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The Law of Investment Treaties

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5

The General Structure of Investment Treaties

5.1 A Structural Overview

An investment treaty is an agreement embodied in one or more written documents by which two or more states agree to certain legal rules to govern investments undertaken by nationals of one treaty party in the territory of another treaty party.[1] A treaty is an instrument of international law that binds the contracting states. Although the specific provisions of individual investment treaties are not uniform and some investment treaties restrict host country governmental action more than others, virtually all investment treaties address the same issues and they generally follow a similar structure. Despite variations in language from treaty to treaty, the investment treaty movement discussed in Chapter 4 has resulted in a detailed definition of what an investment treaty should contain, the development of common legal concepts and rules, and the creation of an agreed-upon legal framework for the protection of foreign investment. If the approximately 3,000 individual investment treaties negotiated over the last six decades constitute a single, integrated global regime for investment, it is because of the strong commonality among them.

To begin with, all investment treaties have a title and preamble. The title usually states the general aim of the treaty and, if it is a bilateral agreement, identifies the parties to it, for example 'Agreement between the Government of the United Kingdom of Great Britain and Northern Ireland and the Government of the Republic of Albania for the Promotion and Protection of Investments'.[2] The title of a multilateral investment treaty usually states its nature but not the names of the parties to it, for example, 'The Energy Charter Treaty'.[3] As noted

[1] Article 1(1)(a) of the Vienna Convention on the Law of Treaties states: '"[T]reaty" means an international agreement concluded between States in written form and governed by international law, whether embodied in a single instrument or in two or more related instruments and whatever its particular designation.' Vienna Convention on the Law of Treaties (adopted 22 May 1969, entered into force 27 January 1980); 1155 UNTS 331; 8 ILM 679; UN Doc A/Conf.39/27 (VCLT).

[2] Agreement between the Government of the United Kingdom of Great Britain and Northern Ireland and the Government of the Republic of Albania for the Promotion and Protection of Investments (30 March 1994), Treaty Series No 17 (1996).

[3] The Energy Charter Treaty (17 December 1994), (1995) 34 ILM 360 (ECT).

previously, the precise designation or title given to a treaty does not affect its status as a binding international agreement.

Directly after the title, an investment treaty normally contains a preamble in which the parties state the aims and purposes of the treaty. While neither the title nor the preamble impose legal obligations, they may be relevant to the interpretation of a treaty's substantive provisions. Article 31(1) of the Vienna Convention on the Law of Treaties[4] provides that '[a] treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in light of *its object and purpose*'(emphasis added). Accordingly, an important source for determining a treaty's objects and purposes is its title and preamble.[5]

An investment treaty usually consists of a single document. However, the parties may use an exchange of letters or separate protocols to explain, modify, or elaborate on certain treaty provisions. For example, an investment treaty may provide that it applies to 'companies controlled by nationals of the other state Party', and a subsequent exchange of letters between the countries' foreign ministers or ambassadors may define in detail the meaning of 'control'.[6] Such documents are considered an integral part of the treaty and have the same binding effect as the treaty text. They are often published as an annex to the treaty in the contracting states' official publications.

With regard to its substantive provisions, the basic structure of most modern investment treaties encompasses at least nine topics:

1. Definitions and Scope of Application
2. Conditions for the Entry of Foreign Investment and Investors
3. General Standards of Treatment of Foreign Investments and Investors
4. Monetary Transfers
5. Expropriation and Dispossession

[4] VCLT (n 1 above).

[5] In the ICSID case of *LG&E Energy*, for example, the tribunal in considering the context within which Argentina and the United States included the fair and equitable treatment standard, and its object and purpose, observed in ¶ 124 that:

> in the Preamble of the Treaty . . . the two countries agreed that 'fair and equitable treatment of investment is desirable in order to maintain a stable framework for investment and maximum effective use of economic resources.' In entering the Bilateral Treaty as a whole, the parties desired to 'promote greater economic cooperation' and 'stimulate the flow of private capital and the economic development of the parties'. In light of these stated objectives, this Tribunal must conclude that stability of the legal and business framework is an essential element of fair and equitable treatment in this case, provided that they do not pose any danger for the existence of the host State itself.

