3 September 2002.

⁶⁴These issues were relevant in the cases of *Suez*, *Sociedad General de Aguas de Barcelona S.A. and Vivendi Universal v Argentina*, ICSID Case No ARB/03/19 and *Aguas del Tunari SA v Bolivia*, ICSID Case No ARB/02/3.

⁶⁵ICSID, *The ICSID Case Load: Statistics (Issue 2014-2)*, 12.

it has been suggested that a government's decision to issue a compulsory license for a patent-protected drug to allow that drug to be produced by a generic manufacturer at a lower price so as to provide increased access to that drug could be challenged as constituting an expropriation of intellectual property.⁶⁶

Investment treaty arbitration tribunals must therefore address the complex question of the extent to which a government may affect the value of investor property by regulation, whether of a general nature or by specific actions in the context of a general regulatory framework, for a legitimate public purpose without effecting an expropriation and having to compensate the investor. In practice, three different approaches to this question can be identified in the jurisprudence. First, some tribunals have looked only at the effect of the measure on the investment in determining whether an expropriation occurred (the controversial 'sole effect' doctrine). The prime example of this occurred in *Metalclad Corporation v Mexico*⁶⁷ in which the establishment of an ecological protection zone was held to amount to expropriation. In that case the tribunal decided that the motivation and intent behind the government measure in question was irrelevant and that what is required to establish an expropriation is 'interference with the use of property which has the effect of depriving the owner, in whole or in significant part, of the use or reasonably-to-be-expected economic benefit of property even if not necessarily to the obvious benefit of the host State'.⁶⁸ This approach is problematic when applied to indirect expropriations as it does not differentiate between *mala fide* discriminatory takings in breach of due process and non-discriminatory measures introduced for a *bona fide* public purpose as the degree of interference with the investor's property may be the same in each case.⁶⁹ In addition, the focus on 'deprivation' in determining the existence of internationally proscribed host state

⁶⁶See Merck & Co Inc, 'Statement on Brazilian government's decision to issue compulsory license for STOCRIN' (4 May 2007) quoted in Henning Grosse Ruse-Khan, 'Protecting intellectual property rights under BITs, FTAs and TRIPS: Conflicting regimes or mutual coherence?' in Chester Brown and Kate Miles (eds), *Evolution in Investment Treaty Law and Practice* (Cambridge University Press 2011) 496-97. Some IIAs contain a provision clarifying that the issuance of compulsory licences in relation to intellectual property rights, to the extent that such issuance is consistent with international agreements regarding intellectual property rights, does not constitute expropriation: see for example Agreement Between the Government of Canada and the Government of the People's Republic of China for the Promotion and Reciprocal Protection of Investments, signed 9 September 2012, entered 1 October 2014, art 10(2).

⁶⁷ICSID Case No ARB(AF)/97/1, Award 30 August 2000.

⁶⁸*ibid*, para 103.

⁶⁹Alexis Martinez, 'Invoking State Defenses in Investment Treaty Arbitration' in Michael Waibel and others (eds), *The Backlash against Investment Arbitration: Perceptions and Reality* (Kluwer 2010) 315-37.

conduct renders the test liable to a potentially very broad interpretation as the concept of ‘deprivation’ is relative and can be easily circumvented by, for example, presenting an investment as consisting of several components, with each of these components possessing an economic value.⁷⁰

However, while the ‘sole effect’ doctrine has been applied by tribunals in a number of cases,⁷¹ the open-ended nature of most expropriation clauses allows for different interpretations. Thus, at the other end of the spectrum, some tribunals have excluded non-discriminatory *bona fide* regulations from the scope of the expropriation clause entirely. Thus, in *Methanex Corporation v United States*,⁷² the tribunal stated that:

As a matter of general international law, a non-discriminatory regulation for a public purpose, which is enacted in accordance with due process and, which affects, inter alios, a foreign investor or investment is not deemed expropriatory and compensable unless specific commitments had been given by the regulating government to the then putative foreign investor contemplating investment that the government would refrain from such regulation.⁷³

This approach accords with the view that ‘police powers’ should be exempted automatically from any duty of expropriation and has been echoed, to some extent, in the text of the US Model BIT and in recent Canadian BITs.⁷⁴ ‘Police powers’ is the international law term used to describe non-discriminatory regulatory measures introduced by a state to protect or enhance the public welfare, which traditionally

⁷⁰Mavluda Sattorova, ‘Investment Treaty Breach as Internationally Proscribed Conduct: Shifting Scope, Evolving Objectives, Recalibrated Remedies?’ (2012) 4 Trade L & Dev 315.

⁷¹*Pope & Talbot Inc v Canada*, UNCITRAL, Interim Award 26 June 2000, para 102; *Enron Corporation and Ponderosa Assets, LP v Argentina*, ICSID Case No ARB/01/3, Award 22 May 2007, para 245; *Corn Products International Inc v Mexico*, ICSID Case No ARB(AF)/04/1, Decision on Responsibility 15 January 2008, para 92; *BG Group plc v Argentina*, UNCITRAL, Award 24 December 2008, paras 270-71.

⁷²UNCITRAL, Final Award of the Tribunal on Jurisdiction and Merits 3 August 2005.

⁷³*ibid*, pt IV, ch D, 4.

⁷⁴US Model BIT (2012), art 6 and annex 2, para 4(b); Agreement between the Government of Canada and the Government of the United Republic of Tanzania for the Promotion and Reciprocal Protection of Investments, signed 17 May 2013, entered into force 9 December 2013, art 10(5); Agreement between Canada and the State of Kuwait for the Promotion and Protection of Investments, signed 26 September 2011, entered into force 19 February 2014, art 10(7); Agreement Between the Government of Canada and the Government of the People’s Republic of China for the Promotion and Reciprocal Protection of Investments, signed 9 September 2012, entered 1 October 2014, annex B.10(3). For a critique of the approach taken in these BITs see Martin Papatrakis, ‘Regulatory Expropriation and Sustainable Development’ in Marie-Claire Cordonier Segger, Markus W Gehring and Andrew Newcombe (eds), *Sustainable Development in World Investment Law* (Kluwer 2011) 321-22.

encompasses measures taken to protect, *inter alia*, public health, safety or morals.⁷⁵ The exact scope of the ‘police powers’ doctrine is unclear however⁷⁶ and the number of expropriation cases in which this approach has been applied to date remains relatively small.⁷⁷

Finally, in between these two approaches is an approach which involves balancing the public interest protected by the impugned measure against the effect of the measure on the investment in order to determine whether an expropriation has occurred, which will be considered further in the following chapter. However, none of these three approaches is currently prevailing and it is difficult to predict how a tribunal will approach the issue of indirect expropriation.⁷⁸ Although this lack of consistency is problematic in itself (and while the *de facto* system of precedent which is emerging in investment treaty arbitration could potentially consolidate the position of the controversial ‘sole effect’ doctrine), on the other hand the fact that the latter two approaches can permissibly be taken by tribunals does indicate the open-ended nature of the expropriation clause and the potential scope for tribunals to take account of public interest considerations in interpreting the clause.

(b) *The FET standard*

The FET standard is contained in most IIAs⁷⁹ and has existed as a concept of international economic law at least since the 1919 Covenant of the League of

⁷⁵UNCTAD, *Expropriation: UNCTAD Series on Issues in International Investment Agreements II* (UNCTAD 2012) 79-90.

⁷⁶For example, it is unclear to what extent (all) human rights form part of the concept of ‘police powers’. Indeed, from the viewpoint of human rights law, the wording ‘police powers’ may signify a particular connotation with civil and political rights: Jasper Krommendijk and John Morijn, ‘Proportional by What Measure(s)? Balancing Investor Interests and Human Rights by Way of Applying the Proportionality Principle in Investor-State Arbitration’ in Pierre-Marie Dupuy, Ernst-Ulrich Petersmann and Francesco Francioni (eds), *Human Rights in International Investment Law and Arbitration* (OUP 2009) 435.

⁷⁷For criticism of this approach see Tra T Pham, ‘International investment treaties and arbitration as imbalanced instruments: a re-visit’ (2010) *Intl Arbitration L Rev* 81.

⁷⁸Markus Perkams, ‘The Concept of Indirect Expropriation in Comparative Public Law – Searching for Light in the Dark’ in Stephan W Schill (ed), *International Investment Law and Comparative Public Law* (OUP 2010) 110.

⁷⁹A study conducted by Knoll-Tudor reviewed 358 BITs and of these only 19 did not mention the FET standard either in their preambles or in the body of the treaty: Ioana Knoll-Tudor, ‘The Fair and Equitable Treatment Standard and Human Rights Norms’ in Pierre-Marie Dupuy, Ernst-Ulrich Petersmann and Francesco Francioni (eds), *Human Rights in International Investment Law and Arbitration* (OUP 2009) 312.

Nations.⁸⁰ The precise meaning of the concept depends on the specific wording of each treaty, as well as the context of the treaty and its negotiating history. The US-Mexico Mixed Claims Commission in the 1926 *Neer* case⁸¹ set out the customary international law standard at that time by stating that a state has breached the fair and equitable treatment obligation when the conduct of the state could be qualified as outrageous, egregious or in bad faith or so below international standards that a reasonable and impartial person would easily recognise it as such. There is an ongoing debate as to whether the FET standard is limited to the international minimum standard of customary international law or whether it is to be constructed independently as a self-contained standard.⁸² The text of the relevant IIA can be determinative in this regard as some IIAs explicitly state that the concept of fair and equitable treatment does not require treatment in addition to, or beyond that, required by the international law minimum standard.⁸³ In practice, there may not be much difference between the two approaches when applied to the specific facts of a case as the international minimum standard is as indeterminate as the FET standard.⁸⁴

It is only in recent years that some shape has been given to the FET standard by investment treaty arbitration tribunals. For many years it was thought that the FET standard could encompass any claims that could not be qualified in a more specific manner, due to the deceptively simple wording used. However, nowadays the FET standard is associated with a number of specific situations, although in future other

⁸⁰Theodore Kill, 'Don't Cross the Streams: Past and Present Overstatement of Customary International Law in Connection with Conventional Fair and Equitable Treatment Obligations' (2007-2008) 106 Mich L Rev 853, 870.

⁸¹*LFH Neer and Pauline Neer (USA) v United Mexican States* (15 October 1926), United Nations, Reports of International Arbitral Awards, 1926, vol IV, 60-66.

⁸²Rudolf Dolzer and Christoph Schreuer, *Principles of International Investment Law* (OUP 2008) 124-30; Katia Yannaca-Small, 'Fair and Equitable Treatment Standard: Recent Developments' in August Reinisch (ed), *Standards of Investment Protection* (OUP 2008) 113-18; Santiago Montt, *State Liability in Investment Treaty Arbitration: Global Constitutional and Administrative Law in the BIT Generation* (Hart Publishing 2009) 298-310.

⁸³See for example Treaty between the United States of America and the Oriental Republic of Uruguay Concerning the Encouragement and Reciprocal Protection of Investment, signed 4 November 2005, entered into force 1 November 2006, art 5.

⁸⁴*Saluka Investments BV v Czech Republic*, UNCITRAL, Partial Award 17 March 2006, para 291; Stephan W Schill, 'Fair and Equitable Treatment, The Rule of Law, and Comparative Public Law' in Stephan W Schill (ed), *International Investment Law and Comparative Public Law* (OUP 2010) 152-54.

scenarios may also be covered.⁸⁵ The cases that consider the FET standard can be divided into two broad categories: the first concerning treatment of investors by the courts of the host state and the second dealing with administrative decision-making. The second category comprises the majority of cases since IIAs generally do not require the exhaustion of local remedies (although recourse to national courts or arbitral tribunals may be mandated under a concession contract concluded with the state or a state agency).⁸⁶ Overall, the FET standard gives expression to a general principle of due process in its application to the treatment of investors: it is concerned primarily with the process of decision-making in the host state, rather than with the prescription of substantive outcomes.⁸⁷ Thus, where the state fails in its obligation of vigilance and protection as regards foreign investment, its responsibility will be engaged. This obligation of vigilance has been considered to be a standard deriving from customary international law.⁸⁸ In such cases the FET standard is considered in conjunction with the guarantee of full protection and security which may be included in IIAs as a separate obligation or which may be contained in the same paragraph as the FET standard.⁸⁹ Similarly, where coercion or harassment by the organs of the host state can be proven, the host state may be held in breach of the FET standard.⁹⁰ Failure to implement or enforce national laws can, in certain contexts, give rise to a breach of the FET standard⁹¹ as can an absence of transparency in host state procedures or arbitrary or discriminatory treatment of the claimant investor by the host state.⁹² Bad faith on the part of host state organs can also in certain situations be sufficient ground to recognise a breach

⁸⁵Ioana Knoll-Tudor, 'The Fair and Equitable Treatment Standard and Human Rights Norms' in Pierre-Marie Dupuy, Ernst-Ulrich Petersmann and Francesco Francioni (eds), *Human Rights in International Investment Law and Arbitration* (OUP 2009) 310.

⁸⁶Campbell McLachlan, Laurence Shore and Matthew Weiniger, *Investment Treaty Arbitration: Substantive Principles* (OUP 2007) 226.

⁸⁷Due process has been defined as 'conduct of legal proceedings according to established rules and principles for the protection and enforcement of private rights': Bryan A Garner (ed), *Black's Law Dictionary* (8th edn, West Group 2004).

⁸⁸*Asian Agricultural Products Limited v Sri Lanka*, ICSID Case No ARB/87/3, 4 ISCID Rep 245, Opinion of Judge Asante, para 639.

⁸⁹See for example Treaty between the United States of America and the Argentine Republic Concerning the Reciprocal Encouragement and Protection of Investment, signed 14 November 1991, entered into force 20 October 1994, art II(2)(a).

⁹⁰Ioana Knoll-Tudor, 'The Fair and Equitable Treatment Standard and Human Rights Norms' in Pierre-Marie Dupuy, Ernst-Ulrich Petersmann and Francesco Francioni (eds), *Human Rights in International Investment Law and Arbitration* (OUP 2009) 329.

⁹¹*GAMI Investments Inc. v Mexico*, UNCITRAL, Final Award 15 November 2004, para 91.

⁹²*Tecnicas Medioambientales Tecmed SA v Mexico*, ICSID Case No ARB(AF)/99/2, Award 29 May 2003, para 154.

of the FET standard although usually it is an additional element to a substantive obligation and is not considered to be a prerequisite to finding that the FET standard has been breached.⁹³

However, perhaps the most important grounds for a finding of breach of the FET standard are where there has been either a denial of justice or where the investor's legitimate expectations have been frustrated. Different views as to the scope of the denial of justice concept have been taken by both scholars and international tribunals ranging from the narrowest view that the term applies only to a refusal to grant access to, or hearing in, a court, or a refusal of a court to pronounce a definite, just sentence, to a broader view that it applies to most acts of the judiciary, to an even broader view that the term encompasses any failure of local remedies and all internationally illegal acts by any branch of government connected with the administration of justice.⁹⁴ Case law to date in the sphere of investment treaty arbitration would seem to indicate that a state will not be held responsible for a breach of international law constituted by a lower court's decision when there was an available, effective and adequate appeal within the state's legal system,⁹⁵ although considerable uncertainty exists on this point.⁹⁶

The legitimate expectations principle is the only part of the FET standard which is not well grounded in customary international law.⁹⁷ However, in *Saluka v Czech Republic* the tribunal referred to the concept as the 'dominant element of that [FET] standard'.⁹⁸ Investment treaty arbitration tribunals have also taken markedly

⁹³Ioana Knoll-Tudor, 'The Fair and Equitable Treatment Standard and Human Rights Norms' in Pierre-Marie Dupuy, Ernst-Ulrich Petersmann and Francesco Francioni (eds), *Human Rights in International Investment Law and Arbitration* (OUP 2009) 321-34.

⁹⁴Gerald Fitzmaurice, 'The Meaning of the Term Denial of Justice' (1932) 13 *British YB Intl L* 93; Dinah Shelton, *Remedies in International Human Rights Law* (2nd edn, OUP 2005) 61.

⁹⁵*Loewen Group Inc & Raymond L Loewen v United States of America*, ICSID Case No ARB(AF)/98/3, Final Award 26 June 2003, para 154; *Generation Ukraine Inc. v Ukraine*, ICSID Case No ARB/00/9, Award 16 September 2003, para 20.30.

⁹⁶The comments in *Loewen* as to the relationship between judicial failure and the local remedies rule were *obiter dicta*. The *Loewen Group* lost on the ground that the company ceased to maintain the continuous nationality needed to maintain an international claim under NAFTA. See also George K Foster, 'Striking a Balance Between Investor Protections and National Sovereignty: The Relevance of Local Remedies in Investment Treaty Arbitration' (2011) 49 *Colum J Transnational L* 201.

⁹⁷The inclusion of the legitimate expectations ground under the FET standard has been criticised by some arbitrators: see *Suez, Sociedad General de Aguas de Barcelona S.A. and Vivendi Universal v Argentina*, ICSID Case No ARB/03/19, Separate Opinion of Arbitrator Pedro Nikken 30 July 2010, para 23; cf Elizabeth Snodgrass, 'Protecting Investors' Legitimate Expectations: Recognizing and Delimiting a General Principle' (2006) 21 *ICSID Rev 1* arguing that the protection for investors' legitimate expectations can be justified as reflecting a 'general principle of law recognised by civilised nations'.

⁹⁸*Saluka Investments BV v Czech Republic*, UNCITRAL, Partial Award 17 March 2006, para 302.

different views on the range of expectations that might potentially qualify as legitimate expectations.⁹⁹ Thus, the narrowest interpretation seems to require that an expectation be based on specific legal entitlements vested in a foreign investor under the law of the host state.¹⁰⁰ A second, broader, view is that a legitimate expectation does not need to be based on legal rights but must be based on specific, unilateral representations made by a government official.¹⁰¹ A third group of decisions suggests that an investor may legitimately expect the regulatory regime in place at the time of the investment to remain in force, even if the government has not promised to retain the regulatory regime and the investor has no legal rights under domestic law to its continuance.¹⁰² Finally, in some cases, the investor has succeeded on the basis of breach of legitimate expectations, despite the identified expectation having no basis in the legal rights of the claimant under domestic law, or in representations made by the host state or the regulatory arrangements in place at the time the investment was made.¹⁰³

Overall therefore, the content of the FET standard is difficult to explain without reference to factual situations¹⁰⁴ since the concepts involved are so interlinked and are broad enough to allow arbitrators to consider a wider range of elements than other standards of treatment.¹⁰⁵ Furthermore, the vast majority of IIAs do not contain any exceptions or derogations limiting the applicability of the FET standard. Thus, the vagueness and broad-ranging nature of the FET standard is such that it ‘goes beyond commonplace assertions in legal theory that law is inherently vague and indeterminative’.¹⁰⁶ This is because the traditional methods of treaty

⁹⁹Michele Potestà, ‘Legitimate Expectations in investment treaty law: Understanding the roots and limits of a controversial concept’ (2013) 28 ICSID Rev 88.

¹⁰⁰*EDF (Services) Limited v Romania*, ICSID Case No ARB/05/13, Award and Dissenting Opinion 8 October 2009, para 217.

¹⁰¹*International Thunderbird Gaming v Mexico*, UNCITRAL, Award 26 January 2006, para 147-67; *Duke Energy v Ecuador*, ICSID Case No ARB/04/19, Award 18 August 2008, para 340; *National Grid v Argentina*, UNCITRAL, Award 3 November 2008, paras 173-79.

¹⁰²*CME v Czech Republic*, UNCITRAL, Partial Award 13 September 2001, para 611; *Enron Corporation Ponderosa Assets, L.P. v. Argentina*, ICSID Case No ARB/01/3, Award 22 May 2007, paras 266-67.

¹⁰³*Walter Bau AG v Thailand*, UNCITRAL, Award 1 July 2009, para 12.

¹⁰⁴*Mondev International Ltd. v United States of America*, ICSID Case No ARB(AF)/99/2, Award 11 October 2002, para 118; *Waste Management, Inc. v Mexico (No 2)*, ICSID Case No ARB(AF)/00/3, Final Award 30 April 2004, para 99.

¹⁰⁵Alec Stone Sweet and Florian Grisel, ‘Transnational Investment Arbitration: From Delegation to Constitutionalization?’ in Pierre-Marie Dupuy, Ernst-Ulrich Petersmann and Francesco Francioni (eds), *Human Rights in International Investment Law and Arbitration* (OUP 2009) 130.

¹⁰⁶Stephan W Schill, *The Multilateralization of International Investment Law* (Cambridge University Press 2009) 263.

interpretation are relatively ineffective in clarifying the meaning of the FET standard and so tribunals have not followed a uniform methodology in interpreting the standard. Thus, some tribunals have merely described the facts of the case and then characterised them as a violation of the FET standard.¹⁰⁷ Other tribunals have merely posited a particular set of requirements as part of FET and subsequently subsumed the facts of the case under this standard.¹⁰⁸ For example, in *Tecmed v Mexico* the FET standard was elucidated as follows:

this provision of the Agreement...requires the Contracting Parties to provide to international investments treatment that does not affect the basic expectations that were taken into account by the foreign investor to make the investment. The foreign investor expects the host State to act in a consistent manner, free from ambiguity and totally transparently in its relations with the foreign investor so that it may know beforehand any and all rules and regulations that will govern its investments, as well as the goals of the relevant policies and administrative practices or directives, to be able to plan its investment and comply with such regulations.¹⁰⁹

This statement broadens the obligation of transparency from the availability of host state rules and regulations to the availability of the goals of host state rules and regulations. Moreover, the notion that an investor, prior to investing, should be entitled to know ‘any and all rules’ applied to its investments introduces a high degree of rigidity, whereby governments cannot change the rules to respond to domestic pressures or changed circumstances.¹¹⁰ This elucidation of the FET standard is now frequently cited by tribunals as the principal authority for the

¹⁰⁷See *Eastern Sugar BV v Czech Republic*, SCC Case No 88/2004, Partial Award 27 March 2007 in which the tribunal extensively recounted the facts relevant to the alleged FET breach in over 100 paragraphs before finding a breach without clearly identifying the standard’s legal meaning and normative content.

¹⁰⁸Kingsbury and Schill note that some awards ‘not only endorse but perhaps even celebrate a broad *ex post facto* “I know it when I see it” control of host State conduct’: Benedict Kingsbury and Stephan Schill, ‘Investor-State Arbitration as Governance: Fair and Equitable Treatment, Proportionality and the Emerging Global Administrative Law’ in Albert Jan van den Berg (ed), *50 Years of the New York Convention: ICCA International Arbitration Conference* (Kluwer 2009) 27.

¹⁰⁹*Tecnicas Medioambientales Tecmed SA v Mexico*, ICSID Case No ARB(AF)/99/2, Award 29 May 2003, para 154.

¹¹⁰Asha Kaushal, ‘Revisiting History: How the Past Matters for the Present Backlash Against the Foreign Investment Regime’ (2009) 50 *Harv Intl L J* 491, 527-28. See also Zachary Douglas, ‘Nothing if not critical for investment treaty arbitration: *Occidental, Eureka and Methanex*’ (2006) 26 *Arbitration Intl* 27, 28.

requirements of the FET standard,¹¹¹ despite the fact that it failed to establish a clear normative content for the FET standard.¹¹²

Thus, due to its inherent flexibility, the FET standard has, in practice, become a ‘master tool’ for dealing with investment disputes and breach of the standard is accordingly the most common allegation made by foreign investors before investment tribunals as well as being the most common successful basis for a claim.¹¹³ The tribunal in *Suez and Vivendi v Argentina* went so far as to state that ‘it is no exaggeration to say that the obligation of a host state to accord fair and equitable treatment to foreign investors is the *Grundnorm* or basic norm of international investment law’.¹¹⁴

(c) *The guarantee of full protection and security*

The guarantee of full protection and security is often contained in the same clause as the FET standard. For example, Article 5(1) of the US Model BIT provides that ‘Each Party shall accord to covered investments treatment in accordance with customary international law, including fair and equitable treatment and full protection and security.’¹¹⁵ The full protection and security guarantee is concerned with failures on the part of the host state to protect the investor’s property from actual damage caused either by miscreant state officials or by others, where the state has failed to exercise due diligence. The cases in which it has figured as the principal cause of action have concerned damage or injury to persons and property during internal armed conflict, riots and acts of violence. Such circumstances are

¹¹¹See for example *MTD Equity Sdn. Bhd. & MTD Chile S.A. v. Chile*, ICSID Case No ARB/01/7, Award 25 May 2004, para 114.

¹¹²International Law Association German Branch/Working Group, ‘General Public International Law and International Investment Law – A Research Sketch on Selected Issues’ 11-12 <<http://telc.jura.uni-halle.de/sites/default/files/BeitraegeTWR/Heft%20105.pdf>> accessed 19 March 2015.

¹¹³Surya P Subedi, *International Investment Law: Reconciling Policy and Principle* (Hart Publishing 2008) 63.

¹¹⁴ICSID Case No ARB/03/19, Decision on Liability 30 July 2010, para 188. See also *International Thunderbird Gaming Corporation v Mexico*, UNCITRAL, Separate Opinion of Thomas Wälde December 2005, para 37.

¹¹⁵See also Treaty between the United States of America and the Argentine Republic Concerning the Reciprocal Encouragement and Protection of Investment, signed 14 November 1991, entered into force 20 October 1994, art II(2)(a). Alternatively, the full protection and security standard is sometimes included in the provision regarding compensation for expropriation: see German Model BIT (2008), art 4.

usually provided for in specific provisions in IIAs¹¹⁶ as well as falling under the general full protection and security standard and a number of IIAs also state that what is required under the full protection and security guarantee is the level of police protection required under customary international law.¹¹⁷ However, in recent years, the question of whether the full protection and security guarantee extends beyond physical security to encompass regulatory and legal security has been raised.¹¹⁸ Some tribunals have accepted this extension of the concept,¹¹⁹ while others has proven reluctant to embrace this approach stating that this interpretation would equate the standard with the FET standard. For example, in *Suez and Vivendi v Argentina*,¹²⁰ the tribunal observed as follows in relation to the FET and full protection and security standards:

in interpreting these two standards of investor treatment it is desirable to give effect to [the] intention [of the Contracting Parties] by giving the two concepts distinct meanings and fields of application. In this respect, this Tribunal is of the view that the stability of the business environment and legal security are more characteristic of the standard of fair and equitable treatment, while the full protection and security standard primarily seeks to protect investment from physical harm.¹²¹

While some IIAs provide that the concepts of FET and full protection and security do not require treatment beyond that which is required by the customary international law minimum standard of treatment of aliens,¹²² given the uncertainty as to the parameters of the customary international law minimum standard, there

¹¹⁶See for example Treaty between the United States of America and the Argentine Republic Concerning the Reciprocal Encouragement and Protection of Investment, signed 14 November 1991, entered into force 20 October 1994, art IV(3).

¹¹⁷Campbell McLachlan, Laurence Shore and Matthew Weiniger, *Investment Treaty Arbitration: Substantive Principles* (OUP 2007) 274-78.

¹¹⁸See for example David Collins, 'Applying the Full Protection and Security Standard of Protection to Digital Investment' (2011) 12 J World Investment & Trade 225 arguing that in future the standard may have to be modified to fit the nature of security threats faced by investors in the twenty first century, namely the integrity of digital investments like computer systems and websites from attacks levied through or against the internet.

¹¹⁹*Azurix v Argentina*, ICSID Case No ARB/01/12, Award 14 July 2006, para 408. See also *Siemens AG v Argentina*, ICSID Case No ARB/02/8, Award 6 February 2007, para 303; George K Foster, 'Recovering 'Protection and Security': The Treaty Standard's Obscure Origins, Forgotten Meaning, and Key Current Significance' (2012) 45 Vanderbilt J Transnational L 1095.

¹²⁰ICSID Case No ARB/03/19, Decision on Liability 30 July 2010, paras 160-79.

¹²¹*ibid*, paras 172-73.

¹²²See for example Agreement between Canada and the Republic of Peru for the Promotion and Protection of Investments, signed 14 November 2006, entered into force 20 June 2007, art 5(2).

still remains scope to argue that the guarantee of full protection and security should extend beyond ensuring the physical security of investors' property.

(d) *The non-discrimination standards*

The national treatment standard and the MFN treatment standard are bound together by the common thread of non-discrimination and are contingent standards since their content is determined by reference to the treatment granted to other persons or entities. By contrast, non-contingent standards (such as the FET standard) are absolute as they apply to protect a given entity irrespective of the treatment granted to others. The national treatment standard, which has a long pedigree in international law, requires a host state to treat foreign investors no less favourably than a domestic investor 'in like circumstances', thus targeting protectionist measures. Both procedural and substantive treatment can be examined under this standard and both direct and indirect discrimination are covered by the prohibitions.¹²³ Similarly, the MFN treatment standard requires foreign investors to be treated no less favourably than investors from other third countries 'in like circumstances', although states often specify certain qualifications or exceptions to the MFN treatment standard when extending MFN treatment to other states.¹²⁴ The two standards combined ensure that foreign investors and their investments obtain the opportunity of equal competition with all other investors and their investments, since applying the national treatment standard alone might not be sufficient as the treatment of domestic investors could fall below the minimum international standard of treatment to which aliens are entitled. A general non-discrimination standard or a prohibition of arbitrary and/or discriminatory measures is sometimes included in IIAs in addition to these two standards.¹²⁵

¹²³Gus Van Harten, *Investment Treaty Arbitration and Public Law* (OUP 2007) 85.

¹²⁴Thus, many IIAs contain an exception for privileges which either of the Contracting States grants to investors of third states on account of its membership of a customs or economic union, a common market, a free trade area or under other treaties, such as double taxation treaties: see for example Treaty between the Federal Republic of Germany and the Islamic Republic of Afghanistan concerning the Encouragement and Reciprocal Protection of Investments, signed 20 April 2005, entered into force 12 October 2007, arts 3(3)-(4). Less frequently, IIAs contain further exceptions allowing for the contracting states to derogate from the national treatment or MFN standards in specific sectors or in exceptional circumstances: see for example Agreement between the Government of the United Kingdom of Great Britain and Northern Ireland and the Government of Antigua and Barbuda for the Promotion and Protection of Investments, signed 12 June 1987, entered into force 12 June 1987, art 3(3).

¹²⁵See for example Treaty between the United States of America and the Argentine Republic Concerning the Reciprocal Encouragement and Protection of Investment, signed 14 November 1991,

In some cases however, there may be legitimate public policy reasons for treating domestic investors more favourably than foreign investors.¹²⁶ In such cases, while the text of most IIAs does not explicitly allow tribunals to consider whether there is a *bona fide* regulatory purpose behind a host state measure,¹²⁷ such purpose can implicitly be taken into account in identifying the relevant comparator. Thus, the tribunal's interpretation of the phrase 'in like circumstances' becomes crucial in setting the boundaries of the host state's right to regulate and, in particular, its right to treat domestic investors more favourably for legitimate policy reasons. Thus, the more broadly a tribunal defines likeness, the more it inhibits the host state's ability to differentiate between different economic actors for policy reasons.¹²⁸ To give a simple example, a state enacts a measure limiting the use of a particular polluting technology, although this technology does significantly increase the efficiency of the production process. The measure affects foreign investors in a particular sector but not domestic investors in the same sector as the (less efficient) domestic investors had not yet introduced this technology. In such circumstances, to construe the term 'in like circumstances' purely in terms of the economic sector in which the claimant investor operates would restrict the state's ability to pursue certain environmental policy goals. Another important question that arises in interpreting the 'in like circumstances' proviso is whether the claimant investor has to show that the impugned treatment reflects a pattern of conduct in the state's treatment of a group or whether a violation can arise from the circumstances of a single investor. The tribunal's answer to this question will also have a significant effect on the degree to which states must alter their regulatory behaviour in order to avoid liability.¹²⁹

(e) *Umbrella clauses*

entered into force 20 October 1994, art II(2)(b); Energy Charter Treaty, 2080 UNTS 95; 34 ILM 360 (1995), art 10(1).

¹²⁶David Schneiderman, *Constitutionalizing Economic Globalization: Investment Rules and Democracy's Promise* (Cambridge University Press 2008) ch 6.

¹²⁷Van Aaken argues that, for discriminatory measures, an 'aims and effect' test could be considered: Anne Van Aaken, 'International investment law between commitment and flexibility: a contract theory analysis' (2009) 12 J Intl Economic L 507, 532.

¹²⁸Gus Van Harten, *Investment Treaty Arbitration and Public Law* (OUP 2007) 85.

¹²⁹*ibid.*

Approximately 40 per cent of IIAs contain umbrella clauses (also known as observance of undertakings clauses).¹³⁰ An umbrella clause is a promise made by one contracting state to an IIA to comply with all obligations or commitments that it has assumed towards investments of investors from the other contracting state. Although they can be worded in different ways and while the specific wording of each clause is crucial to ascertaining its scope and effect, a typical umbrella clause may provide as follows: ‘Each Contracting Party shall observe any obligation it may have entered into with regard to investments of investors of the other Contracting Party.’¹³¹ While this wording appears straightforward, the application of umbrella clauses has become one of the most controversial issues in investment treaty arbitration. In this regard, such clauses can be considered to have two aspects: first, a jurisdictional aspect whereby such clauses grant foreign investors access to an international forum in order to settle disputes about obligations arising out of the alleged breach of investor-state contracts and similar promises and, secondly, a substantive aspect in terms of their effect on the substantive law governing investor-state relations.¹³²

Turning first to the jurisdictional aspect, in general, in the absence of an umbrella clause, tribunals have reserved their jurisdiction over treaty-based claims while declining jurisdiction over contract-based claims on the basis that the forum-selection clause in the contract between host state and investor must be respected in relation to claims under that contract.¹³³ However, where an umbrella clause is

¹³⁰See Katia Yannaca-Small, ‘Interpretation of the Umbrella Clause in Investment Agreements’ OECD Working Papers on International Investment 2006/3.

¹³¹Agreement between the Government of the United Kingdom of Great Britain and Northern Ireland and the Government of the Republic of Argentina for the Promotion and Protection of Investments, signed 11 December 1990, entered into force 19 February 1993, art 2(2). See also Agreement between the Republic of the Philippines and the Swiss Confederation on the Promotion and Reciprocal Protection of Investments, signed 31 March 1997, entered into force 23 April 1999, art X(2); Agreement between Australia and the Republic of Poland on the Reciprocal Promotion and Protection of Investments, signed 7 May 1991, entered into force 27 March 1992, art 10; Agreement between the Republic of India and the Kingdom of the Netherlands for the promotion and protection of investments, signed 6 November 1995, entered into force 1 December 1996, art 4(5).

¹³²Stephan W Schill, ‘Umbrella Clauses as Public Law Concepts in Comparative Perspective’ in Stephan W Schill (ed), *International Investment Law and Comparative Public Law* (OUP 2010).

¹³³See for example *Azinian and ors v Mexico*, ICSID Case No ARB (AF)/97/2), Award on Jurisdiction and Merits 18 October 1999, paras 83-124. See also Stanimir A Alexandrov, ‘Breaches of Contract and Breaches of Treaty – The Jurisdiction of Treaty-based Arbitration Tribunals to Decide Breach of Contract Claims in *SGS v Pakistan* and *SGS v Philippines*’ (2006) 3 *Transnational Dispute Management*.

present in the relevant IIA,¹³⁴ the question arises as to the scope of jurisdiction conferred on the tribunal by the clause and the nature of the investment-related promises covered.¹³⁵ It is only within the last decade that umbrella clauses have found their way into enough IIAs that tribunals have had to grapple with their implications.¹³⁶ However, even in that relatively short time, two competing lines of jurisprudence have developed.

The approach taken in *SGS v Pakistan*¹³⁷ was that the tribunal had jurisdiction over the investor's treaty-based claims but not over its contractual claims, despite the inclusion of an umbrella clause in the Pakistan-Switzerland BIT.¹³⁸ The tribunal instead gave effect to the contractual forum-selection clause. The tribunal held that an umbrella clause can only transform a contractual claim into a treaty claim if clear evidence is provided that the contracting states intended the umbrella clause to have such a far-reaching effect and where the state is acting as a sovereign rather than commercially. On the other hand, the tribunal in *SGS v Philippines*¹³⁹ accepted jurisdiction over 'simple' commercial contractual claims. However, the tribunal decided to give effect to the contract's forum-selection clause and to allow the court selected in the contractual forum-selection clause to determine if and to what extent the agreement was breached. After that determination the tribunal would exercise its jurisdiction in order to decide whether such breach, if established, amounted to a breach of the BIT. Thus, the tribunal in *SGS v Philippines* viewed its task as

¹³⁴An investment treaty arbitration tribunal may also have jurisdiction over contractual disputes where the dispute resolution provision in the relevant IIA is broad enough to cover all disputes, including those that are contractual in nature: see Jörn Griebel, 'Jurisdiction over "contract claims" in treaty-based investment arbitration on the basis of wide dispute settlement clauses in investment agreements' (2007) 4 *Transnational Dispute Management*.

¹³⁵While the application of umbrella clauses to contractual claims will primarily be discussed, umbrella clauses may also apply to unilateral undertakings of host states: see Maria Cristina Gritón Salias, 'Do Umbrella Clauses Apply to Unilateral Undertakings?' in Christina Binder and others (eds), *International Investment Law for the 21st Century: Essays in Honour of Christoph Schreuer* (OUP 2009).

¹³⁶Matthew Wendlandt, 'SGS v Philippines and the Role of ICSID Tribunals in Investor-State Contract Disputes' (2008) 43 *Texas Intl L J* 523, 532.

¹³⁷ICSID Case No ARB/01/13, Decision of the Tribunal on Objections to Jurisdiction, 6 August 2003.

¹³⁸Agreement between the Swiss Confederation and the Islamic Republic of Pakistan on the Promotion and Reciprocal Protection of Investments, signed 11 July 1995, entered into force 6 May 1996, art 11.

¹³⁹ICSID Case No ARB/02/6, Decision of the Tribunal on Objections to Jurisdiction, 29 January 2004.

residual and made a distinction between having jurisdiction over contract-based claims and the admissibility of such claims.¹⁴⁰

Since the decision in *SGS v Philippines*, some tribunals have gone one step further than the *SGS v Philippines* tribunal and have held that, where an umbrella clause is contained in the relevant IIA, the tribunal constituted under the IIA can decide upon the alleged violation of a contract, regardless of the nature of the breach (whether sovereign or commercial), without having to prove some other breach of the relevant IIA.¹⁴¹ However, other tribunals have inclined towards the narrower view expressed in *SGS v Pakistan* that umbrella clauses relate only to breaches of a sovereign nature.¹⁴² Tribunals have also differed as to whether umbrella clauses cover only investor-state contracts or also functional substitutes for such contracts and as to whether umbrella clauses cover obligations that are not due directly from the state to the investor (for example, where either a state agency or an investor subsidiary is party to the relevant contract).¹⁴³ Overall therefore, while the view taken in *SGS v Pakistan* arguably renders the clause redundant,¹⁴⁴ on the other hand, allowing for an alleged breach of contract by a state to be adjudicated upon at an international level can be viewed as a departure from the established norms of international law, which provide that a breach of contract by a state is not sufficient to engage international responsibility on the part of the state in the absence of a denial of justice.¹⁴⁵

¹⁴⁰A simple explanation of the distinction is that jurisdiction concerns whether the tribunal can hear the case or not, whereas admissibility concerns whether the claim is 'hearable' at all: see Jan Paulsson, 'Jurisdiction and Admissibility' (2009) 6 *Transnational Dispute Management*. See also Thomas Kendra, 'State Counterclaims in Investment Arbitration - A New Lease of Life?' (2013) 29 *Arbitration Intl* 575, 590-93.

¹⁴¹*Eureko v Poland*, UNCITRAL, Partial Award 19 August 2005, paras 244-60; *Noble Ventures, Inc. v Romania*, ICSID Case No ARB/01/11, Award 12 October 2005, paras 46-62; *LG&E Energy Corporation v Argentina*, ICSID Case No ARB/02/1, Decision on Liability 3 October 2006, paras 169-75; *Siemens AG v Argentina*, ICSID Case No ARB/02/8, Award 6 February 2007, paras 204-06; *SGS v Paraguay*, ICSID Case No ARB/07/29, Award 10 February 2012, paras 68-95.

¹⁴²*CMS v Argentina*, ICSID Case No ARB/01/8, Award 12 May 2005, paras 296-303; *El Paso Energy International Company v Argentina*, ICSID Case No ARB/03/15, Decision on Jurisdiction 27 April 2006, paras 47-88.

¹⁴³*Noble Ventures, Inc. v Romania*, ICSID Case No ARB/01/11, Award 12 October 2005, paras 68-86; *Gustav FW Hamester GmbH & Co KG v Ghana*, ICSID Case No ARB/07/24, Award 18 June 2010, paras 339-50; *Burlington Resources Inc. v Ecuador*, ICSID Case No ARB/08/5, Decision on Liability 14 December 2012, paras 214-34.

¹⁴⁴Stephan W Schill, 'Umbrella Clauses as Public Law Concepts in Comparative Perspective' in Stephan W Schill (ed), *International Investment Law and Comparative Public Law* (OUP 2010) 330; cf *El Paso Energy International Company v Argentina*, ICSID Case No ARB/03/15, Decision on Jurisdiction 27 April 2006, paras 47-88.

¹⁴⁵LB Sohn and RR Baxter, 'Responsibility of States for Injuries to the Economic Interests of Aliens' (1961) 55 *AJIL* 554, 566-7; International Law Commission, *Draft Articles on Responsibility*

While this jurisdictional function of umbrella clauses can be considered the primary function of such clauses, umbrella clauses also have a substantive aspect.¹⁴⁶ Therefore, while umbrella clauses engage the host state's international responsibility for breaches of its investment-related promises,¹⁴⁷ umbrella clauses do not affect the content of the obligations arising out of the underlying contract or promise or the law applicable to it. In other words, a breach of contract is determined by the treaty-based tribunal on the basis of the applicable domestic law.¹⁴⁸ However, while this principle is clear, its implications are not. In particular, the issue of whether, and to what extent, the host state can regulate or terminate investor-state contracts or other investment-related promises in a non-opportunistic manner and in the public interest is open to question. While it has been argued that a 'police powers' based exception can, and should, be read into the application of umbrella clauses as an implied exception and that a balancing of investor and public interests can occur in determining whether international liability should be imposed in cases of non-opportunistic regulation of investor-state contracts by the host state,¹⁴⁹ this claim remains controversial.¹⁵⁰

The fact that the investor-state contract in question may contain a stabilisation clause heightens the relevance of this question as such clauses attempt to address the risks created by a state's capacity to exercise its sovereign powers to affect its contractual relationship with the investor. Stabilisation clauses are usually included in contracts with states that lack an effectively functioning internal mechanism of

of States for Internationally Wrongful Acts, with commentaries 2001 (2001) 2 YB Intl L Comm'n, UN Doc A/CN.4/SER.A/2001/Add.1 (Part 2) 41.

¹⁴⁶Stephan W Schill, 'Umbrella Clauses as Public Law Concepts in Comparative Perspective' in Stephan W Schill (ed), *International Investment Law and Comparative Public Law* (OUP 2010) 330.

¹⁴⁷Stanimir A Alexandrov, 'Breaches of Contract and Breaches of Treaty – The Jurisdiction of Treaty-based Arbitration Tribunals to Decide Breach of Contract Claims in *SGS v Pakistan* and *SGS v Philippines*' (2006) 3 *Transnational Dispute Management*.

¹⁴⁸*CMS v Argentina*, ICSID Case No ARB/01/8, Decision of the Ad hoc Annulment Committee on the Application for Annulment of Argentina 25 September 2007, para 95(c).

¹⁴⁹Stephan W Schill, 'The Robert E Hudec Article on Global Trade: Enabling Private Ordering: Function, Scope and Effect of Umbrella Clauses in International Investment Treaties' (2009) 18 *Minn J Intl L* 1, 75-77; Srikanth Hariharan, 'Distinction between Treaty and Contract: The Principle of Proportionality in State Contractual Actions in Investment Arbitration' (2013) 14 *J World Investment & Trade* 1019.

¹⁵⁰José Álvarez and Tegan Brink, 'Revisiting the Necessity Defence: Continental Casualty v Argentina' in Karl P Sauvant (ed), *Yearbook of International Investment Law and Policy 2010-2011* (OUP 2012) 338. See also AC Sinclair, 'The Origins of the Umbrella Clause in the International Law of Investment Protection' (2004) 20 *Arbitration Intl* 411, 431 noting that the US Department of State opposed the inclusion of an umbrella clause in the OECD Draft Convention on the Protection of Foreign Property seeing it as 'an undesirable attempt through international law to fetter the US Government's sovereign right of eminent domain and to bargain away its police powers'.

statehood (i.e. where the central government's power is very limited, law and order is outside its control and the judicial system lacks the attributes of a modern Western judicial system) and are potentially problematic as they may go further than the guarantees contained in IIAs in generally requiring compensation for any interference by the host state that increases the costs of a project, thereby precluding a balancing of investor and host state interests.¹⁵¹ Furthermore, the decision of the tribunal in *Duke Energy v Peru*¹⁵² would seem to suggest that stabilisation clauses (depending on their wording) can cover not only regulatory changes but also changes in the judicial or administrative application or interpretation of existing legislation. However, there has yet to be a publicly-available decision suggesting how a tribunal might respond to a stabilisation clause that would limit a host state's capacity to regulate for the public good.¹⁵³

Thus, there remains considerable uncertainty in relation to both the jurisdictional and substantive aspects of umbrella clauses¹⁵⁴ and for this reason such clauses are, in practice, frequently relied upon by investors as a 'catch-all' provision where the host state's conduct may not amount to a breach of other treaty obligations.¹⁵⁵ Most pertinently for these purposes, in terms of the type of state actions that are prohibited by umbrella clauses, while one view, based on comparative public law analysis, is that umbrella clauses do not exclude the state's right to regulate or even

¹⁵¹Paul E Comeaux and N Stephan Kinsella, 'Reducing Political Risk in Developing Countries: Bilateral Investment Treaties, Stabilization Clauses, and MIGA & OPIC Investment Insurance' (1994) 15 *New York Law School J Intl & Comp L* 1, 26-31; cf Antony Crockett, 'Stabilisation clauses and sustainable development: Drafting for the future' in Chester Brown and Kate Miles (eds), *Evolution in Investment Treaty Law and Arbitration* (Cambridge University Press 2011). Admittedly, the modern trend has been to move away from so-called freezing clauses, which provide that the contractual terms will prevail over any inconsistent laws or regulations passed subsequent to the execution of the contract, towards less draconian stabilisation clauses: see Andrea Shemberg, *Stabilization Clauses and Human Rights: A Research Project conducted for IFC and the United Nations Special Representative to the Secretary General on Business and Human Rights*, 27 May 2009.

¹⁵²ICSID Case No ARB/03/28, Award 18 August 2008.

¹⁵³Katja Gehne and Romulo Brillo, 'Stabilization Clauses in International Investment Law: Beyond Balancing and Fair and Equitable Treatment' NCCR Trade Working Paper No 2013/46, January 2014.

¹⁵⁴Anthony C Sinclair, 'The Umbrella Clause Debate' in Andrea K Bjorklund, Ian A Laird and Sergey Ripinsky (eds), *Investment treaty law: current issues. III, Remedies in international investment law emerging jurisprudence of international investment law* (British Institute of International and Comparative Law 2008) 311-12 for a summary of the unsettled issues relating to umbrella clauses.

¹⁵⁵See Matthew Saunders, Kate Knox and Elinor Thomas, 'Umbrella Clauses' <www.practicallaw.com/7-381-7477> accessed 19 March 2015.

terminate investor-state contracts in the public interest,¹⁵⁶ the contrary view is that umbrella clauses effectively create a blanket guarantee against interferences with contractual rights regardless of whether such interferences are non-discriminatory, compliant with due process and/or justified by reference to a rational policy objective.

(f) *Freedom of Transfer Guarantee*

IAs generally contain a provision allowing for the unrestricted transfer of investment-related funds in a freely usable currency. To give an example, Article 8 of the Azerbaijan – Finland BIT¹⁵⁷ provides as follows:

(1) Each Contracting Party shall ensure to investors of the other Contracting Party the free transfer, into and out of its territory, of payments in connection with an investment...

(2) Transfers referred to in paragraph 1 of this Article shall be made without any restriction or delay, in a freely convertible currency and at the prevailing market rate of exchange applicable on the date of transfer in the currency to be transferred. If a market rate is unavailable the applicable rate of exchange shall be the most recent rate of exchange for conversion of currencies into Special Drawing Rights.

(3) Notwithstanding paragraphs 1 and 2 of this Article, a Contracting Party may delay a transfer through the equitable, non-discriminatory and good faith application of measures ensuring investors' compliance with the host Contracting Party's laws and regulations relating to the payment of taxes and dues, provided that such measures and their application shall not unreasonably impair the free and undelayed transfer ensured by this Agreement.

Such clauses therefore restrict the host state's monetary sovereignty. From an investor perspective, this is one of the most important treaty-based obligations but it has not featured in many investment treaty arbitrations or, until recently, in

¹⁵⁶Stephan W Schill, 'Umbrella Clauses as Public Law Concepts in Comparative Perspective' in Stephan W Schill (ed), *International Investment Law and Comparative Public Law* (OUP 2010) 343.

¹⁵⁷Agreement between the Government of the Republic of Azerbaijan and the Government of the Republic of Finland on the Promotion and Protection of Investments, signed 26 February 2003, entered into force 10 December 2004.

academic writings.¹⁵⁸ Since, in times of crisis, a large repatriation of capital by foreign investors may create balance of payments difficulties, some BITs (and most multilateral treaties) contain a balance of payments clause, which allows the parties to temporarily restrict the transfer of funds in such a situation in order to prevent an exacerbation of an economic crisis.¹⁵⁹ However, many BITs do not contain such a safeguard.¹⁶⁰ Given the global economic situation over the last number of years and the protection granted to portfolio investment by most IIAs, the question has been raised as to whether, in the absence of a balance of payments clause or where the conditions of such a clause are not fulfilled, this right of transfer can be suspended or restricted in times of emergency (i.e. whether capital controls can be imposed).¹⁶¹ The fact that US trade and investment treaties, in particular, do not allow for the imposition of capital controls has made this a controversial question.¹⁶² However, this question has yet to be addressed comprehensively in arbitral practice. In *Continental Casualty v Argentina*¹⁶³ the free transfer provision in the Argentina-US BIT (Article V) was considered but the tribunal found that the transfer in question did not fall within the meaning of the term ‘transfers related to an investment’ and thus held that Article V was not breached. The award is therefore inconclusive as to whether a defence based on balance of payments difficulties would succeed.