LG&E Energy Corp v Argentine Republic, ICSID Case No ARB/02/1 (Decision on Liability) (3 October 2006).

[6] See eg the letters annexed to the Agreement between the Government of the French Republic and the Government of the Republic of Argentina on the Reciprocal Encouragement and Protection of Investment (3 July 1991; Journal Officiel du 5 juin 1993, 8164).

6. Operational and Other Conditions
7. Losses from Armed Conflict or Internal Disorder
8. Treaty Exceptions, Modifications, and Terminations
9. Dispute Settlement.

This chapter briefly examines the content of these topics in order to provide a general understanding of investment treaty structure. Subsequent chapters will discuss treaty provisions on each topic in depth and, to the extent possible, consider how courts, arbitration tribunals, and governments have interpreted and applied them.

5.2 Scope of Application of Investment Treaties

The key elements in any investment treaty are its provisions defining the treaty's terms and its scope of application, that is, the persons, organizations, and investments that may benefit from the treaty. Persons, organizations, or investments that falls outside a treaty's terms or scope of application are not entitled to the benefit of its provisions. Thus, if a particular enterprise in a host country lies within the definition of 'investment' in an investment treaty, that enterprise may take advantage of the treaty's privileges and benefits, as well as its enforcement mechanism. If not, then it may not take advantage of the treaty.

Definitions of treaty terms and rules on scope of application are generally found at the beginning of the treaty in sections defining 'investors', 'companies', 'nationals', 'investments', and 'territory'.[7] As a result of entering into an investment treaty, a contracting state owes obligations only to the investors of contracting states who make investments in its territory. Conversely, a contracting state has no obligation to persons or investments that do not come within the definitions of these terms as defined in the treaty document.

In defining the nature of covered investments, most investment treaties take four basic considerations into account: (1) the form of the investment; (2) the area of the investment's economic activity; (3) the time when the investment is made; and (4) the investor's connection with the other contracting state. Chapter 7 will explore these terms in considerable detail. Most investment treaties define the concept of investment broadly so as to include various investment forms: tangible and intangible assets, property, and rights. This

[7] See eg Agreement for the Liberalization, Promotion and Protection of Investment, Japan–Vietnam (14 November 2003), Art 1 (defining 'investor', 'investments', and 'Area'); Treaty Concerning the Reciprocal Encouragement and Protection of Investment (US–Czech Republic) (22 October 1991), Art 1(a)–(b) (defining 'investment' and 'company of a Party'); Treaty concerning the Reciprocal Encouragement and Protection of Investments (US–Turkey) (3 December 1985), Art 1(a), (c), (e) (defining 'company', 'Investment', and 'national').

approach gives the term 'investment' a broad, non-exclusive definition and recognizes that investment forms are constantly evolving in response to the creativity of investors and the rapidly changing world of international finance. The effect is to provide a potentially expanding umbrella of protection to investors and investments.

Another issue faced in investment treaty negotiation is whether investments made prior to the treaty will benefit from its provisions. Developing countries have sometimes sought to limit a treaty's application to future investment only or at least to those investments made in the relatively recent past.[8] Viewing the treaty primarily as an investment promotion mechanism, they claim to see little purpose in granting additional protections to investments already made in the host country. Moreover, they argue that their governments might not have approved such investments if they had realized an investment treaty would later expand the investor's rights and privileges.[9] Capital-exporting states, on the other hand, have generally sought to protect all investments made by their nationals and companies, regardless of when they were made.

Most investment treaties also seek to provide continued protection to investors even after a host country has terminated or withdrawn from the treaty. These continuing effects provisions protect investors who have made investments based on the expectation of treaty protection. The usual period of continued protection is between fifteen and twenty years.