2.4 Reasons for taking account of public interest considerations

Having considered the principal substantive rights typically contained in IIAs, it is clear that these rights are open-ended in nature and lack a well-defined normative content, which means that the scope and substance of investment treaty arbitration

¹⁵⁸Alejandro Turyn and Facundo Perez Aznar, ‘Drawing the Limits of Free Transfer Provisions’ in Michael Waibel and others, *The Backlash against Investment Arbitration: Perceptions and Reality* (Kluwer 2010) 51-78 for a review of the limited case law touching on free transfer provisions.

¹⁵⁹See for example Agreement between Czech Republic and the Republic of Costa Rica for the Promotion and Reciprocal Protection of Investments, signed 21 October 1998, entered into force 5 March 2001, art 6(4); Agreement between the Government of the United Kingdom of Great Britain and Northern Ireland and the Government of the United Mexican States for the Promotion and Reciprocal Protection of Investments, signed 12 May 2006, entered into force 25 July 2007, art 8(4).

¹⁶⁰Abba Kolo, ‘Transfer of Funds: The Interaction between the IMF Articles of Agreement and Modern Investment Treaties: a Comparative Law Perspective’ in Stephan W Schill (ed), *International Investment Law and Comparative Public Law* (OUP 2010) 356.

¹⁶¹ibid; Michael Waibel, ‘BIT by BIT: The Silent Liberalization of the Capital Account’ in Christina Binder and others (eds), *International Investment Law for the 21st Century: Essays in Honour of Christoph Schreuer* (OUP 2009).

¹⁶²Kevin P Gallagher, ‘Reforming United State Trade and Investment Treaties for Financial Stability: the case for Capital Controls’ *Investment Treaty News*, April 2011.

¹⁶³ICSID Case No ARB/03/9, Award 5 September 2008, paras 237-45.

is left unclear to a significant extent. The broad-ranging nature of the investor rights contained in IIAs is arguably somewhat inevitable given that treaty drafters and negotiators cannot predict the range of issues that will arise in an investment dispute and given that a degree of discretion and policy choice is inherent in any process of adjudication.¹⁶⁴ Further, Trachtman notes that such broad framing may permit states ‘to agree to disagree for the moment in order to avoid the political price that may arise from immediate hard decisions or to cloak the hard decisions in the false inevitability of judicial interpretation’.¹⁶⁵ Whatever the reasons for this indeterminacy, its consequence is that while, on the one hand, these rights have the potential to affect a host states’ freedom of action across all branches (executive, legislative and judicial) of a state’s sovereign jurisdiction, on the other hand, they can potentially be interpreted by investment treaty arbitration tribunals in a manner that is sensitive to public interest considerations. This accords a strikingly wide range of discretion to investment treaty arbitration tribunals. From an investor perspective, this is problematic as it is difficult to predict when an investor will be entitled to a remedy. From a host state perspective, the potential for a wide interpretation of investor rights by future tribunals may lead to ‘regulatory chill’, whereby states are discouraged from introducing *bona fide* regulatory measures by the possibility or threat of investor claims.¹⁶⁶ A possible example of this ‘chilling effect’ occurred in Canada:¹⁶⁷ after the tobacco company Philip Morris publicly threatened on several occasions to challenge restrictions on the packaging of

¹⁶⁴Gus Van Harten, *Investment Treaty Arbitration and Public Law* (OUP 2007) 123. See also Anne Van Aaken, ‘Control Mechanisms in International Investment Law’ University of St. Gallen Law School, Law and Economics Research Paper Series Working Paper No. 2013-23, December 2013, 4-5 noting that contract theory finds that overly strict and inflexible contracts may impair the joint surplus of the contracting parties; cf Julie A Maupin, ‘Public and Private in International Investment Law: An Integrated Systems Approach’ (2013-2014) 54 Va J Intl L 367, 380-81 noting that most international legal instruments exposing states to direct financial responsibility are narrowly drafted.

¹⁶⁵Joel P Trachtman, ‘The Domain of WTO Dispute Resolution’ (1999) 40 Harv Intl L J 333, 351. See also Cass R Sunstein, ‘Incompletely Theorized Agreements’ (1995) 108 Harv L Rev 1733.

¹⁶⁶Kyla Tienhaara, *The expropriation of environmental governance: protecting foreign investors at the expense of public policy* (Cambridge University Press 2009); Kevin P Gallagher and Elen Shrestha, ‘Investment Treaty Arbitration and Developing Countries: A Reappraisal’ Global Development and Environmental Institute Working Paper No 11-01 (May 2011).

¹⁶⁷It is not certain that this (or indeed any other example) is a case of regulatory chill as it is rare that a political decision can be adequately explained by one independent variable: Kyla Tienhaara, ‘Regulatory Chill and the Threat of Arbitration: A View from Political Science’ in Chester Brown and Kate Miles (eds), *Evolution in Investment Treaty Law and Arbitration* (Cambridge University Press 2011) 609.

cigarettes under NAFTA and hired a former US Trade Representative to advocate its case, Canadian officials abandoned plans to introduce plain packaging.¹⁶⁸

However, the primary concern associated with wide-ranging investor rights is that the extent to which regulatory sovereignty has been ceded by the contracting states to the relevant IIA is unclear. The question then becomes whether, in concluding an IIA, the contracting states relinquish irrevocably their sovereign right to regulate in circumstances where such regulation could potentially impact upon protected foreign investors. In other words, should investor rights be construed in as broad as possible a manner since the contracting states to the relevant IIA have agreed to cede their regulatory sovereignty to an unspecified extent or, alternatively, should investment treaty arbitration tribunals interpret investor rights in a manner that is cognisant of public interest considerations?

It is submitted that, given the margin of discretion typically afforded to investment treaty arbitration tribunals by IIAs, the latter approach should be favoured for a number of reasons. First, although many investment treaty arbitrations involving investor-state contracts may be closer to commercial disputes between private entities,¹⁶⁹ a number of the disputes which have arisen to date under IIAs have undoubtedly touched on delicate policy issues relating to the ability of the state to legislate in the public interest.¹⁷⁰ These disputes include the more than forty arbitrations concerning the lawfulness of Argentina's legislative response to its economic crisis and sovereign default of 2000 to 2002;¹⁷¹ arbitrations involving water concessions;¹⁷² an arbitration challenging an affirmative action program that

¹⁶⁸Luke Eric Peterson, 'All Roads Lead out of Rome: Divergent Paths of Dispute Settlement in Bilateral Investment Treaties' in Lyuba Zarkasy (ed), *International Investment for Sustainable Development: Balancing Rights and Rewards* (Earthscan Publishing 2005) 139.

¹⁶⁹Julie A Maupin, 'Public and Private in International Investment Law: An Integrated Systems Approach' (2013-2014) 54 Va J Int'l L 367, 400 observing that contract-based disputes likely outnumber treaty-based disputes in any given year. See also David D Caron, 'Investor State Arbitration: Strategic and Tactical Perspectives on Legitimacy' (2008-2009) 32 Suffolk Transnational L Rev 513, 514.

¹⁷⁰William Burke-White and Andreas von Staden, 'The Need for Public Law Standards of Review in Investor-State Arbitrations' in Stephan W Schill (ed), *International Investment Law and Comparative Public Law* (OUP 2010) 691-92.

¹⁷¹See William W Burke-White, 'The Argentine Financial Crisis: State Liability under BITs and the Legitimacy of the ICSID System in Michael Waibel and others (eds), *The Backlash against Investment Arbitration: Perceptions and Reality* (Kluwer 2010).

¹⁷²See for example *Biwater Gauff (Tanzania) Ltd v Tanzania*, ICSID Case No ARB/05/22; *Compañía de Aguas del Aconqija S.A. and Vivendi Universal S.A. v Argentina*, ICSID Case No ARB/97/3; *Suez, Sociedad General de Aguas de Barcelona S.A. and Vivendi Universal v Argentina*, ICSID Case No ARB/03/19.

aimed at remedying the injustices of apartheid in South Africa;¹⁷³ arbitrations challenging the ban of harmful substances;¹⁷⁴ arbitrations challenging measures for the protection of the environment;¹⁷⁵ arbitrations challenging anti-tobacco legislation¹⁷⁶ and Vattenfall's claim for €4.7 billion against the German government in relation to its challenge to Germany's exit from nuclear power production.¹⁷⁷ In dealing with such disputes, the ambiguity of the principal substantive rights typically conferred by IIAs is such that the state could potentially be deprived of its basic freedom to pursue public policies in relation to political, social, cultural and economic matters.¹⁷⁸ Thus, although one could argue that the government of each of the contracting states to a IIA should have taken into account its other obligations before agreeing to be bound by such treaty and that accordingly it (and, at least in democratic states, the people that it represents) should be bound to abide by the terms of the IIA to the full extent,¹⁷⁹ according the broadest possible scope to the rights conferred on investors by IIAs regardless of the circumstances cannot form the basis of a bargain which was concluded by the mutual agreement of states. This is the case as it would be unreasonable to expect a freezing of the *status quo* at the time at which a state entered into the IIA, which would essentially preclude elected authorities and administrative agencies from being able to change policy in the public interest.¹⁸⁰

On a related note, it is questionable the extent to which IIAs, in fact, reflect the democratic choices of states as, first, quite a few of the states participating in the

¹⁷³*Foresti, de Carli and others v Republic of South Africa*, ICSID Case No ARB(AF)/07/1, Award 4 August 2010.

¹⁷⁴See for example *Methanex Corporation v United States of America*, UNCITRAL, Final Award of the Tribunal on Jurisdiction and Merits, 3 August 2005; *Chemtura Corporation (formerly Crompton Corporation) v Government of Canada*, UNCITRAL, Award 2 August 2010.

¹⁷⁵*Metalclad Corporation v Mexico*, ICSID Case No ARB(AF)/97/1, Award 30 August 2000; *SD Myers, Inc. v Canada*, UNCITRAL, First Partial Award 13 November 2000.

¹⁷⁶Tania S Voon and Andrew D Mitchell, 'Time to Quit? Assessing International Investment Claims Against Plain Tobacco Packaging in Australia' (2011) 14 J Intl Economic L 515.

¹⁷⁷*Vattenfall AB v Federal Republic of Germany*, ICSID Case No ARB/12/12 (award pending). See also 'Atomausstieg: Vattenfall verklagt Deutschland auf 4,7 Milliarden Euro', Spiegel Online (Dusseldorf, 15 October 2014) <<http://www.spiegel.de/wirtschaft/unternehmen/vattenfall-verklagt-deutschland-wegen-atomausstieg-auf-4-7-milliarden-a-997323.html>> accessed 19 March 2015.

¹⁷⁸Roland Kläger, *Fair and Equitable Treatment* in *International Investment Law* (Cambridge University Press 2011) 159.

¹⁷⁹James D Fry, 'International Human Rights Law in Investment Arbitration: Evidence of International Law's Unity' (2007) 18 Duke J Comp & Intl L 77, 104.

¹⁸⁰Santiago Montt, *State Liability in Investment Treaty Arbitration: Global Constitutional and Administrative Law in the BIT Generation* (Hart Publishing 2009) 227-28.

international investment regime are not democracies,¹⁸¹ and secondly, even in democratic states, the terms of most IIAs do not contain any exception for legislative decisions even where the legislature makes a decision of a general nature, when it responds to a national crisis or where its decision is supported an overwhelming majority of the country's elected representatives. Furthermore, IIAs generally bind states for a considerable period, only allow a brief window for opting-out before the treaty is automatically renewed and generally maintain the state's obligations for an extended period for foreign investors whose investments existed at the time a treaty is cancelled. For example, Article 12 of the Albania-Finland BIT is quite typical in providing for the treaty to remain in force for 20 years and thereafter for an unlimited period unless either contracting party serves notice on the other party twelve months before its expiration.¹⁸² The treaty is then stated to remain in force for a further twenty years from the date when the notice of termination becomes effective in respect of investments made prior to that date.¹⁸³ This effectively means that the choices of one elected government may bind a future government in a manner which fundamentally restricts its policy options. In this regard, although international law has long held that a change in government does not relieve the state from responsibility for the international undertakings of a former regime,¹⁸⁴ this does not mean that open-ended obligations entered into by a state must be interpreted in a particular manner and, accordingly, does not preclude the taking into account of public interest considerations in interpreting IIAs.¹⁸⁵ Indeed, the longevity of most IIAs can, of itself, be argued to intensify the need for public interest considerations to be taken into account in interpreting IIAs given the

¹⁸¹Julie A Maupin, 'Public and Private in International Investment Law: An Integrated Systems Approach' (2013-2014) 54 Va J Intl L 367, 400.

¹⁸²Agreement between the Government of Finland and the Government of the Republic of Albania on the Promotion and Protection of Investments, signed 24 June 1997, entered into force 20 February 1999.

¹⁸³Renegotiating IIAs can also be cost prohibitive, especially for countries with larger BIT programs: Tra T Pham, 'International investment treaties and arbitration as imbalanced instruments: a re-visit' (2010) Intl Arbitration L Rev 81.

¹⁸⁴See for example *Aguilar-Amory & Royal Bank of Canada Claims (Great Britain v Costa Rica)*, 1 RIAA 369, 377-78. See also James Crawford, 'Democracy and the Body of International Law' in George H Fox and Brad R Roth (eds), *Democratic Governance and International Law* (Cambridge University Press 2000) 97.

¹⁸⁵For a similar view see Jorge E Viñuales, 'Foreign Investment and the Environment in International Law: An Ambiguous Relationship', Centre for Environmental Law Studies, Graduate Institute Geneva, Research Paper No 2, 60. See also Jonathan Bonnitcha, 'Political Change vs. Legal Stability: Problems Arising from the Application of Investment Treaties in Transitions from Authoritarian Rule', Investment Treaty News, February 2015.

range of social, economic and political circumstances that may fall to be addressed in a particular state over such a prolonged period.

Finally and crucially, if investment treaty arbitration tribunals were to consistently accord the broadest possible scope to investor rights without paying any attention to host state regulatory concerns, it is likely that states would exit the system, either as a whole or selectively.¹⁸⁶ This is particularly the case given that investment treaty arbitrators are empowered to adopt a broad interpretation of IIA provisions even where this conflicts with the unanimous submissions of the states that negotiated and concluded that treaty and, potentially, with the right of such states to regulate in the public interest.¹⁸⁷ Furthermore, given that states that traditionally recognised themselves as capital exporters now also see themselves as importers of capital and that countries that once were thought to be capital importers are now finding their nationals investing abroad, it is likely that not only traditional capital importers would exit the system. In fact, one commentator has opined that for arbitrators to proceed ‘with a heavy thumb pressed permanently down on the investors’ side of the scales’ would prove ‘suicidal’.¹⁸⁸ Thus, states could just stop entering into IIAs or could decide to exit IIAs either by not prolonging them or by explicitly renouncing them. Alternatively, states could choose non-compliance with IIAs or could require foreign investors in investor-state contracts to waive their right to pursue investment treaty arbitration in the event of a dispute arising under that contract.¹⁸⁹ Another possibility is that national parliaments or constituent assemblies could set up specific constraints that reduce the negotiating discretion of future governments to include specific provisions in IIAs.¹⁹⁰ Indeed, this phenomenon can already be seen in the denunciation of several Latin American countries of the ICSID Convention,¹⁹¹ in the termination of several IIAs by South

¹⁸⁶Anne Van Aaken, ‘International investment law between commitment and flexibility: a contract theory analysis’ (2009) 12 J Intl Economic L 507, 510.

¹⁸⁷Gus Van Harten, *Investment Treaty Arbitration and Public Law* (OUP 2007) 99.

¹⁸⁸Alec Stone Sweet, ‘Investor-State Arbitration: Proportionality’s New Frontier’ (2010) 4 Law & Ethics of Human Rights 47, 75-76.

¹⁸⁹Gus Van Harten, ‘Five Justifications for Investment Treaties: A Critical Discussion’ (2010) 2 Trade, Law & Development 1, 4.

¹⁹⁰For example, Article 366 of the new Bolivia Constitution forbids recourse to foreign tribunals or jurisdiction for investments in certain sectors: Anne Van Aaken, ‘International investment law between commitment and flexibility: a contract theory analysis’ (2009) 12 J Intl Economic L 507, 532.

¹⁹¹For an overview see UNCTAD, *Denunciation of the ICSID Convention and BITs: Impact on Investor-State Claims* (UNCTAD IIA Issues Note No 2 2010). In conjunction with this development, various states have announced plans to establish an arbitration forum within the

Africa and its publication of a Promotion and Protection of Investment Bill as an alternative to entering into IIAs,¹⁹² and in the position taken by the Australian government in relation to investment treaty arbitration in its 2011 Trade Policy Statement.¹⁹³ The on-going debate as to whether investor-state dispute settlement provisions should be included in the Transatlantic Trade and Investment Partnership Agreement can also be seen as indicative of this phenomenon.¹⁹⁴ Such behaviour can be viewed through the lens of the concepts of ‘Exit’ and ‘Voice’:

Exit is the mechanism of organizational abandonment in the face of unsatisfactory performance. Voice is the mechanism of intra-organizational correction and recuperation...a stronger “outlet” for Voice reduces pressure on the Exit option and can lead to more sophisticated processes of self-correction. By contrast, the closure of Exit leads to demands for enhanced Voice.¹⁹⁵

Thus, if the investment treaty arbitration system as a whole is perceived as giving a ‘voice’ to the concerns of states regarding their ability to regulate in the public interest (even in circumstances where the state’s right to regulate is ultimately subordinated to investor rights in particular factual scenarios), states are less likely to seek to ‘exit’ that system.¹⁹⁶

In conclusion therefore, since the textual provisions of IIAs generally do not relieve the tension between host state regulatory sovereignty and investor protection and since relief of such tension is, for the reasons stated above, necessary, investment

Union of South American Countries (UNASUR) as an alternative to ICSID: see Mariono Tobías de Alba Uribe, ‘Investment Arbitration and Latin America: Irreconcilable Differences?’ Kluwer Arbitration Blog, 21 May 2013.

¹⁹²UNCTAD, *World Investment Report 2013: Global Value Chains: Investment and Trade for Development* (UNCTAD 2013) 108-09; Republic of South Africa, Promotion and Protection of Investment Bill, *Government Gazette*, vol 581 no 36995 (1 November 2013).

¹⁹³Craig Emerson, ‘Gillard Government Trade Policy Statement: Trading Our Way to More Jobs and Prosperity’, 11 December 2013. For developments in Australia (and elsewhere) since the release of this statement see Leon E Trakman, ‘Investor-State Arbitration: Evaluating Australia’s Evolving Position’ (2014) 15 *J World Investment & Trade* 152.

¹⁹⁴See European Commission, *Report: Online public consultation on investment protection and investor-to-state dispute settlement (ISDS) in the Transatlantic Trade and Investment Partnership Agreement (TTIP)* SWD (2015) 3 final.

¹⁹⁵J H H Weiler, ‘The Transformation of Europe’ (1991) 100 *Yale L J* 2403, 2411 drawing on Albert O Hirschman, *Exit, Voice and Loyalty: Responses to Decline in Firms, Organizations and States* (Cambridge University Press 1970). See also Anna T Katselas, ‘Exit, Voice, and Loyalty in Investment Treaty Arbitration’ (2014) 93 *Neb L Rev* 313.

¹⁹⁶See José Álvarez and Tegan Brink, ‘Revisiting the Necessity Defence: Continental Casualty v Argentina’ in Karl P Sauvart (ed), *Yearbook of International Investment Law and Policy 2010-2011* (OUP 2012) 346-47 noting that there is greater possibilities for exit and voice in investment treaty law than under the WTO regime. However, not all states will be able to deploy the exit and voice options equally: see José Álvarez, ‘The Return of the State’ (2011) 20 *Minn J Intl L* 223, 260.

treaty arbitration tribunals must perform this unenviable role. This effectively makes the interpretation of the IIA text by each individual tribunal crucial to maintaining an optimal balance between investor protection and host state regulatory sovereignty. Furthermore, while in recent years, an increasing number of ‘new generation’ IIAs have been concluded which contain preambular statements that refer to social and environmental objectives,¹⁹⁷ provisions that clarify or adjust the scope of IIA rights¹⁹⁸ and/or general exceptions clauses that exclude from the scope of the IIA protections certain actions taken in pursuit of certain social or economic policy objectives,¹⁹⁹ fundamentally such provisions do not displace this balancing role as they do not indicate how much deference should be shown to sovereign regulatory decisions and do not purport to determine to whom the costs associated with the impugned host state measures should be allocated. Accordingly, as noted by Spears, ‘none of the innovations in ‘new generation’ IIAs actually resolve the tension that will continue to arise between competing policy objectives in investor-state cases’.²⁰⁰ Thus, even if such provisions are introduced on a more widespread basis than is currently the case, the interpretation of IIA rights by investment treaty arbitration tribunals will remain crucial in balancing investor rights and public interest considerations.

2.5 Conclusion

This chapter has sought to demonstrate that the rights conferred on investors by IIAs are generally open-ended in nature and to explain why, in interpreting those rights, investment treaty arbitration tribunals take account of public interest considerations. This argument can, it is submitted, be separated from the debate as to whether international investment law constitutes a form of public law or whether

¹⁹⁷See for example US Model BIT (2012).

¹⁹⁸See for example Investment Agreement for COMESA Common Investment Area, signed 23 May 2007, art 20(8); ASEAN Comprehensive Investment Agreement, signed 26 February 2009, entered into force 29 March 2012, annex 2.

¹⁹⁹See for example ASEAN Comprehensive Investment Agreement, signed 26 February 2009, entered into force 29 March 2012, art 17; Energy Charter Treaty, 2080 UNTS 95; 34 ILM 360 (1995), art 24. See also Anne Van Aaken, ‘International investment law between commitment and flexibility: a contract theory analysis’ (2009) 12 J Intl Economic L 507, 524-25; Suzanne A Spears, ‘Making way for the public interest in international investment agreements’ in Chester Brown and Kate Miles (eds), *Evolution in Investment Treaty Law and Arbitration* (Cambridge University Press 2011); UNCTAD, *World Investment Report 2014: Investing in the SDGs: An Action Plan* (UNCTAD 2014) 117.

²⁰⁰Suzanne A Spears, ‘The quest for policy space in a new generation of international investment agreements’ (2010) 13J Intl Economic L 1037, 1071-72.

each IIA constitutes a 'private', quasi-contractual bargain between the contracting states and, accordingly, from the question of whether arbitration is a suitable adjudication model for dealing with disputes under IIAs. The next chapter will proceed to analyse how investment treaty arbitration tribunals have taken into account public interest considerations and will examine the efficacy of the methods utilised by tribunals to date.

Chapter 3: The merits stage and public interest considerations: an uneasy balance

3.1 Introduction

At the merits stage of the investment treaty arbitration process, the question of whether one or more investor rights have been breached is considered by the tribunal. In considering this question, not all international investment disputes will raise matters of public interest. Furthermore, even among those that do, it is far from inevitable that the final result will be an award that negatively affects the public interest. Indeed, a number of empirical studies focussing on case outcomes have tended towards the conclusion that investment treaty arbitration tribunals do not exhibit bias in favour of either claimant investors or respondent states.¹ However, given the broad range of circumstances that may give rise to an IIA dispute and that data on outcomes as a measure of actual behaviour is open to a wide range of possible explanations,² it is submitted that such outcome-based analysis does not provide sufficient evidence of investment treaty arbitration tribunals' engagement with public interest considerations in assessing investor claims at the merits stage of the arbitral process or of the efficacy of the methods used by such tribunals in order to do so. It is on this question that this chapter focusses.

¹Susan D Franck, 'Empirically Evaluating Claims about Investment Treaty Arbitration' (2007) 86 N C L Rev 1; Susan D Franck, 'Development and Outcomes of Investment Treaty Arbitration' (2009) 50 Harv Intl L J 435; Daphna Kapeliuk, 'The Repeat Appointment Factor: Exploring Decision Patterns of Elite Investment Arbitrators' (2010) 96 Cornell L Rev 47; Susan D Franck, 'The ICSID Effect? Considering Potential Variations in ICSID Awards' (2010) 51 Va J Intl L 825; cf Kevin P Gallagher and Elen Shrestha, 'Investment Treaty Arbitration and Development: A Re-Appraisal' Global Development and Environmental Institute Working Paper No. 11-01 (May 2011); Gus Van Harten, 'Arbitrator Behaviour in Asymmetrical Adjudication: An Empirical Study of Investment Treaty Arbitration' (2012) 50 Osgoode Hall L J 211.

²Such explanations include variations in the strength of parties' claims, diversity of fact situations, procedural and structural variations among arbitration forums and varying levels of political influence by states and private actors: Gus Van Harten, 'Arbitrator Behaviour in Asymmetrical Adjudication: An Empirical Study of Investment Treaty Arbitration' (2012) 50 Osgoode Hall L J 211, 223. It is also worth noting that the results of empirical research will vary depending on a number of factors including the topic isolated for study, the choice of methods, the availability of data and the inferences drawn by the researcher: Richard Lempert, 'Empirical Research for Public Policy: With Examples from Family Law' (2008) 5 J Empirical Legal Studies 907.

In this regard and despite a degree of overlap or congruence between the two,³ a distinction can be drawn for analytical purposes between, on the one hand, the balancing of public interest considerations and investor interests in determining the content of substantive treaty obligations and, on the other, the interpretation of IIA rights in a manner consistent with a host state's non-investment related international obligations. A third way of introducing public interest considerations into investment law is through the invocation by a host state of the customary international law defence of necessity and/or through reliance on a NPM clause. It is clear that the first method (namely the balancing of public interest considerations and investor interests) has the broadest application and, due to this, may be considered more likely to allow for a more comprehensive consideration of both investor and host state interests as it allows for a 'thorough airing' of all aspects of the claim.⁴ However, an examination of all three, interrelated, methods is required in order to assess their efficacy as a whole.

3.2 Proportionality analysis

With the notable exception of expropriation clauses, which explicitly require the public purpose underlying a measure to be considered in determining whether an expropriation is lawful or unlawful (but nonetheless require a remedy to be provided to the claimant investor in both cases), the other principal rights typically contained in IIAs do not explicitly require that the public purpose underlying a host state measure be considered in determining whether those rights have been breached. Nevertheless, in recent years, a number of tribunals have referred to the notion of proportionality or have applied some form of proportionality testing in balancing public interest considerations against the effect of the impugned measure on the investment in deciding whether investor rights have been violated. Proportionality analysis, in its pure sense, is an analytical framework originally developed by administrative and constitutional courts in order to manage legal disputes of a particular structure, the paradigmatic example of which concerns a

³See International Law Commission, *Fragmentation of International Law: Difficulties Arising from the Diversification and Expansion of International Law*, UN Doc A/CN.4/L.682 (13 April 2006) (finalised by Martti Koskenniemi) para 412.

⁴José E Álvarez and Tegan Brink, 'Revisiting the necessity defense: Continental Casualty v Argentina' in Karl P Sauvant (ed), *Yearbook of International Investment Law and Policy 2010-2011* (OUP 2012) 358.

tension between, on the one hand, a right and, on the other, a constitutionally recognised public interest pursued by the state.⁵ Traditionally, the analysis has consisted of three criteria: suitability, necessity, and proportionality *stricto sensu*. The criterion of suitability requires that the means be suitable or helpful in some way to achieve a legitimate objective. This allows measures taken for patently illegitimate purposes to be filtered out at an early stage along with measures that are wholly ineffective in pursuing a legitimate purpose. The criterion of necessity requires that the means be necessary to achieve the end. This has been interpreted to mean that the state must choose from among all the potential measures that would achieve its desired objective the measure which would least restrict the applicant's rights and interests while still being capable of producing the same result. Finally, the most stringent criterion – that of proportionality *stricto sensu* – requires that the measure is not excessive with regard to the objective pursued and means that the tribunal must take into account all available factors such as cost-benefit analysis, the importance of the right affected, the importance of the right or interest protected, the degree and length of interference with the affected right and the availability of alternative measures that might be less effective, but also proportionally less restrictive for the right affected.⁶ This third step is crucial as stopping at the necessity test stage would allow restricting a right severely in order to protect a negligible public interest.⁷

Robert Alexy in his seminal work on proportionality analysis proposed that proportionality analysis is suitable for balancing principles as opposed to resolving conflicts between rules. Alexy distinguished between rules and principles on the basis that, whereas a rule is either fulfilled or not fulfilled, principles are capable of being reconciled or harmonised with each other such that each principle is brought to bear to the greatest possible extent given the circumstances. This means that the 'defeated' principle may be used to influence the interpretation and application of the prioritised law.⁸ Therefore, in respect of certain IIA breaches which can be

⁵Alec Stone Sweet and Jud Mathews, 'Proportionality Balancing and Global Constitutionalism' (2008) 47 Colum Journal Transnational L 73.

⁶Jan Jans, 'Proportionality Revisited' (2000) 27 Legal Issues of Economic Integration 239.

⁷Benedict Kingsbury and Stephan Schill, 'Investor-State Arbitration as Governance: Fair and Equitable Treatment, Proportionality and the Emerging Global Administrative Law' in Albert Jan van den Berg (ed), *50 Years of the New York Convention: ICCA International Arbitration Conference* (Kluwer 2009) 40.

⁸Robert Alexy, *A Theory of Constitutional Rights* (Julian Rivers tr, OUP 2002). See International Law Commission, *Fragmentation of International Law: Difficulties Arising from the Diversification*

characterised as rules, the application of proportionality analysis may not be appropriate.⁹ As an example of this, the application of proportionality analysis has not generally been accepted in the context of denial of justice claims. Jan Paulsson, acting as sole arbitrator in *Pantechniki v Albania*, stated that there would appear to be two reasons for this:

The first is that international responsibility does not relate to physical infrastructure; states are not liable for denial of justice because they cannot afford to put at the public's disposal spacious buildings or computerised information banks. What matters is rather the human factor of obedience to the rule of law. Foreigners who enter a poor country are not entitled to assume that they will be given things like verbatim transcripts of all judicial proceedings – but they are entitled to decision-making which is neither xenophobic nor arbitrary. The second is that a relativistic standard would be none at all. International courts or tribunals would have to make ad hoc assessments based on their evaluation of the capacity of each state at a given moment of its development. International law would thus provide no incentive for a state to improve.¹⁰

To give a further example, where a host state can either only comply with its obligations under another non-investment related treaty (such as a human rights treaty) by failing to comply with an IIA (or *vice versa*) or where the goals of one of these treaties frustrates the goals of another treaty without strict incompatibility between their provisions, a direct treaty conflict occurs.¹¹ In such circumstances, this conflict between different treaties simply cannot be resolved through mechanisms such as proportionality (or indeed through application of customary methods of treaty interpretation) as both treaty obligations constitute rules.¹²

and Expansion of International Law, UN Doc A/CN.4/L.682 (13 April 2006) (finalised by Martti Koskenniemi) para 19.

⁹See Benedict Kingsbury and Stephan W Schill, 'Public Law Concepts to Balance Investors' Rights with State Regulatory Actions in the Public Interest – The Concept of Proportionality' in Stephan W Schill (ed), *International Investment Law and Comparative Public Law* (OUP 2010) 78. See also Federico Ortino, 'Refining the content and role of investment 'rules' and 'standards': A bolder approach to international investment treaty-making' (2013) 28 ICSID Rev 152 on the advantages of rules over standards in the context of international investment law.

¹⁰ICSID Case No ARB/07/21, Award 30 July 2009, para 76.

¹¹International Law Commission, *Fragmentation of International Law: Difficulties Arising from the Diversification and Expansion of International Law*, UN Doc A/CN.4/L.682 (13 April 2006) (finalised by Martti Koskenniemi) para 24.

¹²Jan Klabbbers, 'Beyond the Vienna Convention: Conflicting Treaty Provisions' in Enzo Cannizzaro (ed), *The Law of Treaties Beyond the Vienna Convention* (OUP 2011).

Thus, the application of proportionality analysis may not be appropriate in the case of some conflicts between competing rights or interests and its major field of application is rather those cases in which the state redistributes or interferes with property rights in the interest of protecting some non-economic interest by means of general legislation or administrative regulation.¹³ However, even in those awards in which proportionality has been referred to, an award that applies all three steps of suitability, necessity and proportionality *stricto sensu* is rare¹⁴ and, in several awards, tribunals have moved straight to the third step of proportionality analysis – proportionality *stricto sensu* – without considering (at least explicitly) the questions of suitability and necessity. For example, in *Tecmed v Mexico*, which concerned a refusal by a Mexican government agency to renew an authorisation to operate a landfill site, the tribunal proceeded directly to the strict proportionality test by stating that there must be ‘a reasonable relationship of proportionality between the charge or weight imposed to the foreign investor and the aim sought to be realized by any expropriatory measure’.¹⁵ Jurisprudence of the European Court of Human Rights was referred to in support of applying such a test, although the tribunal did not explain its reasons for so doing.¹⁶ In applying the proportionality test, the *Tecmed* tribunal took the view that ‘a serious urgent situation, crisis, need or social emergency’ could be ‘weighed against the deprivation or neutralization of the economic or commercial value of the Claimant’s investment’ to lead to the conclusion that an otherwise expropriatory regulation does not amount to an expropriation under the investment treaty and international law.¹⁷ The tribunal then went on to examine the two main public interest reasons put forward by the host state for its actions: the protection of the environment and public health and the need to provide a response to community pressure. The tribunal concluded on the

¹³Benedict Kingsbury and Stephan W Schill, ‘Public Law Concepts to Balance Investors’ Rights with State Regulatory Actions in the Public Interest – The Concept of Proportionality’ in Stephan W Schill (ed), *International Investment Law and Comparative Public Law* (OUP 2010) 78.

¹⁴Benedict Kingsbury and Stephan Schill, ‘Investor-State Arbitration as Governance: Fair and Equitable Treatment, Proportionality and the Emerging Global Administrative Law’ in Albert Jan van den Berg (ed), *50 Years of the New York Convention: ICCA International Arbitration Conference* (Kluwer 2009) 32; Erlend M Leonhardsen, ‘Looking for Legitimacy: Exploring Proportionality Analysis in Investment Treaty Arbitration’ (2012) 3 J Intl Dispute Settlement 95.

¹⁵ICSID Case No ARB(AF)/99/2, Award 29 May 2003, paras 118-22.

¹⁶Kriebaum notes that the *Tecmed* tribunal used proportionality analysis to determine whether an expropriation had occurred whereas the European Court of Human Rights uses it to determine whether an expropriation is justified: Ursula Kriebaum, ‘Regulatory Takings: Balancing the Interests of the Investor and the State’ (2007) 8 J World Investment & Trade 717, 728.

¹⁷ICSID Case No ARB(AF)/99/2, Award 29 May 2003, para 139.

evidence that the impugned host state measure was motivated in part by the latter socio-political factor but held that ultimately neither the environmental concerns nor the threat of civil disturbance due to public protests could provide a satisfactory justification for the host government's effective taking of the claimant's investment and so an expropriation was deemed to have occurred.¹⁸ Thus, the host state's motivations in adopting the impugned measure were examined as part of proportionality *stricto sensu* analysis rather than at the suitability and necessity stages of the analysis. This approach, which has also been taken in other subsequent cases,¹⁹ is problematic in that it lends itself to decision-making based on arbitrators' value judgments along with a lack of appreciation for the context in which the impugned measures were taken and, in particular, the alternatives available to the host state.²⁰

In addition to this lack of rigour in the application of proportionality analysis, the application of the concept of proportionality has been uneven as across the principal rights conferred by IIAs with indirect expropriation becoming 'the main arena for the development of legal tests close to proportionality'.²¹ This has occurred despite the fact that the application of proportionality analysis to indirect expropriations is particularly problematic given that the public purpose underlying the host state measure must also be considered as one of the criteria in deciding whether the expropriation is lawful or not. Thus, consideration of the purpose of the measure in determining whether an expropriation occurred in the first place (as part of proportionality analysis) can lead to conceptual difficulty as expropriation is not *a priori* prohibited in international law but rather is lawful provided certain requirements are met (i.e. that the measure was taken for a public purpose, on a non-discriminatory basis, in accordance with due process of law and that compensation is provided).²² Despite this difficulty however, references to proportionality are less explicit and the analysis is undoubtedly less well developed under the FET and non-discrimination standards than in respect of indirect

¹⁸ibid, paras 124-47.

¹⁹See for example *Azurix v Argentina*, ICSID Case No ARB/01/12, Award 14 July 2006, paras 311-13.

²⁰Roland Kläger, 'Fair and Equitable Treatment' in *International Investment Law* (Cambridge University Press 2011) 243.

²¹Benedikt Pirker, *Proportionality Analysis and Models of Judicial Review* (Europa Law Publishing 2013) 355.

²²Ursula Kriebaum, 'Regulatory Takings: Balancing the Interests of the Investor and the State' (2007) 8 *J World Investment & Trade* 717, 726.

expropriations.²³ Thus, in relation to the FET standard, instead of applying proportionality analysis, tribunals have instead tended to weigh the investor's reasonable and legitimate expectations against the host state's legitimate regulatory interests in the particular circumstances.²⁴ For example, in *Saluka v Czech Republic* the tribunal noted that no investor could reasonably expect that the circumstances prevailing at the time the investment was made remain totally unchanged and that, in order to determine whether frustration of the foreign investor's expectations was justified and reasonable, the host state's legitimate right to subsequently regulate domestic matters in the public interest should be taken into consideration. The tribunal thus concluded that the determination of whether a breach of the FET standard had occurred 'requires a weighing of the Claimant's legitimate and reasonable expectations on the one hand and the Respondent's legitimate regulatory interests on the other'.²⁵ Similarly, in applying the national treatment and MFN standards, which require comparison of the treatment of the claimant investor with, in the case of the national treatment standard, the treatment of domestic investors in like circumstances, and in the case of the MFN standard, the treatment of other foreign investors in like circumstances, proportionality has generally not been referred to but some tribunals have instead applied the 'like circumstances' concept as a justification mechanism for taking account of public interest considerations.²⁶ For example, in *Parkerings v Lithuania*²⁷ the tribunal stated that the claimant investor and a competitor were not 'in like circumstances' due to differences in the size of the construction projects undertaken by the two as well as a significant extension of the claimant's project into the Old Town area of Vilnius which raised concerns as regards historical and archaeological preservation and environmental protection. Thus, the tribunal determined that the city of Vilnius had legitimate grounds to distinguish between the two projects.²⁸ The national administrative

²³Benedikt Pirker, *Proportionality Analysis and Models of Judicial Review* (Europa Law Publishing 2013) 355-69.

²⁴*ibid.*

²⁵UNCITRAL, Partial Award 17 March 2006, paras 304-07. See also Elizabeth Snodgrass, 'Protecting Investors' Legitimate Expectations: Recognizing and Delimiting a General Principle' (2006) 21 ICSID Rev 1, 57.

²⁶Federico Ortino, 'Non-Discriminatory Treatment in Investment Disputes' in Pierre-Marie Dupuy, Ernst-Ulrich Petersmann and Francesco Francioni (eds), *Human Rights in International Investment Law and Arbitration* (OUP 2009) 360.

²⁷ICSID Case No ARB/05/8, Award 11 September 2007.

²⁸*ibid.*, paras 392-96. See also *SD Myers, Inc. v Canada*, UNCITRAL, First Partial Award 13 November 2000, para 250.

authorities in this case had referred to international treaties, especially the 1972 UNESCO World Heritage Convention, and expressed their fear of infringing their international obligations if the claimant investor's plans were realised.²⁹ To give a further example, in *GAMI v Mexico* the tribunal concluded that the Mexican government had expropriated certain mills on the basis of its perception that it was in the interest of the national economy to have public participation in mills operating at near insolvency and, on that basis, concluded that those mills that had not been expropriated were not in like circumstances as the expropriated mills so as to give rise to a violation of the national treatment standard.³⁰

Overall therefore, indeterminacy of both a procedural and analytical nature surrounds the balancing exercise currently conducted by most investment treaty arbitration tribunals³¹ and, despite the wealth of academic commentary describing the manner in which proportionality testing has been applied to date and discussing how it should be applied in future investment treaty arbitration cases,³² the concept of proportionality has in reality only been mentioned in a relatively small number of investment treaty arbitration awards.³³

There has also been little coherence in arbitral practice to date as to the standard of review to be applied by investment treaty arbitration tribunals.³⁴ While IIAs tend to say nothing, or only very little, about the appropriate standard of review, in fact, the standard of review applied by arbitrators is crucial as proportionality analysis, as a

²⁹ibid, paras 382-92.

³⁰*GAMI Investments, Inc. v Mexico*, UNCITRAL, Final Award 15 November 2004, para 114.

³¹Benedict Kingsbury and Stephan Schill, 'Investor-State Arbitration as Governance: Fair and Equitable Treatment, Proportionality and the Emerging Global Administrative Law' in Albert Jan van den Berg (ed), *50 Years of the New York Convention: ICCA International Arbitration Conference* (Kluwer 2009) 32; Erlend M Leonhardsen, 'Looking for Legitimacy: Exploring Proportionality Analysis in Investment Treaty Arbitration' (2012) 3 J Intl Dispute Settlement 95.

³²See for example Alec Stone Sweet and Jud Mathews, 'Proportionality Balancing and Global Constitutionalism' (2008) 47 Colum J Transnational L 73; Benedict Kingsbury and Stephan W Schill, 'Public Law Concepts to Balance Investors' Rights with State Regulatory Actions in the Public Interest – The Concept of Proportionality' in Stephan W Schill (ed), *International Investment Law and Comparative Public Law* (OUP 2010); Jürgen Kurtz, 'Adjudging the Exceptional at International Law: Security, Public Order and Financial Crisis' (2010) 59 ICLQ 325; Alec Stone Sweet, 'Investor-State Arbitration: Proportionality's New Frontier' (2010) 4 Law & Ethics of Human Rights 47; Benedikt Pirker, *Proportionality Analysis and Models of Judicial Review: A Theoretical and Comparative Study* (Europa Law Publishing 2013) ch 8.

³³See David Schneiderman, 'Legitimacy and Reflexivity in International Investment Arbitration: A New Self-Restraint?' 2011 1 Oñati Socio-Legal Series 16 noting that of 23 decisions between 1994-2010 which mentioned expressly or impliedly proportionality, in only 13 did tribunals approvingly invoke proportionality analysis in discussing the law and, among these, only 8 tribunals actually applied some type of proportionality analysis.

³⁴Caroline Henckels, 'Indirect Expropriation and the Right to Regulate: Revisiting Proportionality Analysis and the Standard of Review in Investor-State Arbitration' (2012) 15 J Intl Economic L 223, 238-39.

method of review, does not produce substantive outcomes or provide any normative guidance to arbitrators.³⁵ Thus, while methods of review are techniques used to determine the permissibility of interference with the primary norm, standards of review refer to the intensity with which the method of review is applied.³⁶ Therefore, as noted by Pirker:

An understanding of proportionality analysis that does not incorporate features like the flexibility of adjudication, the standard of review and the burden of proof is simply incomplete.³⁷

In particular, the crucial effect of the standard of review utilised in interpreting IIA rights has increasingly been recognised by commentators as well as by some investment treaty arbitration tribunals as, depending on the standard of review chosen, a tribunal may either defer entirely to the justifications provided by national authorities, may undertake a completely independent review of the measure in question or may steer a middle course between these two extremes.³⁸ A strict standard of review whereby the tribunal undertakes an independent review of the host state measure and substitutes its own views for those of the host state is problematic in that it can potentially undermine host state regulatory sovereignty, particularly in the case of certain regulatory purposes such as protection of health or of the environment, which operate on a different level of generality to principles of

³⁵Anthea Roberts, 'The Next Battleground: Standards of Review in Investment Treaty Arbitration' (2011) 16 International Council for Commercial Arbitration Congress Series 170. See also William W Burke-White and Andreas Von Staden, 'Private Litigation in a Public Law Sphere: The Standard of Review in Investor-State Arbitrations' (2010) 35 Yale J Intl L 283; Caroline Henckels, 'Indirect Expropriation and the Right to Regulate: Revisiting Proportionality Analysis and the Standard of Review in Investor-State Arbitration' (2012) 15 J Intl Economic L 223; Caroline E Foster, 'Adjudication, Arbitration and the Turn to Public Law "Standards of Review": Putting the Precautionary Principle in the Crucible' (2012) 3 J Intl International Dispute Settlement 525; Stephan Schill, 'Deference in Investment Treaty Arbitration: Re-conceptualizing the Standard of Review' (2012) 3 J Intl Dispute Settlement 577.

³⁶Caroline Henckels, 'Balancing Investment Protection and the Public Interest: The Role of the Standard of Review and the Importance of Deference in Investor-State Arbitration' (2013) 4 J Intl Dispute Settlement 197, 199; cf William W Burke-White and Andreas Von Staden, 'Private Litigation in a Public Law Sphere: The Standard of Review in Investor-State Arbitrations' (2010) 35 Yale J Intl L 283, 334-37 suggesting that proportionality is a standard of review.

³⁷Benedikt Pirker, *Proportionality Analysis and Models of Judicial Review* (Europa Law Publishing 2013) 43.

³⁸Mads Andenas and Stefan Zleptnig, 'Proportionality: WTO Law: in Comparative Perspective' (2006-2007) 42 Tex Intl L J 371, 392-93; Han Xiuli, 'The Application of the Principle of Proportionality in Tecmed v. Mexico' (2007) 6 Chinese J Intl L 633; Benedict Kingsbury and Stephan Schill, 'Investor-State Arbitration as Governance: Fair and Equitable Treatment, Proportionality and the Emerging Global Administrative Law' in Albert Jan van den Berg (ed), *50 Years of the New York Convention: ICCA International Arbitration Conference* (Kluwer 2009) 51-52.

investor protection³⁹ and which do not lend themselves easily to cost-benefit analysis.⁴⁰ Furthermore, given the inability of tribunals to obtain all relevant information after the fact and the lack of proximity of non-tenured arbitrators to the social, economic and political circumstances of the host state at the time the measure was taken,⁴¹ a strict standard of review ignores the greater institutional competence and expertise of host state authorities. In light of both of these issues, a standard of review that accords a degree of deference⁴² to the host state's decisions has been favoured by several commentators,⁴³ with the proviso that a deferential standard of review cannot be applied in all circumstances as to do so would lead to serious procedural flaws and arbitrary behaviour going unsanctioned.⁴⁴ In this regard, some commentators have argued that the 'margin of appreciation' standard of review, most known for its application by the European Court of Human Rights, could be drawn upon.⁴⁵ The 'margin of appreciation' standard of review can be defined as the 'breadth of deference' that the European Court of Human Rights is willing to grant to national decision makers and recognises that the normative

³⁹Anne van Aaken, 'Defragmentation of Public International Law through Interpretation: A Methodological Proposal' (2009) 16 *Ind J Global Legal Stud* 483, 500.

⁴⁰Åsa Romson, 'International Investment Law and the Environment' in Marie-Claire Cordonier Segger, Markus W Gehring and Andrew Newcombe (eds), *Sustainable Development in World Investment Law* (Kluwer 2011) 37-52. See also Caroline E Foster, 'Adjudication, Arbitration and the Turn to Public Law 'Standards of Review': Putting the Precautionary Principle in the Crucible' (2012) 3 *J Intl Dispute Settlement* 525 arguing that greater reference to the precautionary principle could constitute an alternative to reliance on standards of review in investment treaty arbitration in appropriate cases.

⁴¹Bendikt Pirker, *Proportionality Analysis and Models of Judicial Review: A Theoretical and Comparative Study* (Europa Law Publishing 2013) 342.

⁴²Schill defines deference as follows: 'deference is...a parameter of the relationship between international and domestic law and protects a state's domestic policy space against control by international law and international tribunals': see Stephan Schill, 'Deference in Investment Treaty Arbitration: Re-conceptualizing the Standard of Review' (2012) 3 *J Intl Dispute Settlement* 577, 583.

⁴³William W Burke-White and Andreas Von Staden, 'Private Litigation in a Public Law Sphere: The Standard of Review in Investor-State Arbitrations' (2010) 35 *Yale J Intl L* 283; Stephan Schill, 'Deference in Investment Treaty Arbitration: Re-conceptualizing the Standard of Review' (2012) 3 *J Intl Dispute Settlement* 577; Caroline Henckels, 'Balancing Investment Protection and the Public Interest: The Role of the Standard of Review and the Importance of Deference in Investor-State Arbitration' (2013) 4 *J Intl Dispute Settlement* 197; cf José E Álvarez and Kathryn Khamsi, 'The Argentine Crisis and Foreign Investors: a Glimpse into the heart of the Investment Regime' in Karl P Sauvart (ed), *The Yearbook of International Investment Law and Policy 2008-2009* (OUP 2009) 442-47.

⁴⁴Caroline Henckels, 'Balancing Investment Protection and the Public Interest: The Role of the Standard of Review and the Importance of Deference in Investor-State Arbitration' (2013) 4 *J Intl Dispute Settlement* 197, 209. See also Yuval Shany, 'Toward a General Margin of Appreciation Doctrine in International Law?' (2005) 16 *Eur J Intl L* 907, 913-40.

⁴⁵*ibid.* See also Valentina Vadi and Lukasz Gruszczynski, 'Standards of Review in International Investment Arbitration: Multilevel Governance and the Common Weal' (2013) 16 *J Intl Economic L* 613 arguing that WTO standards of review could potentially be used as a reference point in investment treaty arbitration.

requirements articulated in the text of the European Convention on Human Rights can be legitimately met by a range of different measures, which strike an acceptable balance between individual rights and governmental interests.⁴⁶ However, this standard is premised on what binds the members of the European human rights regime, namely their common democratic systems of government,⁴⁷ which unifying principle is not present in the area of investment law.⁴⁸ While this does not, of itself, detract from the argument that a deferential standard of review should be applied in the field of investment treaty arbitration, it does suggest that the conceptual bases for granting deference to host states must be consonant with the specific nature of investment law and of investment treaty arbitration in order to both recognise regulatory autonomy but also to avoid diluting the substance of investor rights on the basis of ‘deference’.⁴⁹ However, investment treaty arbitration tribunals to date have not approached the question of deference to host state authorities in a principled manner and there has been little indication of the development of a coherent standard of review in arbitral practice.⁵⁰

While not wishing to downplay the significance of the issues associated with the lack of coherence displayed by investment treaty arbitration tribunals in the standard of review applied in reviewing host state acts and with the perfunctory engagement of tribunals with proportionality analysis to date,⁵¹ these issues, do not, in and of themselves, go to the efficacy of proportionality analysis. Thus, tribunals could, over time, conceivably begin to apply proportionality analysis more

⁴⁶William Burke-White and Andreas von Staden, ‘The Need for Public Law Standards of Review in Investor-State Arbitrations’ in Stephan W Schill (ed), *International Investment Law and Comparative Public Law* (OUP 2010) 701.

⁴⁷José E Álvarez and Kathryn Khamsi, ‘The Argentine Crisis and Foreign Investors: a Glimpse into the heart of the Investment Regime’ in Karl P Sauvant (ed), *The Yearbook of International Investment Law and Policy 2008-2009* (OUP 2009). See also Julian Arato, ‘The Margin of Appreciation in International Investment Law’ 54 *Va J Intl L* 545 for a more general critique of the application of the margin of appreciation doctrine in the sphere of investment treaty arbitration.

⁴⁸See *Siemens AG v Argentina*, ICSID Case No ARB/02/8, Award 6 February 2007, para 354.

⁴⁹It has been suggested that there are two key bases for deference that are particularly relevant to investor-state arbitration (and international adjudication generally) - considerations of regulatory autonomy and proximity and relative institutional competence and expertise - and that these factors should inform the standard of review applied: Caroline Henckels, ‘Balancing Investment Protection and the Public Interest: The Role of the Standard of Review and the Importance of Deference in Investor-State Arbitration’ (2013) 4 *J Intl Dispute Settlement* 197. See also Stephan Schill, ‘Deference in Investment Treaty Arbitration: Re-conceptualizing the Standard of Review’ (2012) 3 *J Intl Dispute Settlement* 577.

⁵⁰*ibid.*

⁵¹Valentina Vadi and Lukasz Gruszczynski, ‘Standards of Review in International Investment Arbitration: Multilevel Governance and the Common Weal’ (2013) 16 *J Intl Economic L* 613, 614-15.

consistently and to develop conceptual bases for deferring to host state decisions in appropriate circumstances⁵² (albeit that comparative law analysis indicates that other adjudicative fora have had limited success in this regard).⁵³ However, it is submitted that a more fundamental issue is the question of why the majority of investment treaty arbitration tribunals have to date steered clear of proportionality analysis or, more generally, of the notion of proportionality or balancing, despite the wealth of academic commentary on the issue, much of which endorses the application of some form of proportionality analysis in investment treaty arbitration. As suggested above, this reluctance may partly stem from the conceptualisation of certain IIA disputes by claimant investors or by tribunals themselves as involving rules rather than principles.⁵⁴ For example, the elucidation of the FET standard in *Tecmed*⁵⁵ (which has been cited by many subsequent tribunals) and the *Tecmed* tribunal's subsequent decision that the FET standard had been breached⁵⁶ represents an instance of rule-like decision-making,⁵⁷ which rendered the application of proportionality analysis inapposite. This pronouncement can be seen as somewhat ironic given that *Tecmed* is generally regarded as the first publicly available award in which an investment treaty arbitration tribunal explicitly invoked the proportionality principle (such invocation being in the context of the expropriation clause). Incidentally, this highlights a further, more practical, issue with the application of proportionality analysis (i.e. that the effect of the application of proportionality analysis may be limited in circumstances where it is not applied to all alleged breaches of the relevant IIA).

A further reason for the cursory engagement of investment treaty arbitration tribunals with proportionality analysis to date may be doubts on the part of certain

⁵²See Julian Arato, 'The Margin of Appreciation in International Investment Law' 54*Va J Intl L* 545, 572-75 arguing that through judicial dialogue across tribunals over the medium to long term, a more coherent, certain and legitimate approach to the standard of review can be achieved.

⁵³See generally Benedikt Pirker, *Proportionality Analysis and Models of Judicial Review* (Europa Law Publishing 2013).

⁵⁴Since rules and principles are rather extreme norms and more typical norms exhibit both rule-like and principle-like elements, characterising a particular norm as a rule-like provision should be possible in many cases: see Ralf Poscher, 'The Principles Theory - How many theories and what is their merit?' in Matthias Klatt (ed), *Institutionalized Reason: The Jurisprudence of Robert Alexy* (OUP 2011) 29.

⁵⁵*Tecnicas Medioambientales Tecmed SA v Mexico*, ICSID Case No ARB(AF)/99/2, Award 29 May 2003, para 154.

⁵⁶*ibid*, paras 154-74.

⁵⁷See Roland Kläger, 'Fair and Equitable Treatment' in *International Investment Law* (Cambridge University Press 2011) 123-25 for a criticism of rule-like decision making in the context of the FET standard.

tribunals as to whether this quintessentially public law concept (which is typically applied in the fields of human rights or constitutional rights adjudication) should be applied in the field of investment treaty arbitration at all given the hybrid nature of the investment treaty arbitration system.⁵⁸ This uncertainty may be accompanied by concerns as to whether investment treaty arbitration tribunals are best placed to engage in the complex evaluations required to apply proportionality analysis (and, in particular, the criterion of proportionality *stricto sensu*).⁵⁹ While the application of a deferential standard of review could assist in overcoming the latter issue, the hybrid nature of investment treaty arbitration and the distinctions that can be drawn between it and the fields of human rights or constitutional rights adjudication are likely to continue to pose a challenge to the widespread application of proportionality analysis by investment treaty arbitration tribunals.

Finally and crucially, the ‘asymmetric’ nature of the investment treaty arbitration system (i.e. the fact that the system is focussed on the protection of the interests of a particular group of individuals (namely foreign investors))⁶⁰ sits uneasily with the proposition that investor and host state interests should be accorded equal weight in the balancing exercise.⁶¹ Thus, typically proportionality analysis is applied to reconcile the tension between a right on the one hand and a public interest that is recognised within the relevant legal text (such as a constitution or international human rights treaty) and where the text in question may, either expressly or by its tenor, require that a balance between those interests be maintained.⁶² However, there is scant recognition of interests other than those of investors in the text of IIAs. This means that, while the proposition that states have a right to regulate in the public interest is universally recognised, given that the core assumption underlying IIAs can be considered to be that protecting the rights of foreign investors will lead to further foreign investment and economic development (which

⁵⁸See Benedikt Pirker, ‘Seeing the Forest Without the Trees—The Doubtful Case for Proportionality Analysis in International Investment Arbitration’ Highly Commended Essay, Society of International Economic Law/Cambridge University Press Essay Prize 2011 <<http://ssrn.com/abstract=1926166>> accessed 19 March 2015.

⁵⁹*ibid.*

⁶⁰Arguably such treaties need to be asymmetric to address the asymmetry in power that exists as between the state as sovereign and individuals: see Andrea K Bjorklund, ‘The Role of Counterclaims in Rebalancing Investment Law’ (2013) 17 Lewis & Clark L Rev 461, 462.

⁶¹Alec Stone Sweet and Jud Mathews, ‘Proportionality Balancing and Global Constitutionalism’ (2008) 47 Colum J Transnational L 73, 89 noting that ‘the move to balancing makes it clear (a) that each party is pleading a constitutionally-legitimate norm or value; (b) that, *a priori*, the court holds each of these interests in equally high esteem...’

⁶²*ibid.*, 91 for examples.

can be considered in the public interest), uncertainty exists as to what exactly is meant by a public interest in circumstances where such interests are proffered as a reason why investor rights should be curtailed.⁶³ One possible means of differentiating between the two types of interest is that, while investment can be described as going to the ‘efficiency’ aspect of the public interest (i.e. the size of the overall benefits available to society), arguments based on the public interest that aim to limit investor rights may align more closely to the ‘equity’ dimension of the public interest (i.e. the relative distribution of those endowments to individuals under a fair and just process).⁶⁴ However, while useful conceptually, this distinction does not offer substantial guidance as to how the two types of interest should be balanced and the ‘asymmetric’ nature of the investment treaty arbitration system also means that it is not possible to draw guidance from how the concept of public interest has been delineated in other legal contexts.⁶⁵ This uncertainty is problematic as balancing requires clearly defined rights and public interests.⁶⁶ Furthermore, although there are strong arguments to be made in favour of the application of a more deferential standard of review in investment treaty arbitration, the application of a deferential standard of review can nonetheless be seen as somewhat at odds with the nature of the investment treaty system as, within the parameters of such a system, investor rights can be considered fundamental rights and the protection of such rights the primary object of the system, which may suggest that a more intense level of scrutiny is appropriate.⁶⁷

In order to address some of these difficulties associated with the application of proportionality analysis in the sphere of investment treaty arbitration, it has been suggested that a modified form of proportionality analysis be applied which focusses primarily on the first two sub-tests (suitability and necessity). Under this

⁶³Nigel Blackaby, ‘Public Interest and Investment Treaty Arbitration’ in Albert Jan van den Berg (ed), *International Commercial Arbitration: Important Contemporary Questions: ICCA Congress Series 2002* (Kluwer 2003) 355; cf Benedikt Pirker, *Proportionality Analysis and Models of Judicial Review: A Theoretical and Comparative Study* (Europa Law Publishing 2013) 349-52 arguing that it is as yet unclear whether investment is viewed as a public interest under international investment law.

⁶⁴Burton A Weisbrod, ‘Conceptual Perspective on the Public Interest: An Economic Analysis’ in Burton A Weisbrod, Joel F Handler and Neil K Komesar, *Public Interest Law: An Economic and Institutional Analysis* (University of California Berkeley Press 1978) 4.

⁶⁵Benedikt Pirker, *Proportionality Analysis and Models of Judicial Review* (Europa Law Publishing 2013) ch 8.

⁶⁶ibid, 350.

⁶⁷Where fundamental rights are at issue, a stricter level of scrutiny has often been applied under other legal regimes: see Janneke Gerards, ‘Pluralism, Deference and the Margin of Appreciation Doctrine’ (2011) 17 Eur L J 80, 87-101.

modified form of analysis, the final sub-test of proportionality *stricto sensu* would only be applied in exceptional cases.⁶⁸ It has been suggested that this would accord with the ‘asymmetric’ nature of the investment treaty arbitration system as the suitability and necessity sub-tests, while still requiring some value judgment on the part of arbitrators, do not require the balancing of values that is required by the final sub-test of proportionality *stricto sensu*.⁶⁹ However, reducing the role of proportionality *stricto sensu* to a marginal one could potentially allow an investor right to be severely restricted in order to protect a negligible public interest. Conversely, curtailing proportionality analysis in this manner would also reduce the ability of arbitrators to taken into account a range of third party interests, consideration of which may be required in order to ensure that host state interests are optimised.⁷⁰ For example, where a host state measure has been taken to meet two or more separate public policy objectives (as was, for example, the case in *Tecmed*), application of a necessity test only would be ineffective in order to sufficiently take account of both such objectives and recourse to the proportionality *stricto sensu* stage of the analysis (or to some form of balancing test) would appear to be required.⁷¹

In summary therefore, while proportionality analysis offers a transparent and methodologically robust structure for decision-making engaging competing public and private interests,⁷² it is not appropriate for resolving conflicts between rules. In addition, the vagueness of the values underlying the investment treaty arbitration system and the ‘asymmetric’ nature of the system makes it difficult for tribunals to apply proportionality analysis or, more generally, to balance investor and host state interests in making the black-or-white decision as to liability required at the merits stage. Modifying proportionality analysis to reduce the role of proportionality

⁶⁸Benedikt Pirker, *Proportionality Analysis and Models of Judicial Review* (Europa Law Publishing 2013) ch 8. See also Caroline Henckels, ‘Balancing Investment Protection and the Public Interest: The Role of the Standard of Review and the Importance of Deference in Investor–State Arbitration’ (2013) 4 J Intl Dispute Settlement 197.

⁶⁹Benedikt Pirker, *Proportionality Analysis and Models of Judicial Review* (Europa Law Publishing 2013) ch 2.

⁷⁰Alec Stone Sweet, ‘Investor-State Arbitration: Proportionality's New Frontier’ (2010) 4 Law & Ethics of Human Rights 47, 60ff on the advantages of balancing in terms of appreciating the entire context of a dispute.

⁷¹Benedikt Pirker, *Proportionality Analysis and Models of Judicial Review* (Europa Law Publishing 2013) 29.

⁷²Caroline Henckels, ‘Indirect Expropriation and the Right to Regulate: Revisiting Proportionality Analysis and the Standard of Review in Investor-State Arbitration’ (2012) 15 J Intl Economic L 223, 228-29.

stricto sensu does not fully address this issue and is not without its own problems. Comparable issues arise when attempts are made to rely on the host state's non-investment related international obligations as a means of justifying the impugned host state action. These issues will now be considered.

3.3 *Reliance on the state's non-investment related international obligations*

Similarly to the cursory manner in which investment treaty arbitration tribunals have engaged with proportionality analysis to date, host states and *amici curiae* have met with little success in introducing arguments based on the host state's non-investment related treaty obligations and, in particular, their obligations under human rights treaties.⁷³ Thus, investment treaty arbitration tribunals have generally avoided dealing with non-investment related host state obligations or have not regarded such obligations as significant to investment disputes,⁷⁴ although this may be at least partly attributable to the failure of host states to directly plead arguments based on such obligations, in particular human rights obligations, as independent defences.⁷⁵ For example, in *Siemens v Argentina* the tribunal held that the human rights-based argument put forward by Argentina had not been fully developed and that 'without the benefit of further elaboration and substantiation by the parties, it is not an argument that, *prima facie*, bears any relationship to the merits of the case'.⁷⁶ The tribunal also noted that it failed to identify any contradiction between Siemens' contractual rights and Argentina's wider human rights obligations and that Argentina's human rights arguments were thus immaterial to the case. The tribunal

⁷³See High Commissioner for Human Rights, *Human Rights, Trade and Investment*, UN Doc E/CN.4/Sub.2/2003/9 (2003) 57 in which the High Commissioner for Human Rights encourages states to raise their human rights obligations where a decision of a tribunal might affect the enjoyment of human rights.

⁷⁴Anne van Aaken, 'International investment law between commitment and flexibility: a contract theory analysis' (2009) 12 J Intl Economic L 507, 530; Clara Reiner and Christoph Schreuer, 'Human Rights and International Investment Arbitration' in Pierre-Marie Dupuy, Ernst-Ulrich Petersmann and Francesco Francioni (eds), *Human Rights in International Investment Law and Arbitration* (OUP 2009) 82-83.

⁷⁵Tra T Pham, 'International investment treaties and arbitration as imbalanced instruments: a revisit' (2010) Intl Arbitration L Rev 81, 93-94. There is some debate as to whether a tribunal can consider a host state's other obligations, in circumstances where the host state does not raise such obligations itself: see Andrew Newcombe and Lluís Paradell, *Law and Practice of Investment Treaties: Standards of Treatment* (Kluwer 2009) 89-90; Teresa Isele, 'The Principle *Iura Novit Curia* in International Commercial Arbitration' (2010) 1 Intl Arbitration L Rev 14; Chester Brown, 'Bringing Sustainable Development Issues before Investment treaty arbitration tribunals' in Marie-Claire Cordonier Segger, Markus W Gehring and Andrew Newcombe (eds), *Sustainable Development in World Investment Law* (Kluwer 2011) 175-88.

⁷⁶ICSID Case No ARB/02/8, Award 6 February 2007, para 79.

in *CMS v Argentina* also held that there was no ‘collision’ between the relevant BIT and either the Argentine Constitution or the human rights treaties to which Argentina was a party as ‘the Constitution carefully protects the right to property, just as the treaties on human rights do, and secondly because there is no question of affecting fundamental human rights when considering the issues disputed by the parties’.⁷⁷ These pronouncements (albeit somewhat throwaway in nature) would appear to suggest that, unless the host state’s other treaty obligations ‘collide’ (i.e. directly conflict) with its obligations under the relevant IIA (which, as noted above, leads to a ‘stalemate’ that cannot be resolved through application of either proportionality analysis or the customary international law of treaty interpretation), its non-investment related treaty obligations are largely irrelevant to tribunals’ consideration of whether the IIA was breached or not.

Thus, the question of whether (and how) host states can rely on their non-investment related treaty obligations as a defence to IIA claims is far from settled and the engagement by arbitral tribunals (and arguably respondent host states) with arguments based on such obligations has been perfunctory. However, it has been argued that wider regulatory concerns including human rights could potentially be taken into account either by means of reliance on the customary international law of treaty interpretation or through the application of international law as a whole as the applicable law (whether pursuant to Article 42 of the ICSID Convention or otherwise).⁷⁸ However, it is questionable whether the issues of applicable law and interpretation should be considered separately as, first, international law as applicable law must be introduced into the analysis of a claim under an IIA through the medium of treaty interpretation in the first place⁷⁹ and, secondly, characterising the issue as one of applicable law only does not indicate any particular order for the

⁷⁷ICSID Case No ARB/01/8, Award 12 May 2005, para 121. See also *EDF International S.A., SAUR International S.A. and León Participaciones Argentinas S.A. v. Argentina*, ICSID Case No ARB/03/23, Award 11 June 2012, paras 909-14.

⁷⁸Article 42(1) of the ICSID Convention states that, in the absence of an agreement of the parties on the applicable law, the Tribunal shall apply the law of the Contracting State party to the dispute (including its rules on the conflict of laws) and such rules of international law as may be applicable. The reference to international law in Article 42(1) is understood in the sense given to it in Article 38 of the ICJ Statute: see ‘Report of the Executive Directors of the Convention on the Settlement of Investment Disputes between States and Nationals of other States’ 1 ICSID Rep 31, para 40.

⁷⁹Campbell McLachan, ‘Investment Treaties and General International Law’ in Andrea K Bjorklund, Ian A Laird and Sergey Ripinsky (eds), *Investment treaty law: current issues. III, Remedies in international investment law emerging jurisprudence of international investment law* (British Institute of International and Comparative Law 2008) 115.

consideration of the relevant sources of law.⁸⁰ Thus, the question of whether a host state's non-investment related treaty obligations may be considered in investment treaty arbitration will be considered primarily by reference to customary international law principles of treaty interpretation. However, quite apart from the fact that a host state's duty to fulfil its non-investment related treaty obligations is by no means co-extensive with its right to regulate in the public interest, there are a number of other reasons why arguments based on customary interpretative principles are unlikely to evolve into satisfactory means of taking account of public interest considerations.

First, since the rights conferred on investors by IIAs are generally quite vague and lack a well-defined normative content, it is likely to be difficult to determine the ordinary meaning of such provisions in their context and in light of their object and purpose as required by Article 31(1) of the Vienna Convention on the Law of Treaties.⁸¹ In such circumstances, Article 31(3) of the Vienna Convention goes on to state that, together with the context, there shall be taken into account 'any subsequent agreement between the parties regarding the interpretation of the treaty or the application of its provisions' (Article 31(3)(a)), 'any subsequent practice in the application of the treaty which establishes the agreement of the parties regarding its interpretation' (Article 31(3)(b)) and 'any relevant rules of international law applicable in the relations between the parties' (Article 31(3)(c)). Given that subsequent agreements or practices of the nature referred to in Articles 31(3) (a) and 31(3) (b) are relatively infrequent,⁸² Article 31(3) (c) in particular has been focussed upon. This provision embodies a principle of systemic integration⁸³ which, it is argued, raises a presumption that the parties are to refer to general principles of international law for all questions which the treaty itself does not

⁸⁰ *ibid.*, 136.

⁸¹ It has, however, been suggested that, in accordance with Article 31(1) of the Vienna Convention, a good faith reading of IIAs requires a balance to be struck between investor protection and state regulatory powers: see Andreas Kulick, *Global Public Interest in International Investment Law* (Cambridge University Press 2012) 170.

⁸² See generally Anthea Roberts, 'Power and Persuasion in Investment Treaty Interpretation: the Dual Role of States' (2010) 104 *AJIL* 179.

⁸³ See International Law Commission, *Fragmentation of International Law: Difficulties Arising from the Diversification and Expansion of International Law*, UN Doc A/CN.4/L.682 (13 April 2006) (finalised by Martti Koskenniemi) para 420-79.

resolve in express terms and that, in entering into treaty obligations, the parties⁸⁴ do not intend to act inconsistently with generally recognised principles of international law or with previous treaty obligations towards third states.⁸⁵

While, at first glance, this appears promising in terms of the consideration of the host state's non-investment related treaty obligations, the first point to note is that, similarly to proportionality analysis, this technique cannot resolve a conflict between rule-like provisions.⁸⁶ Secondly, the function and scope of application of Article 31(3)(c) rests upon an understanding of the terms 'relevant rules' and 'applicable to the relations between the parties'. Thus, in the context of investment treaty arbitration, the term 'applicable to the relations between the parties' gives rise to questions as to, *inter alia*, whether it is necessary for all the parties to the IIA to also be parties to the treaty being relied upon as the other source of international law for interpretation purposes⁸⁷ and as to whether the application of the IIA should be interpreted in light of the law in force at the time the treaty was drawn up or the law in force at the time when the treaty is applied.⁸⁸ This distinction could be particularly relevant where a host state purports to rely on obligations under multilateral environmental treaties since this is an area of law that has developed rapidly in recent years. Furthermore, the fact that human rights treaties distinguish between those who hold the rights and those who may invoke the responsibility of a state for breach of those rights leads to further complication and means that if the foreign investor's home state is not party to the human rights treaty on which the host state purports to rely in its defence, the international obligations of the host state towards its citizens would not appear to be applicable.⁸⁹ While it has been suggested that the concept of obligations *erga omnes* (obligations that are owed to

⁸⁴The parties in the investment treaty context would seem to refer to the contracting states to the IIA rather than to the investor and the host state: Bruno Simma, 'Foreign investment arbitration: a place for human rights?' (2011) 60 ICLQ 573, 584.

⁸⁵Philippe Sands, 'Treaty, Custom and the Cross-fertilization of International Law' (1998) 1 Yale Hum Rts & Dev L J 85. See also Jörg Kammerhofer, 'Systemic Integration, Legal Theory and the ILC' (2008) 19 Finnish YB Intl L 157 arguing that systemic integration is not about interpretation properly speaking but rather deals with the separate field of norm conflict.

⁸⁶Jan Klabbers, 'Beyond the Vienna Convention: Conflicting Treaty Provisions' in Enzo Cannizzaro (ed), *The Law of Treaties Beyond the Vienna Convention* (OUP 2011).

⁸⁷International Law Commission, *Fragmentation of International Law: Difficulties Arising from the Diversification and Expansion of International Law*, UN Doc A/CN.4/L.682 (13 April 2006) (finalised by Martti Koskenniemi) paras 470-72.

⁸⁸*ibid*, paras 475-78.

⁸⁹Bruno Simma and Theodore Kill, 'Harmonizing investment protection and international human rights: first Steps towards a Methodology' in Christina Binder and others (eds), *International Investment Law for the 21st Century: Essays in Honour of Christoph Schreuer* (OUP 2009) 700-02.

the entire international community as a whole independent of a treaty) could assist in addressing this problem, it is not well established which norms enjoy *erga omnes* status.⁹⁰ The tribunal in *RosInvest v the Russian Federation* referred to these issues in opining that the phrase ‘applicable in relations between the parties’:

must be taken as a reference to the rules of international law that conditioned the performance of the specific rights and obligations stipulated in the Treaty – or else it would amount to a general licence to override the Treaty terms that would be quite incompatible with the general spirit of the Vienna Convention as a whole.⁹¹

The *RosInvest* tribunal went onto note it was ‘open to serious question, whether [multilateral human rights treaties and the constituent instruments of international organisations] are at all analogous to bilateral engagements regulating a particular area of relations between one Party and the other’.⁹²

Perhaps even more fundamentally, it is by no means self-evident that human rights treaties constitute ‘relevant rules’ in the context of international investment law. While some commentators have argued that the term ‘relevant’ should not be automatically equated to relating to the same subject matter,⁹³ it is equally plausible to argue that, in order to fall under Article 31(3)(c), rules should run parallel to the rule being interpreted, which would mean that only other IIAs or similar instruments applicable in the relations between the parties should be considered (and then only where the earlier sub–articles of Article 31 do not allow the meaning of a treaty provision to be ascertained).⁹⁴

Finally and crucially, even in circumstances where an investment treaty arbitration tribunal determines that a particular rule or source of law is relevant to the interpretation of a particular IIA, the extent to which it should be considered is problematic.⁹⁵ Indeed, even those who argue that host states’ obligations under human rights treaties should be considered ‘relevant rules’ for the purposes of

⁹⁰ibid.

⁹¹SCC Case No V 079/2005, Award on Jurisdiction October 2007, para 39.

⁹²ibid, para 40.

⁹³Bruno Simma and Theodore Kill, ‘Harmonizing investment protection and international human rights: first Steps towards a Methodology’ in Christina Binder and others (eds), *International Investment Law for the 21st Century: Essays in Honour of Christoph Schreuer* (OUP 2009) 695.

⁹⁴John Gaffney, ‘Going to Pieces Without Falling Apart: Wälde’s Defence ‘Specialisation’ in the Interpretation of Investment Treaties’ in J Werner and AH Ali (eds), *A Liber Amicorum: Thomas Wälde – Law Beyond Conventional Thought* (Cameron May 2009) 60.

⁹⁵Campbell McLachlan, ‘The Principle of Systemic Integration and Article 31 (3) (c) of the Vienna Convention’ (2005) 54 ICLQ 279, 310.

Article 31(3)(c) admit that, while any international rule can potentially be considered relevant and thus Article 31(3)(c) can open the door to other non-investment related regimes, the impact of a rule on the interpretation of the investment treaty in dispute should be low in cases where the rule is only relevant at a high level of abstraction.⁹⁶ Thus, determining that a particular rule is relevant (which, in itself, is not uncontroversial) may be the ‘easiest and least consequential among several further steps that must be explored if international human rights law is to interact meaningfully with international investment law’⁹⁷ as the tribunal must then go onto decide whether and to what extent these norms affect the arguments advanced by the parties to a dispute.⁹⁸ This brings into play similar issues to those faced by investment treaty arbitration tribunals in attempting to balance investor interests and public interest considerations through proportionality analysis in the context of a system that is ‘asymmetric’ in nature. Indeed, albeit dealt with separately for analytical purposes, proportionality analysis is not an alternative to interpretation but rather informs the exercise of interpreting a treaty with a view to resolving conflicts between competing rights and interests when the rules of treaty interpretation do not indicate priority of one right or interest over the other.⁹⁹ However, while in other international fora, the application of proportionality analysis subsequent to the use of systemic integration has been employed and can be of assistance in determining the extent to which the external norm in question should be considered,¹⁰⁰ as discussed above, the focus of the investment treaty arbitration system on a particular set of interests makes it difficult to apply proportionality *stricto sensu* meaningfully in assessing liability.

Therefore, even if a host state’s non-investment related treaty obligations are considered relevant rules for the purpose of interpretation of an IIA (a proposition

⁹⁶Bruno Simma and Theodore Kill, ‘Harmonizing investment protection and international human rights: first Steps towards a Methodology’ in Christina Binder and others (eds), *International Investment Law for the 21st Century: Essays in Honour of Christoph Schreuer* (OUP 2009) 696.

⁹⁷*ibid.*, 707.

⁹⁸See David Schneiderman, ‘Legitimacy and Reflexivity in International Investment Arbitration: A New Self-Restraint?’ (2011) 1 *Oñati Socio-Legal Series* 4 noting that systemic integration is ‘a technical device that provides no definitive answers to regime collision...’

⁹⁹Benedict Kingsbury and Stephan W Schill, ‘Public Law Concepts to Balance Investors’ Rights with State Regulatory Actions in the Public Interest – The Concept of Proportionality’ in Stephan W Schill (ed), *International Investment Law and Comparative Public Law* (OUP 2010) 78.

¹⁰⁰Yannick Radi, ‘The ‘Human Nature’ of International Investment Law’ (2013) 10 *Transnational Dispute Management*, 7-8. See also International Law Commission, *Fragmentation of International Law: Difficulties Arising from the Diversification and Expansion of International Law*, UN Doc A/CN.4/L.682 (13 April 2006) (finalised by Martti Koskeniemi) paras 433-60.

which is disputed), the extent to which such obligations should be taken into account in determining whether an IIA breach has occurred or not remains open to question. It is submitted that these factors combined prevent arguments based on the customary international law of treaty interpretation from becoming satisfactory means of introducing arguments based on the host state's obligations under other non-investment related treaties into investment treaty arbitration.

3.4 The defence of necessity and NPM clauses

While not co-extensive with a state's right to regulate in the public interest, one particular situation in which a state may be faced with an IIA claim is where the state has acted to protect its essential interests in times of exigency. In such circumstances, states can potentially avail of a number of customary international law defences. Among these secondary rules of customary international law are the defences of *force majeure*, distress and necessity. The defences of *force majeure* and distress are, however, limited in scope. Thus, the defence of *force majeure* can be invoked only where the state is compelled to act in a manner not in conformity with the requirements of an international obligation incumbent upon it. Accordingly, the act must be brought about by an irresistible force or an unforeseen event, which is beyond the control of the state concerned and which makes it materially impossible in the circumstances to perform the obligation.¹⁰¹ The defence of distress is even narrower as a situation of distress is said to occur only when a state has no other way to safeguard a life in its care than to violate a legal rule.¹⁰² It is unsurprising therefore that neither defence has yet been successfully argued in the investment treaty arbitration context.¹⁰³ However, the defence of necessity is potentially of greater utility. The defence of necessity may apply where a state acts to safeguard an essential interest of the state, although this act violates a

¹⁰¹International Law Commission, *Draft Articles on Responsibility of States for Internationally Wrongful Acts, with commentaries 2001* (2001) 2 YB Intl L Comm'n, UN Doc A/CN.4/SER.A/2001/Add.1 (Part 2) art 23.

¹⁰²*ibid*, art 24.

¹⁰³Alexis Martinez, 'Invoking State Defenses in Investment Treaty Arbitration' in Michael Waibel and others (eds), *The Backlash against Investment Arbitration: Perceptions and Reality* (Kluwer 2010) 315-37. See also *Sempra Energy International v Argentina*, ICSID Case No ARB/02/16, Award 28 September 2007, para 246.

legal obligation.¹⁰⁴ Thus, in contrast to *force majeure*, necessity implies an intentional failure to conform to the state's obligations and an awareness of having deliberately chosen to act contrary to these, rather than material impossibility to comply.¹⁰⁵ For this reason, it could be suggested that, since the precise purpose of IIAs is to protect investors in difficult circumstances, states should not be permitted to rely on a general necessity defence in such situations as this would defeat the object of IIAs.¹⁰⁶ However, while investment treaty arbitration tribunals have permitted host states to at least invoke the customary international law defence, the defence of necessity has by no means proven to be a panacea for host states. The problems associated with invoking the defence will now be discussed in the context of the cases in which Argentina attempted to rely on it to defend regulatory measures taken in times of public emergency during the economic and political crisis of 2000 to 2002.¹⁰⁷

The measures taken in an attempt to stem the crisis included a significant devaluation of the peso through the termination of the currency board which had pegged the peso to the US dollar, the 'pesofication' of all financial obligations and the effective freezing of bank accounts. As regards foreign investors in the utility sector, this meant that utility rates and tariffs were redenominated into pesos and that the right of licensees in the regulated public sector to link tariffs to US price indices was extinguished. Since the peso eventually fell to less than one third of a dollar, the income of utility companies fell by more than two thirds. Emergency laws also authorised the executive branch of the government to renegotiate all public service contracts. Argentina has become subject to at least 46 arbitrations

¹⁰⁴Necessity has been explicitly recognised as a customary international law rule by the International Court of Justice: see *Case Concerning the Gabčíkovo-Nagymaros Project (Hungary v Slovakia)*, Judgment 25 September 1997 (1997) ICJ Rep 7, paras 50-51.

¹⁰⁵Maria Agius, 'The Invocation of Necessity in International Law' (2009) *Netherlands Intl L Rev* 101.

¹⁰⁶August Reinisch, 'Necessity in International Investment Arbitration – An Unnecessary Split of Opinions in Recent ICSID Cases? Comments on CMS v. Argentina and LG&E v. Argentina' (2006) 3 *Transnational Dispute Management*. See also *Enron Corporation and Ponderosa Assets, LP v Argentina*, ICSID Case No ARB/01/3, Award 22 May 2007, para 331.

¹⁰⁷The emergency in question consisted of a financial crisis which came to a head in the last weeks of 2001 and which resulted in income per person in dollar terms shrinking from around \$7,000 to \$3,500 and by late 2002 over half the population living below the poverty line. Political instability accompanied the economic crisis. The government collapsed in December 2001 and the consequence of this was the 'tragicomic spectacle of a succession of five presidents taking office over a mere ten days': William W Burke-White and Andreas Von Staden, 'Investment Protection in Extraordinary Times: The Interpretation and Application of Non-Precluded Measures Provisions in Bilateral Investment Treaties' (2008) 48 *Va J Intl L* 307, 309.

brought by investors alleging loss resulting from these measures.¹⁰⁸ By way of background to these developments, Argentina had, in the late 1980s and early 1990s, initiated an extensive privatisation programme, offering a range of specific incentives to private companies who acquired ownership interests in various utility sectors. A Convertibility Law was also enacted in 1991 which pegged the peso to the US dollar and which also required the Central Bank to hold an amount of dollars, gold or foreign exchange at least equivalent to 100 per cent of Argentina's domestic monetary base, the effect of which was to strictly limit the legal authority of the Central Bank to increase the supply of pesos, a limitation intended to reduce inflation and foster the stability necessary to attract foreign investment. Utility companies were given the right to calculate their tariffs in US dollars before converting them to Argentine pesos at the time of billing and also had the right to a semi-annual tariff review based on the US Producer Price Index. The government could not rescind or modify the licenses without the consent of the licensees and the tariff system was not to be subject to further control (and in the event of the government exerting such control, it was to compensate the licensees fully for any resulting losses).¹⁰⁹ One of Argentina's main lines of argument in the cases brought against it was that it should be able to avail of the defence of necessity as the measures which it took in response to the crisis were necessary to uphold Argentina's constitutional order and the basic rights and liberties of the Argentine public.

From a public interest perspective, the first (and most fundamental) problem relating to the defence of necessity is its narrow scope. Thus, the tribunals ruling on the claims against Argentina have all regarded Article 25 of the Draft Articles on Responsibility of States for Internationally Wrongful Acts (the Draft ILC Articles)¹¹⁰ as being a final expression of the customary international law defence of necessity and have relied extensively on Article 25 in their rulings.¹¹¹ Article 25 states:

¹⁰⁸Lucy Reed, 'Scorecard of Investment Treaty Cases against Argentina since 2001' Kluwer Arbitration Blog, 2 March 2009.

¹⁰⁹*CMS v Argentina*, ICSID Case No ARB/01/8, Award 12 May 2005, para 53ff.

¹¹⁰International Law Commission, *Draft Articles on Responsibility of States for Internationally Wrongful Acts, with commentaries 2001* (2001) 2 YB Intl L Comm'n, UN Doc A/CN.4/SER.A/2001/Add.1 (Part 2).

¹¹¹Kurtz notes that there is a legitimate question as to whether Article 25 of the Draft ILC Articles should be taken as a final expression of customary international law in this area: see Jürgen Kurtz,

1. Necessity may not be invoked by a State as a ground for precluding the wrongfulness of an act not in conformity with an international obligation of that State unless the act:
 - (a) is the only way for the State to safeguard an essential interest against a grave and imminent peril; and
 - (b) does not seriously impair an essential interest of States towards which the obligation exists, or of the international community as a whole.
2. In any case, necessity may not be invoked by a State as a ground for precluding wrongfulness if:
 - (a) the international obligation in question excludes the possibility of invoking necessity; or
 - (b) the State has contributed to the situation of necessity.

The stringent conditions of this article and the negative language in which the defence is articulated suggests that states may only avail of the defence in exceptional circumstances and the arbitral decisions on the Argentine measures have, on the whole, stressed the exceptional nature of the defence. Thus, the tribunals in *CMS v Argentina*,¹¹² *Enron v Argentina*,¹¹³ *Sempra v Argentina*¹¹⁴ and in *Suez and Vivendi v Argentina*¹¹⁵ relied on the ‘only way’ requirement in Article 25(1)(a) as excluding the defence of necessity if any other means were available to the government and placed the burden of proof on the host state. For example, in *Sempra v Argentina*, the tribunal concluded that, despite the economic and political crisis, ‘the constitutional order was not on the verge of collapse’ and that hence ‘legitimately acquired rights could still have been accommodated by means of temporary measures and renegotiation’.¹¹⁶ Therefore, Argentina’s claim that the defence of necessity applied was dismissed as it was held that there were other means available of dealing with the crisis, even if these measures were more costly

‘Adjudging the Exceptional at International Law: Security, Public Order and Financial Crisis’ (2010) 59 ICLQ 325, 339.

¹¹²ICSID Case No ARB/01/8, Award 12 May 2005.

¹¹³ICSID Case No ARB/01/3, Award 22 May 2007.

¹¹⁴ICSID Case No ARB/02/16, Award 28 September 2007.

¹¹⁵ICSID Case No ARB/03/19, Decision on Liability 30 July 2010.

¹¹⁶ICSID Case No ARB/02/16, Award 28 September 2007, para 332.

or less convenient.¹¹⁷ Similarly, in *Suez and Vivendi v Argentina* the tribunal noted that, if Argentina had adopted more flexible means to ensure the continuation of water and sewage services to the population, it could have honoured both its human rights and treaty obligations.¹¹⁸

This ‘only way’ condition, particularly as it has been applied to date (but also generally), is difficult to satisfy as, in practice, decision-makers will have a number of options available to them, none of which will provide total certainty that the goal pursued will be attained. Indeed, the restrictive approach taken to the ‘only way’ requirement by the tribunal in *Enron v Argentina* was criticised by the Enron Annulment Committee and, for that and other reasons, the Committee annulled the finding that the defence of necessity was not open to Argentina.¹¹⁹ The Enron Annulment Committee noted that there are two different possible interpretations of this concept – the first being the literal meaning to the effect that there must be no other measures that the state possibly could have adopted in order to address the economic crisis and the second being that there must not be any alternative measures that would not involve a similar or graver breach of international law. The Enron Annulment Committee observed that the Enron tribunal did not address these two different interpretations but instead relied extensively on an economist’s opinion as to whether there were other measures open to Argentina and also failed to address other important questions necessary to addressing the concept such as whether the relative effectiveness of the alternative measures is to be taken into account, who is to make the decision whether there is a relevant alternative and what test is to be applied.¹²⁰ This criticism could be equally applied to the decisions of some of the other tribunals in the Argentine cases.

The other components of Article 25(1) (a) have also been narrowly construed. Thus, the Argentine decisions have also emphasised that, although measures taken to deal with economic crises can theoretically fall within the scope of the necessity defence, the circumstances will have to be dire in order to satisfy the ‘grave and imminent peril’ requirement. For example, the tribunal in *CMS v Argentina*

¹¹⁷See however *Sempra Energy International v Argentina*, ICSID Case No ARB/02/16, Decision on Argentina’s Application for Annulment of the Award 29 June 2010 in which the Annulment Committee annulled the award on the basis that the tribunal had manifestly exceeded its powers.

¹¹⁸ICSID Case No ARB/03/19, Decision on Liability 30 July 2010, paras 235-60.

¹¹⁹ICSID Case No ARB/01/3, Decision on Argentina’s Application for Annulment of the Award 30 July 2010.

¹²⁰*ibid*, paras 368-78.

presented ‘a major breakdown with all its social and political implications’ and ‘total economic and social collapse’ as the operative standard¹²¹ and the tribunal in *Sempra v Argentina* stated that, in order to meet the required threshold, Argentina’s economic crisis would have had to compromise the ‘very existence of the State and its independence’.¹²² Investment treaty arbitration tribunals have also proven reluctant to engage with the idea that preemptory norms or human rights should be considered as falling within the scope of the ‘essential interests’ of the state.¹²³

Finally, the requirement in Article 25(2)(b) that the state must not have contributed to the situation of necessity in order to be able to invoke the defence has also proven to be a stumbling block as the host state must affirmatively demonstrate that it did not contribute to the crisis. For example, in *National Grid v Argentina* the tribunal found that Argentina’s own evidence demonstrated that its contribution to the crisis was substantial and on that basis dismissed the defence of necessity.¹²⁴

Similarly, in *Suez and Vivendi v Argentina* the tribunal observed that ‘if external, global factors alone had created Argentina’s crisis, it is surprising that other countries did not experience a crisis of equal magnitude at the time’.¹²⁵ If read literally, this statement appears to make invocation of the necessity defence almost impossible, unless at least several other countries experience severe economic crises simultaneously. However, even if this requirement were to be interpreted more narrowly in future cases, it will continue to be problematic for host states.

Thus, the Argentine decisions have, in general, interpreted the defence of necessity restrictively, apparently leaving little room for its application in economic crisis situations. Admittedly, the defence could be applied in a manner that accords greater deference to the host state (for example by applying the ‘only way’ requirement less restrictively). However, the defence will always have to be quite narrowly drawn to prevent its abuse by states and this can be argued to be entirely appropriate given that the defence, as a secondary rule of international law, is properly invoked to preclude wrongfulness only once breach of a primary rule has

¹²¹ICSID Case No ARB/01/8, Award 12 May 2005, paras 319 and 355.

¹²²ICSID Case No ARB/02/16, Award 28 September 2007, para 348.

¹²³See Jürgen Kurtz, ‘Adjudging the Exceptional at International Law: Security, Public Order and Financial Crisis’ (2010) 59 ICLQ 325.

¹²⁴UNCITRAL, Award 3 November 2008, para 262.

¹²⁵ICSID Case No ARB/03/19, Decision on Liability 30 July 2010, para 264. See also *Impregilo SpA v Argentina*, ICSID Case No ARB/07/17, Award 21 June 2011, para 356ff.

been established.¹²⁶ Furthermore, the defence may not be particularly suited to addressing sovereign financial crises of the type experienced by Argentina, given the origins of the defence in state practice on the use of force and the right to self-defence, its temporal limitation and the restrictive ‘only way’ and ‘lack of state contribution’ requirements.¹²⁷

A further issue that has arisen in the context of the Argentine cases is the relationship between the customary international law defence of necessity and NPM clauses. Thus, Argentina, in a number of cases, attempted to rely on the provisions of the NPM clause (Article XI) in the Argentina-US BIT in justifying its actions. Article XI of the Argentina-US BIT states as follows:

This Treaty shall not preclude the application by either Party of measures necessary for the maintenance of public order, the fulfilment of its obligations with respect to the maintenance or restoration of international peace or security, or the Protection of its own essential security interests.

Thus, the purpose of NPM clauses generally is to allow states to take measures otherwise inconsistent with the relevant treaty when, for example, the actions are necessary in order to protect certain fundamental interests. Such clauses can cover circumstances such as exceptional threats to internal and external security, economic crisis, terrorism, public health emergencies or natural disasters. In contrast to the customary international law defence of necessity, such clauses comprise a set of primary legal rules that must be adjudicated upon in deciding whether a breach occurred rather than a means of excusing such breach.¹²⁸

Despite this fundamental distinction, a number of the tribunals that have adjudicated on Article XI of the Argentina-US BIT effectively conflated it with the defence of necessity.¹²⁹ For example, in *Sempra v Argentina* the tribunal stated:

¹²⁶The term primary rule refers to specific international law obligations existing, for example, under various treaties; whereas secondary rules, with which the Draft ILC Articles are concerned, deal with the general conditions under international law for the State to be considered responsible for wrongful actions or omissions, and the resultant legal consequences: James Crawford, *The International Law Commission's Articles on State Responsibility: Introduction, Text and Commentaries* (Cambridge University Press 2002) 74.

¹²⁷Michael Waibel, ‘Two Worlds of Necessity in ICSID Arbitration: CMS and LG&E’ (2007) 20 *Leiden J Intl L* 637; cf Christina Binder and August Reinisch, ‘Economic Emergency Powers: a Comparative Law Perspective’ in Stephan W Schill (ed), *International Investment Law and Comparative Public Law* (OUP 2010) 503-39.

¹²⁸See generally OECD, *International Investment Perspectives: Freedom of Investment in a Changing World* (OECD 2007) ch 5.

¹²⁹See *CMS v Argentina*, ICSID Case No ARB/01/8, Award 12 May 2005; *Enron Corporation and Ponderosa Assets, LP v Argentina*, ICSID Case No ARB/01/3, Award 22 May 2007; *Sempra Energy*

the Treaty provision is inseparable from the customary law standard insofar as the definition of necessity and the conditions for its operation are concerned, given that it is under customary law that such conditions have been defined.¹³⁰

Thus, these tribunals took the stance that a number of conditions not expressly mentioned in Article XI must be supplemented by those set forth in customary international law such as the ‘grave and imminent peril’ requirement, the ‘only way’ requirement and the requirement that the state did not create or contribute to the situation of necessity. This approach is problematic as, while the defence of necessity and NPM clauses are broadly similar in intent in that both recognise that the need to protect national interests of paramount importance may justify setting aside or suspending an obligation or preventing liability for its breach, the distinction between the two is significant as combining the requirements of the NPM clause with the stringent conditions imposed by the defence of necessity deprives NPM clauses of much of their potential to excuse host state action in times of crisis.¹³¹ Furthermore, this conflation would seem to run counter to the desire of states in signing IIAs to tailor treaty protections to specific concerns surrounding the entry and operation of foreign investors in host states so as to avoid having to rely on the provisions of customary international law for such purpose.¹³² While not all investment treaty arbitration tribunals have taken this approach and while it has been criticised by annulment committees,¹³³ even where the defence of necessity and the NPM clause have been considered separately, there has been a lack of

International v Argentina, ICSID Case No ARB/02/16, Award 28 September 2007; *El Paso Energy International Company v Argentina*, ICSID Case No ARB/03/15, Award 31 October 2011.

¹³⁰*ibid*, para 376.

¹³¹William W Burke-White and Andreas Von Staden, ‘Investment Protection in Extraordinary Times: The Interpretation and Application of Non-Precluded Measures Provisions in Bilateral Investment Treaties’ (2008) 48 *Va J Intl L* 307, 320-24.

¹³²Jürgen Kurtz, ‘Adjudging the Exceptional at International Law: Security, Public Order and Financial Crisis’ (2010) 59 *ICLQ* 325, 350. On the other hand, it has been pointed out that, in the particular context of the Argentina-US BIT, there was evidence that both states intended that the scope of the NPM clause should be consistent with the customary defence of necessity: José E Álvarez and Kathryn Khamsi, ‘The Argentine Crisis and Foreign Investors: a Glimpse into the heart of the Investment Regime’ in Karl P Sauvant (ed), *The Yearbook of International Investment Law and Policy 2008-2009* (OUP 2009) 408-17, 431-36.

¹³³For example, the decision of the Sempra Annulment Committee found that the tribunal had failed to apply the applicable law in conflating the requirements of customary international law and Article XI and in finding that the customary international law defence ‘trumped’ Article XI: see *Sempra Energy International v Argentina*, Decision on Argentina’s Application for Annulment of the Award 29 June 2010, ICSID Case No ARB/02/16.

clarity to the review employed. For example, the tribunal in *LG&E v Argentina*,¹³⁴ without explicitly so stating, appeared to take a *lex specialis* approach, whereby the NPM clause was prioritised as an expression of *lex specialis*, constituting a specific elaboration or updating of the general customary norm. However, the question of the scope of priority to be accorded to the NPM clause, which can range from allowing the customary international law defence to retain a residual role to the displacement of the customary defence in its entirety still remains and was not addressed by the *LG&E* tribunal.¹³⁵

However, while the relationship between the defence of necessity and NPM clauses may conceivably be clarified by future investment treaty arbitration tribunals and does not constitute an insurmountable problem, NPM clauses, of themselves, are, for several reasons, not a wholly satisfactory means of protecting a state's right to act to protect essential national interests in times of crisis. First, NPM clauses are by no means a feature of every IIA (indeed one estimate from 2007 states that only one in ten of the BITs then in force contained such a clause).¹³⁶ Secondly, their utility from a public interest perspective varies as such clauses differ quite considerably in the range of permissible objectives covered, in the IIA provisions which they apply to and in the requirement as to the nexus between an impugned measure and the objective pursued, thus according host states varying degrees of freedom of action. For example, Article 2102 of NAFTA contains an exception for essential security interests. However, the scope of Article 2102 is quite narrow as it is limited to measures relating to arms traffic, measures taken in time of war or other emergency in international relations or relating to the implementation of national policies or international agreements on the non-proliferation of nuclear weapons.¹³⁷ Some NPM clauses also apply only in respect of certain IIA rights¹³⁸

¹³⁴See *LG&E Energy Corporation v Argentina*, ICSID Case No ARB/02/1, Decision on Liability, 3 October 2006.

¹³⁵For a different approach to the issue see *Continental Casualty v Argentina*, ICSID Case No ARB/03/9, Award 5 September 2008. For a critique of this approach see José Álvarez and Tegan Brink, 'Revisiting the Necessity Defence: Continental Casualty v Argentina' in Karl P Sauvant (ed), *Yearbook International Investment Law and Policy 2010-2011* (OUP 2012).

¹³⁶William W Burke-White and Andreas Von Staden, 'Investment Protection in Extraordinary Times: The Interpretation and Application of Non-Precluded Measures Provisions in Bilateral Investment Treaties' (2008) 48 *Va J Intl L* 307, 313-18.

¹³⁷North American Free Trade Agreement between Canada, The United States and Mexico, signed 17 December 1992, entered into force 1 January 1994.

¹³⁸See for example Agreement between the United Mexican States and the Republic of Austria on the Promotion and Protection of Investments, signed 29 June 1998, entered into force 26 March 2001, art 19.

and there is also variation in the requirement as to the nexus between an impugned measure and the objective pursued.¹³⁹ For example, while many NPM clauses require the measures in question to be ‘necessary’ (whether this is judged by the state itself or is subject to the tribunal’s judgment), others refer to the host state measures being ‘directed to’ the promotion of certain interests¹⁴⁰ or simply to host state measures ‘taken on’, *inter alia*, security, order, public health and morality grounds.¹⁴¹ Finally, the degree to which the tribunal in question is permitted to scrutinise the host state’s actions varies: while some NPM clauses are explicitly self-judging,¹⁴² others are subject to good faith scrutiny while yet another group are subject to the full scrutiny of the tribunal in question.¹⁴³

To summarise therefore, the customary international law defence of necessity has, to date, been interpreted in a restrictive manner by investment treaty arbitration tribunals. While elements of these decisions can be criticised, it is submitted that the purpose and tenor of the defence is such that it must be narrowly drawn and that it may not be suitable for addressing certain types of crisis situation, in particular economic crises. If the relevant IIA is one of the minority of IIAs that contains a NPM clause, this may assist the state in justifying its actions in exceptional circumstances. However, much depends on the range of permissible objectives which the clause in question covers, the requirement as to the nexus between an impugned measure and the objective pursued and the level of permissible scrutiny afforded to the investment treaty arbitration tribunal.