Defining which investors can benefit from the treaty is an important issue, since the goal of the contracting state is to secure benefits for its own nationals, companies, and investors, rather than those of other countries. The problem is essentially one of determining what links need to exist between an investor and a party to a treaty for the investor to benefit from the treaty's provisions. In the case of physical persons, the task is not difficult, since virtually all investment treaties rely on a status that generally is easily determined, such as nationality or citizenship. For investors that are companies or other legal entities, the problem of determining an appropriate link with a contracting state becomes more complex. Such legal forms may be created and owned by persons who have no real connection with the countries that are parties to the treaty. In particular, three types of cases raise problems in this respect: (1) companies organized in a treaty country by nationals of a non-treaty country; (2) companies organized in a non-treaty country by nationals of a treaty country; and (3) companies in which nationals of a non-treaty country hold a substantial interest. For a company to be covered by the treaty, most BITs require that a treaty partner at least be one

[8] See eg Agreement for the Promotion and Protection of Investments (UK–Indonesia) (27 April 1976), Art 2(3) ('The rights and obligations of both Contracting Parties with respect to investments made before 10 January 1967 shall be in no way affected by the provisions of this Agreement'). [9] UNCTAD, *Bilateral Investment Treaties in the Mid-1990s* (1998) 42.

of the following: (1) the country of the company's incorporation;[10] (2) the country of the company's seat, registered office, or principal place of business;[11] or (3) the country whose nationals have control over, or a substantial interest in, the company making the investment.[12] Sometimes these requirements are combined so that an investing company must satisfy two or more to qualify for coverage under a particular investment treaty.

5.3 Conditions for the Entry of Foreign Investment and Investors

Virtually all investment treaties deal with the entry or establishment of investments emanating from treaty partners. A few treaties, like the European Union Treaty, grant investors from EU states the right of establishment in all other EU states. Most investment treaties, however, allow each member state some control over the extent of investments in their territories by investors from treaty partners. Related to the issue of the entry or establishment of investment is the ability of the host country to impose conditions on that entry. One type of condition that host countries often impose on the making and operation of foreign investments is a 'performance requirement' or 'trade-related investment measure' (TRIM). Such conditions may require an investment project, as a condition of entry, to export a certain proportion of its production, restrict its imports to a certain level, or purchase a minimum quantity of local goods and services. Although most investment treaties have not dealt with the question of performance requirements,[13] the United States, with some success, has sought to

[10] See eg Treaty Concerning the Encouragement and Reciprocal Protection of Investment (US–Sri Lanka) (20 September 1991), Art 1(b) ('"[C]ompany" of a Party means any kind of corporation, company, association, partnership or other organization, legally constituted under the laws and regulations of a Party or a political subdivision thereof'). BITs concluded by Denmark, the Netherlands, the United Kingdom, and the United States are frequently of this type. See UNCTAD (n 9 above) 39.

[11] See eg Treaty between the Federal Republic of Germany and the Kingdom of Swaziland Concerning the Encouragement and Reciprocal Protection of Investments (5 April 1990), Art 1(4)(a) ('The term "companies" means ... in respect of the Federal Republic of Germany: any juridical person as well as any commercial or other company or association with or without legal personality having its seat in the German area of application of this Treaty, irrespective of whether or not its activities are directed at profit'). BITs concluded by Belgium, Germany, and Sweden are frequently of this type. UNCTAD (n 9 above) 40.

[12] See eg Agreement on Encouragement and Reciprocal Protection of Investments (Lithuania–Netherlands) (26 January 1994), Art 1(b)(iii):

> The term 'investor' shall comprise with regard to either contracting party: ... (iii). legal persons not constituted under the law of that Contracting Party but controlled, directly or indirectly, by natural persons as defined in (i) [of the Contracting Party's nationality] or by legal persons as defined in (ii) [legal persons constituted under the law of the Contracting Party] above, who invest in the territory of either Contracting Party.

'Ownership or control', as these provisions are called, is used in BITs concluded by the Netherlands, Sweden, and Switzerland. UNCTAD (n 9 above) 39.

[13] UNCTC, *Bilateral Investment Treaties* (1988) 69.

protect its investors from them through its BIT negotiations,[14] as well as through the North American Free Trade Agreement.