3.5 Analysis of the effectiveness of methods of taking account of public interest considerations at the merits stage

¹³⁹See generally UNCTAD, *The Protection of National Security in IIAs: UNCTAD Series on International Investment Policies for Development* (UNCTAD 2009); Andrew D Mitchell and Caroline Henckels, ‘Variations on a Theme: Comparing the Concept of ‘Necessity’ in International Investment Law and WTO Law’ (2013) 14 *Chi J Intl L* 93.

¹⁴⁰See for example New Zealand and China: Agreement on the promotion and protection of investments (with exchange of notes), signed 22 November 1988, entered into force 25 March 1989, art 11.

¹⁴¹See for example Romania and Egypt: Agreement on the promotion and mutual guarantee of capital investments (with protocol), signed 10 May 1976, entered into force 3 April 1996, protocol, para 1.

¹⁴²See for example US Model BIT (2012), art 18.

¹⁴³Anne van Aaken, ‘International investment law between commitment and flexibility: a contract theory analysis’ (2009) 12 *J Intl Economic L* 507, 524-25; José E Álvarez and Kathryn Khamsi, ‘The Argentine Crisis and Foreign Investors: a Glimpse into the heart of the Investment Regime’ in Karl P Sauvant (ed), *The Yearbook of International Investment Law and Policy 2008-2009* (OUP 2009) 463-65.

The foregoing analysis of the application of proportionality analysis, of the taking into account of the host state's non-investment related international obligations through customary international law methods of interpretation and, finally, of the application of the customary international law of necessity and of NPM clauses has outlined a number of the problems and uncertainties associated with each of these methods. Turning first to proportionality analysis, this methodology is not suitable for resolving conflicts between rules and so, for example, it cannot be used to resolve direct treaty conflicts. Secondly, the hybrid nature of investment treaty arbitration and the distinctions that can be drawn between it and human rights or constitutional adjudication mean that there is continuing uncertainty as to whether investment treaty arbitration constitutes an appropriate forum for the use of proportionality analysis, even if the application of proportionality analysis could potentially have a positive effect. Thirdly, the 'asymmetric' nature of IIAs and of the investment treaty arbitration system makes it difficult to effectively balance host state and investor interests, particularly given the uncertainties surrounding what is meant by the public interest in the context of investment treaty arbitration. However, removing balancing from the analysis entirely could potentially be detrimental both to investor interests and also to the optimisation of host state interests. Finally, and on a more practical note, the effect of application of proportionality analysis may be limited if it is not applied in respect of all of the alleged breaches of the relevant IIA.

An analogous problem arises where the non-investment related international obligations of the host state are introduced into investment treaty arbitration through arguments based on customary international law methods of interpretation. Thus, even if such obligations are introduced in this manner (which, in itself, is not uncontroversial), the tribunal must then determine the weight to be attributed to such norms and this is not an easy determination to make, given the focus of the investment treaty system on the protection of a particular set of interests.

Finally, turning to the customary international law defence of necessity, as a consequence of both the object of IIAs to protect the rights of foreign investors in situations of economic difficulty and of the nature of the defence of necessity as a secondary rule of customary international law, the defence of necessity must inexorably be narrowly drawn and, therefore, will be of assistance to host states in exceptional circumstances only. Similarly, NPM clauses, given their variable scope,

are a 'patchy' means of protecting states' right to act to protect essential national interests in times of crisis.

Given these difficulties, it is submitted that the academic literature on taking account of public interest considerations at the merits stage of the investment treaty arbitration process is likely to continue to outstrip arbitral practice. While the fact that there are certain issues associated with taking account of public interest considerations at the merits stage of the arbitral process does not necessarily have as its corollary the proposition that the remedies stage of the arbitral process should constitute a forum for taking account of such considerations, it does at least raise this proposition as a legitimate subject of enquiry. In particular, the unifying point that underlies the specific issues outlined above is that, fundamentally, taking account of public interest considerations at the merits stage can lead only to a black-or-white decision as to liability. This 'all or nothing' approach requires one set of interests (i.e. those of the claimant investor or those of the host state) to be prioritised in order to come to that determination and so may lead to either investor or host state interests not being optimised, particularly in circumstances where one set of interests marginally outweighs the other. Therefore, it is submitted that it is worth questioning whether an 'all or nothing' approach to liability is appropriate to investment treaty arbitration or whether introducing an element of balancing at the remedies stage would be beneficial.¹⁴⁴ Accordingly, the following chapter will examine the operation of the remedies stage of the investment treaty arbitration process and will consider whether the remedies stage should play a role in taking account of public interest considerations.

¹⁴⁴For a similar proposition (in the context of the expropriation clause only) see Ursula Kriebaum, 'Regulatory Takings: Balancing the Interests of the Investor and the State' (2007) 8 J World Investment & Trade 717.

Chapter 4: The remedies stage as a platform for public interest considerations: an assessment

4.1 *An overview of the remedies stage*

Having outlined in Chapter 3 the problems and uncertainties associated with the various methods of taking into account public interest considerations at the merits stage of the investment treaty arbitration process, this chapter will consider the question of whether public interest considerations should be taken into account in formulating the remedy to be awarded to claimant investors. As outlined in Chapter 1, this analysis will be confined to the issue of pecuniary relief, given the difficulties associated with the awarding of non-pecuniary remedies in investment treaty arbitration and given that the remedy awarded by the overwhelming majority of investment treaty arbitration tribunals to date at the final stage of proceedings has been the payment of damages.

In recent years, a sizeable body of literature has emerged that describes in considerable detail the bases for valuation and the relatively complex valuation methods that have been applied by investment treaty arbitration tribunals in assessing damages.¹ However, although a basic understanding of the means by which damages are quantified is important, the operation of the valuation process ranks secondary in importance to the applicable legal standard of compensation and, accordingly, should not dictate the legal principles applicable to a particular dispute or operate as a means of introducing particular standards or theories of compensation through the back door.² Accordingly, the first part of this chapter will focus primarily on the legal standards of compensation but will also provide a brief

¹See for example Sergey Ripinsky with Kevin Williams, *Damages in International Investment Law* (British Institute of International and Comparative Law 2008); Mark Kantor, *Valuation for Arbitration* (Kluwer 2008); Andrea K Bjorklund, Ian A Laird and Sergey Ripinsky (eds), *Investment treaty law: current issues. III, Remedies in international investment law emerging jurisprudence of international investment law* (British Institute of International and Comparative Law 2008) chs 1-7; Irmgard Marboe, *Calculation of Compensation and Damages in International Investment Law* (OUP 2009); Borzu Sabahi, *Compensation and Restitution in Investor-State Arbitration: Principles and Practice* (OUP 2011).

²M Sornarajah, *The International Law of Foreign Investment* (3rd edn, Cambridge University Press 2010) 456, 485-86.

overview of the valuation methods customarily applied by valuation experts and investment treaty arbitration tribunals, in order to give a general sense of the valuation process currently undertaken by investment treaty arbitration tribunals.

In examining the purposes of the remedies stage, a distinction must be drawn between lawful expropriations and unlawful acts. This distinction is necessary since the purpose behind the monetary payment made in each case differs: for unlawful acts the purpose of this payment is that of restitution or full reparation whereas for lawful expropriations the purpose is that of compensation as expropriation is not prohibited in international law but rather is lawful provided certain requirements are met (i.e. that the measure was taken for a public purpose, on a non-discriminatory basis, in accordance with due process of law and that compensation is provided).³ Accordingly, the standard of valuation to be applied in each case differs: the standards of compensation set out in IIAs usually purport to deal only with the valuation of lawfully expropriated assets while customary international law has been applied in respect of unlawful acts. Therefore, these two categories of compensable acts will be considered separately.

(a) *The full reparation principle*

In the case of unlawful acts, the principle applied in quantifying damages is that of full reparation. This principle derives from customary international law⁴ and was elaborated on in the *Chorzów Factory* case.⁵ In that case, the Permanent Court of International Justice (PCIJ) stated that reparation for an act contrary to international law must be equivalent to ‘Restitution in kind, or, if this is not possible, payment of a sum corresponding to the value which restitution in kind would bear.’ As stated by the PCIJ, the payment must, as far as possible, ‘wipe out all the consequences of the illegal act and re-establish the situation that would, in all probability, have existed if that act had not been committed.’⁶ Thus, in order to apply the full

³Ursula Kriebaum, ‘Regulatory Takings: Balancing the Interests of the Investor and the State’ (2007) 8 J World Investment & Trade 717, 726.

⁴See International Law Commission, *Draft Articles on Responsibility of States for Internationally Wrongful Acts, with commentaries 2001* (2001) 2 YB Intl L Comm’n, UN Doc A/CN.4/SER.A/2001/Add.1 (Part 2) arts 31 to 36. It has been widely recognised that the Draft ILC Articles codify the customary law of state responsibility and reparation: see for example *Noble Ventures, Inc. v Romania*, ICSID Case No ARB/01/11, Award 12 October 2005, para 69.

⁵*Case Concerning the Factory at Chorzów (Claim for Indemnity)(Merits)(Germany v Poland)*, Judgment 13 September 1928, Series A, no 17, 47.

⁶ *ibid.*

reparation principle, the actual financial situation of the victim must be compared with the financial situation it most probably would be in without that act and the valuation date should generally be the date of the award.⁷ However, where an unlawful expropriation occurs, it is necessary to compare the value of the expropriated property at the date of expropriation and its value at the date of the award and to award to the claimant investor the higher amount, in order to give effect to the full reparation principle.⁸

Causation principles play a key role in establishing the amount of damages due as, in order for damages to be recoverable in respect of a particular loss or injury suffered by a claimant investor, a causal link between the unlawful acts attributable to the host state⁹ and that loss or injury must be established.¹⁰ Thus, in implementing the full reparation principle, investment treaty arbitration tribunals have relied extensively on causation principles as, when the issue of causation is well-defined, the task of quantifying the damages payable as a result should become more straightforward. However, given that there is little precedent, either nationally or internationally, on quantifying the damages payable in respect of non-expropriatory breaches and that the requisite level of causation is rarely defined in IIAs, tribunals have had to construct an approach to causation on an incremental basis, which makes it difficult to discern a consistent approach.¹¹ However, on a basic level, as described by the tribunal in *Biwater Gauff v Tanzania*, the requirement of causation comprises a number of different elements, including: ‘(a) a sufficient link between the wrongful act and the damage in question, and (b) a threshold beyond which damage, albeit linked to the wrongful act, is considered too

⁷Irmgard Marboe, *Calculation of Compensation and Damages in International Investment Law* (OUP 2009) 139-41.

⁸*ibid.*, 75-77. See also *ADC Affiliate Limited and ADC & ADMC Management Ltd v Hungary*, ICSID Case No ARB/03/16, Award 2 October 2006.

⁹Wrongful conduct is ascribed to states under international law through the theory of attribution. This has been characterised by the International Law Commission as a normative operation, based on criteria determined by international law, rather than as merely an investigation of factual causality: see International Law Commission, *Draft Articles on Responsibility of States for Internationally Wrongful Acts, with commentaries 2001* (2001) 2 YB Intl L Comm’n, UN Doc A/CN.4/SER.A/2001/Add.1 (Part 2) 38-39. See also León Castellanos-Jankiewicz, ‘Causation and International State Responsibility’ Amsterdam Law School Research Paper No 2012-56.

¹⁰Mark Kantor, *Valuation for Arbitration* (Kluwer 2008) 106. See also *Yukos Universal Limited (Isle of Man) v the Russian Federation*, PCA Case No AA 27, Award 18 July 2014, paras 1770-75.

¹¹Campbell McLachlan, Laurence Shore and Matthew Weiniger, *Investment Treaty Arbitration: Substantive Principles* (OUP 2007) 334; Sergey Ripinsky with Kevin Williams, *Damages in International Investment Law* (British Institute of International and Comparative Law 2008) 138.

indirect or remote'.¹² The application of causation principles is not without its problems, however.¹³ For example, especially in host states where there is economic or political volatility, it can be difficult to disaggregate the various causes of the injury ultimately suffered by the claimant investor.

The obligation to make full reparation also includes an obligation to compensate for moral damage.¹⁴ Moral damage includes such items as individual pain and suffering, loss of loved ones or personal affront associated with an intrusion on one's home or private life.¹⁵ Due to this, legal persons (which constitute the majority of claimants under IIAs) will be awarded moral damages in exceptional circumstances only. Moral damages were awarded in *Desert Line Projects v Yemen* as a result of stress and anxiety caused to company executives due to threats and harassment on the part of state entities and the resulting damage to the company's credit and reputation.¹⁶ However, the amount awarded was small relative to the overall claim and the tribunal noted that corporate entities have the right to obtain compensation for moral damage in specific circumstances only.¹⁷ The tribunal gave no information on the method by which it arrived at the \$1 million figure, which represented around one per cent of the amount claimed by the investor stating that 'this amount is at the entire discretion of the Arbitral Tribunal'.¹⁸ Several tribunals have subsequently rejected claims for moral damages (even in circumstances where the host state's mistreatment of the claimant investor was described by the tribunal as 'severe, intentional, and multi-faceted').¹⁹ These tribunals have placed emphasis on the exceptional circumstances of the *Desert Line* case and some tribunals have instead considered that a declaration of liability or the dismissal of the claimant

¹²ICSID Case No ARB/05/22, Award 18 July 2008, para 785.

¹³See generally Andrea K Bjorklund, 'Causation, Morality and Quantum' (2008-2009) 32 Suffolk Transnational L Rev 435.

¹⁴International Law Commission, *Draft Articles on Responsibility of States for Internationally Wrongful Acts, with commentaries 2001* (2001) 2 YB Intl L Comm'n, UN Doc A/CN.4/SER.A/2001/Add.1 (Part 2) art 31; cf Stephen Jagusch and Thomas Sebastian, 'Moral Damages in Investment Arbitration: Punitive Damages in Compensatory Clothing?' (2013) 29 Arbitration Intl 45.

¹⁵ibid, commentaries on art 31.

¹⁶ICSID Case No ARB/05/17, Award 6 February 2008. Moral damages were also awarded in the case of *Benvenuti & Bonfant v Congo*, ICSID Case No ARB/77/2, Final Award 8 August 1980, para 4.4. However, that case was decided *ex aequo et bono* and can therefore be considered of limited relevance.

¹⁷ibid, para 289.

¹⁸ibid, para 297.

¹⁹*Stati v Kazakhstan*, SCC Arbitration V (116/2010), Award 19 December 2013, para 1783.

investor's claims along with an order to pay costs constituted, of itself, sufficient reparation for the moral damage suffered.²⁰

(b) *The IIA standard of compensation*

Where a lawful expropriation is deemed to have occurred (i.e. where the expropriation was implemented in furtherance of a public purpose, in accordance with due process of law and in a non-discriminatory manner), it is questionable whether the established sources of international law provide support for the standard of full compensation.²¹ Nowadays however, this question has become somewhat moot as the standard applicable in determining the quantum of compensation is usually determined by the provisions of the relevant IIA.²² The payment of compensation in such cases can be seen as a primary obligation as opposed to the secondary obligation to pay damages in accordance with the full reparation principle following the breach of an international obligation.²³ The majority of recent IIAs tend towards using the 'Hull formula' of 'prompt, adequate and effective'²⁴ compensation, although a minority of IIAs instead describe the required compensation as being that which is 'just', 'appropriate' or 'fair and equitable',²⁵ albeit that such terms are not necessarily indicative of a different

²⁰ibid, *Lemire v Ukraine*, ICSID Case No ARB/06/18, Award 28 March 2011, paras 310-45. See also Isabelle Michou, 'Compensation of the moral injury in investor-state arbitration' (2011) Intl Bus L J 41.

²¹M Sornarajah, *The International Law of Foreign Investment* (3rd edn, Cambridge University Press 2010) 452-79.

²²One possible explanation for this lies in the NIEO debates of the 1960s and 1970s as at that time the debate focused on how much compensation was due as a result of expropriation since those espousing the NIEO view assumed that expropriation was always lawful. This assumption may have impacted the structure and content of modern IIAs: Don Wallace Jr, observations made in the Investor State Dispute Resolution Seminar, Georgetown University Law Center, 16 March 2009 as recorded in Borzu Sabahi, *Compensation and Restitution in Investor-State Arbitration: Principles and Practice* (OUP 2011) 100.

²³Marboe notes that the failure of many tribunals and commentators to distinguish between 'compensation' as an element of lawful behaviour and 'damages' as a consequence of unlawful behavior leads to a conflation of lawful and unlawful expropriations at the remedies stage: Irmgard Marboe, *Calculation of Compensation and Damages in International Investment Law* (OUP 2009) 395.

²⁴See generally Frank G Dawson and Burns H Weston, "'Prompt, Adequate and Effective": A Universal Standard of Compensation?' (1962) 30 Fordham L Rev 727.

²⁵See for example Agreement on economic cooperation between the Government of the Kingdom of the Netherlands and the Government of the Republic of Singapore, signed 16 May 1972, entered into force 7 September 1973, art IX(c); Agreement between the Government of the United Kingdom of Great Britain and Northern Ireland and the Government of the Republic of India for the Promotion and Protection of Investments, signed 14 March 1994, entered into force 6 January 1995, art 5(1).

standard of compensation.²⁶ In any event, given that it has some objective basis, the fair market value as at the time immediately before the time at which the taking occurred or the decision to take the asset became publicly known²⁷ has, in practice, prevailed in the text of IIAs as the decisive criterion for the measurement of compensation in respect of lawful expropriations.

Fair market value has been defined as:

the price, expressed in terms of cash equivalents, at which property would change hands between a hypothetical willing and able buyer and a hypothetical willing and able seller, acting at arm's length in an open and unrestricted market, when neither is under an obligation to buy or sell and when both have reasonable knowledge of the relevant facts.²⁸

Fair market value thus constitutes an objective or impersonal standard of compensation in that it discounts those elements of value that are personal to a given owner of property and instead bases the value on the price which a hypothetical buyer would have paid for the property. In doing so, it takes into account the future prospects (or likely future profitability)²⁹ of the expropriated property rather than merely reimbursing invested capital or providing compensation based on the value of individual assets. On the other hand however, it does not necessarily equate to full compensation since the investor may not be reimbursed fully for all the financial loss it has suffered as the calculation is based on the opinion of a hypothetical third person as to the value of the property.

Although IIAs generally limit the application of the fair market value standard to lawful expropriations only, at times, the fair market value standard has also been

²⁶See World Bank, *Report to the Development Committee on the Legal Framework for the Treatment of Foreign Investment introducing the World Bank Guidelines on the Treatment of Foreign Direct Investment*, 31 ILM 1363, 1376 (1992), guideline IV.

²⁷This usually equates to the date of the expropriation: see, for example, NAFTA, Article 1110, para 2 which states that: 'Compensation shall be equivalent to the fair market value of the expropriated investment immediately before the expropriation took place ("date of expropriation") and shall not reflect any change in value occurring because the intended expropriation had become known earlier.' On the difficulties of determining the valuation date in cases where the expropriation is indirect or creeping in nature see *Azurix v Argentina*, ICSID Case No ARB/01/12, Award 14 July 2006, para 417.

²⁸'Concepts Fundamental to Generally Accepted Valuation Principles' in IVSC, *International Valuation Standards* (London 2007) 27.

²⁹While the Iran-United States Claims Tribunal attempted to draw a distinction between 'future prospects' and 'lost profits' in *Amoco International Finance Corporation v Iran*, this distinction has been dismissed as being artificial and impractical: see Irmgard Marboe, 'Compensation and Damages in International Law and the Limits of "Fair Market Value"' (2006) 7 J World Investment & Trade 723, 728.

applied in respect of unlawful expropriations. For example, in *Kardassopoulos and Fuchs v Georgia*³⁰ the tribunal recognised that usually a distinction should be made between lawful and unlawful expropriations as regards the standard of compensation to be applied and the chosen valuation date. However, the tribunal noted that it is only appropriate to compensate for value gained between the date of the expropriation and the date of the award in cases where it is demonstrated that the claimants would, but for the taking, have retained their investment. In the present case, the evidence was that the claimant investors would not have done so and thus damages were calculated based on the fair market value of the investment on a date one day prior to the expropriatory decree.³¹

More controversially however,³² the difference in the fair market value of an investment resulting from a breach has quite frequently been applied to give effect the full reparation principle, particularly where both parties have agreed to such application and where an expropriation claim has been advanced in parallel with claims of non-expropriatory breaches.³³ For example, in *CMS v Argentina*³⁴ fair market value was applied as the operative valuation standard in determining the value of the loss suffered by the claimant investor by comparing the fair market value of its investment with and without the impugned host state measures in circumstances where the tribunal had determined that a violation of the FET standard and of the treaty's umbrella clause had occurred. The tribunal stated that 'the cumulative nature of the breaches...is best dealt with by resorting to the standard of fair market value.'³⁵ Similarly, the tribunal in *SD Myers v Canada*, in justifying its use of fair market value as the basis for valuation, took the view that

³⁰ICSID Case Nos ARB/05/18 and ARB/07/1, Award 3 March 2010.

³¹ibid, paras 501-17. See also *Funnekotter and ors v Zimbabwe*, ICSID Case No ARB/05/6, Award 22 April 2009, paras 111-20.

³²Diane A Desierto, 'ICESCR Minimum Core Obligations and Investment: Recasting the Non-Expropriation Compensation Model during Financial Crises' (2012) 44 *Geo Wash Intl L Rev* 473, 494-513; Diane Desierto, 'Calibrating Human Rights and Investment in Economic Emergencies: Prospects of Treaty and Valuation Defenses' (2012) 9 *Manchester J Intl Economic L* 162.

³³Brent C Kaczmarek, 'Compensation for Non-Expropriatory Treaty Violations: An Analytical Framework' (2006) 3 *Transnational Dispute Management* 16; Irmgard Marboe, *Calculation of Compensation and Damages in International Investment Law* (OUP 2009) 91-97; Pierre Yves Tschanz and Jorge E. Viñuales, 'Compensation for Non-expropriatory Breaches of International Investment Law' (2009) 26 *J Intl Arbitration* 729.

³⁴ICSID Case No ARB/01/8, Award 12 May 2005.

³⁵ibid, para 410. See also *Azurix v Argentina*, ICSID Case No ARB/01/12, Award 14 July 2006, para 424; *Enron Corporation and Ponderosa Assets, LP v Argentina*, ICSID Case No ARB/01/3, Award 22 May 2007, para 361; *Sempra Energy International v Argentina*, ICSID Case No ARB/02/16, Award September 28 2007, para 404; *El Paso Energy International Company v Argentina*, ICSID Case No ARB/03/15, Award 31 October 2011, para 703.

the silence of the treaty indicated the intention of the drafters ‘to leave it open to tribunals to determine a measure of compensation appropriate to the specific circumstances of the case’ adding that ‘whatever precise approach is taken, it should reflect the general principle of international law that compensation should undo the material harm inflicted by a breach of an international obligation.’³⁶

(c) *Bases of valuation and customary valuation methods*

Once a standard of valuation, such as that of fair market value, is identified, the valuation date and other principles important to the valuation must be identified as IIAs generally do not prescribe or mandate a particular valuation basis. This basis of valuation then provides the framework within which valuation experts apply various valuation methods. The first and most commonly used basis of valuation is the market value basis. This represents an objective or impersonal approach to valuation and can be considered synonymous with fair market value for the purposes of investment treaty arbitration. Other bases of value focus on the damage actually incurred by the injured party and are subjective concepts and include bases of value such as investment value (the value of the property to the particular investor which may not necessarily be the same as the market value of the property) and the contractual value (the value as determined in accordance with a definition set out in a statute or a contract).

After the establishment of the basis of value, one or more appropriate valuation methods must be selected. In contrast to the basis for valuation, which sets out what is to be measured, the term ‘valuation method’ refers to generally accepted alternative methodologies of application.³⁷ According to the International Valuation Standards, the most common valuation methods used in practice are the market approach, the income capitalisation approach and the asset-based approach.³⁸ While the use of the term ‘market approach’ may lead one to believe that this is synonymous with fair market value, in fact the market approach, along with the income capitalisation approach and the asset-based approach are all potentially applicable to both market-based valuations (such as the determination of fair market value) and to valuations under the other bases of value.

³⁶UNCITRAL, First Partial Award 13 November 2000, paras 309 and 315.

³⁷Irmgard Marboe, *Calculation of Compensation and Damages in International Investment Law* (OUP 2009) 186.

³⁸International Valuation Standards Council, *International Valuation Standards* 2013.

(i) *Market Approach*

The market or sales comparison approach considers the sale of similar or comparable properties and related market data, and estimates a value estimate by comparison with these sales. For the comparison to be reasonable, the businesses being compared should be in the same industry or in an industry that responds to the same economic variables. The three most common sources of data used in order to implement the market approach are public stock markets in which ownership interests of similar businesses are traded, the acquisition market in which entire businesses are bought and sold, and prior transactions in shares or offers for the ownership of the subject business.³⁹ A variant of the market approach is the use of multiples. Thus, one takes a particular variable of the company's performance such as cash flow, earnings or EBITDA and multiplies this figure by a certain factor which is specific to the particular enterprise or industry. This approach to valuation has been applied by investment treaty arbitration tribunals in circumstances where a comparison can reasonably be drawn such as where the company is publicly traded and thus a stock price is available,⁴⁰ where an actual willing buyer has made an offer for the business or where real property is concerned.⁴¹

(ii) *Income Capitalisation Approach*

This approach considers income and expense data relating to the property being valued and estimates value through a capitalisation process. The process essentially is aimed at ascertaining the present value of future benefits. This approach is most commonly used in relation to objective valuation standards (such as the calculation of fair market value). However, the income approach can also be used to determine the subjective value of the property to a particular investor, although in such circumstances, a rate of return may be applied that is non-market and particular

³⁹International Valuation Standards Council, 'IVS 200 Businesses and Business Interests', para C16 <http://www.ivsc.org/sites/default/files/ivs200_businesses_and_business_interests.pdf> accessed 19 March 2015.

⁴⁰See however *Enron Corporation and Ponderosa Assets, LP v Argentina*, ICSID Case No ARB/01/3, Award 15 May 2007, para 383 in which the tribunal rejected market capitalisation as a measure of fair market value as, although the shares of Enron's subsidiary TGS were traded on the New York and Buenos Aires stock exchanges, the illiquidity and limited volume of transactions in TGS's shares meant that distorted results would be produced.

⁴¹Sergey Ripinsky with Kevin Williams, *Damages in International Investment Law* (British Institute of International and Comparative Law 2008) 214-15.

only to that investor.⁴² While the World Bank Guidelines advise using the income approach only in relation to going concerns,⁴³ this does not necessarily have to be the case under international valuation standards. Nevertheless, the absence of record of past performance is frequently relied on as a reason for rejecting this approach.⁴⁴

Different methodologies are used to capitalise income and estimate value, the most important being the capitalisation of earnings method (also known as the capitalised cash flow (CCF) method) and the discounted cash flow (DCF) method. These methodologies are based on the same premises but on different income bases and discount rates. 'Cash flow' is more often used as the basis for measuring future income stream than net earnings or future profit as it is seen to be a better indicator of value. Therefore, the DCF method is the most commonly used methodology within the income capitalisation approach.⁴⁵

The DCF method values the asset lost according to its income-producing capabilities and so, in theory, the method fully compensates the claimant investor by awarding an amount that reflects both the loss incurred and the gain of which the claimant was deprived.⁴⁶ The method involves first calculating the future cash flows of the enterprise being valued during a specific projected period, then ascertaining the present value of those cash flows. Future cash flows are not as valuable as current cash flows because of the time value of money and the risk that future circumstances might change in a way that would reduce or eliminate the anticipated future cash flows. The terminal or residual value of the cash flows arising at the end of the projected period may, if appropriate be ascertained and aggregated with the present value of cash flows within the projection period. This terminal or residual value represents 'the amount the business would be worth if it

⁴²Irmgard Marboe, *Calculation of Compensation and Damages in International Investment Law* (OUP 2009) 206.

⁴³World Bank, *Report to the Development Committee on the Legal Framework for the Treatment of Foreign Investment introducing the World Bank Guidelines on the Treatment of Foreign Direct Investment*, 31 ILM 1363, 1376 (1992), guideline IV.

⁴⁴See for example *Metalclad Corporation v Mexico*, ICSID Case No ARB(AF)/97/1, Award 30 August 2000, paras 119-22; *AIG Capital Partners, Inc. and CJSC Tema Real Estate Company v Kazakhstan*, ICSID Case No ARB/01/6, Award 7 October 2003, paras 12.1.10 and 12.2.

⁴⁵One quantitative study of ISCID awards has found that the DCF method is the second most common valuation methodology used by tribunals in ISCID arbitrations overall: see Credibility International, 'Study of Damages in International Center for the Settlement of Investment Disputes Cases' (1st edn, June 2014) 12.

⁴⁶World Bank, *Report to the Development Committee on the Legal Framework for the Treatment of Foreign Investment introducing the World Bank Guidelines on the Treatment of Foreign Direct Investment*, 31 ILM 1363, 1376 (1992), guideline IV.

was sold at market value at the end of the specific projection period, discounted back to the present value as of the valuation date.⁴⁷ Finally, the fair market value of the enterprise's debt must be deducted to arrive at a net cash flow figure.⁴⁸ Given these variables, there remains a certain degree of scepticism as to this approach to valuation and tribunals have declined to apply it in certain circumstances, most notably where the company was not an ongoing business with a proven record of profitability or where there is a striking divergence between the amount invested in the host state and the present value of future income.⁴⁹ It has also been suggested that investment treaty arbitration tribunals may be reluctant to apply the DCF method as it may be seen as putting too much of a burden on the respondent state.⁵⁰

(iii) *Asset-Based Approach*

This approach involves estimating the value of a business using methods based on the value of individual business assets less liabilities. This traditional approach avoids the uncertainty associated with the income capitalisation approach since it looks into the past performance of the business. However, this approach does not consider the value of the entity as a whole and fails to measure with certainty important factors such as the enterprise's contractual rights, know-how, goodwill and management skills.⁵¹ Furthermore, this method measures value as recorded on a balance sheet rather than the ability of the business to generate profit in the future.⁵² Thus, valuation experts generally advise against using the asset-based approach except in certain circumstances such as where the business is valued on a basis other than as a going concern, where it is a start-up business with no proven record

⁴⁷Mark Kantor, *Valuation for Arbitration* (Kluwer 2008) 182.

⁴⁸*ibid*, ch 4.

⁴⁹See for example *Metalclad Corporation v Mexico*, ICSID Case No ARB(AF)/97/1, Award 30 August 2000, paras 113-25; *PSEG v Turkey*, ISCID Case No ARB/02/5, Award 19 January 2007, paras 310-15.

⁵⁰Sergey Ripinsky, 'Damnum Emergens and Lucrum Cessans in Investment Arbitration: Entering through the back door' in Andrea K Bjorklund, Ian A Laird and Sergey Ripinsky (eds), *Investment treaty law: current issues. III, Remedies in international investment law emerging jurisprudence of international investment law* (British Institute of International and Comparative Law 2008) 54.

⁵¹Mark Kantor, *Valuation for Arbitration* (Kluwer 2008) 235.

⁵²Wälde and Sabahi note that the discrepancy between the forward and backward-looking approach is most dramatic in industries such as the petroleum industry. In such industries, considerable amounts may have been expended on land and exploratory drilling. However, if the drilled holes are dry, the value of such land will be minimal. If a drilling operation resulted in discovery of a large oilfield, the value will have no relation with what was spent; the value will essentially be the likely production multiplied by the likely oil price minus likely production cost (including likely taxes): Thomas Wälde and Borzu Sabahi, 'Compensation, Damages and Valuation' in Peter Muchlinski, Federico Ortino and Christoph Schreuer (eds), *The Oxford Handbook of International Investment Law* (OUP 2008) 1049.

of profitability, where its value lies in tangible, easily saleable assets (such as shipping or real estate companies) or where no alternative value can be obtained from the market.⁵³ Three common methods used to implement this approach and establish the present value of the assets of a business are book value,⁵⁴ replacement value⁵⁵ and liquidation value.⁵⁶ In addition, on occasion, investment treaty arbitration tribunals have granted recovery for actual losses (i.e. the costs of the investment),⁵⁷ which has sometimes been referred to as a variant of the book value method (albeit that this is not entirely accurate given that the book value by definition is reduced by depreciation).⁵⁸

(iv) *Other Approaches*

Apart from these three principal valuation methods, other approaches have been raised in valuation practice and by investment treaty arbitration tribunals. Thus, some tribunals have attempted to avoid the speculative nature of income-based valuation approaches by applying an asset or cost-based valuation and then increasing the resulting figure by an extra amount to allow for the loss of income opportunity. Application of this ‘mixed approach’ often makes it difficult to discern

⁵³Irmgard Marboe, *Calculation of Compensation and Damages in International Investment Law* (OUP 2009) 268. See also Mark Kantor, ‘Valuation for Arbitrators: Uses and Limits of the Adjusted Book Value Method in Energy-Related Disputes’ (2007) 4 *Transnational Dispute Management* 14.

⁵⁴Book value refers to the difference between the enterprise’s assets and liabilities as recorded on its financial statements or the amount at which the expropriated tangible assets appear on the balance sheet of the enterprise in accordance with generally accepted accounting principles: International Valuation Standards Council, *International Valuation Standards 2013*. If book value is adjusted to take into account factors such as inflation and/or by disregarding the accounting conventions regarding depreciation of assets and instead measuring the real devaluation of the asset in question, it can be useful as at least a reference point for the purposes of valuation, particularly in relation to recently established businesses: Mark Kantor, *Valuation for Arbitration* (Kluwer 2008) ch 7. See also Thomas Stauffer, ‘Valuation of Assets in International Takings’ (1996) 17 *Energy L J* 459, 485-86.

⁵⁵Replacement value refers to the current cost of a similar item having the nearest equivalent utility as the item being valued. This method may be appropriate where the business being valued is not a going concern: Irmgard Marboe, *Calculation of Compensation and Damages in International Investment Law* (OUP 2009) 283-84.

⁵⁶Liquidation value means the amounts at which individual assets comprised in the enterprise or the entire assets of the enterprise could be sold under conditions of liquidation to a willing buyer, less any liabilities which the enterprise has to meet. It is most appropriate to apply this method when the valuation object demonstrates a lack of profitability and/or a lack of future prospects such that the best use of the asset would be its sale: Sergey Ripinsky with Kevin Williams, *Damages in International Investment Law* (British Institute of International and Comparative Law 2008) 224-26.

⁵⁷Indeed, one quantitative study of ISCID awards has found that valuations based on the cost of the investment is the most common valuation methodology used by tribunals in ICSID arbitrations: see Credibility International, ‘Study of Damages in International Center for the Settlement of Investment Disputes Cases’ (1st edn, June 2014) 12.

⁵⁸Irmgard Marboe, *Calculation of Compensation and Damages in International Investment Law* (OUP 2009) 278-79; David Collins, ‘Reliance Remedies at the International Center for the Settlement of Investment Disputes’ (2009) 29 *Nw J Intl L & Business* 195.

how the tribunal arrives at the final figure but it is nevertheless quite commonly applied by tribunals and often features in submissions.⁵⁹ Other tribunals have relied on the ‘insurance value’ or ‘tax value’ of a particular asset when carrying out their valuations, despite the fact that the amount insured depends on many factors other than the value of the asset and similarly the valuation of companies and assets for tax purposes serves specific purposes, which are not necessarily related to the true value of the asset.⁶⁰ Yet another approach which has been mentioned but not applied in investment arbitration practice is the ‘real option’ approach. Thus, in *CMS v Argentina* the tribunal mentioned (but did not apply) a ‘comparable transaction’ approach which reviews comparable transactions in similar circumstances (though this has similarities to the market approach) and a ‘real option’ approach which studies the alternative uses that could be made of the assets in question and the costs and benefits associated with such uses.⁶¹

Finally, where an investor-state contract is also in place with the claimant investor, contractual provisions may be relied on for valuation purposes.⁶² This can render the valuation process more straightforward if, for example, the contract includes provisions on ‘redemption prices’ or similar mechanisms that allow for prior estimation of the ‘cost’ of a breach. However, it is not uncommon for investor-state contracts to leave open the nature of damages that will be available for breach or at least not to adequately provide for the situation at issue, particularly if the contract is subject to adjustment mechanisms and other possible variations with the passing of time.⁶³ For example, in *PSEG v Turkey* the tribunal acknowledged that binding contractual revenue obligations could, in certain cases, overcome the absence of an operating history for the investment.⁶⁴ However, in *PSEG* the contract was not sufficiently detailed as the parties had never finalised the essential commercial terms of the contract.⁶⁵ Accordingly, the tribunal chose to award to the claimant

⁵⁹Irmgard Marboe, *Calculation of Compensation and Damages in International Investment Law* (OUP 2009) 294-98.

⁶⁰*ibid.*, 298-99.

⁶¹ICSID Case No ARB/01/8, Award 12 May 2005, para 403.

⁶²See for example *Mobil Cero Negro Limited vs Petróleos de Venezuela, S.A. and PDVSA Cerro Negro, S.A.*, ICC Arbitration Case No 15416/JRF/CA, Award 23 December 2011. See also Borzu Sabahi, *Compensation and Restitution in Investor-State Arbitration: Principles and Practice* (OUP 2011) 126.

⁶³Irmgard Marboe, *Calculation of Compensation and Damages in International Investment Law* (OUP 2009) 301-04.

⁶⁴ICSID Case No ARB/02/5, Award 19 January 2007, paras 310-11.

⁶⁵*ibid.*, para 313.

investor only the investment expenses, subject to some downward adjustments.⁶⁶ Thus, while, for example, a liquidated damages clause in an investor-state contact may be a permissible method of placing a cap on the amount of damages to be awarded, a clause stipulating a general approach to the determination of the quantum of damages would be insufficient.⁶⁷

(d) *Analysis of the approach taken by investment treaty arbitration tribunals to date at the remedies stage*

In summary, investment treaty arbitration tribunals have generally awarded the fair market value of the expropriated asset in cases of lawful expropriation and, in respect of unlawful acts, have applied the full reparation principle (albeit quite frequently relying on the difference in the fair market value of an investment resulting from the breach in question to achieve this). In giving effect to these principles, investment treaty arbitration tribunals apply one or more valuation methods, which, although useful tools, are based on assumptions of what would have transpired in the absence of the breach, and so are necessarily based on subjective judgment and speculation. Thus, the tribunal in *Amco v Indonesia (II)* observed as follows in relation to the DCF method:

it is not a mechanistic device. The method itself relies upon the application of assumptions which are necessarily judgmental. The DCF method is at once a flexible tool that allows for an application of factors and elements judged as relevant. At the same time, it allows for the application of these judgmental elements to be articulated.⁶⁸

Accordingly, even if the parties' valuation experts apply the same valuation method, they are likely to come to differing (and often widely disparate) results in applying differing assumptions. For example, in *Tecmed v Mexico* the tribunal noted the 'remarkable disparity' between the estimates of the parties' valuation experts, both of whom applied the DCF valuation method – the claimant's expert valued damages at \$52 million plus interest while the respondent's expert valued

⁶⁶ibid, paras 317-40.

⁶⁷See *Kardassopoulos and Fuchs v Georgia*, ICSID Case Nos ARB/05/18 and ARB/07/15, Award 3 March 2010, para 481.

⁶⁸ICSID Case No ARB/81/1, Resubmitted Case Award 5 June 1990 and Decision on Supplemental Decisions and Rectification 17 October 1990, 1 ICSID Rep 569, para 199.

the loss at between \$1.8 and \$2.1 million.⁶⁹ By necessity therefore, a considerable degree of discretion is required to be exercised by investment treaty arbitration tribunals in quantifying damages and the remedies stage of the arbitral process is subject to a much larger degree of arbitrator discretion than is considered acceptable at either the jurisdiction or merits stage.⁷⁰ As was noted by the tribunal in *Lemire v Ukraine*:

Valuation is not an exact science. The Tribunal has no crystal ball and cannot claim to know what would have happened under a hypothesis of no breach; the best any tribunal can do is to make an informed and conscientious evaluation, taking into account all the relevant circumstances of the case...in the end there is no denying that the calculation of damages...inevitably requires a certain amount of conjecture as to how things would have evolved “but for” the actual behaviour of the parties. This difficulty in calculation cannot, however, deprive an investor, who has suffered injury, from his fundamental right to see his losses redressed.⁷¹

Therefore, the discretion exercised by tribunals in quantifying damages is exercised ‘pursuant to customary international law, and not...instead of customary international law’.⁷² However, the exercise of discretion by tribunals has, on occasion, led to awards in which the tribunal in question, when faced with divergent party valuations, has simply ‘split the baby’ (i.e. awarded a figure somewhere in between the figures proffered by the parties). For example, in *Santa Elena v Costa Rica*⁷³ the tribunal noted that there was little evidence of what the property was worth at the date of the expropriation (apart from the valuations provided by the claimant and respondent). The tribunal then went on to state that, because of this, it had ‘proceeded by means of a process of approximation’ based on the parties’ appraisals. The tribunal then arrived at a figure lying between those two valuations, stating by way of explanation that the assessment was informed by ‘the evidence submitted by the parties and the factors relevant to the value of the Santa Elena

⁶⁹ICSID Case No ARB(AF)/99/2, Award 29 May 2003, para 186.

⁷⁰*Rumeli v Kazakhstan*, ICSID Case No ARB/05/16, Decision of Committee on the Application for Annulment 25 March 2010, paras 140-78.

⁷¹ ICSID Case No ARB/06/18, Award 28 March 2011, paras 248-49.

⁷²*Azurix v Argentina*, ICSID Case No ARB/01/12, Decision on the Application for Annulment of the Argentine Republic 1 September 2009, para 320.

⁷³ ICSID Case No ARB/96/1, Final Award 17 February 2000.

Property in 1978'.⁷⁴ However, although the award in *Santa Elena* can be viewed as a form of 'rough justice', the tribunal's focus in exercising its discretion to quantify the compensation payable was on ensuring, in the face of uncertainty, that a reasonable estimate of the losses of the claimant investor was achieved rather than on taking into account interests extraneous to those of the claimant investor. Similarly, in the relatively few cases in which the partial defence of contributory fault or the related plea of failure to mitigate loss has been accepted,⁷⁵ investment treaty arbitration tribunals have exercised considerable discretion in apportioning responsibility as between the claimant investor and the host state. Thus, Sabahi and Duggal observe that 'Ultimately, [the apportionment of responsibility] seems to be a very subjective exercise, because its nature defies any mathematical precision'.⁷⁶ It is of course possible (and perhaps probable) that some investment treaty arbitration tribunals may have taken into account public interest considerations into account in exercising this considerable discretion without acknowledging that they are so doing through a process of 'reverse engineering' (i.e. envisaging a fair result and then developing reasoning to justify that outcome).⁷⁷ However, investment treaty arbitration tribunals have, to date, generally not explicitly referred to public interest considerations at the remedies stage or purported to adjust the compensation or damages payable by respondent host states on the basis of such considerations and, perhaps as a consequence of this, host states have rarely raised public-interest based arguments in their submissions relating to the remedies stage.⁷⁸

⁷⁴ *ibid*, paras 90-95.

⁷⁵ *MTD Equity Sdn. Bhd. and MTD Chile S.A. v Republic of Chile*, ICSID Case No ARB/01/7, Award 25 May 2004, paras 242-46; *Occidental Petroleum Corp., Occidental Exploration and Prod. Co. v Ecuador*, ICSID Case No ARB/06/11, Award 5 October 2012, paras 668-70; *Yukos Universal Limited (Isle of Man) v the Russian Federation*, PCA Case No AA 27, Award 18 July 2014, para 1594 ff. See also *Middle East Cement Shipping and Handling Co SA v Egypt*, ICSID Case No ARB/99/6, Award 12 April 2002 paras 166-71 for acceptance, in principle, of the plea of failure to mitigate loss; cf *AIG Capital Partners, Inc. and CJSC Tema Real Estate Company v Kazakhstan*, ICSID Case No ARB/01/6, Award 7 October 2003, para 10.6.4.

⁷⁶ Borzu Sabahi and Kabir Duggal, 'Case Comment: Occidental Petroleum v Ecuador (2012): Observations on Proportionality, Assessment of Damages and Contributory Fault' (2013) 28 ICSID Rev 279, 289.

⁷⁷ Mark Kantor, *Valuation for Arbitration* (Kluwer 2008) 135-37.

⁷⁸ See however *Siemens AG v Argentina*, ICSID Case No ARB/02/8, Award 6 February 2007, para 346 noting an argument by Argentina, based on European Court of Human Rights jurisprudence, that the fair market value standard should not apply to expropriations which become necessary for social policy reasons.

Arguably the only exceptions to this general proposition are, first, the distinction drawn between, on the one hand, the compensation payable in respect of a lawful expropriation and, on the other, the damages payable in respect of an unlawful expropriation and, secondly, the effect on the damages obligation of successful invocation of the customary international law defence of necessity. Turning to the first exception, in *ADC v Hungary*⁷⁹ the full reparation principle rather than the valuation standard set out in the relevant IIA in respect of lawful expropriations was applied in circumstances where an unlawful expropriation has occurred. Accordingly, since the value of the investment had increased between the date of the taking and the date of the award, that extra amount was awarded to the claimant. Since *ADC v Hungary*, this distinction has increasingly been drawn by other investment treaty arbitration tribunals.⁸⁰ Such a distinction is desirable (and takes account of public interest considerations to some extent) as a failure to distinguish between unlawful and lawful expropriations could be said to give states little incentive to comply with due process and the non-discrimination principle in exercising their regulatory sovereignty.⁸¹ However, as was noted by the tribunal in *ADC v Hungary*, since an increase in value between the date of the taking and the date of the award (as occurred in *ADC*) is unusual, if not unique,⁸² the real effect of this distinction is quite limited.⁸³

Similarly, while adjusting the damages payable to take account of successful invocation of the defence of necessity could potentially constitute a means of taking account of public interest considerations,⁸⁴ the effect of successful invocation of the

⁷⁹*ADC Affiliate Limited and ADC & ADMC Management Ltd v Hungary*, ICSID Case No ARB/03/16, Award 2 October 2006, paras 480-96.

⁸⁰*Siag and Vecchi v Egypt*, ICSID Case No ARB/05/15, Award 1 June 2009, paras 539-41; *Saipem SpA v Bangladesh*, ICSID Case No ARB/05/7, Award 20 June 2009, para 201; *Yukos Universal Limited (Isle of Man) v the Russian Federation*, PCA Case No AA 27, Award 18 July 2014, paras 1763-69. See also Borzu Sabahi and Nicholas J Birch, 'Comparative Compensation for Compensation' in Stephan W Schill (ed), *International Investment Law and Comparative Public Law* (OUP 2010).

⁸¹Campbell McLachlan, Laurence Shore and Matthew Weiniger, *Investment Treaty Arbitration: Substantive Principles* (OUP 2007) 331-32.

⁸²*ADC Affiliate Limited and ADC & ADMC Management Ltd v Hungary*, ICSID Case No ARB/03/16, Award 2 October 2006, para 496.

⁸³See also JH Dalhuisen and AT Guzman, 'Expropriatory and Non-Expropriatory Takings under International Investment Law' (2013) 10 *Transnational Dispute Management* 19 arguing that fair market value and full reparation are both compatible with the notion of full compensation and that the real difference is the possibility of physical re-instatement or specific performance.

⁸⁴The effect of successful reliance on a NPM clause is not dealt with here. Since NPM clauses comprise a set of primary legal rules that must be adjudicated upon in deciding whether a breach occurred rather than a means of excusing such breach, this would seem to require that the obligation

defence remains unsettled.⁸⁵ In this regard, Article 27 of the Draft ILC Articles provides that the invocation of a circumstance precluding wrongfulness (such as the defence of necessity) is without prejudice to ‘the question of compensation for any material loss caused by the act in question’.⁸⁶ While the reference to ‘material loss’ in Article 27 of the Draft ILC Articles is narrower than the concept of full reparation and it is explicitly stated in the commentaries to the Draft ILC Articles that Article 27 is not concerned with compensation within the framework of full reparation for wrongful conduct,⁸⁷ Article 27 does not attempt to specify in what circumstances (or to what extent) compensation should be payable.⁸⁸ Indeed, even if it did so, the applicability of such a conclusion in the sphere of investment treaty arbitration would be questionable, given the difference between invoking such defence in the context of an inter-state relationship and in the context of an investor-state relationship.⁸⁹ Thus, while the potential for public interest considerations to be taken into account at the remedies stage when the defence of necessity is invoked exists, this potential has not yet crystallised. Overall therefore, it is fair to say that reference to, or explicit consideration of, the host state’s right to

to compensate the claimant investor is excluded entirely: see *Sempra Energy International v Argentina*, ICSID Case No ARB/02/16, Decision on Argentina’s Application for Annulment of the Award 29 June 2010, para 118; William W Burke-White and Andreas Von Staden, ‘Investment Protection in Extraordinary Times: The Interpretation and Application of Non-Precluded Measures Provisions in Bilateral Investment Treaties’ (2007-2008) 48 *Va J Intl L* 307, 398; cf Diane A Desierto, ‘Necessity and National Emergency Clauses: Sovereignty in Modern Treaty Interpretation’ (Martinus Nijhoff Publishers 2012) 198.

⁸⁵See William W Burke-White and Andreas Von Staden, ‘Investment Protection in Extraordinary Times: The Interpretation and Application of Non-Precluded Measures Provisions in Bilateral Investment Treaties’ (2007-2008) 48 *Va J Intl L* 307; José E Álvarez and Kathryn Khamsi, ‘The Argentine Crisis and Foreign Investors: a Glimpse into the heart of the Investment Regime’ in Karl P Sauvant (ed), *The Yearbook of International Investment Law and Policy 2008-2009* (OUP 2009) 458-60; Borzu Sabahi, *Compensation and Restitution in Investor-State Arbitration: Principles and Practice* (OUP 2011) 180; Andreas Kulick, *Global Public Interest in International Investment Law* (Cambridge University Press 2012) ch 4.