5.4 General Standards of Treatment of Foreign Investments and Investors

The totality of obligations that a host country owes a foreign investor or investment is generally referred to as the *treatment* owed to the investor or the investment. The word 'treatment' has thus become a term of art in investment treaties and investor–state arbitration. Investment treaties stipulate the standard of treatment a host country must accord to a foreign investment in two respects. They define certain *general* standards of treatment and also state *specific* standards for particular matters such as monetary transfers, the seizure of investment property, the employment of foreign personnel, and the resolution of disputes with the host government. In addition, some general standards, such as guarantees of full protection and security or fair and equitable treatment, are absolute in nature. Others, such as national treatment and most-favoured-nation treatment, are considered contingent or relative because their application depends on the treatment accorded by the state to other investors.

One may identify six general standards of treatment: (a) fair and equitable treatment; (b) full protection and security; (c) protection from unreasonable or discriminatory measures; (d) treatment no less than that accorded by international law; (e) the requirement to respect obligations made to investors and investments; and (f) national and/or most-favoured-nation treatment. An individual investment treaty may provide for some or all of these treatment standards. Each treatment standard is considered briefly below but will be explored in greater depth in subsequent chapters.

(a) Fair and equitable treatment

One of the most common standards of treatment found in investment treaties is an obligation that the host country accord foreign investment 'fair and equitable treatment'.[15] A common statement in international law, the phrase has been the subject of much commentary and state practice.[16] Nonetheless, its precise meaning in specific situations has been open to varying interpretations. A vague and ambiguous expression on its face, the term 'fair and equitable' is not

[14] See eg Treaty Concerning the Encouragement and Reciprocal Protection of Investment, (US–Albania) (11 January 1995), Art VI (prohibiting four specified types of performance requirements).

[15] MI Khalil, 'Treatment of Foreign Investment in Bilateral Investment Treaties' (1992) 7 ICSID Rev—FILJ 339, 351.

[16] UNCTC, *Bilateral Investment Treaties*, UN Doc ST/CTC/65 (1988) 41–5.

defined in investment treaties even though virtually all such treaties include it as a mandatory standard of treatment. It has been interpreted in a large number of arbitral awards and has been extensively analysed by scholars. Indeed, it is invoked so often in contemporary investor–state arbitration that one observer has labelled it 'an almost ubiquitous presence' in investment litigation.[17]

(b) Full protection and security

Another general standard of treatment found in most investment treaties is the obligation of the host country to accord 'full protection and security' or 'constant protection and security' to investments made by nationals and companies of its treaty partners. Here too, the precise meaning of the term may be open to widely varying interpretations in different situations. Consequently, courts, including the International Court of Justice, and arbitration tribunals have struggled to determine the proper scope of its protection. Cases interpreting this treaty standard have held that it does not make the host country responsible for all injuries that befall the investment.[18] Thus, although the host country is not a guarantor, it is liable when it fails to show due diligence in protecting the investor from harm. One definition of due diligence that was cited favourably by an ICSID arbitral tribunal is 'reasonable measures of prevention which a well-administered government could be expected to exercise under similar circumstances'.[19] Consequently, the failure by a host government to take reasonable measures to protect the investment against threats, such as attacks by brigands or violence by police and security officers, renders that government liable to compensate an investor for resulting injuries.

(c) Unreasonable or discriminatory measures

Many investment treaties provide protection promising that 'no Contracting Party shall in any way impair by unreasonable or discriminatory measures the management, maintenance, use, enjoyment or disposal' of an investment.[20] The

[17] R Dolzer, 'Fair and Equitable Treatment: A Key Standard in Investment Treaties' (2005) 39 Int'l Lawyer 87.

[18] cf *Asian Agricultural Products Ltd v Sri Lanka*, ICSID Case No ARB/87/3 (Final Award) (27 June 1990) (1991); 6 ICSID Rev—FILJ 526 (interpreting the words 'full protection and security' in the UK–Sri Lanka BIT), and *Elettronica Sicula SPA (US v Italy)* 1989 ICJ 15 (20 July) (interpreting the words 'constant protection and security' in the US–Italy Treaty of Friendship, Commerce and Navigation).

[19] *Asian Agricultural Products Ltd v Sri Lanka*, ICSID Case No ARB/87/3 (Final Award) (27 June 1990) (1991); 6 ICSID Rev—FILJ 558, citing AV Freeman, *Responsibility of States for Unlawful Acts of Their Armed Forces* (1957) 15–16.