⁸⁶See *CMS v Argentina*, ICSID Case No ARB/01/8, Award 12 May 2005, paras 383-94; *Enron Corporation and Ponderosa Assets, LP v Argentina*, ICSID Case No ARB/01/3, Award 22 May 2007, paras 343-45.

⁸⁷International Law Commission, *Draft Articles on Responsibility of States for Internationally Wrongful Acts, with commentaries 2001* (2001) 2 *YB Intl L Comm’n*, UN Doc A/CN.4/SER.A/2001/Add.1 (Part 2), para 4 of the commentary on art 27.

⁸⁸Borzu Sabahi, *Compensation and Restitution in Investor-State Arbitration: Principles and Practice* (OUP 2011) 180.

⁸⁹Indeed, albeit that investment treaty arbitration tribunals have frequently relied upon the Draft ILC Articles, their relevance to investment treaty arbitration generally has been disputed: see Kaj Hobér, ‘State Responsibility and Investment Arbitration’ (2005) 2 *Transnational Dispute Management*; Carole Malinvaud, ‘Non-pecuniary Remedies in Investment Treaty and Commercial Arbitration’ in Albert Jan van den Berg (ed), *50 Years of the New York Convention: ICCA International Arbitration Conference* (Kluwer 2009) 225; Irmgard Marboe, ‘State Responsibility and Comparative State Liability for Administrative and Legislative Harm to Economic Interests’ in Stephan W Schill (ed), *International Investment Law and Comparative Public Law* (OUP 2010) 377.

regulate or the legitimate purposes behind such regulation has been scant at the remedies stage. In fact, the Separate Opinion of Professor Ian Brownlie in *CME v Czech Republic*, in which he argued that the award of damages in investment treaty disputes should take into account the fact that such disputes are not purely ‘commercial’ in nature, as they concern sovereign states responsible for the well-being of their people, remains the only substantial exposition of the general proposition that host state interests should influence the computation of damages in investment treaty arbitration.⁹⁰

Having, in the first part of this chapter, provided a general overview of the valuation process undertaken by investment treaty arbitration tribunals, the second part of this chapter will assess whether, despite the scant recognition of public interest considerations in assessing damages to date, the remedies stage of the investment treaty arbitration process in fact constitutes an appropriate platform for such considerations.

4.2 An assessment of the remedies stage as a platform for public interest considerations

As was demonstrated in Chapter 3, the various methods of taking account of public interest considerations at the merits stage are not entirely satisfactory. One of the primary reasons for this is that, given the ‘asymmetric’ nature of IIAs and of the investment treaty arbitration process, it is difficult to determine the weight to be attributed to public interest considerations *vis-à-vis* investor interests (and accordingly to balance investor interests and public interest considerations). On a related note, the extent to which the non-investment related international obligations of the host state should be considered in informing the interpretation of IIA rights is unclear. Finally, the black-or-white decision as to liability required at the merits stage ultimately means that one particular set of interests must be prioritised, which may lead to either investor or host state interests not being optimised. These factors combined give rise to the question of whether the

⁹⁰*CME v Czech Republic*, UNCITRAL, Separate Opinion on the Issues at the Quantum Phase by Ian Brownlie, 13 March 2003, paras 58-77.

introduction of an element of flexibility or balancing of interests would be beneficial in determining the quantum of damages payable to claimant investors.⁹¹

In addressing this question, a distinction can be drawn between, on the one hand, taking into account countervailing interests in order to promote or take account of such interests and, on the other, taking into account those interests indirectly for pragmatic reasons (such as the difficulty of enforcing the ‘ideal’ remedy), albeit that there may be a significant overlap between the two categories in certain circumstances. Thus, the latter tendency arises due to the fact that the remedies stage constitutes the point of the legal process at which principle meets reality as it must lead to a ‘real’ and enforceable remedy.⁹² In order to attain this goal, it is perhaps inevitable (and arguably desirable) that factors such as the cost of a remedy awarded to the tax-payer or public resistance to a particular remedy are considered. While not acknowledging that they are so doing, it is likely that investment treaty arbitration tribunals already consider the practicalities of enforcing their awards (such as the host state’s payment capacity) in formulating remedies and in exercising their inherent discretion in assessing claimant investors’ losses.⁹³ However, this pragmatic impulse, which is driven by the desire to ensure that the claimant is granted an enforceable remedy, differs qualitatively from the deliberate and acknowledged consideration of third party or public interests in formulating remedies and it is this latter category with which this thesis is concerned.⁹⁴

The deliberate and acknowledged consideration of third party or public interests is not unprecedented in the law of remedies, particularly in the sphere of state liability law in domestic legal systems. Thus, where on the domestic level, wrongful state action causing harm to private law subjects occurs, this is addressed as a matter of

⁹¹See UNCTAD, *Fair and Equitable Treatment: UNCTAD Series on Issues in International Investment Agreements II* (UNCTAD 2012) 89 noting that ‘While the question of liability is ultimately black and white – either there is a breach or not – the compensation stage potentially allows additional room for balancing of relevant interests’.

⁹²Paul Gewirtz, ‘Remedies and Resistance’ (1982-1983) 92 Yale L J 585.

⁹³Mark Kantor, *Valuation for Arbitration* (Kluwer 2008) 135-36; Thomas Wälde and Borzu Sabahi, ‘Compensation, Damages and Valuation in International Investment Law’ in Peter Muchlinski, Federico Ortino and Christoph Schreuer (eds), *The Oxford Handbook of International Investment Law* (OUP 2008) 1054.

⁹⁴Admittedly, some commentators have somewhat conflated this distinction: see Abram Chayes, ‘The Role of the Judge in Public Law Litigation’ (1976) 89 Harv L Rev 1281; Paul Gewirtz, ‘Remedies and Resistance’ (1982-1983) 92 Yale L J 585; Kent Roach, ‘The Limits of Corrective Justice and the Potential of Equity in Constitutional Remedies’ (1991) 33 Ariz L Rev 859; Margaux J Hall and David C Weiss, ‘Human Rights and Remedial Equilibration’ (2011) 36 Brook J Intl L 453, 499-500.

state liability law.⁹⁵ The rules applicable in determining the liability of public authorities and the remedies available to individuals harmed by wrongful state conduct are, depending on the legal system in question, incorporated either in public law or in the private law of torts (or delict) or, more frequently, in both.⁹⁶ In recognition of the rights and duties of the state to act for the public benefit, the rules of state liability generally differ from the law applicable in determining liability as between private individuals and aim at achieving a balance as between the interests of the harmed individuals and those rights and duties of the state.⁹⁷ Thus, for example, state liability in respect of legislative and judicial acts is generally limited and references to state interests, to the state's margin of discretion and to the effect which the liability regime has on the discretion accorded to certain regulatory and supervisory authorities are common in assessing state liability and in formulating remedies.⁹⁸

However, although there are certain similarities in function between domestic state liability law and investment treaty arbitration (including controlling state power, upholding the rule of law and providing remedies to private law subjects for state misconduct),⁹⁹ it is clear that the extent to which, and manner in which, public interest considerations are taken into account within a particular legal regime must

⁹⁵For comparative surveys of the liability of public authorities see D Fairgrieve, M Andenas and J Bell (eds), *Tort Liability of Public Authorities in Comparative Perspective* (British Institute for International and Comparative Law 2002); Duncan Fairgrieve, *State Liability in Tort: A Comparative Law Study* (OUP 2003); R Rebhahn, 'Public Liability in Comparison: England, France, Germany' in H Koziol and B Steininger (eds), *European Tort Law 2005* (Springer 2006). On the topic of the remedies specifically see David Gaukrodger and Kathryn Gordon, *Investor-state dispute settlement: A scoping paper for the investment policy community*, OECD Working Papers on International Investment No 2012/3 (OECD 2012), Annex 4.

⁹⁶Irmgard Marboe, 'State Responsibility and Comparative State Liability for Administrative and Legislative Harm to Economic Interests' in Stephan W Schill (ed), *International Investment Law and Comparative Public Law* (OUP 2010) 378.

⁹⁷It is however important to note that state liability regimes vary as between jurisdictions (reflecting the specific features of that legal system and the historical evolution of norms regarding the role of the state in that particular society) and also differ depending on the nature of the governmental act, the governmental entity involved and the type of harm suffered by the claimant: see Gus Van Harten, *Investment Treaty Arbitration and Public Law* (OUP 2007) 108.

⁹⁸Hanna Wilberg, 'Defensive Practice or conflict of duties? Policy concerns in public authority negligence claims' (2010) 126 LQR 420; David Gaukrodger and Kathryn Gordon, *Investor-state dispute settlement: A scoping paper for the investment policy community*, OECD Working Papers on International Investment No 2012/3 (OECD 2012) Annex 4. See also Irmgard Marboe, 'State Responsibility and Comparative State Liability for Administrative and Legislative Harm to Economic Interests' in Stephan W Schill (ed), *International Investment Law and Comparative Public Law* (OUP 2010) 408-11.

⁹⁹Gus Van Harten, *Investment Treaty Arbitration and Public Law* (OUP 2007); Benedict Kingsbury, 'The Concept of Law' in Global Administrative Law' (2009) 20 Eur J Intl L 23; Stephan W Schill (ed), *International Investment Law and Comparative Public Law* (OUP 2010).

reflect the nature and purpose of the legal regime in question.¹⁰⁰ Therefore, quite apart from doctrinal-related difficulties,¹⁰¹ it is submitted that, from a policy perspective, it is not necessarily desirable that the approach taken to remedies under domestic state liability systems be automatically transplanted into the sphere of investment treaty arbitration. This is the case not least because the overall structure of IIAs and their dispute settlement provisions encourage (and arguably mandate) application of the bilateral notion of corrective justice (which focusses on fairness to the victim of wrongdoing and on ensuring that any harm done to the victim is rectified)¹⁰² while state liability regimes can be conceptualised as falling closer to the distributive justice end of the remedial spectrum (which focusses on multilateral considerations and on the proper distribution of the benefits and burdens that are held in common by all that belong to a community).¹⁰³ This disparity, of itself, should not preclude public interest considerations from being taken into account to temper the ‘pure’ notion of corrective justice in order to accommodate government discretion in appropriate cases.¹⁰⁴ However, it does point towards the conclusion that justification which reflects the distinctive features of the investment treaty arbitration system is necessary to support the proposition that public interest considerations should be taken into account in quantifying the damages payable to investors under IIAs. The remainder of this section will focus on providing such normative justification.

¹⁰⁰Steven R Ratner, ‘Regulatory Takings in Institutional Context: Beyond the Fear of Fragmented International Law’ (2008) 102 AJIL 475; Valentina Sara Vadi, ‘Critical Comparisons: The Role of Comparative Law in Investment Treaty Arbitration’ (2010) 39 Denver J Intl L & Policy 97.

¹⁰¹Such difficulties include the fact that there is insufficient homogeneity between different state liability regimes for ‘general principles’ (within the meaning of Article 38 of the ICJ Statute) to be elucidated so as to influence investment treaty arbitration and the fact that, in contrast to the pre-eminence of non-pecuniary remedies under state liability regimes, damages are the most common remedy awarded by investment treaty arbitration tribunals: see J Bell, ‘Mechanisms for Cross-fertilisation of Administrative Law in Europe’ in J Beatson and T Tridimas (eds), *New Directions in European Public Law* (Hart Publishing 1998); Robert Thomas, *Legitimate Expectations and Proportionality in Administrative Law* (Hart Publishing 2000); Andreas Kulick, ‘Publication Review: International Investment Law and Comparative Public Law edited by Stephan W. Schill’ (2011) Eur J Intl L 917, 922.

¹⁰²E J Weinrib, ‘Corrective Justice in a Nutshell’ (2002) 52 U Toronto L J 349.

¹⁰³*ibid.* See also Santiago Montt, *State Liability in Investment Treaty Arbitration: Global Constitutional and Administrative Law in the BIT Generation* (Hart Publishing 2009) 10-11.

¹⁰⁴For a similar argument see Francois du Bois, ‘Human Rights and the Tort Liability of Public Authorities’ (2011) 127 LQR 589, 598. See also Santiago Montt, *State Liability in Investment Treaty Arbitration: Global Constitutional and Administrative Law in the BIT Generation* (Hart Publishing 2009) 26.

(a) *Normative arguments in favour of taking account of public interest considerations at the remedies stage*

In Chapter 2, the need to ensure that states continue to participate in, and co-operate in achieving the goals of, the investment treaty arbitration system was cited as one of the principal reasons why a balancing of investor and host state interests is required in the field of investment treaty arbitration.¹⁰⁵ Naturally, the introduction of an element of balancing or reciprocity is likely to require certain trade-offs to be made in terms of achieving the other goals of the investment treaty arbitration system (such as that of protecting foreign investors against the effects of host state regulation and providing investors with full compensation).¹⁰⁶ However, these trade-offs are required in order to ensure the continuing viability of the system as a whole.¹⁰⁷ The need for an element of reciprocity in order to ensure that the underlying purposes of IIAs are fostered and that states continue to participate in the investment treaty arbitration system was alluded to by the tribunal in *Saluka v Czech Republic* in stating as follows:

The protection of foreign investments is not the sole aim of the Treaty, but rather a necessary element alongside the overall aim of encouraging foreign investment and extending and intensifying the parties' economic relations. That in turn calls for a balanced approach to the interpretation of the Treaty's substantive provisions for the protection of investments, since an interpretation which exaggerates the protection to be accorded to foreign investments may serve to dissuade host States from admitting foreign investments and so undermine the overall aim of extending and intensifying the parties' mutual economic relations.¹⁰⁸

¹⁰⁵On the importance of state co-operation in the field of international law see: Anne Van Aaken, 'International investment law between commitment and flexibility: a contract theory analysis' (2009) 12 J Intl Economic L 507; Omar E García-Bolívar, 'Economic Development at the Core of the International Investment Regime' in Chester Brown and Kate Miles (eds), *Evolution in Investment Treaty Law and Arbitration* (Cambridge University Press 2011) 587; Anne van Aaken, 'Shared Responsibilities in International Law: A Political Economy Analysis', University of St Gallen Law School, Law and Economics Research Paper Series, Working Paper No 2014-04, March 2014.

¹⁰⁶Anne van Aaken, 'Shared Responsibilities in International Law: A Political Economy Analysis', University of St. Gallen Law School, Law and Economics Research Paper Series, Working Paper No 2014-04, March 2014.

¹⁰⁷Gus Van Harten, *Sovereign Choices and Sovereign Constraints: Judicial Restraint in Investment Treaty Arbitration* (OUP 2013) 47.

¹⁰⁸*Saluka Investments BV v The Czech Republic*, UNCITRAL, Partial Award 17 March 2006, para 300. See also Legal Opinion of M Sornarajah in *El Paso Energy International Company v*

This passage also points to a further reason why an element of reciprocity or balancing of interests is required in investment treaty arbitration, namely that, while the protection of foreign investors is the primary object of IIAs, the rights accorded to investors under IIAs are not directed at protecting the fundamental interests of investors as an end in and of itself.¹⁰⁹ The resistance of tribunals to investor claims which characterise rights under IIAs as human rights can be seen as indicative of this.¹¹⁰ Rather IIAs reflect a policy choice to protect foreign direct investment generally on the assumption that this will assist in promoting future investment and economic development, which can itself be considered to be in the public interest.¹¹¹ Therefore, the promotion of investment or of further economic co-operation can be described as an intermediary purpose of IIAs with the promotion of development being the ultimate purpose.¹¹² These purposes are explicitly recognised in the preambles to some IIAs and have been referred to by some investment treaty arbitration tribunals¹¹³ but, it is submitted, such purposes undergird the entire investment treaty arbitration system.¹¹⁴

Argentina, ICSID Case ARB/03/15, 5 March 2007, para 27 arguing that rights that are not consistent with the aim of development lose their basis for treaty protection.

¹⁰⁹Christoph Schreuer, *ICSID Convention: A Commentary* (2nd edn, Cambridge University Press 2009) 4-8; Andrew Newcombe and Lluís Paradell, *Law and Practice of Investment Treaties: Standards of Treatment* (Kluwer 2009) 262-63.

¹¹⁰See *Biloune and Marine Drive Complex Limited v Ghana Investments Centre and the Government of Ghana*, UNCITRAL, Award on Jurisdiction and Liability 27 October 1989; *Patrick Mitchell v Congo*, ICSID Case No ARB/99/7, Decision on Application for Annulment of the Award 1 November 2006.

¹¹¹See Report of the Executive Directors on the Convention on the Settlement of Investment Disputes Between States and Nationals of Other States, 18 March 1965, 4 ILM 524 (1965) para 9.

¹¹²See Isabelle Buffard and Karl Zemanek, 'The 'Object and Purpose' of a Treaty: An Enigma?' (1998) 3 *Austrian Rev Intl & Eur L* 311, 326 for the distinction between the object of a treaty and its purpose.

¹¹³See for example Treaty between the Federal Republic of Germany and the Islamic Republic of Afghanistan concerning the Encouragement and Reciprocal Protection of Investments, signed 20 April 2005, entered into force 12 October 2007, preamble; Agreement between the Czech Republic and the Republic of Albania, signed 27 June 1994, entered into force 7 July 1995, preamble; Agreement between Australia and the Republic of Hungary on the Reciprocal Promotion and Protection of Investments, signed 15 August 1991, entered into force 10 May 1992, preamble; Agreement between the Belgium-Luxembourg Economic Union and the Government of the People's Republic of China on the Reciprocal Promotion and Protection of Investments, signed 6 June 2005, entered into force 1 December 2009, preamble; Treaty between the Government of the United States of America and the Government of the Republic of Rwanda concerning the Encouragement and Reciprocal Protection of Investments, signed 19 February 2008, entered into force 1 January 2012, preamble.

¹¹⁴Jeswald W Salacuse, *The Law of Investment Treaties* (OUP 2010) 111; Anne van Aaken, 'Smart Flexibility Clauses in International Investment Treaties and Sustainable Development: A Functional View', University of St Gallen Law School, Law and Economics Research Paper Series Working Paper No 2013-18 March 2013, 26. See also ICSID Convention, Preamble.

Therefore, a question arises as to the stage of the arbitral process at which an element of reciprocity or balancing of interests should be incorporated, while simultaneously recognising the fact that (rightly or wrongly) states have, as an exercise of sovereignty, entered into IIAs and in doing so agreed to limit the exercise of some of their sovereign rights for the benefit of foreign investors. Given that the primary object of the investment treaty system is the protection of foreign investors and given the ‘gateway’ function of the jurisdiction stage of the arbitral process,¹¹⁵ placing severe restrictions on the ability of investors to bring claims for the purpose of achieving such reciprocity would not seem appropriate. Turning to the merits stage, although there are certain difficulties associated with taking into account public interest considerations at the merits stage, to completely disregard public interest considerations in determining liability would limit host state sovereignty to an unacceptable extent as it would preclude examination of the context and purpose of host state measures and would therefore likely increase the number of IIA violations found by investment treaty arbitration tribunals. This would be undesirable from a public interest perspective as a tribunal’s conclusion that a state has breached investor rights under an IIA can cause country risk to increase significantly which can lead to a decline in foreign investment, higher political risk rating (and thus insurance premiums) and a higher threshold hurdle rate of return to compensate for such risk.¹¹⁶ Thus, the tribunal’s evaluation of the host state’s action at the merits stage must balance investor interests with other legally relevant interests, and take into consideration a number of countervailing factors, before it can establish that a violation of an investor right, that warrants compensation, has actually occurred.¹¹⁷

However, it is submitted that, to complement this recognition of public interest considerations at the merits stage and to allow for a more nuanced reflection of

¹¹⁵See George A Bermann, ‘The “Gateway” Problem in International Commercial Arbitration’ (2012) 37 Yale J Intl L 1.

¹¹⁶F Marrella and I Marboe, ‘“Efficient Breach” and Economic Analysis of International Investment Law’ (2007) 4 Transnational Dispute Management 13; Todd Allee and Clint Peinhardt, ‘Contingent Credibility: The Reputational Effects of Investment Treaty Disputes on Foreign Direct Investment’ (2011) 65 Intl Organization 401; cf Andreas Kulick, ‘Sneaking Through the Backdoor – Reflections on Public Interest in International Investment Arbitration’ (2013) 29 Arbitration Intl 435, 450 arguing that, in contrast to other international disputes, in investment arbitration, states care much less whether they are found to have violated international law but rather focus primarily on the amount of compensation or damages payable.

¹¹⁷See *Lemire v Ukraine*, ICSID Case No ARB/06/18, Decision of Jurisdiction and Liability 14 January 2010, para 285.

such considerations than the ‘all or nothing’ decision as to liability required in determining whether an IIA breach has occurred or not, balancing of interests at the remedies stage may be appropriate in certain circumstances. This would assist arbitrators in reconciling the ‘asymmetric’ nature of IIAs and the need to ensure effective protection of investor interests with the need to introduce an element of reciprocity into the investment treaty arbitration process. Furthermore, it should ensure that the approach taken at the remedies stage advances, rather than interferes with, the substantive values at stake in a particular dispute. Thus, although the process of quantifying damages may appear to be a neutral process that exists in isolation from those substantive issues, this is by no means the case. To the contrary, rights and remedies are inextricably connected and, accordingly, the parameters of a particular remedy are crucial to the strength of the right being protected by that remedy and to how that right is balanced with public policy goals. Accordingly, as a general principle, the normative propositions that underpin the evaluation of rights at the merits stage should carry through to the remedies stage so as to ensure that the two stages of the adjudicative process work in tandem with each other in promoting those norms.¹¹⁸

The fact that investment treaty arbitration tribunals are already well-accustomed to exercising discretion in formulating remedies (albeit, to date, primarily to overcome the uncertainties associated with quantifying claimant investors’ losses) and that the exercise of such discretion has been widely accepted as necessary¹¹⁹ makes this proposition a less radical proposal than may, at first blush, appear to be the case. Indeed, while arguments in favour of the granting of non-pecuniary remedies in investment treaty arbitration have become more frequent amongst academic commentators, it is submitted that the remedy of damages may, in fact, afford investment treaty arbitration tribunals greater scope than certain other remedies in terms of taking account of countervailing interests.¹²⁰ However, in considering

¹¹⁸See Christopher Serkin, ‘The Meaning of Value: Assessing Just Compensation for Regulatory Takings’ (2004-2005) 99 Nw U L Rev 677, 742 making this point in the context of the compensation payable in respect of takings under US law.

¹¹⁹See *Lemire v Ukraine*, ICSID Case No ARB/06/18, Award 28 March 2011, paras 248-49; Irmgard Marboe, *Calculation of Compensation and Damages in International Investment Law* (OUP 2009) 145.

¹²⁰See Julie A Maupin, ‘Public and Private in International Investment Law: An Integrated Systems Approach’ (2013-2014) 54 Va J Intl L 367, 424 arguing that moderating the amount of damages payable in appropriate circumstances could well lead to a decrease in the percentage of annulment and set-aside requests lodged by states under the applicable enforcement conventions, an

when balancing of interests at the remedies stage is appropriate, it must be kept in mind that there is a danger that, if host states are granted a ‘second bite of the cherry’ at the remedies stage, the importance of vindicating investor rights could be undermined and the granting of inappropriately narrow remedies could result in rights dilution.¹²¹ In addition, there is a danger that reopening the case to determine whether the facts justify reducing the quantum of damages in light of important host state interests could result in a difficult, long and expensive procedure, which, in turn, impacts on host state resources that might otherwise be available to fulfil important social functions.¹²²

It is submitted, however, that these dangers are more likely to manifest themselves in circumstances where interests that are considered insufficient to override investor rights at the merits stage are considered *de novo* at the remedies stage. This contrasts with an approach whereby only those interests that are not capable of being considered (or considered sufficiently) at the merits stage in defining the scope of the right in question are considered at the remedies stage. Thus, under the latter approach, the extent to which such interests were taken into account at the merits stage is assessed and the question of whether, in order to ensure an optimal balance between investor protection and host state regulatory sovereignty, such interests need to be taken into account at the remedies stage is thereby evaluated. While in practice there is unlikely to be a bright-line distinction between these two approaches, it is submitted that the latter approach is more appropriate to counter the potential danger of rights dilution and to ensure that the principal focus of the system on the protection of investor rights is maintained. Accordingly, this analysis focusses on identifying factors that are not capable of being considered sufficiently (or at all) at the merits stage and in identifying why the remedies stage is an appropriate alternative forum for such considerations.

Thus, perhaps the principal reason why public interest considerations may need to be taken into account at the remedies stage is in circumstances where the host state was acting in furtherance of a *bona fide* public purpose in introducing the impugned measure and this is not capable of being taken into account sufficiently at the merits

improvement in pay-out rates on arbitral awards and potentially a reduction in civil society opposition to the international investment regime.

¹²¹Paul Gewirtz, ‘Remedies and Resistance’ (1982-1983) 92 Yale L J 585.

¹²²Ioana Knoll-Tudor, ‘The Fair and Equitable Treatment Standard and Human Rights Norms’ in Pierre-Marie Dupuy, Ernst-Ulrich Petersmann and Francesco Francioni (eds), *Human Rights in International Investment Law and Arbitration* (OUP 2009) 344.

stage. One situation in which this circumstance arises is where a direct treaty conflict occurs (i.e. where a host state can either only comply with its obligations under another non-investment related treaty (such as a human rights treaty) by failing to comply with an IIA (or *vice versa*) or where the goals of one of these treaties frustrates the goals of another treaty without strict incompatibility between their provisions).¹²³ In such a situation, the fact that the host state had an obligation to, for example, regulate to protect certain human rights and that the impugned measures were implemented to achieve such public purpose should first be considered at the merits stage of the arbitral process in assessing the circumstances surrounding the host state measures and in determining the extent to which the investor's expectations can be considered legitimate. Thus, as noted by the tribunal in *Suez and Vivendi v Argentina*:

in interpreting the meaning of fair and equitable treatment to be accorded to investors, the Tribunal must balance the legitimate and reasonable expectations of the Claimants with Argentina's right to regulate the provision of a vital public service.¹²⁴

However, as was noted in Chapter 3, a direct treaty conflict is fundamentally not capable of being resolved at the merits stage as the fact that there is a direct collision of obligations leads to application of proportionality analysis or of interpretative techniques such as systemic integration being of no avail.¹²⁵ Thus, for example, a direct treaty conflict could occur where a host state is simultaneously confronted with the duty to comply with its minimum core obligations under the ICESCR as well as the duty to compensate investors for breaches of substantive IIA rights.¹²⁶ For example, the ICESCR requires states to ensure access to water to the population (including physical and economic access) and has described the right to water as falling 'within the category of guarantees essential for securing an

¹²³International Law Commission, *Fragmentation of International Law: Difficulties Arising from the Diversification and Expansion of International Law*, UN Doc A/CN.4/L.682 (13 April 2006) (finalised by Martti Koskenniemi) para 24.

¹²⁴ICSID Case No ARB/03/19, Decision on Liability 30 July 2010, para 236.

¹²⁵Jan Klabbbers, 'Beyond the Vienna Convention: Conflicting Treaty Provisions' in Enzo Cannizzaro (ed), *The Law of Treaties Beyond the Vienna Convention* (OUP 2011). See also Marko Milanović, 'Norm conflict in international law: whither human rights?' (2009) 20 *Duke J Comp & Intl L* 69, 74-75.

¹²⁶Diane Desierto, 'Human Rights and Investment in Economic Emergencies: Conflict of Treaties, Interpretation, Valuation Decisions', Society of International Economic Law (SIEL), 3rd Biennial Global Conference, SIEL Working Paper No 2012/47, 20-21.

adequate standard of living'.¹²⁷ Accordingly, state parties to the ICESCR are obliged, even in circumstances of economic crisis, to ensure the satisfaction of, at the very least, minimum essential levels of each of the ICESCR rights and to demonstrate that every effort has been made to use all resources that are at its disposition in an effort to satisfy those minimum obligations as a matter of priority.¹²⁸ The liberalisation and privatisation of essential services in various sectors such as the provision of drinking water, electricity and other essential public services¹²⁹ increases the likelihood of regulation of this nature conflicting with investor rights under IIAs.¹³⁰

Thus, for example, in an economic crisis, modification of the regulatory regime governing privatised companies involved in water distribution and sanitation may be necessary in order to ensure that water is affordable to the beleaguered host state population. However, such modification may result in the investor's expectations as to its revenues not being met in circumstances where it was previously guaranteed that tariffs of a certain level could be charged by that investor.¹³¹ In such a situation, it could be argued that the host state in question ceded a certain degree of regulatory freedom in entering into the IIA and had a duty to conduct a due diligence exercise to ascertain whether any conflict arises between its obligations under the IIA and its other non-investment related domestic and international obligations.¹³² This would

¹²⁷United Nations Committee on Economic, Social and Cultural Rights, *General Comment 15, The right to water* (Twenty-ninth session, 2003), UN Doc E/C.12/2002/11 (2002), para 3.

¹²⁸United Nations Committee on Economic, Social and Cultural Rights, *General Comment 3, The nature of States parties' obligations* (Fifth session, 1990), UN Doc E/1991/23 (1990), paras 10-12. Guidance has also been given as to the type of measures that would be acceptable to implement the ICESCR during economic crises: see Ariranga G Pillay (Chairperson, United Nations Committee on Economic, Social and Cultural Rights), 'Letter to all States Parties to the International Covenant on Economic, Social and Cultural Rights dated 16 May 2012' <<http://www2.ohchr.org/english/bodies/cescr/docs/LetterCESCRtoSP16.05.12.pdf>> accessed 19 March 2015.

¹²⁹An essential public service can be defined as one that is burdened with carrying out an activity necessary for the furtherance of a 'public interest' or for pursuing public policy objectives: see Antenor Hallo de Wolf, 'Human Rights and the Regulation of Privatised Essential Services' (2013) 60 *Netherlands Intl L Rev* 165, 172.

¹³⁰This has been referred to as the 'privatisation paradox' (ie the fact that privatisation does not necessarily lead to a smaller role for the state, albeit that it does lead to a shift in the activities and role from producer or provider to regulator): J Freeman, 'Extending Public Law Norms Through Privatization' (2003) 116 *Harv L Rev* 1285.

¹³¹See for example *Suez, Sociedad General de Aguas de Barcelona S.A. and Vivendi Universal v Argentina*, ICSID Case No ARB/03/19, Decision on Liability 30 July 2010.

¹³²Indeed, the ICESCR requires that, in relation to the conclusion of other international agreements, state parties should take steps to ensure that these instruments do not adversely impact upon ICESCR rights, including the right to health and the right to water: see United Nations Committee on Economic, Social and Cultural Rights, *General Comment 14, The right to the highest attainable standard of health* (Twenty-second session, 2000), UN Doc E/C.12/2000/4 (2000), para 39; United

lead to the conclusion that the fact that a measure was taken in order to comply with a non-investment related treaty obligation (namely the right to water) cannot affect the damages payable.¹³³ However, there are several reasons why this is too stark a conclusion to draw.

First, while in ‘normal times’ it may be expected that the host state should be able to reconcile all of its obligations throughout its engagement with a given investor, in times of economic and political turmoil, limited public budgets and highly volatile economic environments may necessitate steering and committing resources in different directions and, in such circumstances, reconciliation of competing obligations may no longer be possible.¹³⁴ Secondly, it should be borne in mind that investors are under a parallel obligation to take due notice of the host state’s social, economic and political circumstances (and arguably of its human rights obligations) and to conduct a risk assessment in this regard.¹³⁵ Thirdly, unlike under the WTO regime,¹³⁶ the standards of behaviour required of a particular state under IIAs generally do not allow for differentiated or specially tailored obligations for the lesser developed of the state parties to a treaty.¹³⁷ The lack of differentiated obligations means that in circumstances where a developing host state acts to protect ICESCR or other human rights, it may not be given any lenience in terms of the scope of its liability under the relevant IIA. Indeed, such states can be considered more likely to be confronted with such situations due to both the difficulty posed by compliance with the obligation to ensure the satisfaction of minimum essential levels of ICESCR rights¹³⁸ and because such states are likely to

Nations Committee on Economic, Social and Cultural Rights, ‘General Comment No 15, The right to water’ (Twenty-ninth session, 2003), UN Doc E/C.12/2002/11 (2002), para 35.

¹³³*Suez, Sociedad General de Aguas de Barcelona S.A. and Vivendi Universal v Argentina*, ICSID Case No ARB/03/19, Decision on Liability 30 July 2010, para 262.

¹³⁴Jorge Daniel Taillant and Jonathan Bonnitcha, ‘International Investment Law and Human Rights’ in Marie-Claire Cordonier Segger, Markus W Gehring and Andrew Newcombe (eds), *Sustainable Development in World Investment Law* (Kluwer Law International 2011) 60-61.

¹³⁵*ibid.* See also Thomas Wälde and Borzu Sabahi, ‘Compensation, Damages and Valuation in International Investment Law’ in Peter Muchlinski, Federico Ortino and Christoph Schreuer (eds), *The Oxford Handbook of International Investment Law* (OUP 2008) 1062; International Council on Mining and Metals, *Integrating Human Rights Due Diligence into Corporate Risk Management Processes* (2012).

¹³⁶UNCTAD, *International Investment Agreements: Flexibility for Development: UNCTAD Series on Issues in International Investment Agreements* (UNCTAD 2000) 36.

¹³⁷See however ASEAN Comprehensive Investment Agreement, signed 26 February 2009, entered into force 29 March 2012, art 23; Investment Agreement for COMESA Common Investment Area, signed 23 May 2007, art 14(3).

¹³⁸Matthew Craven, *The International Covenant on Economic, Social and Cultural Rights: A Perspective on its Development* (OUP 1995) 152. See also Noel G Villaroman, ‘The Need for Debt

lack the administrative and institutional capacity to adopt the regulatory models required to develop a framework for dealing with such conflicts of obligations.¹³⁹ Finally, imposing full liability on the host state when a clash between treaty obligations occurs would seem inequitable given that states cannot avoid such obligations as corporations have the potential to do by, for example, changing the location and organisation of assets. In this regard, Professor Brownlie's comments in his Separate Opinion in *CME v Czech Republic* are apposite:

The resources of a corporation entail considerable flexibility in changing the location of assets and in changing the organization of assets. The resources of a country, its human and natural resources, are a given: they are necessarily fixed.¹⁴⁰

Thus, where a direct treaty conflict occurs, taking account of the purpose underlying the impugned host state measures at the remedies stage would introduce a necessary element of differentiation and of reciprocity in that it would recognise the host state's attempt to observe its non-investment related international obligations as well as taking into account, to some extent, the capacity of, and obligation on, potential investors to conduct due diligence in respect of the host state's social, economic and political circumstances.

Similar arguments can be made in favour of reducing the damages payable where the impugned host state measures were introduced in furtherance of the fundamental rights provisions contained in the host state's highest law (such as its constitution).¹⁴¹ While, from the point of view of international law, a direct conflict between obligations would not exist in such circumstances,¹⁴² to disregard entirely

Relief: How Debt Servicing Leads to Violations of State Obligations under ICESCR' (2010) 9 J of Human Rights 487.

¹³⁹C Kirkpatrick and D Parker, 'Regulation and the Privatisation of Water Services in Developing Countries: Assessing the Impact of the General Agreement on Trade in Services (GATS)', Paper No 67, Centre on Regulation and Competition, Institute for Development Policy and Management, University of Manchester (2004).

¹⁴⁰*CME v Czech Republic*, UNCITRAL, Separate Opinion on the Issues at the Quantum Phase by Ian Brownlie, 13 March 2003, para 76. See also *Glamis Gold, Ltd. v United States of America*, UNCITRAL, Award 8 June 2009, para 8.

¹⁴¹Julie A Maupin, 'Public and Private in International Investment Law: An Integrated Systems Approach' (2013-2014) 54 Va J Intl L 367, 423 proposing a provision that, where a state's IIA obligations potentially conflict with its other treaty obligations and/or the fundamental rights provisions contained in the state's highest law, the tribunal 'must calculate the amount of compensation due to claimant(s) ...in such a manner as to avoid making it infeasible, either in law or in fact, for the host State to simultaneously satisfy its obligations to the claimant under this treaty and its concomitant obligations to other persons'.

¹⁴²See Vienna Convention on the Law of Treaties, art 27. See also Malcolm N Shaw, *International Law* (6th edn, Cambridge University Press 2008) 133-37.

the purpose for which the measure was introduced would, it is submitted, not lead to an optimal balance between investor protection and host state regulatory sovereignty and, given the importance of those norms within the host state's domestic legal framework, would fail to introduce a necessary element of reciprocity into the investment treaty arbitration process.

A second, somewhat related, situation in which public interest considerations may need to be recognised at the remedies stage is in circumstances where the customary international law defence of necessity is successfully invoked by the host state. Although, as demonstrated in Chapter 3, the defence of necessity has been (and will always have to be) quite narrowly drawn, it is submitted that, where a host state fulfils the requirements of the defence, this should be regarded as an extenuating circumstance.¹⁴³ This should be the case as, while to require the host state to provide full reparation to the investor would deprive the defence of its *raison d'être* (at least in the investment treaty arbitration context),¹⁴⁴ invocation of the defence nonetheless implies an intentional failure to conform to the state's obligations to foreign investors and an awareness of having deliberately chosen to act contrary to such obligations. Thus, two competing imperatives exist: on the one hand, the need to introduce an element of reciprocity by recognising that reconciliation of competing obligations or interests may not be possible in circumstances of economic and political turmoil and that the host state acted to safeguard its essential interests (while also satisfying the other stringent conditions required to successfully invoke the defence) and, on the other, the fact that IIAs exist precisely to protect foreign investors in such difficult situations and, therefore, that the defence of necessity cannot act as an 'escape route' for the host state from its IIA obligations.¹⁴⁵ These competing imperatives cannot meaningfully be reconciled at the merits stage given the black-or-white decision as to liability required. Thus, it is submitted that these factors should be taken into account at the

¹⁴³United Nations, *Third Report on International Responsibility by F V Garcia-Amador, Special Rapporteur*, UN Doc A/CN.4/111 (1958), arts 13-14 and associated commentary.

¹⁴⁴The dynamics underlying investor-state disputes are different to those underlying inter-state disputes so this conclusion may not necessarily apply to the latter: see Dinah Shelton, *Remedies in International Human Rights Law* (2nd edn, OUP 2005) 2.

¹⁴⁵See *Enron Corporation and Ponderosa Assets, LP v Argentina*, ICSID Case No ARB/01/3, Award 22 May 2007, para 331.

remedies stage in determining the quantum of damages payable to the claimant investor.¹⁴⁶

Thirdly and finally, it is submitted that the question of whether the host state acted in furtherance of a *bona fide* public purpose in introducing the impugned measure should also be considered at the remedies stage in the case of breaches of a procedural nature (i.e. where the wrongful act relates to the procedure applied by the host state authorities or the manner in which a particular measure is introduced by the host state). In such circumstances, the host state may be held liable to compensate the claimant investor for all of the loss that the claimant investor has suffered, even where it is likely or even highly probable that the substantive outcome of the host state measures would have been the same in the absence of the procedural breach (i.e. had the host state acted lawfully in terms of public international law).¹⁴⁷ Procedural breaches are treated in this manner as, although it would seem difficult to establish a causal link between the procedural breach and the loss suffered by the claimant investor in such circumstances, it is regarded as important as a matter of policy to afford reparation in respect of such breaches, even where there is a risk that this may potentially lead to an award of damages which exceeds the loss actually caused by the wrongful act.¹⁴⁸ Thus, one such policy justification for awarding damages in such circumstances may be the desire to maximise the welfare of foreign investors, on the assumption that such is in the interests of the wider public. Perhaps more importantly however, procedural guarantees are seen as being valuable in and of themselves for a number of inter-related reasons. First, procedural guarantees are regarded as central in ensuring that

¹⁴⁶Albeit that the end result may be similar, such an adjustment can be distinguished conceptually from adjustments made to avoid over-compensating the investor given the likelihood that significant damages would have been incurred by the investor in the absence of the breach, in light of the circumstances of crisis prevailing in the host state: see Sergey Ripinsky, 'State of Necessity: Effect on Compensation' (2007) 4 *Transnational Dispute Management*, 16; José E Álvarez and Kathryn Khamsi, 'The Argentine Crisis and Foreign Investors: a Glimpse into the heart of the Investment Regime' in Karl P Sauvant (ed), *The Yearbook of International Investment Law and Policy 2008-2009* (OUP 2009) 407; Kathryn Khamsi, 'Compensation for Non-Expropriatory Investment Treaty Breaches' in Michael Waibel and others (eds), *The Backlash Against Investment Arbitration: Perceptions and Reality* (Kluwer 2010) 174. See also *CMS v Argentina*, ICSID Case No ARB/01/8, Award 12 May 2005, para 356.

¹⁴⁷See *Amco Asia Corporation and others v Republic of Indonesia (II)*, ICSID Case No ARB/81/1, Resubmitted Case Award 5 June 1990 and Decision on Supplemental Decisions and Rectification 17 October 1990, 1 ICSID Rep 569. See also Sergey Ripinsky with Kevin Williams, *Damages in International Investment Law* (British Institute of International and Comparative Law 2008) 118.

¹⁴⁸Zachary Douglas, *The International Law of Investment Claims* (Cambridge University Press 2009) 102-03.

the rule of law is upheld (i.e. they help to ensure that, regardless of what the substantive content of the law actually is, the law is open, clear, stable, general and applied by an impartial judiciary so that an individual can plan ahead and foresee with some degree of certainty the consequences of his or her actions).¹⁴⁹ Secondly, procedural guarantees assist in protecting individual rights and interests against undue encroachment in the name of public or societal interests and, where such individual rights have to be sacrificed in favour of public interests, in making that sacrifice acceptable.¹⁵⁰ Finally, the existence of certain procedural guarantees can be said to confer greater assurance that a substantive decision reached in compliance with those guarantees is just.¹⁵¹

Crucially however, it is submitted that these justifications do not apply to the same extent in respect of all procedural breaches.¹⁵² Thus, at the one hand, if a denial of justice has been deemed to occur due to the extent and nature of the procedural irregularities at issue, a strong rationale exists for requiring the host state to compensate the claimant investor for the full extent of losses suffered by that investor in order to ensure that the rule of law is upheld in the host state and given that, where such serious procedural irregularities are at issue, there can be assumed to be a higher likelihood that the substantive decision reached by the host state authorities is also unjust. On the other hand however, where the procedural irregularities at issue do not meet the high threshold of denial of justice, these rule of law-based justifications for awarding damages in respect of procedural breaches do not apply to the same extent and, accordingly, the rationale for compensating the investor for all of its losses is not as compelling. Furthermore, compensating the investor for all of its losses in such circumstances may not lead to an optimal balance between investor protection and host state regulatory sovereignty, where the host state acted in furtherance of a *bona fide* public purpose and where the same (or substantial) losses would likely to have been incurred by the claimant investor in any event had the state organ in question acted lawfully. It is therefore submitted

¹⁴⁹This conception of the rule of law constitutes a formal conception – it is also possible to conceive of the rule of law from a substantive perspective: see Paul P Craig, ‘Formal and substantive conceptions of the rule of law: an analytical framework’ (1997) PL 467.

¹⁵⁰Søren Schönberg, *Legitimate Expectations in Administrative Law* (OUP 2000) 31. See also Jerry L Mashaw, *Greed, Chaos and Governance: Using Public Choice to Improve Public Law* (Yale University Press 1997) 52.

¹⁵¹*ibid.*

¹⁵²*ibid.*, 17.

that, in respect of procedural breaches, a balancing of interests should occur at the remedies stage which would consider, in quantifying the damages payable, not only the loss suffered by the claimant investor but also the nature and intensity of the procedural breach and the public purpose being pursued (which would include consideration of whether the substantive outcome would likely have been the same in the absence of the breach). It is submitted that this ‘sliding scale’ approach would allow for the policy-based justifications for awarding damages for procedural breaches to be upheld while also accommodating the public purpose underlying the host state actions and potentially the development status of the host state.

Indeed, it is submitted that this approach could prove to be particularly suitable in addressing a breach of a claimant investor’s legitimate expectations. In this regard, four situations in which legitimate expectations are liable to be disappointed by administrative decision-making have been identified by Schønberg: the first situation arises when a public authority makes a formal decision about a person, or a limited group, which it subsequently seeks to revoke; the second situation arises when a public authority explicitly or implicitly represents that it will follow a certain procedure or policy in relation to a specific individual or group and subsequently makes a decision which differs from the representation; the third situation arises when a public authority makes a general representation about the procedure or policy it will follow in relation to certain types of decisions, but subsequently departs from the procedure or policy in the particular case and the fourth situation arise when the authority departs from its general representation in the light of a shift in general procedure or policy which has occurred between the initial representation and the decision.¹⁵³ It is clear from this classification that the concept of legitimate expectations potentially covers a broad range of host state conduct and that the rule of law-based justifications for protecting legitimate expectations are stronger in certain circumstances than in others. Thus, Schønberg notes that the rule of law-based justification for protecting legitimate expectations would appear stronger in respect of the first and third situations identified above than it is in the second and fourth situations.¹⁵⁴ Accordingly, while the protection to be afforded to investor expectations should, in certain circumstances, be considered

¹⁵³Søren Schønberg, *Legitimate Expectations in Administrative Law* (OUP 2000) 8ff. These situations were identified by reference to domestic administrative law but can be considered equally relevant to international investment law.

¹⁵⁴*ibid.*

akin to that afforded in respect of legally enforceable rights, in others, the rationale for protecting investor expectations is less compelling and must be balanced against other important considerations (such as the right of the host state to regulate in the public interest). In recognition of this, it has been suggested that the damages payable to claimant investors for frustration of their (legitimate) expectations should be limited in some manner.¹⁵⁵ One suggestion in this regard is that only the ‘negative interest’ (i.e. the expenditure the investor has undertaken in reliance on the reliability of the government position communicated) should be awarded where legitimate expectations are breached.¹⁵⁶ However, given the broad range of conduct covered by the concept, it is submitted that this distinction would not always give adequate expression to a fair balance between compensating for harm caused to an individual and the public interest.¹⁵⁷ Therefore, rather than applying this proposition rigidly, it is submitted that a ‘sliding scale’ approach which would consider the nature of the interest or expectation being protected, the degree of interference with such interest or expectation and the legitimacy (or otherwise) of the interests underlying the host state’s conduct (including the likelihood that the substantive outcome would have been the same in the absence of the breach) is more appropriate.¹⁵⁸

To give an example, consider a situation in which a statutory body tasked with protecting the environment and monitoring compliance with environmental regulations imposes certain restrictions on the operation of a chemical plant including a requirement to put in place a substantial ring-fenced fund in respect of decommissioning of the facility and reinstatement of the site and a requirement to monitor emissions from the plant to an extent which exceeds international best practice in that particular industry. These requirements lead to the stagnation of a previously expanding business and have led to payments under some of the investor’s loan facilities being accelerated due to breach of certain financial

¹⁵⁵*International Thunderbird Gaming Corp v United Mexican States*, UNCITRAL, Separate Opinion of Thomas Wälde December 2005, paras 119-21.

¹⁵⁶*ibid.* See also André Von Walter, ‘The Investor’s Expectations in International Investment Arbitration’ (2009) 6 *Transnational Dispute Management*; David Collins, ‘Reliance Remedies at the International Center for the Settlement of Investment Disputes’ (2009) 29 *Nw J Intl L & Business* 195.

¹⁵⁷Søren Schønberg, *Legitimate Expectations in Administrative Law* (OUP 2000) 10ff.

¹⁵⁸For a comparable argument see Hector A Mairal, ‘Legitimate Expectations and Informal Administrative Representations’ in Stephan W Schill (ed), *International Investment Law and Comparative Public Law* (OUP 2010) 448.

covenants in those facilities. The regulatory requirements introduced by the host state run contrary to undertakings given by a number of government officials (of varying levels of specificity and formality) and statements in the publicly available literature circulated by the statutory body in question to the effect that the government would follow international best practice in regulating the industry in question and contrary also to a requirement under the relevant regulatory regime to notify and consult with affected persons prior to introducing such requirements. However, in requiring the claimant investor to take these measures, the statutory body in question was motivated (at least in part) by a desire to protect the environment and public health, as the measures were introduced after a preliminary soil and water study (commissioned following reports of unexplained illness in humans and animals in the area) identified the presence of contaminants in the area surrounding the facility.¹⁵⁹ In this case, although there is little consensus as to the point at which government representations become so significant that a failure to honour them amounts to a violation of that obligation and it is questionable whether government representations of themselves should amount to an IIA breach,¹⁶⁰ combined with the failure to consult as required under the relevant regulatory regime, a tribunal could reasonably determine that the FET standard was breached on the basis of frustration of the claimant investor's legitimate expectations.¹⁶¹ However, this determination, of itself, would not pay due regard to the host state's duty to regulate to protect the public welfare, given the nature of the procedural breaches at issue and given the likelihood that substantial losses would in any event have been incurred by the claimant investor had the host state acted in conformity with the law. Thus, it is submitted that a 'sliding scale' approach, which would

¹⁵⁹The state's actions could therefore potentially be said to be in accordance with the 'precautionary principle'. This principle arguably forms part of customary international law and is enshrined in domestic legislation in many countries: European Commission, *Communication from the Commission on the precautionary principle*, COM/2000/0001 final. See also *Case concerning Pulp Mills on the River Uruguay (Argentina v Uruguay)*, Judgment 20 April 2010 (2010) ICJ Rep 14. On the evidential difficulties associated with environment-related disputes in investment treaty arbitration generally see Jorge E Viñuales, 'Foreign Investment and the Environment in International Law: An Ambiguous Relationship', Centre for Environmental Law Studies, Graduate Institute Geneva, Research Paper No 2, 30-34.

¹⁶⁰See JH Dalhuisen and AT Guzman, 'Expropriatory and Non-Expropriatory Takings under International Investment Law' (2013) 10 *Transnational Dispute Management* 14. See also Paul P Craig, *Administrative Law* (2nd edn, Sweet & Maxwell 2008) Chapter 16 on the difficulties which arise where a representation is *ultra vires* the public body or the particular officer who made the representation.