[20] See eg Treaty concerning the Reciprocal Encouragement and Protection of Investment, (US–Turkey) (3 December 1985), Art 2(3) ('Neither Party shall in any way impair by arbitrary or discriminatory measures the management, operation, maintenance, use, enjoyment, acquisition, expansion, or disposal of investments').

specific application of this provision to the individual case depends on the facts involved; however, it is worth noting that the term 'unreasonable' may give host countries significant grounds to defend actions taken against foreign investors.

(d) International law

Many investment treaties provide that in no case should foreign investments be given less favourable treatment than that required by international law. Thus, this provision constitutes the minimum international standard of treatment discussed in Chapter 3. The application of this principle in individual cases is subject to a variety of interpretations, particularly on issues where there is significant dispute among developing countries. One example is the efforts made by developing countries to secure a New International Economic Order, discussed in Chapter 4. A further question is whether the reference to 'international law' is limited only to customary international law or if it includes treaty provisions and general principles on investments.

(e) State obligations

To the extent that a contracting party has entered into obligations with an investor or investment, many investment treaties require a signatory state to respect those obligations. These provisions, then, act as counter to the claim, advanced during the era of the New International Economic Order, that host countries should be able to unilaterally revise contracts that they have made with foreign investors. It may also mean that, as a result of such a provision in an investment treaty, the state has an obligation under international law to respect contracts between foreign investors and host governments that are otherwise normally subject to only host country law.[21]

(f) National and/or most-favoured-nation treatment

In addition to these general standards, many investment treaties contain relative standards, particularly with respect to non-discrimination in relation to both foreign and national investors. They thus provide for *national treatment*, which requires that a host country treat an investor, or an investment, no less favourably than they treat their own national investors or investments made by their own nationals. They may also provide for *most-favoured-nation treatment*, which means that a host country may not treat an investor or investment from an investment treaty party less favourably than its own investors or investments from any other country. National treatment allows protected foreign investors to take advantage of any benefits that a host country grants to

[21] UNCTAD (n 9 above) 56–7.

its own nationals. Some developing countries, recognizing the disparity in financial and technological resources between their national enterprises and those of foreign companies, have resisted or sought to limit the scope of the national treatment guarantee in investment treaties. In particular, they have tried to avoid giving foreign investors benefits and subsidies designed to strengthen national industries.[22]

Most-favoured-nation treatment, on the other hand, has the effect of granting to protected foreign investors any benefit or advantage granted by the host country to investors from any third country. They thus enable such investors to take advantage of the higher standards of investor protection that may be contained in investment treaties to which the host country is a party.

Certain investment treaties, like those negotiated by the United States, combine both of these standards and require host countries to grant investors national treatment or most-favoured-nation treatment, *whichever is the more favourable.*

5.5 Monetary Transfers

For any foreign investment project, the ability to repatriate income and capital, to pay foreign obligations in another currency, and to purchase raw materials and spare parts from abroad are crucial to a project's success. For this reason, in investment treaty negotiations capital-exporting states have pressed for unrestricted freedom for their investors to undertake these monetary operations. Such operations are collectively referred to as 'transfers'.[23] Like the word 'treatment', 'transfer' also has become a term of art in investment treaties and basically means 'monetary transfers'. The monetary transfer provisions of most investment treaties deal with five basic issues: (1) the general nature of the investor's rights to make monetary transfers; (2) the types of payments that are covered by the right to make transfers; (3) the currency with which the payment may be made; (4) the applicable exchange rate; and (5) the time within which the host country must allow the investor to make transfers.

Developing countries facing chronic balance-of-payments difficulties and needing to conserve foreign exchange to pay for essential goods and services are often unable or unwilling to grant foreign investors an unrestricted right to make such monetary transfers. Moreover, many developing countries have exchange-control laws to regulate the conversion and transfer of currency abroad.[24] As a result of this fundamental conflict in goals, the negotiation of

[22] ibid 64–5. [23] Khalil (n 15 above) 360.
[24] JW Salacuse, 'Host Country Regulation and Promotion of Joint Ventures and Foreign Investment' in DN Goldsweig and RH Cummings, *International Joint Ventures: A Practical Approach to Working with Foreign Investors in the US and Abroad* (1990) 107, 122–3.

treaty provisions on monetary transfers are sometimes difficult to conclude. Capital-exporting countries seek broad, unrestricted guarantees on monetary transfers while developing countries press for limited guarantees subject to a variety of exceptions.

5.6 Expropriation and Dispossession

One of the primary functions of any investment treaty is to protect foreign investments against nationalization, expropriation, and other forms of interference with property rights by host country governmental authorities. Despite opposition by some developing nations in multilateral forums, virtually all investment treaties adopt some variation of the traditional western view of international law that a state may not expropriate an alien's property except: (1) for a public purpose; (2) in a non-discriminatory manner; (3) upon payment of just compensation; and, in most instances, (4) with provision for some form of judicial review. The various elements of the traditional rule have taken different formulations in different treaties, some more and some less protective of investor interests. Perhaps the greatest variations in treaty provisions and the most difficult negotiations arise with respect to standards of compensation. Nonetheless many, if not most, investment treaties have adopted the traditional rule or its equivalent, often expressed in the so-called 'Hull Formula'[25] that compensation must be 'prompt, adequate, and effective'.[26] They then proceed to define the meaning of each of these words in the particular circumstances.[27]

5.7 Operational and Other Conditions

Investment treaties sometimes provide treatment standards with respect to certain operational conditions, such as the investor's right to enter the country, employ foreign nationals, and be free of performance requirements. One of the most important conditions, of course, is the ability of the investor's employees to freely enter the host country and manage and operate the investment. Most investment treaties do not grant the investor an automatic right to enter and stay in a host country. German BITs, for example, provide that each contracting party will give 'sympathetic consideration' to applications for entry.[28] Similarly,

[25] GH Hackworth, *Digest of International Law* (1942) 655–64.
[26] See eg UNCTAD (n 9 above) 69.
[27] See eg Agreement for the Promotion and Reciprocal Protection of Investments (UK–Costa Rica) (7 September 1982), Art 5.
[28] Treaty Concerning the Encouragement and Reciprocal Protection of Investments (Federal Republic of Germany–Swaziland) (5 April 1990), Art (3)(c).

US BITs give 'nationals' of contracting parties the right to enter for purposes of establishing or operating investments subject to the laws of the host state.[29]

5.8 Losses from Armed Conflict or Internal Disorder

Many investment treaties also deal with investment losses due to armed conflict or internal disorder within the host country. They do not, however, normally establish an absolute right to compensation in such cases. Instead, many treaties promise that foreign investors will be treated in the same manner as nationals of the host country with respect to compensation.[30] Some also provide for most-favoured-nation treatment on this question. The ICSID case of *Asian Agricultural Products Ltd v Sri Lanka*[31] is one of the few cases that has considered this provision in detail with regard to a dispute between an injured investor and a host country government. The tribunal concluded that in addition to any specific compensatory actions taken for the benefit of other investors the treaty provision in question would make any promised higher standard available to an injured investor. Such a different standard could come, for example, from another BIT granted to investors from other countries.

5.9 Treaty Exceptions, Modifications, and Terminations

Because of the great diversity of national policies and situations, it is natural that in negotiating investment treaties individual states seek to introduce exceptions to their investment treaties' obligations in order to take a into account national policies and situations. Thus, most investment treaties have provisions that carve out exceptions to the general standards of treatment that they seek to apply to investments between the two countries. Investors considering a particular investment should understand the scope and force of such treaty exceptions.

No treaty is ever permanent and never changing. Thus, most international agreements, including investment treaties, contain provisions describing the process for terminating a treaty and in a few instances for modifying treaty provisions.

[29] See eg Treaty Concerning the Encouragement and Reciprocal Protection of Investment (US–Sri Lanka) (20 September 1991), Art 2(3).
[30] See eg Agreement for the Promotion and Reciprocal Protection of Investments (UK–Ukraine) (10 February 1993), Art 5.
[31] *Asian Agricultural Products Ltd v Sri Lanka*, ICSID Case No ARB/87/3 (Final Award) (27 June 1990) (1991); 6 ICSID Rev—FILJ 526.