¹⁶¹See *Middle East Cement Shipping and Handling Co. S.A. v. Egypt*, ICSID Case No ARB/99/6, Award 12 April 2002, para 143.

potentially permit a downward adjustment of the damages payable to the claimant investor, would be appropriate in such circumstances.¹⁶²

In summary therefore, having discussed, and gleaned guidance from, some general normative arguments as to why public interest considerations should be taken into account at the remedies stage of the arbitral process (including the need to introduce an element of reciprocity into the investment treaty arbitration process), a number of specific circumstances in which it may be appropriate to recognise public interest considerations at the remedies stage have been identified. These circumstances do not, it is submitted, constitute an exhaustive list of situations in which public interest considerations may fall to be considered at the remedies stage. However, they are all based on a common premise: namely that, in some cases, the fact that the host state acted in pursuance of a *bona fide* public purpose in introducing the measures challenged under an IIA may need to be considered at the remedies stage as, for a variety of reasons (some related to doctrine and some more to policy), this fact may not be capable of being considered sufficiently at the merits stage so as to ensure an optimal balance between investor protection and host state regulatory sovereignty.

4.3 The ‘special case’ of lawful expropriations

The analysis of the remedies stage as a platform for public interest considerations has thus far focussed on unlawful (primarily non-expropriatory) acts. This is reflective of the fact that the vast majority of investment treaty arbitrations to date have concerned unlawful acts.¹⁶³ Indeed, the expropriation clause can be considered as an outlier in the context of international investment law as a whole since, unlike the non-expropriatory standards typically contained in IIAs, the expropriation enquiry focusses primarily on the loss caused by government conduct rather than on the character of such conduct. This has the consequence that, even where an expropriation may have been undertaken for a public purpose, in accordance with

¹⁶²See Jorge E Viñuales, ‘Foreign Investment and the Environment in International Law: An Ambiguous Relationship’, Centre for Environmental Law Studies, Graduate Institute Geneva, Research Paper No 2, 70-71 noting that where an action falls within the police powers of the host state but where the host state has given specific assurances to the investor that an adverse regulation will not be adopted, the balancing of environmental and investment protection could be reflected in the quantum of damages payable.

¹⁶³Borzu Sabahi, *Compensation and Restitution in Investor-State Arbitration: Principles and Practice* (OUP 2011) 96.

due process and in a non-discriminatory manner, compensation is still payable. The tribunal in *Santa Elena v Costa Rica* put this in stark terms in stating that the fact that the property in question was taken for a legitimate public purpose such as the protection of the environment did not alter the level of compensation to be paid nor did the international source of the obligation to protect the environment make any difference to the level of compensation payable.¹⁶⁴ However, although the focus and structure of the expropriation enquiry differs from that in respect of other IIA rights, the need to introduce an element of reciprocity and to recognise public interest considerations at the remedies stage still applies. Indeed, the need to acknowledge host state regulatory sovereignty at the remedies stage is amplified where lawful expropriations are concerned as, currently, the pronouncement that an expropriation is lawful does not have any meaningful consequence.¹⁶⁵ Thus, in many cases, the quantum of compensation may *de facto* equate to that payable in respect of an unlawful expropriation, particularly where (as is often the case) the lost future profits that the enterprise would have earned are used in estimating the fair market value of an expropriated asset.¹⁶⁶ This effectively means that due regard is not paid to the public function that the state is performing and that the elements of public purpose, non-discrimination and due process are relevant to a deprivation only insofar as their absence may add ‘an additional sense of grievance in cases where the host state has, in the first instance, failed to pay the investor “prompt, adequate, and effective compensation”’.¹⁶⁷ Furthermore, where the expropriation in question is indirect in nature, the rationale for affording recognition to public interest considerations in quantifying the compensation payable can be said to be more compelling as, while awarding fair market value in respect of a direct expropriation of property can be said to encourage efficient government and investor decisions by forcing governments to consider the costs that the measure could impose on individuals and factoring those costs into its overall cost-benefit

¹⁶⁴ICSID Case No ARB/96/1, Award 17 February 2000, paras 71-72.

¹⁶⁵Ursula Kriebaum, ‘Regulatory Takings: Balancing the Interests of the Investor and the State’ (2007) 8 J World Investment & Trade 717.

¹⁶⁶UNCTAD, *Expropriation: UNCTAD Series on Issues in International Investment Agreements II* (UNCTAD 2012) 114.

¹⁶⁷Patrick M Norton, ‘Back to the Future: Expropriation and the Energy Charter Treaty’ in Thomas Wälde (ed), *The Energy Charter Treaty: An East-West Gateway for Investment and Trade* (Kluwer 1996) 374. While this statement is true where an expropriation has been deemed to have occurred, these elements may, in certain cases, prevent a deprivation from being categorised as an expropriation in the first place pursuant to the ‘police powers’ doctrine, where pre-eminent public interests are invoked.

analysis of the measure,¹⁶⁸ it is difficult to assess the extent (if any) to which such efficiency-based arguments apply to general regulatory measures which may adversely affect an investor.¹⁶⁹ Thus, it is submitted that, from a normative perspective, there are strong grounds for taking into account public interest considerations in quantifying the compensation payable in respect of lawful expropriations (particularly those of a regulatory nature). Admittedly, the prescription of fair market value as the applicable standard of valuation in the majority of IIAs in respect of lawful expropriations may create some doctrinal difficulties in terms of applying such an approach, which will be considered in the following chapter. However, this should not detract from the normative arguments supporting such an approach.

4.4 Conclusion

To date, the question of whether public interest considerations should influence the assessment of damages in investment treaty arbitration has not been explored to any significant extent in arbitral practice. This chapter has argued that the remedies stage of the investment treaty arbitration process constitutes an appropriate platform for public interest considerations, given the need to introduce an element of reciprocity into the process while simultaneously giving due recognition to the primary focus of the system on investment protection. Accordingly, affording recognition to public interest considerations at the remedies stage would allow for a more nuanced reflection of such considerations than the ‘all or nothing’ decision as to liability required in determining whether an IIA breach has occurred or not. That is not to say however that public interest considerations can be disregarded at the merits stage: rather the remedies stage should play a complementary role to the merits stage in taking account of public interest considerations and only those interests that are not capable of being considered (or considered sufficiently) at the

¹⁶⁸Frank Michelman, ‘Property, Utility and Fairness: Comments on the Ethical Foundations of “Just” Compensation Law’ (1967) 80 Harv L Rev 1165; Lawrence E Blume and Daniel L Rubinfeld, ‘Compensation for takings: an economic analysis’ (1984) 72 California L Rev 569; Ed Nosal, ‘The Taking of Land: Market Value Compensation should be Paid’ (2001) 82 J Public Economics 431; Emma Aisbett, Larry Karp and Carol McAusland, ‘Police Powers, Regulatory Takings and the Efficient Compensation of Domestic and Foreign Investors’ (2010) 86 The Economic Record 367.

¹⁶⁹Jonathan Bonnitcha, ‘Outline of a normative framework for evaluating interpretations of investment treaty protections’ in Chester Brown and Kate Miles (eds), *Evolution in Investment Treaty Law and Arbitration* (Cambridge University Press 2011) 124.

merits stage in defining the scope of the right in question should be considered at the remedies stage.

However, while the normative arguments in favour of such an approach have been outlined and stand apart from the issue of the doctrinal basis for such an approach, the question of whether this approach can be implemented doctrinally is a question that is also important to consider and this will be the focus of the following chapter. In particular, the following chapter will consider whether there is a doctrinal basis for taking account of public interest considerations at the remedies stage under existing IIAs or whether treaty reform would be required in order to do so. The relationship between remedies-related reforms and proposed reforms affecting earlier stages of the arbitral process will also be considered.

Chapter 5: From policy to implementation: taking account of public interest considerations at the remedies stage

In fairness discourse, the most restrained justice-based claims may be advanced in the form of equity, which embodies a set of principles designed to analyse the law critically without seeming to depart too radically from the traditional preference for normativity in the exercise of authority, nor to present too bold a challenge to the community's expectations of legitimacy in legal rules and processes.¹

Having discussed in the preceding chapter a number of normative arguments why recognition of public interest considerations at the remedies stage of the arbitral process would be appropriate, this chapter will explore possible means by which such an approach may be implemented. Addressing this question is important for a number of reasons: first, there are significant practical difficulties associated with terminating or renegotiating IIAs (such as the costs associated with termination or renegotiation and the fact that IIAs generally maintain the state's obligations for an extended period for foreign investors whose investments existed at the time of termination)² and, secondly, the fact that, notwithstanding the existence of normative arguments that support the taking into account of public interest considerations at the remedies stage, practically speaking, such an approach is unlikely to gain traction if it requires a complete schism between the approach taken to quantifying damages in investment treaty arbitration and the requirements of the customary international law of state responsibility.

This issue will be considered in the context of both existing IIAs and new or renegotiated IIAs. In the context of existing IIAs, this gives rise to the question of whether any doctrinal basis exists for application of such an approach, which will be addressed in the first part of this chapter. The expropriation clause will, for this purpose, be considered separately from the other rights conferred on investors by IIAs. Following on from this, an evaluation of a number of possible provisions

¹Thomas M Franck, *Fairness in International Law and Institutions* (OUP 1998) 47.

²Julie A Maupin, 'Public and Private in International Investment Law: An Integrated Systems Approach' (2013-2014) 54 Va J Intl L 367, 434.

which could potentially be included in new or renegotiated IIAs and which broadly provide for some degree of balancing of investor and host state interests at the remedies stage will be conducted. Finally, this chapter will consider the relationship between the recognition of public interest considerations at the remedies stage and reforms that have been proposed as means of facilitating the consideration of certain public interests in investment treaty arbitration and which primarily affect the earlier stages of the arbitral process.

5.1 The doctrinal basis for taking account of public interest considerations under existing IIAs: the role of equity

Public interest considerations may only be taken into account in the context of existing IIAs to the extent that the means of introducing such considerations does not conflict with the valuation standards applied by tribunals under those IIAs (i.e. the customary international law principle of full reparation in respect of unlawful acts and (generally) the fair market value standard in the case of lawful expropriations).³ This restraint would, at first glance, seem to substantially narrow the possibilities for taking into account public interest considerations at the remedies stage. However, in analysing the extent to which public interest considerations can be taken into account under existing IIAs, it is worth noting that, as described in Chapter 4, investment treaty tribunals, of necessity, exercise a considerable degree of discretion in quantifying damages and, secondly, while this ‘normal’ exercise of discretion is separate to the application of equity,⁴ equity can also play a role in the damages quantification process, without the need for an explicit reference to equity or equitable principles in the relevant IIA.⁵

Indeed, given that equity has, in the domestic law context, been described as an ‘instrument for nice adjustment and reconciliation between the public interest and

³The customary international law principle of full reparation has been applied by tribunals as IIAs have, to date, generally not specified the valuation standard applicable to remedying IIA violations: one survey found that only 9% of the IIAs in the sample which had provisions dealing with investor-state dispute settlement included, in those provisions, some language on remedies and about 3% of the IIAs in the sample expressly mentioned pecuniary remedies: David Gaukrodger and Kathryn Gordon, *Investor-state dispute settlement: A scoping paper for the investment policy community*, OECD Working Papers on International Investment No 2012/3 (OECD 2012) 29.

⁴Irmgard Marboe, *Calculation of Compensation and Damages in International Investment Law* (OUP 2009) 145.

⁵See generally *North Sea Continental Shelf Cases (Federal Republic of Germany v Denmark; Federal Republic of Germany v Netherlands)*, Judgment 20 February 1969 (1969) ICJ Rep 3. See also Christian Tietje and Emily Sipiorski, ‘Offset of Benefits in Damages Calculation in International Investment Arbitration’ 29 *J Intl Arbitration* 545, 551.

private needs’,⁶ a question worth exploring is the extent to which equity and equitable principles have been applied by investment treaty arbitration tribunals to date and whether equity can provide a basis to take account of public interest considerations at the remedies stage under existing IIAs.⁷ Before considering this question however, an examination of the meaning of equity, including an analysis of the role of equity in international law, is required.

(a) *The meaning of equity*

The general concept of equity is one of some antiquity,⁸ featuring prominently in the writings of Greek and Roman philosophers.⁹ In particular, Aristotle described the universality and completeness of the law which necessarily includes broad concepts of justice and equity and, at the same time, recognised the need for systemic correction of shortcomings in the law due, in effect, to that very generality or universality. He thus described the function of equity as the corrective of law in special cases:

When...the law lays down a general rule, but a particular case occurs which is an exception to this rule, it is right...to make good this deficiency, just as the lawgiver himself would do if he were present, and as he would have provided in the law itself if the case had occurred to him...And the essence of what is equitable is that it is an amendment of the law, in those points where it fails through the generality of its language.¹⁰

This conception of equity influenced Roman law (at least from the time of establishment of the Roman Republic).¹¹ Thus, Justinian’s Digest (which, as part of

⁶*Lemon v Kurtzman* (1972) 411 US 192, 200-201 (quoting *Hecht Co. v Bowles* (1944) 321 US 321, 329-330).

⁷See Sonja Starr, ‘Rethinking “Effective Remedies”: Remedial Deterrence in International Courts’, University of Maryland School of Law, Legal Studies Research Paper, No 2008-33, 73 noting, in a different context, that international courts could potentially find doctrinal support for a balancing of interests at the remedies stage in the tradition of equity.

⁸See generally Howard L Oleck, ‘Historical Nature of Equity Jurisprudence’ (1951) 20 *Fordham L Rev* 23.

⁹*ibid*. See also Mauro Bussani and Francesca Fiorentini, ‘The Many Faces of Equity: A Comparative Survey of the European Civil Law Tradition’ in Daniela Carpi (ed), *The Concept of Equity: An Interdisciplinary Assessment* (Winter Verlag 2007).

¹⁰*The Nicomachean Ethics of Aristotle* (F Peters, tr Kegan Paul, Trench 1893) Book V, Chapter X, 175–76.

¹¹Hessel E Yntema, ‘Equity in the Civil Law and the Common Law’ (1966-1967) 15 *Am J Comp L* 60, 66-73 noting however that, while it is clear that, through the schools of rhetoric, the teachings of Greek philosophy had been imported into aristocratic circles in Rome at least before the last century of the Republic, the nature and extent of the influence of the concept of equity as formulated by

Justinian's *Corpus Iuris Civilis*, forms the bedrock of today's Continental legal systems as well as the indirect basis of much common law) begins with Celsus' statement that *ius est ars boni et aequi* (law is the art of the good and the equitable).¹² Concepts analogous to equity can also be found in ancient Chinese law, in Hindu philosophy and in the teachings of some Islamic schools.¹³ Throughout history therefore, there has been widespread recognition of the need to correct or supplement the law in certain circumstances in order to attain justice. Inevitably however, ideas of equity vary according to the interests and culture of different societies and states.¹⁴ In particular, the manner in which the concept of equity manifests itself in common law systems differs from its manifestation in civil law systems. Fundamentally however, although common law and civil law systems differ in terms of their organisation and the techniques used by each system to apply the concept of equity, 'below the surface the two systems are nourished by the same sources and ideals'.¹⁵ Despite this shared foundation however, the dichotomy between the common law and civil law traditions has had a significant influence on the manner in which equity has been accepted into international law and so merits further examination.¹⁶

Turning first to the common law systems, within such systems, it is possible to identify a law of equity and (at least historically) separate courts of equity through which that law was administered. Thus, from approximately the mid fourteenth century onwards in England, extraordinary justice remedying the defects of the common law on grounds of conscience and natural justice was administered through a separate court to the common law courts (the Court of Chancery) and Courts of Chancery subsequently became a feature of other common law systems.¹⁷ While this separation of common law and equitable jurisdictions is, at times,

Greek philosophy upon the Roman legal system is controversial. See also Howard L Oleck, 'Historical Nature of Equity Jurisprudence' (1951) 20 Fordham L Rev 23, 27-29.

¹²James Edelman, 'Equity', University of Oxford Legal Research Paper Series Paper No 69/2010, October 2010, 2.

¹³Margaret White, 'Equity – A General Principle of Law Recognised by Civilised Nations?' (2004) 4 Queensland University of Technology L J 103, 104.

¹⁴*ibid*, 103.

¹⁵G M Razi, 'Reflections on Equity in the Civil Law Systems' (1963) 13 Am University L Rev 24, 44.

¹⁶See Christopher R Rossi, *Equity and International Law: A Legal Realist Approach to International Decisionmaking* (Transnational Publishers 1993) 21-22 noting the importance of understanding how equity has been applied municipally in order to understand the influences contributing to the formation of the concept of equity in international law.

¹⁷Howard L Oleck, 'The Historical Nature of Equity Jurisprudence' (1951) 20 Fordham L Rev 23, 24-26.

conceptualised as a unique feature of the common law tradition (and is often used in the common law tradition to delineate what is meant by equity),¹⁸ such a separation of equity from law is not in fact unique to the common law and was, for example, also a feature of Roman law up to the second century AD.¹⁹ Initially the Court of Chancery operated according to the dictates of ‘conscience’, a notion which was influenced by the Church’s moral teaching.²⁰ Over time however (and as common lawyers rather than ecclesiastics began to be appointed as Chancellors),²¹ although the Court of Chancery remained a ‘court of conscience’, a system of precedent began to develop and the Court of Chancery began to grant relief on the basis of certain identifiable principles, which operated as ‘glosses on the common law’.²² This ‘systemisation’ of the law of equity arose in recognition of the need to ensure a degree of certainty and consistency in the law so as to ensure the fair administration of justice and to protect against arbitrary and capricious decisions.²³ Thus, as the law of equity developed within the Courts of Chancery:

Equity [became] less a principle or a set of principles which assisted, or supplemented, or even set aside the law in order that justice might be done in individual cases, and more a settled system of rules which supplemented the law in certain cases and in certain defined ways.²⁴

Despite this ‘systemisation’ of equity however, fundamentally the concept of equity remains flexible enough to have the capacity to correct or supplement the common

¹⁸See for example Hilary Delany, *Equity and the Law and Trusts in Ireland* (4th edn, Round Hall Publishing 2007) 1 describing equity as ‘the branch of the law administered by the Court of Chancery prior to the enactment of the Judicature (Ireland) Act 1877’.

¹⁹Ralph A Newman, ‘Equity in Comparative Law’ (1968) 17 Int'l & Comp L Q 807, 809. See also Mauro Bussani and Francesca Fiorentini, ‘The Many Faces of Equity: A Comparative Survey of the European Civil Law Tradition’ in Daniela Carpi (ed), *The Concept of Equity: An Interdisciplinary Assessment* (Winter Verlag 2007) 106-107 describing the role of the Praetor as a source of equity.

²⁰Joseph Charles Campbell, ‘The Development of Principles in Equity in the Seventeenth Century: An Introduction for Non-Lawyers’ (31 March 2015) Sydney Law School Research Paper No 15/25.

²¹Hilary Delany, *Equity and the Law and Trusts in Ireland* (4th edn, Round Hall Publishing 2007) 5.

²²Hessel E Yntema, ‘Equity in the Civil Law and the Common Law’ (1966-1967) 15 Am J Comp L 60, 84.

²³See for example Sir John Selden’s often-cited criticism of the Chancery: ‘Equity is a roguish thing: for law we have a measure, [and] know what to trust to. Equity is according to the conscience of him that is Chancellor; and as that is larger, or narrower, so is Equity. 'Tis all one, as if they should make the standard for the measure we call a Foot, the Chancellor’s foot. What an uncertain measure would this be? One Chancellor has a long foot; another a short foot; a third an indifferent foot. 'Tis the same thing in the Chancellor’s conscience’: see John Selden, *The Table Talk of John Selden* (Federick Pollock ed, 1927) 43.

²⁴William Holdsworth, *A History of English Law Vol V* (3rd edn, Methuen & Co London 1945) 217-18. See also Hilary Delany, *Equity and the Law and Trusts in Ireland* (4th edn, Round Hall Publishing 2007) 5 noting that much of the ‘systemisation’ of the principles of equity took place from the time of the chancellorship of Lord Nottingham (1673-1682) until the time of Lord Eldon (1801-1806 and 1807-1827).

law in a particular case and there is potential for the scope of equitable doctrines to be extended if the justice of a particular case so requires (albeit that the judicial willingness to do so may vary).²⁵ However, although, in most common law jurisdictions,²⁶ the courts of law and courts of equity have now ‘fused’ such that responsibility for the administration of both law and equity is now vested in one court,²⁷ the intrinsic difference between legal and equitable rights and remedies remains unaffected.²⁸ Thus, as noted by Ashburner, ‘the two streams of jurisdiction, though they run in the same channel, run side by side and do not mingle their waters.’²⁹ A significant example of the continuing distinction between legal and equitable rights is that, whereas in order to obtain an equitable remedy, a litigant must rely on the court’s discretion, if he seeks a common law remedy, once he has established that a right existing at common law has been breached, a remedy will be granted. Given this continuing distinction between the two ‘streams of jurisdiction’, the challenge in seeking to ensure that equitable principles are applied in common law systems is ‘the...need to receive the principles of equity into the general [common law] norms’.³⁰

In contrast, in civil law systems, there is no identifiable law of equity nor were separate courts of equity a feature of such systems. In addition, the courts in such systems are extremely reluctant to be seen to base their decisions on equity or on equitable principles.³¹ This reluctance is attributable, at least in part, to the influence of legal positivism on Continental legal systems together with the phenomenon of codification, both of which place emphasis on the supremacy and

²⁵*ibid*, 3; Raymond Evershed, ‘Equity is not presumed to be past the age of child-bearing’ (1953-1955) 1 Sydney L Rev 1. See also *Campbell Discount Co Ltd v Bridge* [1961] 1 QB 445, 459, per Harman LJ noting that ‘since the time of Lord Eldon the system of equity for good or evil has been a very precise one, and equitable jurisdiction is exercised only on well-known principles’.

²⁶In the US, some vestiges of the dual system of courts of law and courts of equity remain. While in forty-three states in the US there is no longer any distinction in judicial structure between law and equity, Delaware, Mississippi, and Tennessee retain at least some separate courts for equity; New Jersey and Cook County, Illinois have separate divisions for law and equity within a single court; Georgia distinguishes equity for trial and appellate jurisdiction; and Iowa has unified courts that administer what the state constitution calls ‘distinct and separate jurisdictions’ for law and equity.

²⁷In England, see, in particular, the Supreme Court of Judicature Act 1873 (36 & 37 Vict c. 66) and the Supreme Court of Judicature Act 1875 (38 & 39 Vict c. 77).

²⁸See generally Hilary Delany, *Equity and the Law and Trusts in Ireland* (4th edn, Round Hall Publishing 2007) 7-12 for a discussion of whether the ‘fusion’ of law and equity is of a procedural nature only.

²⁹Walter Ashburner, *Principles of Equity* (2nd edn, Butterworth 1933) 18.

³⁰Ralph A Newman, ‘Equity in Comparative Law’ (1968) 17 Int'l & Comp L Q 807, 830.

³¹See G M Razi, ‘Reflections on Equity in the Civil Law Systems’ (1963) 13 Am University L Rev 24, 40 observing that ‘civilian courts, of any rank, would never base a decision on equity.’

autonomous nature of positive rules and downplay the role of the jurist as a law-maker.³² This fosters the view that recourse to equity is only permitted when positive law expressly admits such recourse.³³ However, despite these apparent restrictions on the extent to which courts in civil law jurisdictions can rely on equity, such courts will nonetheless ‘do what they can to do equity.’³⁴

Thus, the introduction of the principles of equity has been facilitated in many civil systems by either provisions in the relevant civil codes to the effect that when the written law is silent, the judge may determine the law or through references to underlying moral standards (such as doctrines of natural law, natural equity, general principles of law or doctrines of equity).³⁵ An example of this is the *Generalklauseln* in the German Civil Code (the *Bürgerliches Gesetzbuch* or BGB) which, for example, require judgments to be based upon good morals (*gute Sitte*) or necessary care (*erforderliche Sorgfalt*), thereby obliging the judge to seek the legal grounds for the decision outside of positive law.³⁶ On a related note, the concept of good faith, which is a feature of many civil codes,³⁷ has also played an important role in facilitating civil law courts in doing equity. Indeed, the content of good faith is analogous to that of equity in English law and can be regarded as civil law’s equity as it is used by judges to create new rules, which are concretisations, supplements or corrections to positive law.³⁸ For example, § 242 BGB, in requiring debtors to perform their duties according to the requirements of good faith taking customary practice into consideration, has been used by the German courts to create several duties additional to those expressly stated by contract clauses or by positive

³²The advent of positivism was, of course, not unique to Continental legal systems but, when combined with the phenomenon of private law codification in those systems, it can be said to have acquired a ‘centripetal force that it previously did not possess’: Mauro Bussani and Francesca Fiorentini, ‘The Many Faces of Equity: A Comparative Survey of the European Civil Law Tradition’ in Daniela Carpi (ed), *The Concept of Equity: An Interdisciplinary Assessment* (Winter Verlag 2007) 113-14.

³³*ibid.*

³⁴G M Razi, ‘Reflections on Equity in the Civil Law Systems’ (1963) 13 *Am University L Rev* 24, 40.

³⁵Ralph A Newman, ‘Equity in Comparative Law’ (1968) 17 *Int'l & Comp L Q* 807, 831; Margaret White, ‘Equity – A General Principle of Law Recognised by Civilised Nations?’ (2004) 4 *University of Technology L J* 103, 107. See also Swiss Civil Code, Articles 1 and 4; Italian Civil Code, Article 12.

³⁶See for example §§ 138, 817, 819, 826 (regarding good morals); §§ 241a, 259, 276, 831, 833, 2028 (regarding necessary care).

³⁷See for example § 242 BGB and Article 1134(3) of the French *Code civil*.

³⁸Martijn W Hesselink, ‘The Concept of Good Faith’ in A S Hartkamp, E H Hondius, C A Joustra, C E du Perron and M Veldman (eds), *Towards a European Civil Code* (3rd edn, Kluwer Law International 2004) 217-20.

law, to guard against the abusive exercise of rights and as a basis to grant extraordinary remedies.³⁹ Finally, it has been observed that, even outside of the discretion afforded to judges by the good faith principle and other ‘equitable’ concepts, it is likely that judges covertly take account of equitable principles in other ways through, for example, determining the ‘equitable’ solution to a case and then developing reasoning based on the positive law as to why that solution should be reached.⁴⁰ Despite the various devices used by judges to ‘do equity’ however, the official discourse in civil law systems is to the effect that equity is irrelevant except to the extent permitted by the positive law and, thus, it can be stated that, in such systems, ‘the conflict between the clashing objectives of certainty and of ideal justice, has prevented a complete integration of law and equity’.⁴¹ Nonetheless, despite this lack of integration (which is a feature shared with the common law albeit for different reasons), there is a striking similarity in the equitable content of common law systems and civil law systems. For example, the common law maxims of equity, which act as guiding principles for the application of rules of law, have also been accepted as principles of law in civil law jurisdictions.⁴²

Accordingly, while the differing role afforded to equity by different legal systems was one of the primary reasons why equity was not expressly included as a source of law in Article 38 of the ICJ Statute,⁴³ there is a broad consensus that transcends legal traditions as to what it means to ‘do equity’, which is linked to the origins of equity in a sense of justice that is innate to human nature.⁴⁴ Thus, it is now widely (if not universally) recognised that equity constitutes either a ‘general principle of law recognised by civilised nations’ or, alternatively, forms part of customary international law⁴⁵ and can therefore play a role in international law disputes

³⁹Mauro Bussani and Francesca Fiorentini, ‘The Many Faces of Equity: A Comparative Survey of the European Civil Law Tradition’ in Daniela Carpi (ed), *The Concept of Equity: An Interdisciplinary Assessment* (Winter Verlag 2007) 124-25. See also Steven Reinhold, ‘Good Faith in International Law’ (2013) 2 UCL J L and Jurisprudence 40, 42-43.

⁴⁰*ibid*, 120-22 and 129-30 noting this tendency in French law and in Italian law.

⁴¹Ralph A Newman, ‘Equity in Comparative Law’ (1968) 17 Int'l & Comp L Q 807, 809.

⁴²G M Razi, ‘Reflections on Equity in the Civil Law Systems’ (1963) 13 Am University L Rev 24, 41. See also Roscoe Pound, ‘The Maxims of Equity. I of Maxims Generally’ (1921) 34 Harv L Rev 809 describing the historical origins of the maxims of equity.

⁴³P van Dijk, ‘Equity: a Recognized Manifestation of International Law?’ in M Bos and W Heere (eds), *International Law and its Sources* (Kluwer 1989) 11.

⁴⁴See Howard L Oleck, ‘The Historical Nature of Equity Jurisprudence’ (1951) 20 Fordham L Rev 23, 44 noting that equity can be described as ‘the principal technique thus far developed to ensure that law will always be readily adaptable for, and directed towards, the achievement of justice’.

⁴⁵See generally Anastasios Gourgourinis, ‘Delineating the Normativity of Equity in International Law’ (2009) 11 Intl Community L Rev 327, 343-45.

without the express authorisation of the parties.⁴⁶ However, neither the concept nor the role of equity in international law is coterminous with equity's characteristics in domestic law.⁴⁷ Therefore, the role of equity in international law generally and, in particular, in the formulation of remedies merits further examination.

(b) *The role of equity in international law*

While, even within the parameters of a particular domestic legal system, the concept and role of equity is difficult to concretise, that problem becomes even more acute in an international context given the lack of homogeneity of values. Therefore, although it can be stated that equity as it has been recognised and developed in international law is most closely related to Western legal traditions,⁴⁸ the role of equity in international law is even more uncertain than is the case in domestic legal systems,⁴⁹ albeit that its influence on legal rules and principles can be regarded as being at least as strong as in other legal systems.⁵⁰

Perhaps due to this uncertainty as to what is meant by equity in an abstract sense or to the specific connotations that the term equity has in the common law tradition, international courts and tribunals have, with the notable exception of international maritime boundary delimitation cases,⁵¹ proven reluctant to cite equity as the basis for, or the guiding principle underlying, their decisions.⁵² Instead, there has been a tendency on the part of international courts and tribunals to have recourse to specific rules and principles of an equitable nature which enjoy acceptance across a

⁴⁶*Diversion of Waters from the River Meuse (Netherlands v Belgium)*, Individual Opinion of Judge Hudson, PCIJ Series A/B, No 70, 76-77; Ruth Lapidot, 'Equity in International Law' (1987-1988) 22 Israel L Rev 161, 176. cf Benedetto Conforti and Angelo Labella, *An Introduction to International Law* (Martinus Nijhoff 2012) 48-49.

⁴⁷Shabtai Rosenne, 'The Position of the International Court of Justice on the Foundations of the Principle of Equity in International Law' in Arie Bloed and Pieter van Dijk (eds), *Forty Years of the International Court of Justice: Jurisdiction, Equity and Equality* (Europa Instituut 1988) 85. See also Steven Reinhold, 'Good Faith in International Law' (2013) 2 UCL J L and Jurisprudence 40, 63 noting that, while good faith as a general principle of law is familiar from municipal law, it is applied in quite a different manner in international law.

⁴⁸Margaret White, 'Equity – A General Principle of Law Recognised by Civilised Nations?' (2004) 4 Queensland University of Technology L J 103, 104.

⁴⁹Wolfgang Friedmann, 'The North Sea Continental Shelf – A Critique' (1970) 64 AJIL 229; Michael Akehurst, 'Equity and General Principles of Law' (1976) 25 ICLQ 801.

⁵⁰Vaughan Lowe, 'The Role of Equity in International Law' (1988-1989) 12 Australian YB Intl L 54, 54.

⁵¹See generally Ian Brownlie, *Principles of Public International Law* (6th edn, OUP 2003) 173-222. See also Shi Jiuyong, 'The Wang Tieya Lecture in Public International Law: Maritime Delimitation in the Jurisprudence of the International Court of Justice' (2010) 9 Chinese J Intl L 271.

⁵²Margaret White, 'Equity – A General Principle of Law Recognised by Civilised Nations?' (2004) 4 Queensland University of Technology L J 103.

broad range of municipal legal systems and which are (or at least seem to be) capable of being defined and stated in a ‘pure’ form.⁵³

For example, in the *Diversion of Water from the River Meuse*⁵⁴ case, Judge Hudson, although concurring in the Court’s decision, confirmed in his separate opinion that two maxims of equity - namely that equality exists between parties and a party who seeks equity must do equity - constituted general principles of international law.⁵⁵

In referring to the latter principle, he noted as follows:

in a proper case, and with scrupulous regard for the limitations which are necessary, a tribunal bound by international law ought not to shrink from applying a principle of such obvious fairness.⁵⁶

Similarly, the principle of estoppel has been accepted into international law as a general principle of law, resting on principles of good faith and consistency.⁵⁷

Fundamentally, the concept of estoppel obliges a state ‘to be consistent in its attitude to a given factual or legal situation’.⁵⁸ This same notion underlies both the various types of estoppel in common law jurisprudence (including promissory estoppel, proprietary estoppel and estoppel by silence) and the civil law concepts of preclusion, debarment and foreclosure.⁵⁹ However, while estoppel-like concepts in municipal law are quite precisely formulated, international law has not adopted the ‘manifold refinements grafted onto [the concept of estoppel] by domestic legal systems’⁶⁰ and has instead generally⁶¹ favoured a more basic conception of estoppel which requires only that a state makes an unconditional representation to another state with proper authority on which the state invoking estoppel must rely.⁶² Thus, as noted by Judge Alfaro in the *Temple of Preah Vihear* case:

⁵³ibid.

⁵⁴PCIJ Series A/B, No 70, 4.

⁵⁵ibid, 77.

⁵⁶ibid. See also *La Grand (Germany v United States)*, Judgment 27 June 2001, (2001) ICJ Rep 466.

⁵⁷See generally Alexander Ovchar, ‘Estoppel in the Jurisprudence of the ICJ: A principle promoting stability threatens to undermine it’ (2009) 21 Bond L Rev Article 5.

⁵⁸Iain MacGibbon, ‘Estoppel in International Law’ (1958) 7 ICLQ 458, 468.

⁵⁹Alexander Ovchar, ‘Estoppel in the Jurisprudence of the ICJ: A principle promoting stability threatens to undermine it’ (2009) 21 Bond L Rev Article 5, 3.

⁶⁰Anthony D’Amato, ‘Consent, Estoppel, and Reasonableness: Three Challenges to Universal International Law’ (1969) 10 Va J Intl L 1, 8.

⁶¹Christopher Brown, ‘A Comparative and Critical Assessment of Estoppel in International Law’ (1995-1996) 50 U Miami L Rev 369, 397-98 noting some cases in which a narrower version of estoppel, corresponding more closely to estoppel by representation in Anglo-American law, was invoked.

⁶²D W Bowett, ‘Estoppel before International Tribunals and its Relation to Acquiescence’ (1957) 33 British YB Intl L 176; Alexander Ovchar, ‘Estoppel in the Jurisprudence of the ICJ: A principle promoting stability threatens to undermine it’ (2009) 21 Bond L Rev Article 5, 3-6.

there is a very substantial difference between the simple and clear-cut rule adopted and applied in the international field and the complicated classifications, modalities, species, sub-species and procedural features of the municipal system.⁶³

Thus, it is questionable whether the principle of estoppel as it has been developed in international law possesses any greater specificity than equity as a general concept.⁶⁴ Indeed, in a description which could equally be used to describe the role of equity, it has been observed that ‘estoppel is often employed as a catch all term to create a legal effect which the regime should otherwise provide’.⁶⁵

This example (which is quite representative of the manner in which equitable principles have been translated into international law)⁶⁶ suggests that, notwithstanding a certain reluctance on the part of international courts and tribunals to use the term equity, such courts and tribunals endeavour to ‘do equity’ through reliance on a variety of principles of an equitable nature,⁶⁷ which are regarded as being of a corrective nature.⁶⁸ Thus, equity does not confer unlimited discretion on the decision maker to override the law but rather allows for the correction of a lack of subtlety and flexibility in the strict law, where ‘the letter of the rule would kill its spirit’.⁶⁹ This facilitates a weighing up of what is right in all the circumstances in

⁶³*Case concerning the Temple of Preah Vihear (Cambodia v Thailand)*, Judgment 15 June 1962, Separate Opinion of Judge Alfaro, (1962) ICJ Rep 6, 39.

⁶⁴See Iain MacGibbon, ‘Estoppel in International Law’ (1958) 7 ICLQ 458, 477. See also Christopher Brown, ‘A Comparative and Critical Assessment of Estoppel in International Law’ (1995-1996) 50 U Miami L Rev 369, 383-84 noting that ‘what passes for a rule of estoppel in international practice is little more than a maxim exhorting parties to act consistently.’

⁶⁵*ibid*, 406.

⁶⁶See Steven Reinhold, ‘Good Faith in International Law’ (2013) 2 UCL J L and Jurisprudence 40. See also *El Paso Energy International Company v Argentina*, ICSID Case No ARB/03/15, Award 31 October 2011, para 622 noting that principles deriving from national law must be adapted to ‘become suitable for application on the level of public international law’.

⁶⁷Other examples include the principles of abuse of rights and abuse of discretion, *pacta sunt servanda* and acquiescence, which (together with the principle of estoppel) are conceptualised as concretisations of the principle of good faith in international law: Steven Reinhold, ‘Good Faith in International Law’ (2013) 2 UCL J L and Jurisprudence 40, 47-57.

⁶⁸M W Janis, ‘The Ambiguity of Equity in International Law’ (1983) 9 Brooklyn J Intl L 7, 19. See also *Maritime Delimitation in the Area between Greenland and Jan Mayen (Denmark v Norway)*, Separate Opinion of Judge Weeramantry 14 June 1993 (1993) ICJ Rep 38, para 17 noting that equity has been the source that has given international law the concept of international mandates and trusts, of good faith, of *pacta sunt servanda*, of *jus cogens*, of unjust enrichment, of *rebus sic stantibus* and of abuse of right.

⁶⁹Thomas M Franck, *Fairness in International Law and Institutions* (OUP 1998) 58.

order to correct or supplement the law and to ameliorate the gross unfairness which might occasionally result from the strict application of legal rules.⁷⁰

Accordingly, the different modes of application of equity within international law have been categorised as equity *infra legem* and equity *praeter legem*.⁷¹ Equity *infra legem* refers to ‘that form of equity which constitutes a method of interpretation of the law in force, and is one of its attributes’,⁷² or equity ‘used to adapt the law to the facts of individual cases’,⁷³ while equity *praeter legem* refers to equity being used to fill lacunae in the law, without derogating from, or undermining, the spirit of the law itself. Thus, as has been emphasised by the ICJ, equity *praeter legem* refers to equity used ‘not...with a view to filling a social gap in law, but...in order to remedy the insufficiencies of international law and fill in its logical lacunae’.⁷⁴

While equity, so conceived, brings with it a considerable degree of flexibility and facilitates the adaptation and adjustment of legal principles, rules and concepts to the realities and circumstances of a particular case, it does not confer unlimited discretion on the decision maker. In particular, while equity could potentially serve as a broad synonym for distributive justice (and indeed that meaning has been adopted in other contexts),⁷⁵ this use of equity has not been universally accepted in

⁷⁰See *Maritime Delimitation in the Area between Greenland and Jan Mayen (Denmark v Norway)*, Separate Opinion of Judge Weeramantry 14 June 1993 (1993) ICJ Rep 38, para 73 in which he opines that equity in international law is ‘a force that supplements the law and helps it forward on its course of delivering just results in disputes between parties’.

⁷¹There is also a third mode of application of equity: equity *contra legem*. However, this envisages derogation from general law, in order to remedy its social inadequacies. Therefore, given that the boundary between equity *contra legem* and resolution of a dispute *ex aequo et bono* is far from clear, equity *contra legem* enjoys little doctrinal support in international law and may not be invoked save with the express authorisation of the parties: see *North Sea Continental Shelf Cases (Federal Republic of Germany v Denmark; Federal Republic of Germany v Netherlands)*, Separate Judgment of Judge Ammoun (1969) ICJ Rep 3, 139; Shabtai Rosenne, ‘The Position of the International Court of Justice on the Foundations of the Principle of Equity in International Law’ in Arie Bloed and Pieter van Dijk (eds), *Forty Years of the International Court of Justice: Jurisdiction, Equity and Equality* (Europa Instituut 1988) 88-89; Owen McIntyre, ‘Utilization of shared international freshwater resources – the meaning and role of “equity” in international water law’ (2013) 38 *Water Intl* 112, 115-16.

⁷²*Case Concerning the Frontier Dispute (Burkina Faso v Mali)*, Judgment 22 December 1986 (1986) ICJ Rep 554, 567-68.

⁷³Michael Akehurst, ‘Equity and General Principles of Law’ (1976) 25 *ICLQ* 801, 801.

⁷⁴*Case Concerning the Barcelona Traction, Light and Power Company, Limited (Second Phase)*, Separate Judgment of Judge Ammoun (1970) ICJ Rep 3. See also Vaughan Lowe ‘The Role of Equity in International Law’ (1988-1989) 12 *Australian YB Intl L* 54, 56-63 arguing that the functions fulfilled by equity *infra legem* and equity *praeter legem* can be fulfilled within the law without the necessity of recourse to a separate concept of equity.

⁷⁵See *Maritime Delimitation in the Area between Greenland and Jan Mayen (Denmark v Norway)*, Separate Opinion of Judge Weeramantry 14 June 1993 (1993) ICJ Rep 38, para 110 noting Oscar

international law.⁷⁶ Thus, the ICJ noted in the *Libya/Tunisia Continental Shelf* case that:

it is bound to apply equitable principles as part of international law, and to balance up the various considerations which it regards as relevant in order to produce an equitable result. While it is clear that no rigid rules exist as to the exact weight to be attached to each element in the case, this is very far from being an exercise of discretion or conciliation; nor is it an operation of distributive justice.⁷⁷

Furthermore, the discretion conferred on an adjudicative body by the concept of equity does not permit it to decide purely on the basis of what it considers right or just as this would amount to resolving the dispute *ex aequo et bono*, which requires the express authorisation of the parties.⁷⁸ The ancient concept of *ex aequo et bono* holds that adjudicators should decide disputes according to their concept of what is fair and just in the circumstances. Thus, while decisions in equity are deemed to form part of the law, decisions *ex aequo et bono* are attributed to a moral, social or political realm that is external to (and is sometimes conceptualised as being contrary to) the law. The rationale behind this distinction is that, while adjudicators may ‘fill gaps’ in the law based on principles of equity, they should not base their decisions on subjective notions of fairness or justice that have not been reduced to principles and rules of law.⁷⁹ Thus, as the late Justice Lauterpacht of the International Court asserted:

adjudication *ex aequo et bono* amounts to an avowed creation of new relations between the parties...it differs clearly from the application of the

Schachter’s analysis of the uses of equity. See also Anastasios Gourgourinis, ‘Delineating the Normativity of Equity in International Law’ (2009) 11 Intl Community L Rev 327, 340-46.

⁷⁶This comment relates to the role of equity in international law as a general principle of international law or as part of customary international law. However, references to equity in particular treaties may be imbued by notions of distributive justice: see for example the United Nations Convention for the Law of the Sea, 21 ILM 1261 (1982), art 70(1). See also Dinah L Shelton, ‘Intergenerational Equity’ in Rüdiger Wolfrum and Chie Kojima (eds), *Solidarity: a Structural Principle of International Law* (Springer 2010) 144-48 noting references to the concept of intergenerational equity (which is primarily a principle of distributive justice) in international legal instruments.

⁷⁷*Case Concerning the Continental Shelf (Tunisia v Libya)*, Judgment 24 February 1982 (1982) ICJ Rep 18, 60. See also *Case Concerning the Continental Shelf (Libya v Malta)* (1985) ICJ Rep 13; cf Thomas M Franck, *Fairness in International Law and Institutions* (OUP 1998) 66-68.

⁷⁸See Article 38(4) ICJ Statute and Article 42(3) ICSID Convention.

⁷⁹Leon E Trakman, ‘Ex Aequo et Bono: Demystifying an Ancient Concept’ (2007-2008) 8 Chi J Intl L 621, 627. See also Alexander J Bělohávek, ‘Application of Law in Arbitration, *Ex Aequo et Bono* and *Amiable Compositur*’ (2013) Czech (& Central European) Yearbook of Arbitration 25.

rules of equity, which form part of international law as indeed, of any legal system.⁸⁰

However, while it is possible to distinguish the application of the rules of equity from adjudication *ex aequo et bono* on a conceptual level, the distinction between the two is by no means a bright-line distinction.⁸¹ Therefore, some commentators have asserted that, instead of insisting on a formal divide between application of the rules of equity and adjudication *ex aequo et bono*, it may be more accurate to evaluate adjudicative discretion along a spectrum of decision-making ranging from, at one end, decisions that clearly had a basis in law in well-established equitable principles to, on the other end, decisions that were clearly made outside the law based solely on the adjudicator's conception of what was fair.⁸² This less structured approach reflects the continuum along which adjudicative discretion is, in reality, exercised and also recognises that decisions based on equity and decisions made *ex aequo et bono* share similar substantive ends, principally, arriving at a fair result in the circumstances of a particular case.⁸³

Overall therefore, equity in international law can be regarded as a concept that operates as a means of considering all the relevant circumstances in a particular case and which may temper the rigours of the law in light of those circumstances and introduce considerations of fairness, reasonableness and good faith into the decision-making process, either as general concepts or through the introduction of specific principles of legal reasoning associated with fairness and reasonableness.⁸⁴ The relevance of equity to the international law of remedies in particular will now be considered.

(c) *Equity in the international law of remedies*

Equity has been found to be relevant in a number of ways under the international law of remedies. First, as noted by the ICJ in the *Ahmadou Sadio Diallo* case,

⁸⁰Hersch Lauterpacht, *The Development of International Law by the International Court* (Grotius Publications Ltd 1982) 213.

⁸¹Ian Brownlie, *Principles of Public International Law* (6th edn, OUP 2003) 25-26; Leon E Trakman, 'Ex Aequo et Bono: Demystifying an Ancient Concept' (2007-2008) 8 Chi J Intl L 621, 628.

⁸²Leon E Trakman, 'Ex Aequo et Bono: Demystifying an Ancient Concept' (2008) 8 Chi J Intl L 621; Alexander J Bělohávek, 'Application of Law in Arbitration, *Ex Aequo et Bono* and *Amiable Compositeur*' (2013) Czech (& Central European) Yearbook of Arbitration 25.

⁸³*ibid*, 628.

⁸⁴Rosalyn Higgins, *Problems and Process: International law and How We Use It* (Clarendon Press 1994) 221. See also *Case Concerning the Continental Shelf (Tunisia v Libya)*, Separate Opinion of Judge Jiménez de Aréchaga, 24 February 1982 (1982) ICJ Rep 18, para 24.

damages in respect of non-material injury must, of necessity, be quantified by reference to equitable considerations.⁸⁵ As support for this statement, the ICJ cited the decision of the European Court of Human Rights in *Al-Jedda v United Kingdom*, which noted that, in determining reparation for non-material injury, the Court's 'guiding principle' is equity.⁸⁶ The Court went on to describe the role of equity as follows:

[equity] above all involves flexibility and an objective consideration of what is just, fair and reasonable in all the circumstances of the case, including not only the position of the applicant but the overall context in which the breach occurred.⁸⁷

Secondly, equity and reasonableness have been cited as the grounds for determining whether restitution is an appropriate remedy or whether compensation should instead be granted.⁸⁸ Thirdly, proportionality, which can be considered a component part of (or a legal principle derived from) the tradition of equity,⁸⁹ occupies a significant and established position under the international law of remedies. This is particularly due to the fact that, while in domestic law, one rarely encounters situations where the remedy for a violation of law is a right granted to the affected party to also violate the law, in international law, remedies frequently (or even usually) take this form and the proportionality of such countermeasures is crucial in determining their legality.⁹⁰ Thus, the Draft ILC Articles provide that, in taking countermeasures in order to procure the cessation of the wrongful act and to achieve reparation for the injury, such measures must be a proportionate response to an internationally wrongful act of the state against which they are taken, taking into

⁸⁵See *Ahmadou Sadio Diallo (Republic of Guinea v Democratic Republic of the Congo)*, Judgment 19 June 2012, (2012) ICJ Rep 334, para 24. See also Sergey Ripinsky with Kevin Williams, *Damages in International Investment Law* (British Institute of International and Comparative Law 2008) 312.

⁸⁶ Application No 27021/08, Judgment 7 July 2011, (2011) 53 EHRR 23, para 114.

⁸⁷*ibid.*

⁸⁸International Law Commission, *Draft Articles on Responsibility of States for Internationally Wrongful Acts, with commentaries 2001* (2001) 2 YB Intl L Comm'n, UN Doc A/CN.4/SER.A/2001/Add.1 (Part 2), para 11 of the commentary on art 35.

⁸⁹See generally Thomas Cottier and others, 'The Principle of Proportionality in International Law' NCCR Trade Working Paper No 2012/38 December 2012. See also *Case Concerning the Continental Shelf (Tunisia v Libya)*, Judgment 24 February 1982 (1982) ICJ Rep 18, para 104.

⁹⁰Thomas Sebastian, 'World Trade Organization Remedies and the Assessment of Proportionality: Equivalence and Appropriateness' (2007) 48 Harv Intl L J 337, 338.

account the gravity of the internationally wrongful act and the rights in question.⁹¹ Furthermore, where the remedy for an internationally wrongful act is to take the form of reparation rather than countermeasure, the Draft ILC Articles state that the reparation granted to the injured party must be proportionate to the injury caused by a wrongful act and that this proportionality requirement is addressed in different ways in the context of each form of reparation, taking into account its specific character. Thus, restitution is excluded if it would involve a burden out of all proportion to the benefit gained by the injured state or other party.⁹² Similarly, satisfaction must not be out of proportion to the injury and ‘may not take a form humiliating to the responsible state.’⁹³ Turning finally to the remedy of damages, the requirement for proportionality between the remedy awarded and the injury suffered is stated to be addressed by limiting the recoverable loss to damage actually suffered as a result of the internationally wrongful act and in excluding damage which is indirect or remote.⁹⁴ However, the Draft ILC Articles would also appear to endorse (or require)⁹⁵ consideration of equity in applying the full reparation principle in noting, in the context of elaborating on the application of the full reparation principle, that:

the appropriate heads of compensable damage and the principles of assessment to be applied in quantification, ...will vary depending on the content of particular primary obligations, an evaluation of the respective behaviour of the parties and, more generally, a concern to reach an equitable and acceptable outcome.⁹⁶

⁹¹International Law Commission, *Draft Articles on Responsibility of States for Internationally Wrongful Acts, with commentaries 2001* (2001) 2 YB Intl L Comm’n, UN Doc A/CN.4/SER.A/2001/Add.1 (Part 2), art 51.