5.10 Dispute Settlement

The issues discussed above form the basic architecture of most investment treaties. In theory at least, the scope of protection seems broad in that these issues govern most, if not all, of the foreign investor's principal areas of concern regarding the political risks associated with a foreign investment. A fundamental, practical question, of course, is whether countries actually respect their treaty commitments and, if not, whether an injured investor has effective legal redress against a host country's treaty violations. For foreign investors and their governments, one of the great deficiencies of customary international law has been its lack of effective and binding mechanisms to resolve investment disputes. One aim of the investment treaty movement has been to remedy this situation.

Most investment treaties provide for two distinct dispute settlement mechanisms: one for disputes between the two contracting states and another for disputes between a host country and an aggrieved foreign investor. With respect to the former, contemporary investment treaties usually stipulate that in the event of a dispute over the interpretation or application of the treaty, the states concerned will first seek to resolve their differences through negotiation and then, if that fails, through ad hoc arbitration.

With respect to the latter, the trend among more recent investment treaties is to provide a separate international arbitration procedure, often under the auspices of ICSID, for disputes between aggrieved foreign investors and host country governments. By agreeing to an investment treaty, a state often simultaneously gives the consent needed to establish the jurisdiction of ICSID or another arbitral forum for any future dispute between one contracting state and a national of another contracting state. Although the investor must first try to resolve the conflict through negotiation and may also have to exhaust remedies available locally, the investor ultimately has the power to invoke compulsory arbitration in order to secure a binding award.[32]

Granting a private party the right to bring an action against a sovereign state in an international tribunal regarding an investment dispute is a revolutionary innovation that now seems to be largely taken for granted. Yet its uniqueness and power should not be overlooked. The field of international trade law, for example, contains no similar procedure. Violations of trade law, even though they strike at the economic interests of private parties, are resolved directly and solely by states. The World Trade Organization (WTO) does not give a remedy to private persons injured by trade law violations.[33] It should also be noted that modern investment treaties grant aggrieved investors the right to prosecute their

[32] See eg Agreement for the Liberalization, Promotion and Protection of Investment (Japan–Vietnam) (14 November 2003), Art 13.
[33] See eg GT Schleyer, 'Power to the People: Allowing Private Parties to Raise Claims before the WTO Dispute Resolution System' (1997) 65 Fordham Int'l L R 2275, 2277.

claims independently, without regard to the concerns and interests of their home country governments. It is this mechanism that gives important, practical significance to an investment treaty, and which truly enables investment treaties to afford protection to foreign investment. As a result of this mechanism, foreign investors are bringing increasing numbers of arbitration claims when they believe host countries have denied them protection under a treaty. In many cases, arbitral tribunals have rendered substantial awards against host countries, and it appears that host countries have generally paid them. One effect of such awards, along with other judgments rendered against sovereign states in favour of individual private investors, is to cause host countries to take their treaty responsibilities seriously. Investment treaty provisions, their enforcement mechanisms, and the fact that arbitral tribunals hold host countries accountable, each exert an external discipline upon governments' behaviour in their relations with foreign investors. Together, this results in a relatively effective system of foreign investment protection. It is also to be noted that decisions of arbitral tribunals, although unfortunately not always made public, tend to be lengthy, reasoned, and scholarly decisions that form part of the jurisprudence of this emerging international investment law and also solidify and give force to investment treaty provisions.

5.11 Conclusion

Although the nearly 3,000 investment treaties concluded since the mid-twentieth century tend to cover the same issues, they differ in how they treat those issues. Some are more protective than others. For example, the BITs negotiated by the United States generally exhibit higher standards of protection than the BITs of many other countries.[34] Nonetheless, despite divergence among individual treaties, as a group investment treaties demonstrate many commonalities, including their coverage of similar issues and their use of equivalent or comparable legal concepts and vocabulary. It is these commonalities, despite individual differences, that are contributing to the creation of an international framework for investment and ultimately a global regime for international investment.

[34] P Juillard, *L'Evolution des sources du droit des investissements* (1994); 250 *Recueil des Cours de L'Academie de Droit International* 74, 211 (asserting that the level of protection achieved by US BITs is superior to the level of protection achieved by European BITs).