⁹²*ibid*, art 35(b).

⁹³*ibid*, art 37(3).

⁹⁴*ibid*, para 5 of the commentary on art 34.

⁹⁵See Diane Desierto, ‘ICESCR Minimum Core Obligations and Investment: Recasting the Non-Expropriation Compensation Model during Financial Crises’ (2012) 44 *Geo Wash Intl L Rev* 473, 483 arguing that the determination of compensation under Article 36 of the Draft ILC Articles is intended to produce an ‘equitable outcome’ for both the injured state and the injuring state and that this requirement should not be overlooked when the injured party is an investor. See also Anthony Aust, *Handbook of International Law* (2nd edn, Cambridge University Press 2010) 387.

⁹⁶International Law Commission, *Draft Articles on Responsibility of States for Internationally Wrongful Acts, with commentaries 2001* (2001) 2 YB Intl L Comm’n, UN Doc A/CN.4/SER.A/2001/Add.1 (Part 2), para 7 of the commentary on art 36. See also *Diversion of Waters from the River Meuse (Netherlands v Belgium)*, Individual Opinion of Judge Hudson, PCIJ Series A/B, No 70, 78-79 noting that ‘in a particular case in which it is asked to enforce the obligation to make reparation, a court of international law cannot ignore special circumstances which may call for the consideration of equitable principles’.

Finally, while economics is often regarded as providing a policy basis for the partial defences of contributory fault and failure to mitigate loss, those defences, which operate to reduce the damages payable, can also be considered to be underpinned by fundamental principles of fairness and equity.⁹⁷ Thus, the commentaries to Article 39 of the Draft ILC Articles acknowledge that the notion of contributory fault is consistent not only with the principle that full reparation and nothing more is due in respect of the injury but also with fairness as between the responsible state and the victim of the breach.⁹⁸ Furthermore, the international decisions that have recognised the relevance of contributory fault include several cases in which the claimant has engaged in an unlawful or otherwise prohibited act at the time the claim arose, which suggests that contributory fault is consonant with the equitable doctrine of ‘clean hands’.⁹⁹ Similarly, the partial defence of failure to mitigate loss, in requiring the victim of breach to take reasonable steps to limit the damage sustained, can also be considered to be consistent with fairness as between the responsible state and the victim of the breach and also with the ‘clean hands’ principle¹⁰⁰ and, thus, can be conceptualised as an equitable concept.¹⁰¹

Overall therefore, it is clear that equity plays a significant role under the public international law of remedies both in determining the type of remedy to be granted and, where damages are to be awarded, in assessing the quantum of such damages. In practice however, the role of equity in quantifying damages is not so clear-cut – in particular, although the exercise of ‘normal’ discretion in quantifying damages can, on a conceptual level, be considered separate to the application of equity, the two are often conflated.¹⁰² Therefore, given the permeable boundary between the two concepts (and the somewhat amorphous nature of equity as a general concept), before assessing equity’s potential role in taking account of public interest considerations at the remedies stage, the extent to which equity has been received

⁹⁷See Gary T Schwartz, ‘Contributory and Comparative Negligence: a Reappraisal’ (1977-1978) 87 Yale L J 697 arguing that economics, standing alone, does not provide a persuasive basis for any contributory negligence defence but that such a basis is adequately provided by reasons of fairness.

⁹⁸ibid, para 2 of the commentary on art 39.

⁹⁹David J Bederman, ‘Contributory Fault and State Responsibility’ (1989-1990) 30 Va J Intl L 335, 338-355.

¹⁰⁰See Ciarán Burke, *An Equitable Framework for Humanitarian Intervention* (Bloomsbury 2013) 315 noting that the clean hands principle also applies prospectively, meaning that one who seek’s equity’s assistance must be prepared to act in an equitable manner.

¹⁰¹Ralph A Newman, ‘Equity in Comparative Law’ (1968) 17 Int’l & Comp L Q 807, 813-29.

¹⁰²Irmgard Marboe, *Calculation of Compensation and Damages in International Investment Law* (OUP 2009) 145.

into investment treaty arbitration to date (both generally and at the remedies stage in particular) must be analysed.

(d) *The influence of equity in international investment law*

Investment treaty arbitration has not remained immune from the influence of equity and equitable principles. For example, the principle of good faith has assumed an important role in assessing the initiation of claims under IIAs. Thus, where the claimant investor failed to comply with the law in making its investment, investment treaty arbitration tribunals have generally either declined jurisdiction over the investor's claims or, alternatively, have held that the investor's claims were inadmissible.¹⁰³ The requirement that only investments made in accordance with the law be protected under an investment treaty can either be an explicit requirement of the relevant IIA¹⁰⁴ or it can be considered an implicit obligation based on general principles of law.¹⁰⁵ Where the latter is the case, the principle of good faith has played a key role in both providing a basis for such obligation and in establishing its limits. Thus, in *Plama Consortium Ltd v Bulgaria*,¹⁰⁶ the Energy Charter Treaty did not contain an express provision requiring the investment's conformity to a given law and the tribunal based its determination that the investor's claim was inadmissible on breach by the investor of the principle of good faith, an element of both Bulgarian and international law, and on the principle that a claimant should not be permitted to profit from his own wrongdoing (*nemo auditur*

¹⁰³See for example *Inceysa Vallisoletana SL v Republic of El Salvador*, ICSID Case No ARB/03/26, Award 2 August 2006, paras 155, 252–64; *Fraport AG Frankfurt Airport Services Worldwide v Republic of the Philippines*, ICSID Case No ARB/03/25, Award 16 August 2007, paras 396–401; *Phoenix Action Ltd v Czech Republic*, ICSID Case No ARB/06/5, Award 15 April 2009, paras 101–105. On the distinction between declining jurisdiction over a claim and declaring a claim inadmissible see Andrew Newcombe, 'Investor misconduct: Jurisdiction, admissibility or merits?' in Chester Brown and Kate Miles (eds), *Evolution in Investment Treaty Law and Arbitration* (Cambridge University Press 2011) 192–93.

¹⁰⁴See for example Agreement between the Federal Republic of Germany and the Republic of the Philippines for the Promotion and Reciprocal Protection of Investments, signed 18 April 1997, entered into force 1 February 2000, art 1.

¹⁰⁵See Rahim Moloo and Alex Khachaturian, 'The Compliance with the Law Requirement in International Investment Law' (2011) 34 *Fordham L J* 1473 arguing that where the relevant treaty contains an explicit compliance with law requirement, non-compliance with law is a jurisdictional issue but, where that obligation is implicit, non-compliance with law goes to the admissibility of the investor's claims; cf Zachary Douglas, 'The Plea of Illegality in Investment Treaty Arbitration' (2014) 29 *ICSID Rev* 155.

¹⁰⁶ICSID Case No ARB/03/24, Award 27 August 2008.

propiam turpitudinem allegans).¹⁰⁷ The influence of good faith can also be seen in the recognition of exceptions to the general principle that a claimant who has acted contrary to law will be denied treaty protection. Thus, it has been recognised that, where the violation of law committed by the investor arose due to an error made in good faith, the investor shall not be denied the benefits of treaty protection.¹⁰⁸ Similarly, where the host state government knowingly overlooked violations of its law by an investor, it has been accepted that the host state should be estopped from raising such violations as a barrier to jurisdiction/admissibility.¹⁰⁹

The good faith principle and the narrower, though related, concepts of abuse of rights or abuse of process have also been relied upon to deny a claimant investor treaty protection where, for example, a claimant has engaged in corporate restructuring purely in order to gain access to investment arbitration.¹¹⁰ Thus, in *Phoenix Action Ltd v Czech Republic*,¹¹¹ the shares in two Czech companies had been transferred by a Czech national to an Israeli company owned by the wife of the Czech national in question essentially in order to elevate a domestic dispute to an international level. In finding that it lacked jurisdiction over the claimant's request, the tribunal opined as follows:

States cannot be deemed to offer access to the ICSID dispute settlement mechanism to investments not made in good faith. The protection of international investment arbitration cannot be granted if such protection would run contrary to the general principles of international law, among which the principle of good faith is of utmost importance.¹¹²

While, in the examples mentioned above, the principle of good faith has been relied on in assessing investor conduct, this principle has also been used in assessing host

¹⁰⁷ibid, paras 135-46. See also *Gustav FW Hamester GmbH & Co KG v Ghana*, ICSID Case No ARB/07/24, Award 18 June 2010, para 123.

¹⁰⁸*Fraport AG Frankfurt Airport Serv Worldwide v Republic of the Philippines*, ICSID Case No ARB/03/25, Award 16 August 2007, para 396; *Desert Line Projects v Yemen*, ICSID Case No ARB/05/17, Award 6 February 2008, paras 116-17.

¹⁰⁹ibid, para 346. See also Rahim Moloo and Alex Khachaturian, 'The Compliance with the Law Requirement in International Investment Law' (2011) 34 Fordham L J 1473, 1497-99.

¹¹⁰See generally Eric de Brabandere, 'Good Faith', 'Abuse of Process' and the Initiation of Investment Treaty Claims' (2012) 3 J Intl Dispute Settlement 609; Filip Černý, 'Short Flight of the Phoenix: A Few Thoughts on Good Faith, the Abuse of Rights and Legality in Investment Arbitration' (2012) Czech YB Intl L 183.

¹¹¹ICSID Case No ARB/06/5, Award 15 April 2009.

¹¹²ibid, para 106.

state conduct, particularly under the FET standard.¹¹³ These roles range from the absence of good faith being held to constitute one of the indicators of breach of the FET standard, to good faith being considered the basis for, or as informing the content of, more specific rules regarding respect for the investor's legitimate expectations and lack of arbitrariness to good faith forming the basis of the FET obligation itself.¹¹⁴ Similarly, the application of proportionality analysis at the merits stage in order to balance public and private interests can be considered to be linked to equity, given that equity can be considered synonymous with a weighing up of what is right in all the circumstances.¹¹⁵ Thus, it is clear that equitable principles have had an influence at both the jurisdiction and merits stages of the arbitral process and have, at least in some cases, operated as a means of taking account of public interest considerations, either directly (through, for example, the application of proportionality analysis) or indirectly (through taking into account the conduct of the claimant investor).

However, at the remedies stage of the investment treaty arbitration process, equity and equitable principles have arguably been afforded less prominence.¹¹⁶ Thus, only a handful of investment treaty arbitration tribunals have made even passing reference to 'equitable considerations' or 'equitable principles' in quantifying damages.¹¹⁷ Indeed, a review of 86 publicly available awards rendered between

¹¹³By virtue of its explicit reference to 'equity' or 'equitable' treatment, the FET standard, of itself, can be interpreted as requiring consideration of all circumstances of the case, including the conduct of the claimant investor: Peter Muchlinski, "'Caveat Investor'?: The Relevance of the Conduct of the Investor under the Fair and Equitable Treatment Standard' (2006) 55 ICLQ 527.

¹¹⁴See generally Martins Paparinskis, 'Good Faith and Fair and Equitable Treatment in International Investment Law' in Andrew D Mitchell, M Sornarajah and Tania Voon (eds), *Good Faith and International Economic Law* (OUP 2015).

¹¹⁵See Thomas Cottier and others, 'The Principle of Proportionality in International Law' NCCR Trade Working Paper No 2012/38 December 2012; Peter Muchlinski, "'Caveat Investor'?: The Relevance of the Conduct of the Investor under the Fair and Equitable Treatment Standard' (2006) 55 ICLQ 527, 532. cf Joshua Karton and others, 'Is Investment Treaty Arbitration a Mechanism to Second-guess Governments' Exercise of Administrative Discretion: Public Law or Lex Investoria?' in Ian A Laird, Borzu Sabahi, Frédéric G Sourgens and Todd Weiler (eds), *Investment Treaty Arbitration and International Law Volume 8* (Juris 2015) 280 arguing that there are two separate rules of proportionality in international law.

¹¹⁶Meriam N Alrashid, 'The Arbitral Tribunal's Discretion in Quantifying Damages' in Ian A Laird, Borzu Sabahi, Frédéric G Sourgens and Todd Weiler (eds), *Investment Treaty Arbitration and International Law Volume 8* (Juris 2015) 344 noting that, since the turn of the century, damages considerations have not tended towards overt considerations of equity; cf Juan Felipe Merizalde Urdaneta, 'Proportionality, Contributory Negligence and Other Equity Considerations in Investment Treaty Arbitration' in Ian A Laird, Borzu Sabahi, Frédéric G Sourgens and Todd Weiler (eds), *Investment Treaty Arbitration and International Law Volume 8* (Juris 2015).

¹¹⁷See for example *American Manufacturing & Trading, Inc. v Zaire*, ICSID Case No ARB/93/1, Award 21 February 1997, paras 7.02 and 7.16; *Tecnicas Medioambientales Tecmed SA v Mexico*, ICSID Case No ARB(AF)/99/2, Award 29 May 2003, para 190. See also *Himpurna Cal Energy Ltd.*

1990 and 2014 indicates that only 4 of those awards contained some reference to equity or equitable principles in setting out the principles applicable to the quantification of damages or compensation.¹¹⁸ Furthermore, those passing references that have been made have not been linked to public interest considerations and many would appear to be intended as a form of justification for exercising the ‘normal’ discretion required to be exercised by arbitral tribunals in circumstances where the extent of the claimant’s loss was uncertain. For example, in *AMT v Zaire* the tribunal noted that, in choosing between different methods of assessment of damages, the method chosen should be ‘equitable in the circumstances of the present case’ and also noted that ‘for practical reasons founded on equitable principles’ Zaire was under a duty to compensate AMT for certain losses.¹¹⁹ Similarly, although the tribunal’s reasoning is not entirely clear, in *Tecmed v Mexico*, the context in which the reference to equity was made suggests that the tribunal was primarily concerned with remedying the claimant’s loss as the tribunal noted that it could consider equitable principles when determining the compensation owed to the claimant, without assuming the role of an arbitrator *ex aequo et bono* before concluding, in the same paragraph, that ‘any difficulty in determining the compensation does not prevent the assessment of such compensation where the existence of damage is certain’.¹²⁰ Similarly, the partial defence of contributory fault has only been accepted in a relatively small number of cases, where either, in the case of host state regulatory action, the claimant investor should have anticipated the relevant regulatory risk or, alternatively, where the investor’s conduct was unreasonable and prompted the host state to act¹²¹ and the related plea of failure to mitigate loss has not yet been applied in the sphere of

(Bermuda) v PT (Persero) Perusahaan Listrik Negara (Indonesia), 14 Mealey’s Intl Arbitration Reports A-1, A-57 (December 1999) in which the tribunal relied particularly on the equitable principle of abuse of rights.

¹¹⁸Review conducted by the author of awards hosted on the www.italaw.com database and on the basis that they contained some consideration of the question of damages.

¹¹⁹*American Manufacturing & Trading, Inc. v Zaire*, ICSID Case No ARB/93/1, Award 21 February 1997, paras 7.02 and 7.16.

¹²⁰*Tecnicas Medioambientales Tecmed SA v Mexico*, ICSID Case No ARB(AF)/99/2, Award 29 May 2003, para 190.

¹²¹*MTD Equity Sdn. Bhd. and MTD Chile S.A. v Republic of Chile*, ICSID Case No ARB/01/7, Award 25 May 2004, paras 242-46; *Occidental Petroleum Corp., Occidental Exploration and Prod. Co. v Ecuador*, ICSID Case No ARB/06/11, Award 5 October 2012, paras 668-70; *Yukos Universal Limited (Isle of Man) v the Russian Federation*, PCA Case No AA 27, Award 18 July 2014, para 1594 ff.

investment treaty arbitration (albeit that there has been some indications of its acceptance in principle).¹²²

The reluctance on the part of tribunals to rely on equity or equitable principles in quantifying damages may be partly attributable to the fear that reference to equity could potentially render a tribunal's award liable to challenge on the basis that the tribunal decided *ex aequo et bono*.¹²³ It may also partly stem from a view that, since the full reparation principle is, in itself, of a very general and flexible nature, specific recourse to equity may not be necessary in order to achieve an 'equitable' result.¹²⁴ However, it is submitted that the dynamism of equity can open the door to what has been referred to as 'the enlightened exercise of remedial discretion'¹²⁵ and can also reinforce the doctrinal basis for taking account of public interest considerations when applying the full reparation principle. The next section of this chapter will examine this proposition both generally and by reference to the specific examples identified in Chapter 4 of circumstances in which public interest considerations should be taken into account at the remedies stage.

(e) *Equity and the full reparation principle*

As the theoretical foundation of, or rationale underlying, reparations remains undeveloped in international law,¹²⁶ the full reparation principle is of a very general nature and 'does not offer a conceptual framework for the recovery of damages that would be comparable in specificity to the 'value' approach generally applicable in

¹²²See *Middle East Cement Shipping and Handling Co SA v Egypt*, ICSID Case No ARB/99/6, Award 12 April 2002 paras 166-71; cf *AIG Capital Partners, Inc. and CJSC Tema Real Estate Company v Kazakhstan*, ICSID Case No ARB/01/6, Award 7 October 2003, para 10.6.4.

¹²³See *Klöckner Industrieranlagen GmbH and others v Cameroon*, ICSID Case No ARB/81/2, Decision on Annulment 3 May 1985, para 59. See also Craig Miles and others, 'Awarding Damages: Proportionality, Contributory Fault, and Arbitral Tribunals' Discretion or Toss of a Coin?' in Ian A Laird, Borzu Sabahi, Frédéric G Sourgens and Todd Weiler (eds), *Investment Treaty Arbitration and International Law Volume 8* (Juris 2015) 369-70.

¹²⁴See for example Irmgard Marboe, *Calculation of Compensation and Damages in International Investment Law* (OUP 2009) 152 who notes that economic realities, including the effects of a financial crisis, may be reflected in the damages calculation without relying on equity as a comparison of the hypothetical financial situation of the affected investor to his actual situation should reflect such economic realities. See also Borzu Sabahi, *Compensation and Restitution in Investor-State Arbitration* (OUP 2011) 187.

¹²⁵Kent Roach, 'The Limits of Corrective Justice and the Potential of Equity in Constitutional Remedies' (1991) 33 *Ariz L Rev* 859, 863.

¹²⁶Dinah Shelton, 'Righting Wrongs: Reparations in the Articles on State Responsibility' (2002) 96 *AJIL* 833, 844.

expropriation cases.’¹²⁷ The lack of a conceptual framework for applying the full reparation principle means that tribunals are afforded a considerable margin of discretion in quantifying damages¹²⁸ and that causation principles operate as the primary means by which the quantum of damages payable in a particular case is delimited.¹²⁹ However, as the law of state responsibility is largely silent on the nature of the causal link leading to reparation (merely requiring that the injury should be a consequence of the wrongful act),¹³⁰ and as causation principles are themselves informed by equity,¹³¹ causation principles, in fact, afford tribunals the flexibility to take account of a broad range of factors in quantifying damages. Indeed, Gray goes so far as to opine that causation principles in international law constitute ‘a useful policy instrument for the exclusion of whatever damage the arbitrator does not wish to compensate’.¹³²

Similarly, although the partial defence of contributory fault and the related plea of failure to mitigate loss are influenced by notions of equity and fairness, they can be applied without necessarily referring to equity and can serve as means of taking account of public interest considerations. Admittedly, taking account of investor conduct through application of these doctrines does not directly take account of a host state’s right to regulate or the legitimate purposes behind such regulation. However, these doctrines do introduce a certain public interest dimension into the damages quantification process, given that investor conduct and host state regulatory sovereignty may be linked (such as where the regulatory measures

¹²⁷Sergey Ripinsky with Kevin Williams, *Damages in International Investment Law* (British Institute of International and Comparative Law, 2008) 90.

¹²⁸See Diane Desierto, ‘ICESCR Minimum Core Obligations and Investment: Recasting the Non-Expropriation Compensation Model during Financial Crises’ (2012) 44 *Geo Wash Intl L Rev* 473, 511-12, opining that the assessment of damages for non-expropriatory breaches of IIAs is ‘largely discretionary’ in nature.

¹²⁹International Law Commission, *Draft Articles on Responsibility of States for Internationally Wrongful Acts, with commentaries 2001* (2001) 2 *YB Intl L Comm’n*, UN Doc A/CN.4/SER.A/2001/Add.1 (Part 2), para 5 of commentary on art 34. See also León Castellanos-Jankiewicz, ‘Causation and International State Responsibility’ *Amsterdam Law School Research Paper No 2012-56*.

¹³⁰Campbell McLachlan, Laurence Shore and Matthew Weiniger, *Investment Treaty Arbitration: Substantive Principles* (OUP 2007) 335; Brigitte Stern, ‘The Obligation to Make Reparation’ in J Crawford, A Pellet and S Olleson (eds), *The Law of International Responsibility* (OUP 2010) 570.

¹³¹A M Honoré, ‘Causation and Remoteness of Damage’ in A Tunc (ed), *International Encyclopedia of Comparative Law* (Mohr 1983) para 59. See also León Castellanos-Jankiewicz, ‘Causation and International State Responsibility’ *Amsterdam Law School Research Paper No 2012-56*.

¹³²Christine D Gray, *Judicial Remedies in International Law* (Clarendon Press 1990) 23.

introduced by the host state were introduced in response to investor conduct)¹³³ and given that the host state and its citizens have a legitimate interest in ensuring that negligent investors are not compensated for damage caused by their own acts or omissions.¹³⁴ As both doctrines are dependent on the relevant tribunal's appreciation of the causal factors that underpin liability,¹³⁵ investment treaty arbitration tribunals are, in practice, afforded significant discretion in applying these doctrines.¹³⁶ Thus, as noted by the *ad hoc* Annulment Committee in *MTD Equity v Chile*, '[a]s is often the case with situations of comparative fault, the role of the two parties contributing to the loss was very different and only with difficulty commensurable, and the Tribunal had a corresponding margin of estimation.'¹³⁷ Therefore, as public interest considerations may already be taken into account at the remedies stage to a certain degree through the application of causation principles,¹³⁸ through the 'normal' discretion afforded to tribunals in quantifying damages and, in certain cases, through application of contributory fault or of the plea of failure to

¹³³See generally Peter Muchlinski, "'Caveat Investor'?: The Relevance of the Conduct of the Investor under the Fair and Equitable Treatment Standard" (2006) 55 ICLQ 527.

¹³⁴Counterclaims can, for analogous reasons, also serve as means of taking account of public interest considerations. However, jurisdiction has only rarely been accepted over counterclaims in investment treaty arbitration. Indeed, the decision in *Goetz v Burundi* was the first known investment treaty arbitration in which the tribunal affirmed its jurisdiction over the host state's counterclaim (although it went on to dismiss the counterclaim on the merits): *Goetz and S.A. Affinage des Metaux v Burundi*, ICSID Case No ARB/01/2, Award 21 June 2012, paras 267-87. See also H E Veenstra-Kjos, 'Counterclaims by Host States in Investment Treaty Arbitration' (2007) 4 Transnational Dispute Management; Pierre Lalive and Laura Halonen, 'On the Availability of Counterclaims in Investment Treaty Arbitration' (2011) Czech YB Intl L 141; Thomas Kendra, 'State Counterclaims in Investment Arbitration - A New Lease of Life?' (2013) 29 Arbitration Intl 575.

¹³⁵The plea of failure to mitigate loss requires that some part of the injury can be shown to be severable in causal terms from that attributable to the responsible state (with the burden of proof being placed on the responsible state) while the defence of contributory fault requires that only those actions or omissions which can be considered as wilful or negligent (i.e. which manifest a lack of due care on the part of the victim of the breach for his or her own property or rights) can be taken into account in determining whether the injured party contributed to the loss caused to it: International Law Commission, *Draft Articles on Responsibility of States for Internationally Wrongful Acts, with commentaries 2001* (2001) 2 YB Intl L Comm'n, UN Doc A/CN.4/SER.A/2001/Add.1 (Part 2), arts 31 and 39 and related commentary.

¹³⁶For a critical view of the contributory fault doctrine as it has been applied in investment treaty arbitration to date see Juan Felipe Merizalde Urdaneta, 'Proportionality, Contributory Negligence and Other Equity Considerations in Investment Treaty Arbitration' in Ian A Laird, Borzu Sabahi, Frédéric G Sourgens and Todd Weiler (eds), *Investment Treaty Arbitration and International Law Volume 8* (Juris 2015).

¹³⁷ICSID Case No ARB/01/7, Decision on Annulment 21 March 2007, para 101. See also *Occidental Petroleum Corp., Occidental Exploration and Prod. Co. v Ecuador*, ICSID Case No ARB/06/11, Award 5 October 2012, paras 662-87.

¹³⁸See Andreas Kulick, 'Sneaking Through the Backdoor – Reflections on Public Interest in International Investment Arbitration' (2013) 29 Arbitration Intl 435, 443-49, citing *Biwater v Tanzania* as an example of a case in which causation principles were applied in a strict manner and arguing that this was done in order to afford recognition to certain public interest considerations.

mitigate loss, the question arises as to whether the concept of equity adds anything to tribunals' 'toolbox' in terms of reinforcing the doctrinal basis for the taking into account of public interest considerations.¹³⁹

In this regard, it is worth recalling that equity in international law is regarded as having a corrective or supplementary function in that it can be used as a means of ensuring that justice is achieved having regard to all of the circumstances of a particular case or as a means of filling gaps in the law without derogating from, or undermining the law itself. Thus, given the dearth of guidance otherwise afforded to tribunals by customary international law as to how the full reparation principle should be implemented (and in particular regarding the application of causation principles),¹⁴⁰ it is submitted that equity and equitable principles can be used to guide tribunals in exercising their discretion in quantifying damages and in applying causation principles and can, at least in some cases, reinforce the doctrinal basis for taking account of public interest considerations.

To give an example, while, as described above, serious misconduct on the part of the claimant investor may be addressed at the jurisdiction or merits stages of arbitral proceedings by reference to the principle of good faith, circumstances may also arise where misconduct on the part of the investor may more appropriately be addressed at the remedies stage.¹⁴¹ Examples of such circumstances include, first, where the claimant investor's conduct constituted an underlying reason for implementation of the host state measure (albeit not constituting a complete justification as in such circumstances the case should be disposed of at the jurisdiction or merits stage),¹⁴² secondly, where human rights violations were

¹³⁹See Francesco Francioni, 'Compensation for Nationalisation of Foreign Property: The Borderland of Law and Equity' (1975) 24 Intl & Comp LQ 255 who poses a similar question in relation to the compensation payable in respect of nationalisations. See also Meriam N Alrashid, 'The Arbitral Tribunal's Discretion in Quantifying Damages' in Ian A Laird, Borzu Sabahi, Frédéric G Sourgens and Todd Weiler (eds), *Investment Treaty Arbitration and International Law Volume 8* (Juris 2015) 345.

¹⁴⁰Sergey Ripinsky with Kevin Williams, *Damages in International Investment Law* (British Institute of International and Comparative Law, 2008) 90-91.

¹⁴¹Andrew Newcombe, 'Investor misconduct: Jurisdiction, admissibility or merits?' in Chester Brown and Kate Miles (eds), *Evolution in Investment Treaty Law and Arbitration* (Cambridge University Press 2011) 189. See also United Nations, *Third Report on International Responsibility by F V Garcia-Amador, Special Rapporteur*, UN Doc A/CN.4/111 (1958), arts 13-14 and associated commentary.

¹⁴²Peter Muchlinski, "'Caveat Investor'?: The Relevance of the Conduct of the Investor under the Fair and Equitable Treatment Standard' (2006) 55 ICLQ 527, 528. See also Patrick Dumberry and Gabrielle Dumas-Aubin, 'When and How Allegations of Human Rights Violations can be Raised in Investor-State Arbitration' (2012) 13 J World Investment & Trade 349, 367.

committed by an investor in the context of another investment project in the country that is unrelated to the investment about which the investor has commenced arbitration proceedings and, thirdly, where human rights violations committed by the investor did not fall within the scope of the dispute resolution clause in the relevant IIA.¹⁴³ Even given the inherent flexibility of causation principles, a causal connection between the investor misconduct and the loss ultimately suffered by the investor as a result of the host state's action may well be difficult to establish in such circumstances. However, given that one of the basic principles of equity is that the conduct of disputants may affect their rights and obligations in the context of a dispute (and that this principle has, as described above, been put into effect at both the jurisdiction and merits stage of the arbitral process), it is submitted that equity can strengthen the doctrinal basis for consideration of investor behaviour at the remedies stage, either as a supplement to, or in certain cases in substitution for, the doctrines of contributory fault and failure to mitigate loss.

Turning to the specific examples identified in Chapter 4 of circumstances in which public interest considerations should be taken into account at the remedies stage, while it may not be possible in all cases to point to a particular equitable principle to inform the approach taken by tribunals in examining such issues, it is submitted that equity nonetheless has a role to play in conditioning the exercise of arbitral discretion to allow for recognition of the sovereignty implications underlying a particular dispute.¹⁴⁴ Thus, where a direct treaty conflict occurs or where the impugned host state measures were introduced in furtherance of the fundamental rights provisions contained in the host state's highest law, two interrelated issues fall to be addressed: first, the question of whether the claimant investor should have conducted due diligence in respect of and, accordingly, anticipated and possibly mitigated its exposure to, the risk of such a conflict arising¹⁴⁵ and, secondly, whether, in order to achieve an optimal balance between investment protection and host state regulatory sovereignty, it is otherwise desirable that public interest considerations be taken into account in quantifying the damages payable for the IIA breach. It is submitted that, while these issues can arguably be taken into account

¹⁴³ibid, 361-67.

¹⁴⁴Sergey Ripinsky with Kevin Williams, *Damages in International Investment Law* (British Institute of International and Comparative Law 2008) 124-26.

¹⁴⁵See generally Diane Desierto, 'Sovereign Policy Flexibility for Social Protection: Managing Regulatory Risk in International Investment Agreements' (28 November 2012), Mauritius International Arbitration Conference, December 2012, 56, 62 and 85.

within the parameters of the valuation methods customarily applied in quantifying damages (such as through adjustment of the discount rate used in applying the DCF method), as it is not possible to precisely identify, estimate and track a host state's other non-investment related treaty obligations (especially as they relate to, or will affect, the investment in question),¹⁴⁶ in reality this amounts to an equitable adjustment of the damages award.¹⁴⁷ In this regard, Desierto, in discussing the effect that a host state's simultaneous observance of the ICESCR minimum core obligation during an economic emergency should have on the damages payable in respect of non-expropriatory breaches of IIAs, acknowledges the role of equity in quantifying such damages¹⁴⁸ and observes as follows:

it would be contrary to the public function and just purposes of reparations to require 'expectancy interest' compensation levels that beggar, punish, and extort from host States pursuing social protection measures under the ICESCR in good faith.¹⁴⁹

Desierto bases this conclusion at least partially on the premise that, under the law of state responsibility, tribunals are tasked with reaching an equitable outcome in applying the full reparation principle and that the International Law Commission has emphasised the importance of proportionality to the law of reparations.¹⁵⁰ Thus, it is submitted that equity's corrective function within international law provides support for the taking into account of a host state's good faith efforts to comply with its non-investment related obligations in quantifying the damages payable for an IIA breach.

¹⁴⁶See Diane A Desierto and Desiree A Desierto, 'Investment Pricing and Social Protection: a proposal for an ICESCR-adjusted Capital Asset Pricing Model (2013) 28 ICSID Rev 405, 416-19 noting that this is not yet possible in relation to a state's minimum core obligations under the ICESCR but noting that efforts towards developing empirical, quantitative and qualitative criteria for verifying state compliance with the ICESCR are ongoing. However, under, for example, international environmental treaties, the parameters of state obligations are, and are likely to remain, relatively unclear given that there is no system of compulsory adjudication capable of developing and refining the specific contents of broad environmental obligations: see Jorge E Viñuales, 'The Environmental Regulation of Foreign Investment Schemes Under International Law' in Pierre-Marie Dupuy and Jorge E Viñuales (eds), *Harnessing Foreign Investment to Promote Environmental Protection: Incentives and Safeguards* (Cambridge University Press 2013) 311.

¹⁴⁷*ibid*; Diane Desierto, 'ICESCR Minimum Core Obligations and Investment: Recasting the Non-Expropriation Compensation Model during Financial Crises' (2012) 44 *Geo Wash Intl L Rev* 473.

¹⁴⁸Diane Desierto, 'ICESCR Minimum Core Obligations and Investment: Recasting the Non-Expropriation Compensation Model during Financial Crises' (2012) 44 *Geo Wash Intl L Rev* 473, 511.

¹⁴⁹*ibid*, 503-20.

¹⁵⁰*ibid*.

Turning next to a situation in which the defence of necessity is successfully invoked, as was mentioned in Chapter 4, Article 27 of the Draft ILC Articles does not attempt to specify in what circumstances (or to what extent) compensation should be payable where the defence is successfully invoked,¹⁵¹ albeit that it is made clear that Article 27 is not concerned with compensation within the framework of full reparation for wrongful conduct. Given the lack of guidance provided as to how the compensation payable should be delimited therefore, it is submitted that, as is the case in respect of compensation payable for non-material injury, equity is well suited to the task of reconciling the two competing imperatives which arise in such circumstances (namely the need to recognise that the host state acted to protect essential interests in a situation of turmoil and the simultaneous need to recognise that IIAs exist to protect foreign investors in such difficult situations) in order to arrive at an appropriate award of damages.¹⁵²

Finally, in cases of procedural breach (and, in particular, in cases where the claimant investor's legitimate expectations have been frustrated), a 'sliding scale' approach that would consider, in quantifying the damages payable, the loss suffered by the claimant investor, the nature and intensity of the procedural breach and the public purpose being pursued (including the likelihood that the substantive outcome would have been the same in the absence of the breach) was proposed in Chapter 4. While it is clear that the loss suffered by the claimant investor is central to the quantification of damages, whether the other enumerated factors may permissibly be considered as part of the damages quantification process is less obvious. Turning first to the question of whether the nature and intensity of the procedural breach and the public purpose being pursued by the host state may permissibly be considered in quantifying damages, while, under the law of state responsibility, the obligation to make reparation is defined principally by reference to the injury arising from wrongful conduct rather than by reference to the content of the particular primary rule at issue, it has nonetheless been recognised that primary rules have a subsidiary role to play in the assessment of reparation and that secondary rules cannot be

¹⁵¹International Law Commission, *Draft Articles on Responsibility of States for Internationally Wrongful Acts, with commentaries 2001* (2001) 2 YB Intl L Comm'n, UN Doc A/CN.4/SER.A/2001/Add.1 (Part 2), para 6 of the commentary on art 27.

¹⁵²See *CMS v Argentina*, ICSID Case No ARB/01/8, Decision of the *Ad hoc* Annulment Committee on the Application for Annulment of Argentina 25 September 2007, paras 137-47 in which the Annulment Committee opined that Article 27 of the ILC Articles allows the matter of compensation to be decided on a case-by-case basis.

detached from, or be considered to operate autonomously of, primary rules.¹⁵³ Accordingly, it is submitted that the nature and intensity of a particular breach and the public purpose being pursued by the host state may (and arguably must)¹⁵⁴ be considered within the parameters of the ‘normal’ discretion afforded to investment treaty arbitration tribunals in quantifying damages, as supplemented by the role of equity, and that the latter would facilitate an overall examination of the context in which the breach of the primary rule occurred. In particular, in the case of a breach of legitimate expectations, equity would facilitate consideration of the purpose underlying the host state’s actions as well as of the nature of the expectation protected (e.g. whether, on one end of the spectrum, it arose from a formal decision made by a public authority about a person or a limited group or whether, on the other, it arose from a general representation that the public authority subsequently departed from in light of a shift in general procedure or policy).¹⁵⁵

Turning finally to the question of whether the likelihood that the substantive outcome would have been the same in the absence of the breach may be considered in quantifying the damages payable to a claimant investor, consideration of this issue as one factor amongst others in quantifying the damages payable constitutes quite a different proposition to applying the plea of ‘hypothetical alternative lawful conduct’¹⁵⁶ which would require the hypothetical alternative course that the host state could have lawfully taken (i.e. had it pursued the same policy and complied with the applicable, procedural and/or substantive rules) to be plotted and the investor to be restored to the position it would have been in had the host state taken that course.¹⁵⁷ Given that the latter plea would effectively nullify the purpose of

¹⁵³International Law Commission, *Draft Articles on Responsibility of States for Internationally Wrongful Acts, with commentaries 2001* (2001) 2 YB Intl L Comm’n, UN Doc A/CN.4/SER.A/2001/Add.1 (Part 2), para 7 of the commentary on art 36; Ian Brownlie, *Principles of Public International Law* (6th edn, OUP 2003) 447. See also Statement by James Crawford, Special Rapporteur, ILC 2634th Meeting of 8 June 2000, YB Intl L Commission 2000, vol 1, 177, para 54.

¹⁵⁴Graham Mayeda, ‘Sustainable International Investment Agreements: Challenges and Solutions for Developing Countries’ in Marie-Claire Cordonier Segger, Markus W Gehring and Andrew Newcombe (eds), *Sustainable Development in World Investment Law* (Kluwer 2011) 557.

¹⁵⁵Søren Schönberg, *Legitimate Expectations in Administrative Law* (OUP 2000) 8ff.

¹⁵⁶For application of this plea in domestic law see Kristoffel Grechenig and Alexander Stremitzer, ‘Der Einwandrechtmäßigen Alternativverhaltens - Rechtsvergleich, Ökonomische Analyse und Implikationen für die Proportionalhaftung’ (2009) 73 *Rabels Zeitschrift für ausländisches und internationales Privatrecht* 336.

¹⁵⁷See generally Jonathan Schaffer, *Contrastive Causation in the Law* (2010) 16 *Legal Theory* 259.

procedural guarantees, it has not been accepted in international law generally¹⁵⁸ nor was it accepted by the tribunal in *Amco v Indonesia (II)*, a case involving, *inter alia*, the revocation of the claimant investor's investment licence by Indonesia (which Indonesia argued was justified on the basis that the claimant investor had violated domestic and applicable international law). In that case, the tribunal noted as follows:

To argue, as did Indonesia, that although there had been procedural irregularities, a 'fair BKPM' [the governmental body acting on behalf of Indonesia] would still have revoked the licence, because of Amco's own shortcomings, is to misaddress causality. The Tribunal cannot pronounce on what a 'fair BKPM' would have done. This is both speculative, and not the issue before it. Rather, it is required to characterise the acts that BKPM did engage in and to see if those acts, if unlawful, caused damage to Amco.¹⁵⁹

While, at first glance, this pronouncement would appear to preclude any consideration of the question of whether the investor would have suffered substantial damages had the host state acted lawfully, the malleable nature of causation principles and the need to ensure that the claimant investor is not put in a better financial position than it would be in without the damaging event allow for consideration of this factor. Furthermore, it is submitted that equity could guide the tribunal in its application of causation principles and in its consideration of the context in which the procedural breach occurred as well as the position of both parties.

Therefore, it is submitted that equity, when combined with the application of customary valuation methods and of causation principles, affords sufficient flexibility to tribunals to take account of public interest considerations in a manner which allows for the introduction of a degree of reciprocity into the process and which takes account of the specific situations in which, it was argued, public interest considerations should be taken into account at the remedies stage. Furthermore, it is submitted that recourse to equity can, at least in some cases, reinforce the doctrinal basis for taking account of public interest considerations at

¹⁵⁸Sergey Ripinsky with Kevin Williams, *Damages in International Investment Law* (British Institute of International and Comparative Law 2008) 118.

¹⁵⁹ICSID Case No ARB/81/1, Resubmitted Case Award 5 June 1990 and Decision on Supplemental Decisions and Rectification 17 October 1990, 1 ICSID Rep 569, para 174.

the remedies stage. Overall however, the role of equity at the remedies stage should adhere quite closely to the law (albeit that the law is itself flexible).¹⁶⁰

Thus, given that equity can play a role in the damages quantification process without the need for an explicit reference to equity or equitable principles in the relevant IIA, a more open attitude to the application of equity may be all that is required in order to take account of public interest considerations at the remedies stage. Although it is arguable that tribunals may take account of equitable principles implicitly in exercising their ‘normal’ discretion,¹⁶¹ it is submitted that, in order to enhance the legitimacy and transparency of the exercise, tribunals should explicitly acknowledge their reliance on equitable principles so that justice can not only be done but can also be seen to be done.¹⁶² However, as noted above, tribunals may be reluctant to acknowledge the influence of equity as reference to equity could potentially render a tribunal’s award liable to post-award challenge and it is therefore arguable that a stronger doctrinal basis is required to either support tribunals’ reliance on equity and/or to allow for public interest considerations to be taken into account at the remedies stage. Accordingly, the next section of this chapter will consider the merits and demerits of several proposals in relation to the inclusion of language relating to remedies in new or renegotiated IIAs. However, before doing so, the question of whether the recognition of public interest considerations is possible in quantifying the compensation payable in respect of lawful expropriations must be considered separately, given that the nature and structure of the expropriation enquiry and the applicable standard of compensation differs from that applicable in respect of unlawful breaches.

(f) *The ‘special case’ of lawful expropriations*

¹⁶⁰This conception of the role of equity mirrors the maxim *Aequitas sequitur legem* or ‘equity follows the law’.

¹⁶¹T W Wälde and Borzu Sabahi, ‘Compensation, Damages and Valuation’ in Peter Muchlinski, Federico Ortino and Christoph Schreuer (eds), *The Oxford Handbook of International Investment Law* (OUP 2008) 1105.

¹⁶²See Borzu Sabahi, *Compensation and Restitution in Investor-State Arbitration* (OUP 2011) 188 noting that failure to acknowledge reliance on equitable principles could leave the award open to annulment for lack of stated reasons. See also Kent Roach, ‘The Limits of Corrective Justice and the Potential of Equity in Constitutional Remedies’ (1991) 33 *Ariz L Rev* 859, 882-883. On the importance of the quality of legal reasoning provided in awards to the legitimacy of investment treaty arbitration generally see Federico Ortino, ‘Legal Reasoning of International Investment Tribunals: A Typology of Egregious Failures’ (2012) 3 *J Intl Dispute Settlement* 31, 33–35.

While the full reparation principle, as a subjective valuation approach, is inherently flexible and so allows for public interest considerations to be accommodated, the fair market value standard, which has emerged as the dominant criterion under IIAs for the quantification of compensation in respect of lawful expropriations, is considerably less flexible. This is the case as the fair market value standard of compensation is objective or impersonal in nature in that it discounts those elements of value that are personal to a given owner of property and instead bases the value on the price which a hypothetical buyer would have paid for the property. This has led tribunals and commentators to the conclusion that there is little room for public interest considerations to be taken into account, or for equity to be introduced, in applying the standard.¹⁶³ Admittedly, like the application of the full reparation principle, application of the fair market value standard involves a significant element of discretionary choice, particularly given that fair market value in most international investment cases must be constructed inferentially from a variety of evidence.¹⁶⁴ The question therefore is whether the exercise of this ‘normal’ discretion by investment treaty arbitration tribunals is sufficient to take account of public interest considerations in quantifying the compensation payable in respect of lawful expropriations. It is submitted that this is not the case as, although, in constructing the value of an expropriated asset, the social and economic circumstances of the host state are taken into account in determining the price which a hypothetical third party would pay for the particular asset, this does not encompass the regulatory function that the host state is performing.

Accordingly, in order to take account of public interest considerations at the remedies stage in respect of lawful expropriations, deviation from the fair market value standard is required and this would need to be provided for in the text of new or renegotiated IIAs. The next section will describe some general factors to be considered by IIA negotiators and drafters in providing for the taking into account

¹⁶³*Santa Elena v Costa Rica*, ICSID Case No ARB/96/1, Award of 17 February 2000, paras 71-72; Elihu Lauterpacht, ‘Issues of Compensation and Nationality in the Taking of Energy Investments’ (1990) 8 *J Energy and Natural Resources* L 241, 249; Ursula Kriebaum, ‘Regulatory Takings: Balancing the Interests of the Investor and the State’ (2007) 8 *Journal of World Investment and Trade* 717, 720. See also Diane A Desierto, ‘ICESCR Minimum Core Obligations and Investment: Recasting the Non-Expropriation Compensation Model during Financial Crises’ (2012) 44 *Geo Wash Intl L Rev* 473, 494-513 criticising the application by tribunals of the fair market value standard when giving effect to the full reparation principle on the basis that it does not afford sufficient flexibility to consider all relevant circumstances and to reach an ‘equitable outcome’.

¹⁶⁴Thomas Merrill, ‘Incomplete Compensation for Takings’ (2002) 11 *NYU Environmental L J* 110, 131-34.

of public interest considerations at the remedies stage and will also analyse some specific alternative options for quantifying both the damages payable for unlawful acts and the compensation payable for lawful expropriations.

5.2 *New or renegotiated IIAs*

UNCTAD's 2013 World Investment Report notes that, since BIT-making activity peaked in the 1990s and has bottomed out since then, the IIA regime is now at a juncture that, due to the imminent expiry of many BITs, there exists 'a window of opportunity to effect systemic improvement'.¹⁶⁵ However, while it may therefore be the optimum time at which to consider the inclusion of language in the text of new or renegotiated IIAs which explicitly authorises tribunals to take account of public interest considerations in formulating remedies, a number of factors should be considered by treaty negotiators and drafters before doing so. First, while inclusion of such language could arguably provide investment treaty arbitration tribunals with a more concrete basis for introducing public interest considerations at the remedies stage in quantifying the damages payable in respect of unlawful acts,¹⁶⁶ on the other hand, enshrining definitive provisions within IIAs could have the unintended effect of reducing the discretion or flexibility afforded to tribunals in quantifying damages, which could, in fact, result in tribunals being constrained in terms of their ability to take account of such considerations. Conversely, in evaluating the type of language that may be appropriate, care should be taken to ensure that the proposed language is not too amorphous to provide sufficient guidance to arbitrators. It is submitted that this is an important factor to be considered in circumstances where the IIA provision in question is intended to displace the conceptually (if not actually) straightforward full reparation principle or the objective fair market value standard.

(a) *Alternatives to the full reparation principle*

¹⁶⁵UNCTAD, *World Investment Report 2013: Global Value Chains: Investment and Trade for Development* (UNCTAD 2013) 108. See also Jürgen Kurtz, 'The Shifting Landscape of International Investment Law and its Commentary' (2012) 106 AJIL 686, 686 describing the current phase of the evolution of investment treaty arbitration as that of 'recalibration'.

¹⁶⁶For a similar argument see J Anthony VanDuzer, Penelope Simons and Graham Mayeda, *Integrating Sustainable Development into International Investment Agreements: A Guide for Developing Country Negotiators* (Commonwealth Secretariat 2013) 448.

Turning first to possible alternatives to the application of the full reparation principle, one potential option would be to specify that, while full reparation is presumptively required in respect of unlawful breaches, derogation from that principle is permissible where significant countervailing public interest considerations are present. These considerations could be listed or could be left to the discretion of the tribunal and whether the burden of proof in terms of rebutting the presumption of full reparation is placed on the host state¹⁶⁷ or whether the tribunal can of its own motion consider facts that could rebut the presumption should also be specified.¹⁶⁸ Examples of considerations which could be listed include the purpose underlying the host state action, the nature of the breach and of the interest protected, whether the measure was taken in pursuance of the host state's duty to comply with non-investment related treaty obligations and the intention of the host state in implementing the measure. On the one hand, such a provision would provide tribunals with a baseline from which to work in the form of the full reparation principle. However, on the other hand, presumptively requiring that full reparation be accorded to the claimant investor arguably constitutes a more prescriptive approach than that required under the customary international law of state responsibility and, therefore, it could constrain tribunals in taking account of public interest considerations, particularly if the burden of proof in terms of rebutting the presumption of full reparation is placed on the host state. Furthermore, where public interest considerations are expressed as matters to be taken into account separately to the application of the full reparation principle, there is potentially a risk that the full reparation principle may be applied by tribunals without regard to the taking into account of such considerations within the parameters of that principle. Therefore, it is submitted that, while such a provision appears promising, it could, in fact, constrain tribunals in their ability to take account of public interest considerations.

¹⁶⁷Most of the arbitration rules, national arbitration laws and international arbitration conventions do not contain rules on the burden or standard of proof. However, Article 24(1) of the UNCITRAL Rules provides that 'each party shall have the burden of proving the facts relied on to support his claim or defense'. However, it is generally agreed that Article 24(1) does not override specific rules on the burden of proof and legal presumptions contained in the applicable substantive law: Florian Haugeneder and Christop Liebscher, 'Investment Arbitration - Corruption and Investment Arbitration: Substantive Standards and Proof' in Christian Klausegger and others (eds), *Austrian Arbitration Yearbook 2009* (CH Beck, Stämpfli & Manz 2009) 544-45.

¹⁶⁸See generally Giuditta Cordero Moss, 'Is the Arbitral Tribunal bound by the Parties' Factual and Legal Pleadings?' (2006) 3 *Stockholm Intl Arbitration Rev* 1.

Turning to a less prescriptive formulation, UNCTAD's Investment Policy Framework for Sustainable Development (IPFSD) suggests a drafting option which provides that the amount of damages should be 'equitable in light of the circumstances of the case'.¹⁶⁹ IPFSD then goes on to suggest that specific rules on damages for treaty breach could potentially be delineated such as excluding recoverability of punitive and/or moral damages, limiting the recoverability of lost profits (up to the date of the award) and ensuring that the amount of damages payable is commensurate with the country's level of development,¹⁷⁰ albeit that the connection between damages being 'equitable' and these specific rules (if a connection was indeed intended) is somewhat unclear. Such a formulation could be said to accord with the dictum in the commentaries on the Draft ILC Articles that an 'equitable and acceptable outcome' should be reached in applying the full reparation principle. However, the IPFSD provision in fact goes further than that dictum as it does not in any way connect the notion of an award being 'equitable' to the full reparation principle. While some commentators have criticised the application of the full reparation principle in the sphere of investment treaty arbitration,¹⁷¹ as was argued in Chapter 4, the dispute settlement provisions contained in IIAs together with their overall structure encourage application of the bilateral notion of corrective justice. In that context, it is submitted that a provision which facilitates a complete disaggregation of the amount of damages payable from the claimant's loss (by, for example, requiring that the damages payable be equitable in light of the circumstances of the case) is not consonant with the nature and functions of the investment treaty arbitration system. Potentially a provision that refers to the desirability of reaching an equitable outcome in conjunction with

¹⁶⁹UNCTAD, *Investment Policy Framework for Sustainable Development* (UNCTAD 2012) 57. See also Graham Mayeda, 'Sustainable International Investment Agreements: Challenges and Solutions for Developing Countries' in Marie-Claire Cordonier Segger, Markus W. Gehring and Andrew Newcombe (eds), *Sustainable Development in World Investment Law* (Kluwer Law International 2011) 557; UNCTAD, *Fair and Equitable Treatment: UNCTAD Series on Issues in International Investment Agreements II* (UNCTAD 2012) 111.

¹⁷⁰*ibid.*

¹⁷¹See for example Thomas Wälde and Borzu Sabahi, 'Compensation, Damages and Valuation' in Peter Muchlinski, Federico Ortino and Christoph Schreuer (eds), *The Oxford Handbook of International Investment Law* (OUP 2008) 1049. See also Zachary Douglas, *The International Law of Investment Claims* (Cambridge University Press, 2009) 103-04 arguing that, by virtue of Article 33(2) and the *lex specialis* reservation in Article 55 of the Draft ILC Articles, the secondary consequences of a violation of an investment treaty are not governed by Part Two of the Draft ILC Articles and that the reliance by tribunals on Chapter II of Part Two of the Draft ILC Articles is 'stunting the development of a coherent substantive law of investment treaty obligations' and is 'preventing [the] emergence of distinct remedial responses for each investment treaty obligation'.

the application of full reparation principle offers more promise. While such a provision may not necessarily confer any additional powers on tribunals in terms of their ability to consider public interest considerations, it could be of assistance in encouraging arbitrators (and host states) to have greater regard to the role of equity in the formulation of remedies.

A third possible provision that could be included in new or renegotiated IIAs could, as suggested by Kulick, require the tribunal to first determine the quantum of damages payable to the investor exclusively by considering the effect on the investment of the host state's infringement and, in a second step, to consider whether the amount of damages payable should be limited according to the outcome of a proportionality *stricto sensu* assessment (i.e. whether a lower quantum of damages is necessary, suitable and the least restrictive measure to address the public interest considerations underlying the host state measure).¹⁷² In making this assessment, Kulick suggests a number of (over-lapping) factors which can guide arbitrators, including the gravity of the infringement by the host state, the legitimate expectations of the investor, the importance of the public purpose underlying the impugned measure and the seriousness of the host state in pursuing that public purpose in light of the evidence as well as the importance of the investor right both *in abstracto* and *in concreto*.¹⁷³ However, it is submitted that such a provision, in focussing solely on the claimant's loss in the first step of the analysis, may constitute a more prescriptive approach than that required under the customary international law of state responsibility and, particularly given that the application of proportionality *stricto sensu* in the sphere of investment treaty arbitration is difficult, would seem, in the second step, to allow for adjustment of the damages payable only in very limited circumstances.

Finally, rather than attempting to allow for public interest considerations to be reflected at the remedies stage generally, more limited provisions could potentially be included in new or renegotiated IIAs to deal with specific situations in which it may be desirable to recognise public interest considerations at the remedies stage (such as where the defence of necessity has been successfully invoked or where a fundamental change in the circumstances prevailing in the host state has occurred).

¹⁷²Andreas Kulick, *Global Public Interest in International Investment Law* (Cambridge University Press 2012) 209-17. See also Ursula Kriebaum, 'Regulatory Takings: Balancing the Interests of the Investor and the State' (2007) 8 J World Investment & Trade 717.

¹⁷³*ibid.*

Thus, one could specify that, where the defence of necessity or another ‘circumstance precluding wrongfulness’ (such as the defences of *force majeure* or distress) has been accepted as applicable, this should lead to a downward adjustment of the damages payable, or alternatively, that the amount expended by the investor should constitute the upward limit on the amount to be awarded.¹⁷⁴ While this approach broadly aligns with current international law, arguably the latter provision would constitute a more prescriptive approach than that set out in Article 27 of the Draft ILC Articles and, thus, could constrain tribunals in their consideration of all of the circumstances surrounding the host state breach. Similarly, given that a conflict between the host state’s right, or duty, to regulate and its IIA obligations may be considered more likely to occur in a crisis situation or where a fundamental change in the circumstances prevailing in the host state has occurred, a new or renegotiated IIA could provide that, where the IIA breach in question occurred in the context of a fundamental change of circumstances, either suspension of the host state’s obligations under the IIA or, alternatively, derogation from the full reparation principle is permissible.¹⁷⁵ This would accord with the rationale underlying the defence of fundamental change of circumstances or *rebus sic stantibus* which is derived from notions of equity and justice and is recognised under the domestic law of many countries and in customary international law as confirmed by Article 62 of the Vienna Convention on the Law of Treaties (and, in particular, Article 62(3) which provides that fundamental change of circumstances can be invoked not only as a ground for terminating or withdrawing from a treaty but also as a ground for suspending the operation of the treaty).¹⁷⁶ Such a provision could be of assistance in addressing, for example, a situation of direct treaty conflict or a conflict between IIA provisions and the fundamental rights provisions contained in the host state’s highest law in time of crisis. This is particularly important given that the lack of flexibility that has been displayed by investment

¹⁷⁴See United Nations, *Second Report on State Responsibility by Mr James Crawford, Special Rapporteur*, UN Doc A/CN.4/498 and Add.1-4 (1999), para 339 noting that, where necessity is successfully invoked, the invoking state may not have to pay full reparation but perhaps should be required to recompense the injured party for actual losses incurred.

¹⁷⁵For a comparable approach which allows derogation from IIA obligations where the host state can invoke a fundamental change of circumstances see UNCTAD, *Investment Policy Framework for Sustainable Development* (UNCTAD 2012) 29, para 2.2.7.

¹⁷⁶See *Fisheries Jurisdiction Case (UK v Iceland)* Judgment 2 February 1973 (1973) ICJ Rep 3, 18, para 36 noting that Article 62 ‘may in many respects be considered as a codification of existing customary law on the subject’.

arbitrators in interpreting long-term contracts and IIAs when dealing with fundamental changes in circumstances has been identified as a key factor underlying the backlash against investment treaty arbitration.¹⁷⁷ On the other hand however, since the socio-economic situation of the host state may largely be reflected within the parameters of customary valuation methods (as supplemented by equity) and since the customary international law defence of fundamental change of circumstances already permits suspension of treaty obligations (albeit that such defence has not been prominent in investment treaty arbitration),¹⁷⁸ it is arguable that such provision is not necessarily required. Indeed, as such a provision would not address the range of circumstances in which taking account of public interest considerations may be appropriate, it could potentially constrain tribunals in taking account of public interest considerations, particularly in the absence of clarification that the provision does not purport to limit the ability of tribunals to take account of matters of public interest in less extreme circumstances.

In conclusion, while, at first blush, it might seem that the inclusion of language relating to remedies in new or renegotiated IIAs would add certainty and ensure that public interest considerations are taken into account in the formulation of remedies, this is not necessarily the case. Indeed, care must be taken to ensure that the wording does not inadvertently constrain arbitrators' ability to take account of such considerations. Furthermore, in evaluating possible provisions, it is submitted that the full reparation principle should form the basis for assessing damages and that a complete disaggregation of the amount of damages payable from the claimant's loss does not accord with the nature and functions of the investment treaty arbitration system. Overall therefore, while inclusion of certain language in new or renegotiated IIAs (such as a provision that refers to the desirability of reaching an equitable outcome in applying the full reparation principle) could potentially encourage arbitrators to utilise their existing ability to take into account public interest considerations through the thoughtful application of customary valuation methods and through the application of equitable principles, it is difficult to conceive of provisions that go further than that without becoming overly prescriptive. Therefore, treaty negotiators should, it is submitted, be cautious in

¹⁷⁷Louis T Wells, 'Backlash to Investment Arbitration: Three Causes' in Michael Waibel and others (eds), *The Backlash against Investment Arbitration: Perceptions and Reality* (Kluwer 2010) 341-52.

¹⁷⁸Hermann Ferré and Kabir Duggal, 'The world economic crisis as a changed circumstance' *Columbia FDI Perspectives*, No 43, 1 August 2011.

deviating from the current approach whereby IIAs generally do not specify the approach to be taken to remedying unlawful breaches.

(b) *Alternatives to the fair market value standard*

In considering alternatives to the fair market value standard, many of the same considerations apply as when considering alternatives to the full reparation principle, albeit that the need to consider alternatives to the fair market value standard is greater, given that public interest considerations cannot currently be taken into account within the parameters of that standard. Such considerations include the need to ensure that sufficient guidance is provided to arbitrators and, conversely, the need to ensure that such provisions are flexible enough to allow for public interest considerations to be taken into account where the circumstances so require. The question therefore is the extent to which deviation from the market value paradigm should occur.¹⁷⁹

In this regard, it has been suggested that deviation from the fair market value standard should be permitted in cases of non-discriminatory large-scale social or economic reform programmes as such large-scale takings ultimately relate to a state's right to determine its own political and economic system (which is a right recognised by public international law). Therefore, it is argued that takings of that nature can be considered a separate phenomenon to individual expropriations¹⁸⁰ and that if prompt and adequate compensation is required in such cases, this would render implementation of any major economic or social programme impossible since 'few states can produce the capital value of a large proportion of their economies promptly'.¹⁸¹ This proposal finds some support in the World Bank Guidelines on the Legal Treatment of Foreign Investment¹⁸² and in the case law of

¹⁷⁹This assumes that compensation should continue to be payable in respect of lawful expropriations. This proposition has been disputed by some commentators and by certain states but will not be discussed further here given the focus of this chapter on determining how public interest considerations can be taken into account when a remedy is awarded.

¹⁸⁰Francesco Francioni, 'Compensation for Nationalisation of Foreign Property: The Borderland of Law and Equity' (1975) 24 Intl & Comp LQ 255, 258; Sergey Ripinsky with Kevin Williams, *Damages in International Investment Law* (British Institute of International and Comparative Law 2008) 77.

¹⁸¹Ian Brownlie, *Principles of Public International Law* (6th edn, OUP 2003) 513.

¹⁸²World Bank, *Report to the Development Committee on the Legal Framework for the Treatment of Foreign Investment introducing the World Bank Guidelines on the Treatment of Foreign Direct Investment*, 31 ILM 1363, 1376 (1992), guideline IV(10).

the Iran-US Claims Tribunal¹⁸³ and of the European Court of Human Rights. In particular, the European Court of Human Rights has granted compensation at an amount less than the fair market value of the property immediately prior to the taking where non-discriminatory, large-scale social reforms entailing large-scale interference with private property rights have occurred.¹⁸⁴ For example, in *James v United Kingdom*,¹⁸⁵ which concerned a challenge to the acquisition of tenants of the freeholds of property for below market value under the Leasehold Reform Act 1967, the United Kingdom argued that the tenants should not be required to pay for the building, because the typical long lease required the tenant to maintain the property and, over the period of a long lease, the cost of maintenance would equal or exceed the cost of constructing from new. Hence, it was claimed that the owner had no moral claim to be compensated and that the legislation was introduced in order to secure greater social justice. The European Court of Human Rights accepted this argument and, in relation to the availability and amount of compensation, recognised that, where measures are introduced for legitimate public interest objectives including measures of economic reform and measures designed to enhance social justice, reimbursement of less than full market value may be justified.¹⁸⁶

This approach has the advantage of not significantly deviating from the fair market value standard, which brings with it the advantage of certainty (at least conceptually). However, this exception is very specific in nature and would be capable of being invoked only in rare circumstances. For example, one might believe that the Argentine gas and water concession cases would constitute perfect candidates for such an approach. However, while the takings which took place in those cases occurred against a background of severe economic and political instability (where unemployment had reached almost 25 per cent, one quarter of the population could not afford the minimum amount of food required to ensure their subsistence and per capita spending on social services had been reduced by 74 per

¹⁸³See *INA v Iran*, Award 13 August 1985, 8 Iran-US CTR 373, 378.

¹⁸⁴See William W Burke-White and Andreas Von Staden, 'Private Litigation in a Public Law Sphere: The Standard of Review in Investor-State Arbitrations' (2010) 35 *Yale J Intl L* 283, 310 for case references. See also Tom Allen, 'Liberalism, social democracy and the value of property under the European Convention on Human Rights' (2010) 59 *ICLQ* 1055.

¹⁸⁵Application No 8973/79, Judgment 21 February 1986, (1986) 8 *EHRR* 123.

¹⁸⁶*ibid*, para 54.

cent),¹⁸⁷ they still amounted to takings of specific investments as opposed to forming part of a scheme for large-scale social reform. Given the narrow parameters of this exception therefore, it is unlikely that it would be effective in allowing for public interest considerations to be taken into account.

A potentially more broad-ranging exception would be to specify that the fair market value valuation standard continues to be the primary or default standard for lawful expropriations but that the awarding of compensation of less than fair market value is not precluded where such is necessary to maintain a fair balance between the public interest and the protection of the investor's rights or to take account of all relevant circumstances including the purpose of the expropriation. As an example of this general approach, the SADC Model BIT suggests the following as a potential drafting option:

Fair and adequate compensation shall normally be assessed in relation to the fair market value of the expropriated investment immediately before the expropriation took place (“date of expropriation”) and shall not reflect any change in value occurring because the intended expropriation had become known earlier. However, where appropriate, the assessment of fair and adequate compensation shall be based on an equitable balance between the public interest and interest of those affected, having regard for all relevant circumstances and taking account of: the current and past use of the property, the history of its acquisition, the fair market value of the investment, the purpose of the expropriation, the extent of previous profit made by the foreign investor through the investment, and the duration of the investment.¹⁸⁸

This approach has the advantage of being based on the relative certainty of the fair market value standard while allowing the flexibility of deviating from that standard where the circumstances so require.

Finally, on the other end of the spectrum to the narrow exception which would permit deviation from the fair market value standard only in cases of non-discriminatory large-scale social or economic reform are provisions that potentially allow for the compensation payable in respect of lawful expropriations to be

¹⁸⁷Facts extracted from *LG&E Energy Corporation v Argentina*, ICSID Case No ARB/02/1, Award 25 July 2007, para 234.

¹⁸⁸SADC, ‘SADC Model Bilateral Investment Treaty Template with Commentary’ para 6.2 <<http://www.iisd.org/itn/wp-content/uploads/2012/10/sadc-model-bit-template-final.pdf>> accessed 19 March 2015.

disaggregated completely from the market value of the expropriated asset. Such provisions include those that require the compensation payable to be ‘fair and adequate’ or ‘appropriate, just or equitable’ without providing any further guidance as to how this should be assessed.¹⁸⁹ While reference to concepts such as fairness, justice and equity would seem, on the one hand, to give free rein to arbitrators to take account of public interest considerations in quantifying the compensation payable, it is submitted that such an approach, by failing to provide sufficient guidance to arbitrators, could equally lead to tribunals awarding compensation equating to the fair market value of the expropriated property. Indeed, the dangers of using amorphous standards already manifested itself during the NIEO debates in which the term ‘appropriate compensation’ as the standard of compensation applicable in respect of lawful expropriations received support from developing countries as the standard of compensation applicable in respect of lawful expropriations, the implication being that the compensation awarded would take into account the state of development of the country in question, but was simultaneously held out by capital-exporting nations as requiring the payment of full compensation to investors.¹⁹⁰

Somewhat similarly, it has been suggested that an ‘enrichment’ standard could be included in the text of new or renegotiated IIAs which would rank equally with the fair market value standard for the purposes of determining compensation in investment treaty disputes.¹⁹¹ The application of such a standard would be based on the equitable principle of unjust enrichment and would focus on what the host state has gained from the expropriation rather than on the loss suffered by the affected investor. However, as with provisions requiring ‘fair and adequate’ or ‘appropriate, just and equitable’ compensation to be awarded where a lawful expropriation has occurred, the lack of certainty as to the scope of the unjust enrichment principle in international law could lead (and, in fact, has led) to the principle being cited as justification for awarding full compensation to the claimant investor.¹⁹²

¹⁸⁹See for example UNCTAD, *Investment Policy Framework for Sustainable Development* (UNCTAD 2012) 52, para 4.5.2.

¹⁹⁰Irmgard Marboe, ‘Compensation and Damages in International Law and the Limits of “Fair Market Value”’ (2006) 7 *J World Investment & Trade* 723, 729.

¹⁹¹Mark Kantor, *Valuation for Arbitration* (Kluwer 2008) 104-05; Ana Vohryzek, ‘Unjust Enrichment Unjustly Ignored: Opportunities and Pitfalls in Bringing Unjust Enrichment Claims under ICSID’ (2009) 31 *Loy LA Intl & Comp L Rev* 501.

¹⁹²Christoph H Schreuer, ‘Unjustified Enrichment in International Law’ (1974) 22 *Am J Comp L* 281, 289. See also Ana Vohryzek, ‘Unjust Enrichment Unjustly Ignored: Opportunities and Pitfalls

Furthermore, since it is difficult (if not impossible) to place a monetary value on the ‘gain’ made by the host state as a result of regulatory actions, in particular in the case of measures introduced to effect large-scale public goods such as measures introduced for environmental or health-related purposes,¹⁹³ it is likely that the alternative of the fair market value standard would be applied in such cases. Thus, while the amount of unjust enrichment can be (and has been) taken into account as an equitable factor when applying both the fair market value standard and the full reparation principle and while the extent to which the host state was unjustly enriched can be relied on as evidence where there are difficulties in estimating the claimant’s loss,¹⁹⁴ it is submitted that inclusion of a separate ‘enrichment’ standard would not necessarily have the desired result of reducing the compensation payable to claimant investors where a lawful expropriation has occurred, particularly where that expropriation was indirect in nature.

Overall therefore, it is submitted that IIA negotiators and drafters should be cautious in completely disaggregating the compensation payable for lawful expropriations from the market value paradigm in order to take account of public interest considerations as disaggregation may not necessarily have such an effect and, moreover, would result in the loss of the certainty-related benefits associated with the fair market value standard. Instead, it is submitted that provisions that allow for deviation from the fair market value standard in exceptional circumstances are more likely to address the competing imperatives of conceptual certainty and affording sufficient flexibility to allow for public interest considerations to be recognised.

Having analysed in this section some possible provisions that could be included in new or renegotiated IIAs to address public interest considerations at the remedies stage, the next, and final, section of this chapter will consider how it is envisaged that an approach which allows for public interest considerations to be taken into account at the remedies stage (whether facilitated by equity or through the inclusion of appropriate language in the relevant IIA) would inter-relate with provisions that

in *Bringing Unjust Enrichment Claims under ICSID* (2009) 31 *Loy LA Intl & Comp L Rev* 501, 509 noting the varied ways in which the concept is applied in domestic law.

¹⁹³See *Sea-Land Service, Inc v Iran* (1984) 6 *Iran-US CTR* 149, 169-172. See also the facts in *Tecmed Tecnicas Medioambientales Tecmed SA v Mexico*, ICSID Case No ARB(AF)/99/2 and *Metalclad Corporation v Mexico*, ICSID Case No ARB(AF)/97/1.

¹⁹⁴Sergey Ripinsky with Kevin Williams, *Damages in International Investment Law* (British Institute of International and Comparative Law 2008) 129-34.

may potentially be included in new or renegotiated IIAs and that broadly aim at introducing a balancing of investor and host state interests into the investment treaty arbitration process, particularly at the merits stage.

5.3 Relationship between the remedies stage and reforms affecting earlier stages of the arbitration process

Since the taking into account of public interest considerations at the remedies stage is primarily aimed at taking account of public interest considerations that have not been taken into account either at all or sufficiently at the earlier stages of the arbitral process, this naturally gives rise to the question of how it is envisaged that the taking into account of public interest considerations at the remedies stage would relate to other public interest/sustainable development-related reforms that primarily affect the earlier stages of the arbitral process.¹⁹⁵ Examples of such reforms will be drawn from drafting options proposed in IPFSD,¹⁹⁶ in the IISD Model Agreement on Investment¹⁹⁷ and in the SADC Model BIT,¹⁹⁸ which collectively constitute the most prominent examples of model treaty templates which seek to promote foreign investment for sustainable development, which encompasses, amongst other things, recognition of public interest considerations in investment treaty arbitration.¹⁹⁹

In this regard, a distinction can be drawn between, on the one hand, reforms that would complement a balancing of interests at the remedies stage while not substantially affecting its sphere of operation and, on the other, reforms which would seem to reduce the need for such balancing.

¹⁹⁵Drawing examples from these model treaty templates is subject to the proviso that evaluating individual drafting options in isolation is difficult given that these templates envisage (to a greater or lesser extent) reform of the entire framework for addressing investor-state disputes.

¹⁹⁶UNCTAD, *Investment Policy Framework for Sustainable Development* (UNCTAD 2012).

¹⁹⁷IISD, 'IISD Model International Agreement on Investment for Sustainable Development' <https://www.iisd.org/pdf/2005/investment_model_int_agreement.pdf> accessed 19 March 2015.

¹⁹⁸SADC, 'SADC Model Bilateral Investment Treaty Template with Commentary' <<http://www.iisd.org/itn/wp-content/uploads/2012/10/sadc-model-bit-template-final.pdf>> accessed 19 March 2015.

¹⁹⁹Indeed, a number of such reforms have already been implemented in some more recent IIAs in recognition of the potential conflict between investor protections and public policy objectives: see generally Suzanne A Spears, 'Making way for the public interest in international investment agreements' in Chester Brown and Kate Miles (eds), *Evolution in Investment Treaty Law and Arbitration* (Cambridge University Press 2011). See also UNCTAD, *World Investment Report 2014: Investing in the SDGs: An Action Plan* (UNCTAD 2014) 116-18.

As an example of the former, reforms affecting the jurisdiction stage of the arbitral process such as the introduction of narrower definitions of ‘investment’, the removal of certain types of investment from the scope of protection of IIAs or the introduction of differentiation between different types of investment in terms of the extent of protection conferred,²⁰⁰ while potentially beneficial from a public interest/sustainable development perspective, do not directly go to the question of how investor and public interests can be, or should be, balanced.²⁰¹ Similarly, the inclusion of non-investment related policy objectives in the preambles of new or renegotiated IIAs²⁰² would accord with the rationale underlying the balancing of interests at the remedies stage, as it would emphasise that the promotion of development (rather than the promotion of the rights of investors as such) constitutes the ultimate purpose of IIAs. While such preambular statements could potentially influence the approach taken by tribunals at the merits stage as preambular statements form part of the context of the treaty for the purposes of interpretation,²⁰³ such statements would not obviate the need for a balancing of interests at the remedies stage.

On the other hand, reforms which either directly clarify or adjust the scope of the existing substantive rights granted to investors under IIAs or which directly affect the interpretation of such rights or, similarly, those reforms which introduce new carve-outs for measures taken in pursuit of legitimate social or economic policy objectives have greater potential to reduce the need for a balancing of interests at the remedies stage or to interfere with its sphere of operation. Examples of provisions which fall into this category include Article 5 of the IISD Model Agreement on Investment which stipulates that clarification should be inserted to ensure that the concept of ‘in like circumstances’ used in the context of non-discrimination standards requires an overall examination of the circumstances of the case, including its effects on third persons and the legal community and the aim

²⁰⁰See for example ‘SADC Model Bilateral Investment Treaty Template with Commentary’ 9-14 <<http://www.iisd.org/itn/wp-content/uploads/2012/10/sadc-model-bit-template-final.pdf>> accessed 19 March 2015; IISD, ‘IISD Model International Agreement on Investment for Sustainable Development’ 6-10 <https://www.iisd.org/pdf/2005/investment_model_int_agreement.pdf> accessed 19 March 2015.

²⁰¹Marek Jeżewski, ‘Development Considerations in Defining Investment’ in Marie-Claire Cordonier Segger, Markus W Gehring and Andrew Newcombe (eds), *Sustainable Development in World Investment Law* (Kluwer 2011) 233-34.

²⁰²See for example Free Trade Agreement between Canada and the Republic of Colombia, signed 21 November 2008, entered into force 15 August 2011, preamble.

²⁰³Vienna Convention on the Law of Treaties, art 31(2).

of the impugned measure²⁰⁴ and Article 7 of the IISD Model Agreement on Investment which stipulates that the concepts of fair and equitable treatment and full protection and security are included within the customary international law minimum standard of treatment of aliens and do not create additional substantive rights.²⁰⁵ Examples of ‘carve-out’ type provisions include a provision stipulating that non-discriminatory measures taken by a host state to comply with its international obligations under other treaties would not constitute a breach of the IIA²⁰⁶ and provisions which create a general exception for non-discriminatory measures taken in good faith and designed and applied to achieve certain public purposes such as measures taken to protect human, animal or plant life, public health, the environment or national security.²⁰⁷ Similarly, each of IPFSD, the IISD Model Agreement on Investment and SADC Model BIT suggest that, to avoid the expropriation clause imposing undue constraints on a state’s ability to regulate, criteria could be included in future or renegotiated IIAs to distinguish (to the extent possible) between, on the one hand, indirect expropriations and, on the other hand, legitimate regulation that does not require compensation.²⁰⁸ Such criteria could, for example, include a provision that specifies that *bona fide*, non-discriminatory regulatory measures that are designed and applied to protect or enhance legitimate public welfare objectives do not constitute indirect expropriations.²⁰⁹

²⁰⁴See also SADC, ‘SADC Model Bilateral Investment Treaty Template with Commentary’ art 4(2) <<http://www.iisd.org/itn/wp-content/uploads/2012/10/sadc-model-bit-template-final.pdf>> accessed 19 March 2015; Investment Agreement for COMESA Common Investment Area, signed 23 May 2007, art 17(2).

²⁰⁵See also UNCTAD, *Investment Policy Framework for Sustainable Development* (UNCTAD 2012) 51 which suggests that clarifications be inserted, with a view to giving interpretative guidance to arbitral tribunals, to the effect that the FET standard does not preclude states from adopting good faith regulatory or other measures that pursue legitimate policy objectives and that the investor’s conduct is relevant in determining whether the FET standard has been breached as is the host state’s level of development.

²⁰⁶See for example IISD, ‘IISD Model International Agreement on Investment for Sustainable Development’ art 25 <https://www.iisd.org/pdf/2005/investment_model_int_agreement.pdf> accessed 19 March 2015; SADC, ‘SADC Model Bilateral Investment Treaty Template with Commentary’ art 20 <<http://www.iisd.org/itn/wp-content/uploads/2012/10/sadc-model-bit-template-final.pdf>> accessed 19 March 2015.

²⁰⁷See for example Energy Charter Treaty, 2080 UNTS 95; 34 ILM 360 (1995), art 24; ASEAN Comprehensive Investment Agreement, signed 26 February 2009, entered into force 29 March 2012, art 17. See also Marie-Claire Cordonier Segger and Andrew Newcombe, ‘An Integrated Agenda for Sustainable Development in International Investment Law’ in Marie-Claire Cordonier Segger, Markus W Gehring and Andrew Newcombe (eds), *Sustainable Development in World Investment Law* (Kluwer 2011).

²⁰⁸UNCTAD, *Investment Policy Framework for Sustainable Development* (UNCTAD 2012) 43-45.

²⁰⁹*ibid.* See also IISD ‘IISD Model International Agreement on Investment for Sustainable Development’ art 8(I) <https://www.iisd.org/pdf/2005/investment_model_int_agreement.pdf> accessed 19 March 2015; SADC, ‘SADC Model Bilateral Investment Treaty Template with

Turning first to reforms which adjust or clarify existing substantive investor rights, such provisions, while indicating, by their tenor, that investor rights should not unquestioningly be accorded a broad scope, fundamentally do not make redundant the role of investment treaty arbitration tribunals in balancing investor and public interests. For example, Article 7 of the IISD Model Agreement on Investment does little to clarify the boundary between permissible and impermissible host state conduct given that the international minimum standard of treatment of aliens is as indeterminate as the FET standard itself²¹⁰ and given that the international minimum standard evolves over time.²¹¹ In the same way, the clarification to the ‘in like circumstances’ concept proposed by Article 5 of the IISD Model Agreement on Investment leaves open the question of the extent to which the enumerated factors should be considered. Therefore, in interpreting such provisions, it would still fall to the tribunal in question to balance investor and host state interests and to determine the standard of review to be applied in respect of host state conduct.²¹² Furthermore, it is open to question whether the introduction of ‘general exceptions’ clauses would necessarily afford host states greater freedom to regulate.²¹³ In particular, a problem arises in relation to applying general exceptions to minimum standards of treatment as, if a measure meets the requirements of a general exception provision (e.g. that it is necessary to meet one of the enumerated exceptions, that it was applied in a manner which would not constitute arbitrary or unjustifiable discrimination and that it does not constitute a disguised restriction on international investment),²¹⁴ it is difficult to envisage a situation in which it would have violated minimum standards of treatment in the first place.²¹⁵

Commentary’ art 6(7) <<http://www.iisd.org/itn/wp-content/uploads/2012/10/sadc-model-bit-template-final.pdf>> accessed 19 March 2015.

²¹⁰*Saluka Investments BV v Czech Republic*, UNCITRAL, Partial Award 17 March 2006, para 291. See also Stephan W Schill, ‘Fair and Equitable Treatment, The Rule of Law, and Comparative Public Law’ in Stephan W Schill (ed), *International Investment Law and Comparative Public Law* (OUP 2010) 152-54.

²¹¹See for example *Glamis Gold, Ltd. v United States*, UNCITRAL, Award 8 June 2009, para 616.

²¹²Suzanne A Spears, ‘The quest for policy space in a new generation of international investment agreements’ (2010) 13J Intl Economic L 1037, 1071-72.

²¹³Aaron Cosbey, ‘The Road to Hell? Investor Protections in NAFTA’s Chapter 11’ in Lyuba Zarsky (ed), *International Investment for Sustainable Development: Balancing Rights and Rewards* (Earthscan Press 2005) 165; Andrew Newcombe, ‘General Exceptions in International Investment Agreements’ in Marie-Claire Cordonier Segger, Markus W. Gehring and Andrew Newcombe (eds), *Sustainable Development in World Investment Law* (Kluwer 2011) 355-70.

²¹⁴These requirements are based on those contained in general exception clauses which are based on GATT, Article XX. Other general exception clauses contain different requirements for successful invocation: see Andrew Newcombe, ‘General Exceptions in International Investment Agreements’

Similarly, in accordance with the customary international law doctrine of ‘police powers’, it is arguably already the case that non-discriminatory regulatory measures that are designed and applied to protect or enhance legitimate public welfare objectives should not be considered to be expropriatory in nature. Thus, the inclusion of clarificatory language in new or renegotiated IIAs may not necessarily radically change the approach taken by tribunals in distinguishing between indirect expropriations and legitimate regulation and investment treaty arbitration tribunals would still be required to balance host state and investor interests.

Finally, even assuming that the introduction of such reforms would lead to a narrower interpretation of certain investor rights, the wide-ranging nature of other IIA rights could effectively defeat such interpretation. For example, if an umbrella clause is included in the relevant IIA, a broad interpretation of such clause could allow the claimant investors to use investment treaty arbitration in order to seek relief for any breach of an investment-related promise by the host state, independent of the nature of the obligation and independent of the nature of the breach, without having to rely upon another breach of the relevant IIA.²¹⁶ Similarly, unless it was specified that the MFN clause does not apply in respect of certain rights and unless all IIAs entered into by a particular state are simultaneously amended, reforms which purport to narrow the scope of such rights could potentially be rendered ineffective by the importation, via the MFN clause, of broader, ‘unreformed’, rights from other IIAs to which the state is party.

Thus, while it is, in reality, impossible to predict how provisions of the nature described above may affect the application or interpretation of substantive investor rights in future (and without discounting the possibility that provisions that better taken account of public interest considerations may be developed), there are grounds for suggesting that such provisions would not constitute a panacea in respect of the balancing of investor and host state interests and would not obviate the need for taking account of public interest considerations at the remedies stage. Furthermore, the effect of introducing such reforms would need to be carefully

in Marie-Claire Cordonier Segger, Markus W Gehring and Andrew Newcombe (eds), *Sustainable Development in World Investment Law* (Kluwer 2011) 355-70.

²¹⁵Andrew Newcombe, ‘The Use of General Exceptions in IIAs: increasing legitimacy or uncertainty?’ in Armand De Mestral and Céline Lévesque (eds), *Improving International Investment Agreements* (Routledge 2013).

²¹⁶The effect of an umbrella clause may be amplified where the underlying investor-state contract contains a stabilisation clause.

considered so as not to undermine the protection granted to investors by IIAs. For example, in the context of the FET standard, while there is a need to take public interest considerations into account, stipulating certain factors to be taken into account in determining whether the FET standard has been breached could potentially undermine its effectiveness as a bulwark against unfair or capricious decisions on the part of host state courts or administrative agencies.²¹⁷

5.4 Conclusion

In conclusion, in taking account of public interest considerations at the remedies stage, it is submitted that recourse to equity would enrich the valuation process as it may be used to guide tribunals in exercising their discretion in quantifying damages and in applying causation principles in a manner which takes account of public interest considerations and, in some cases, it may reinforce the doctrinal basis for doing so. Therefore, notwithstanding the overlap between the role of equity and the ‘normal’ discretion exercised by arbitrators in quantifying damages, it is submitted that arbitrators should avowedly adopt a more open attitude towards the application of equitable principles at the remedies stage of the arbitral process.²¹⁸ Inclusion of language in new or renegotiated IIAs that explicitly authorises the application of such principles by arbitrators could potentially assist in this regard. However, care should be taken in formulating any such wording to ensure that it, on the one hand, affords sufficient guidance to arbitrators and, on the other, does not inadvertently constrain the existing ability of arbitrators to take into account a broad range of considerations in quantifying damages. Similar issues arise when considering alternatives to the fair market value standard, albeit that the need for reform is perhaps more compelling given that there is limited capacity to take account of public interest considerations or to have recourse to equity within the parameters of the fair market value standard. Finally, while it is impossible to predict how suggestions for reform that are targeted at the merits stage may affect the application or interpretation of IIA rights, there are reasons to suggest that such

²¹⁷For a similar argument see Ioana Tudor, *The Fair and Equitable Treatment Standard in the International Law of Foreign Investment* (OUP 2008) ch 7.

²¹⁸For a similar argument see Thomas M Franck, *Fairness in International Law and Institutions* (OUP 1998) 79-80 arguing that, since the judicial process of the international legal system includes no jury, it is all the more urgent that judges themselves introduce an element of flexibility or fairness through the medium of equity.

provisions, if introduced in new or renegotiated IIAs, will not obviate the need for taking account of public interest considerations in the formulation of remedies.

Chapter 6: Conclusions

[W]ays must be found for arbitration of international investment disputes to become more sensitive to the need for governments to discharge their obligations under international human rights law, and to meet other legitimate public interest objectives, even as they ensure investor protection.¹

This quotation from an article by Professor John Ruggie encapsulates perhaps the most significant issue that falls to be addressed in order for investment treaty arbitration and IIAs to continue to operate as an effective means of protecting foreign investment. Implicit in this statement is recognition that, although entering into an IIA constitutes a commitment by each of the contracting states to limit the exercise of some of its sovereign rights (including potentially its right to regulate in the public interest), the making of this commitment by states cannot be taken to mean that public interest considerations are irrelevant in resolving disputes between claimant investors and respondent host states under IIAs. Indeed, as the field of investment treaty arbitration has developed, the need to take account of public interest considerations in resolving disputes under IIAs has been increasingly acknowledged by both academic commentators and investment treaty arbitration tribunals. This is the case as it has become progressively clearer that a degree of balance between investor and host state interests is necessary not only to preserve host state regulatory autonomy in light of the open-ended nature of the rights typically conferred on investors by IIAs but also, crucially, to ensure the continued participation of states in the investment treaty arbitration system.

Furthermore, while a balancing of investor and public interests may seem more compatible with the characterisation of international investment law as a public law system, it is submitted that public interest considerations should be taken into account regardless of whether one characterises international investment law as forming part of public law or whether one views each IIA as a ‘private’, quasi-contractual arrangement between sovereign states. Thus, although agreement is

¹JG Ruggie, ‘Business and Human Rights: A Political Scientist’s Guide to Survival in a Domain where Lawyers and Activists Reign’ (2009) 6 *Transnational Dispute Management* 3.

unlikely to be reached at least in the near future as to the characterisation of international investment law (and the related issue of the suitability of arbitration as an adjudication model), an arguably more limited, but nonetheless important, consensus is emerging as to the need for public interest considerations to be taken into account in resolving IIA disputes.

Against the backdrop of this incipient consensus however, the question of how such considerations should be taken into account remains a contentious one. This thesis has argued that public interest considerations can, and should, be taken into account at the remedies stage of the investment treaty arbitration process in a manner that complements the recognition of such considerations at the merits stage of the arbitral process. The remedies stage constitutes an interesting topic of enquiry in this regard for a number of reasons, not least because the manner in which remedies are shaped can be used to achieve different purposes or policy goals within a particular legal system.² In many senses therefore, remedies are more powerful than rights since, as encapsulated by the Latin maxim *ubi jus ibi remedium*, rights standing alone constitute simply an expression of social values. Remedies therefore define rights by providing specificity and concreteness to otherwise abstract values. Furthermore, remedies (and, in particular, the remedy of damages) potentially allow for a more nuanced reflection of interests than the black-or-white decision as to liability required in determining whether or not a particular right has been violated at the merits stage of the adjudicative process. However, despite the potential of the remedies stage in this regard and although, in recent years, both the operation of the remedies stage and the need to balance host state and investor interests as part of the investment treaty arbitration process have each separately received increasing attention in the academic literature, the interaction between public interest considerations and the remedies stage of the investment treaty arbitration has not previously been comprehensively addressed. In particular, the possible inter-relationship between the merits stage and the remedies stage in terms of taking account of such considerations has not been explored nor has the question of whether any doctrinal basis exists under the existing investment treaty regime for taking account of public interest considerations at the remedies stage been analysed.

²For an overview of the differing aims that can be pursued by remedies see Dinah Shelton, *Remedies in International Human Rights Law* (2nd edn, OUP 2005) 7-21.

One possible reason for this lacuna in the academic literature may be the focus of much of the literature on remedies on describing the mechanics of the valuation methods that are customarily applied in assessing damages as such a technical discussion does not easily facilitate consideration of more amorphous issues such as the balancing of host state and investor interests. This tendency is also evident in arbitral awards as investment treaty arbitration tribunals have, to date, generally not referred to public interest considerations at the remedies stage or purported to adjust the compensation or damages payable by respondent host states on the basis of such considerations. Furthermore, the predominant focus on the more technical aspects of the damages quantification process may have contributed to the perception of the remedies stage as being the ‘poor cousin’ of the jurisdiction and merits stage (at least from the perspective of lawyers).³ Thus, although an understanding of the valuation process is essential to any understanding of how damages are quantified, the bases for valuation and valuation methods customarily used in quantifying damages rank secondary in importance to the issue of the applicable legal standard of compensation. Furthermore, viewing the remedies stage through the prism of legal principles rather than from a technical standpoint has the advantage of allowing issues such as the balancing of host state and investor interests to come into sharper focus.

In considering the suitability of the remedies stage as a platform for public interest considerations, it is clear that justification reflecting the distinctive features of the investment treaty arbitration system is necessary. Thus, while, on the one hand, there is a need to introduce an element of reciprocity into the investment treaty arbitration process in order to ensure continuing state co-operation and to reflect the underlying purposes of IIAs, on the other, the primary object of the system remains the protection of foreign investors and the overall structure of IIAs and their dispute settlement provisions encourage application of the bilateral notion of corrective justice. Thus, in order to take account of these competing imperatives, it has been argued that an approach which takes account of public interest considerations at the remedies stage where such considerations cannot be taken into account either sufficiently or at all at the merits stage of the arbitration process is desirable. This

³Thomas Wälde and Borzu Sabahi, ‘Compensation, Damages and Valuation’ in Peter Muchlinski, Federico Ortino and Christoph Schreuer (eds), *The Oxford Handbook of International Investment Law* (OUP 2008) 1049.

approach contrasts with an approach which would allow public interest considerations that are considered insufficient to override investor rights at the merits stage to subsequently be considered *de novo* in quantifying damages, which, it has been argued, would not be consonant with the nature and functions of the investment treaty arbitration system and would likely lead to rights dilution. Bearing these guiding principles in mind, a number of specific situations in which recognition of public interest considerations at the remedies stage may be appropriate have been identified: first, where the impugned host state measure was taken in furtherance of the host state's obligations under a non-investment related treaty or in furtherance of the fundamental rights provisions contained in the host state's highest law; secondly, where the customary international law defence of necessity has been successfully invoked and, finally, in the case of certain breaches of a procedural nature.

Thus, where a host state can either only comply with its obligations under another non-investment related treaty (such as a human rights treaty) by failing to comply with an IIA (or *vice versa*) or where the goals of one of these treaties frustrates the goals of another treaty without strict incompatibility between their provisions (i.e. where a direct treaty conflict occurs), the fact that the host state had an obligation to, for example, regulate to protect certain human rights should undoubtedly be considered at the merits stage. Fundamentally however, such a direct treaty conflict is not capable of being resolved at the merits stage since it involves a direct collision of obligations. In such circumstances, taking account of the purpose of the impugned host state measures at the remedies stage would introduce a necessary element of reciprocity in that it would recognise the host state's attempt to observe its non-investment related treaty obligations as well as taking into account the capacity of, and obligation on, potential investors to apprise themselves of the socio-economic circumstances of the host state. Similarly, where the impugned host state measures were introduced in furtherance of the fundamental rights provisions contained in the host state's highest law (such as its constitution), to disregard the purpose for which the measure was introduced would fail to introduce a necessary element of reciprocity into the investment treaty arbitration process, given the importance of those norms within the host state's domestic legal framework.

Secondly, where the host state has successfully invoked the defence of necessity, two competing imperatives exist: on the one hand, the fact that the host state has chosen to act in contravention of its obligation to protect foreign investors (albeit in circumstances of social and economic collapse) and, on the other, the fact that reconciliation of the host state's competing obligations or interests may not be possible in such circumstances and that the host state acted in order to protect crucial state interests. Accordingly, given that IIAs are intended to protect foreign investors in difficult situations and the status of the defence as a secondary rule of customary international law, it is submitted that reconciliation of these competing imperatives should most appropriately occur at the remedies stage.

Finally, turning to the question of procedural breaches, while, on the one hand, it is important to recognise the value of procedural guarantees from a rule of law perspective, on the other, in circumstances where the procedural irregularities in question are of a less egregious nature and where countervailing factors exist, the justification for compensating the investor for all the loss it has suffered is less compelling. Accordingly, it is submitted that a 'sliding scale' approach in respect of quantification of damages that takes account of factors such as the degree of interference with the investor's interests, the nature and intensity of the procedural breach, the public purpose being pursued and the likelihood that the substantive outcome would have been the same in the absence of the breach should be considered. In particular, it is submitted that this 'sliding scale' approach, in allowing sufficient flexibility for both the nature of the interests underlying the host state's conduct and the nature of the investor's interest or expectation to be taken into account, could prove to be particularly suitable in respect of breaches relating to frustration of a claimant investor's legitimate expectations, given the broad range of conduct covered by that concept.

These circumstances do not constitute an exhaustive list of situations in which public interest considerations may fall to be considered at the remedies stage. However, they are all based on a common premise: namely that, in some cases, the fact that the host state acted in pursuance of a *bona fide* public purpose in introducing the measures challenged under an IIA may need to be considered at the remedies stage as this fact may not be capable of being considered sufficiently at

the merits stage so as to ensure an optimal balance between investor protection and host state regulatory sovereignty. This premise equally applies in respect of expropriations (and in particular lawful expropriations), notwithstanding the focus of the expropriation clause on the loss caused by governmental conduct rather than on the nature of that conduct.

While the normative arguments made in favour of taking account of public interest considerations at the remedies stage stand apart from the legal principles applicable in quantifying damages and while doctrinal difficulties should not, in principle, detract from such arguments, it is nonetheless important to consider whether there is a doctrinal basis for taking account of public interest considerations at the remedies stage under existing IIAs or whether treaty reform would be required in order to do so. In this regard, although the full reparation principle, in requiring that the victim be placed in the same position it would have been in had the wrongdoing not occurred, initially appears rather clear-cut and unaccommodating towards public interest considerations, in fact application of the principle requires significant discretionary judgment. This ‘normal’ discretion, the exercise of which is always necessary,⁴ may, in appropriate circumstances, be enhanced through the application of equity as, although there is undoubtedly an overlap between the two concepts, it is submitted that the dynamism of equity confers on it an additional capacity to enlighten the exercise of arbitral discretion and, in some cases, to reinforce the doctrinal basis for taking into account public interest considerations at the remedies stage. Therefore, the application of equity combined with the application of customary valuation methods and of causation principles (which are themselves necessarily influenced by equity) affords sufficient flexibility to tribunals to take account of public interest considerations in quantifying damages. Effectively this means that, since equity can be invoked without the need for an explicit reference to equity or equitable principles in the relevant IIA and without the tribunal resolving the dispute *ex aequo et bono*, investment treaty arbitration tribunals already possess the tools required in order to take account of public interest considerations in the formulation of remedies for unlawful acts.

⁴Meriam N Alrashid, ‘The Arbitral Tribunal’s Discretion in Quantifying Damages’ in Ian A Laird, Borzu Sabahi, Frédéric G Sourgens and Todd Weiler (eds), *Investment Treaty Arbitration and International Law Volume 8* (Juris 2015) 333.

Accordingly, given the degree of flexibility currently afforded to tribunals by the customary international law principle of full reparation and the conceptual certainty associated with that principle, it is submitted that treaty negotiators should be cautious in deviating from the current approach whereby IIAs are generally silent as to the approach to be taken to remedying unlawful acts. Similar considerations come into play in considering alternatives to the fair market value standard for quantifying the compensation payable for lawful expropriations, albeit that the need for treaty reform is greater than in respect of unlawful acts given that the objective fair market value standard is not, in itself, accommodative of public interest considerations.

Overall therefore, the question of whether, and in what circumstances, the taking into account of public interest considerations at the remedies stage of the investment treaty arbitration process (and, in particular, in the quantification of the damages payable) should occur is potentially a bold one. Indeed, the question is somewhat reminiscent of proposals during the NIEO debates for the compensation payable in cases of expropriation to be determined in accordance with the laws of the nationalising state (thereby potentially allowing states to abrogate entirely their responsibility to pay compensation).⁵ However, despite the potentially bold or controversial nature of the question, the answer proposed by this thesis is arguably of a modest nature as, first, it assumes that the procedural framework for investment treaty arbitration and its focus on investment protection will remain unchanged and, secondly, it proposes that the remedies stage should complement rather than displace the merits stage in taking account of public interest considerations. Thus, it is proposed that public interest considerations should be taken into account in quantifying damages in certain circumstances only and that substantial derogation from the spirit of the full reparation principle is not necessarily required in order to implement such an approach.

The ‘modest’ nature of the proposal is driven by the fact that states have, as an exercise of sovereignty, entered into IIAs and in doing so have ceded part of their regulatory sovereignty as, fundamentally, the remedies granted within such a

⁵See ‘General Assembly Resolution on Permanent Sovereignty over Natural Resources’, GA Res 3171, 17 December 1973 (1974) 13 ILM 238; ‘Declaration on the Establishment of a New International Economic Order’ GA Res 3201, 1 May 1974 (1974) 13 ILM 715, 717; ‘Charter of Economic Rights and Duties of States’ GA Res 3281, 12 December 1974 (1975) 14 ILM 251.

system must reflect that reality as well as the single-minded purpose of the system. Nevertheless, it is submitted that, within the parameters of the investment treaty arbitration system, this proposal would lead to a more nuanced reflection of public interest considerations than the ‘all or nothing’ decision as to liability required at the merits stage in determining whether a breach has occurred or not.

Of course, the question of how the proposals put forward in this thesis would relate to other public interest/sustainable development-related reforms affecting either the jurisdiction or merits stage of the arbitral process (and which are likely to become an increasing feature of IIAs over the coming years) remains open to question. However, there are grounds to suggest that the interpretation of the IIA text by individual tribunals will remain crucial in maintaining an optimal balance between investor protection and host state regulatory sovereignty even for this ‘new generation’ of IIAs and that the need for public interest considerations to be reflected at the remedies stage will continue to exist. In particular, although certain reforms aimed at clarifying or adjusting the scope of existing IIA rights could potentially reduce the need for public interest considerations to be taken into account at the remedies stage, such reforms may not obviate that need and the introduction of such reforms must always tread the thin line between ensuring that the protection conferred on investors by IIAs is not undermined and simultaneously ensuring that host state interests are effectively taken into account. This reflects the tension between investment protection and host state regulatory sovereignty which constitutes (and will continue to constitute) an inherent feature of the international investment law regime.

Thus, while the proposals put forward in this thesis cannot, and do not purport to, constitute a complete solution to the problem of how to reconcile these competing interests, it is submitted that they do constitute a part of the answer to Professor Ruggie’s appeal to find ways to make the investment treaty arbitration system more sensitive to the needs of governments and to the public interest, while still ensuring that its principal beneficiaries – foreign investors – are effectively protected. This conclusion does not mean that more wide-ranging reforms of the investment treaty arbitration system cannot, or should not, occur. However, it is to argue that ‘system-internal’ reforms must be considered in conjunction with more wide-ranging reforms so as to ensure that, as the investment treaty arbitration regime matures and

external forces shape its contours, the baby is not thrown out with the proverbial bathwater.

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(c) *Other International Cases and Arbitration Awards*

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Sea-Land Service, Inc v Iran, Award 22 June 1984, 6 Iran-US CTR 149

(d) *Domestic Case Law*

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Parsons & Whittemore Overseas Co. Inc. v Société Générale de l'Industrie du Papier RAKTA and Bank of America, 508 F. 2d 969 (2nd Cir, 1974)

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Agreement between the Federal Republic of Germany and the Republic of the Philippines for the Promotion and Reciprocal Protection of Investments, signed 18 April 1997, entered into force 1 February 2000

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Agreement between the Republic of the Philippines and the Swiss Confederation on the Promotion and Reciprocal Protection of Investments, signed 31 March 1997, entered into force 23 April 1999

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Agreement on economic cooperation between the Government of the Kingdom of the Netherlands and the Government of the Republic of Singapore, signed 16 May 1972, entered into force 7 September 1973

Agreement on encouragement and reciprocal protection of investments between the Kingdom of the Netherlands and the Argentine Republic, signed 20 October 1992, entered into force 1 October 1994

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May 1969, entered into force 27 January 1980