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6

The Interpretation of Investment Treaties

6.1 The Task of Interpretation

Investment treaties take a written form and usually, though not always, consist of a single instrument.[1] For investment treaties to become a reality, however, and actually influence the behaviour of governments and investors, they must be interpreted and applied by government officials, lawyers, corporate executives, and arbitrators. Government officials interpret them in order to decide whether actions and policies affecting investors meet treaty commitments. Corporate executives and their counsel interpret them in planning investment projects and in negotiating with host governments about past and future treatment. And arbitrators interpret them to settle disputes between investors and states.

Treaty interpretation is never easy, but the task of interpreting investment treaties is rendered particularly difficult by two factors: first, the generality and vagueness of many of the terms used in their texts, such as 'fair and equitable treatment', 'full protection and security', and 'expropriation and measures tantamount to expropriation', which are rarely defined in the treaty text itself and which reasonable persons may interpret differently. The second difficulty is the factual and legal complexity of the investment transactions and relationships to which investment treaties are applied. As a result of these complexities, arbitral tribunals and lawyers must devote significant effort and time to give meaning to words that at first glance appear simple but usually are not. Further, these definitions must be painstakingly applied to determine whether actions taken by governments in their complex dealings with investors over lengthy periods of time comply or violate treaty standards.

The purpose of this chapter is to examine some of the issues that arise in the interpretation of investment treaties and to provide guidance on treaty interpretation.

[1] The Vienna Convention on the Law of Treaties, Art 1(a) defines a 'treaty' as 'an international agreement concluded between States in written form and governed by international law, whether embodied in a single instrument or in two or more related instruments and whatever its particular designation'. Vienna Convention on the Law of Treaties (22 May 1969); UN Doc A/Conf.39/27; 1155 UNTS 331; (1969) 8 ILM 679; (1969) 63 AJIL 875 (VCLT).

6.2 Rules of Interpretation

The basic rules of investment treaty interpretation are found in Articles 31, 32, and 33 of the Vienna Convention on the Law of Treaties.[2] Article 31 sets down the general rules of interpretation, Article 32 guides the use of supplementary means of interpretation when a treaty text is ambiguous or obscure, and Article 33 applies to the interpretation of treaties that are authenticated in two or more languages, a situation which affects most investment treaties.

Arbitral tribunals faced with the task of interpreting investment treaty provisions invariably begin by invoking Article 31(1) of the Vienna Convention. Article 31(1), which sets out the basic rule of treaty interpretation, provides that '[a]treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in light of its object and purpose'. This provision points to four essential elements in the interpretation of a treaty: (1) the treaty text; (2) the ordinary meaning of the terms; (3) the context of the treaty terms; and (4) the treaty's object and purpose. The following sections of this chapter examine each of these elements.

6.3 The Treaty Text

(a) Sources of investment treaty texts

Essential to the process of treaty interpretation is the existence of an authentic treaty text to interpret. The texts of investment treaties are found in three types of sources: (i) government sources; (ii) international organization sources; and (iii) unofficial and non-governmental sources. Each is examined in turn below.

(i) Government sources

Governments of states nearly always publish the authoritative texts of treaties to which they have agreed in an official publication. Depending upon the laws of the particular country concerned, the publication will usually be the official and definitive source of laws, legal instruments, and treaties. Normally, such publications appear regularly in the country concerned, although the frequency of publication may vary depending on the amount of legislation and treaties needing to be published. The publications have differing names, including 'official gazette', 'official journal', or 'official bulletin'. Thus, in Austria the publication is known as *Bundesgesetzblatt*, in Bahrain and many Arabic-speaking countries as *Al-Jaridah al-Rasmiyah*, in Chile and many Spanish-speaking countries as *Diario Oficial*, in France and in many French-speaking countries as

[2] ibid.

Journal Officiel de la République, in Korea as *Kwanbo*, and in Japan as *Kampo*.[3] Despite the variation in title, these governmental publications all serve the same function: they are official sources of treaty texts.

Certain countries adopt a different approach to treaty publication. They publish the agreements they conclude with other countries in treaty series. For example, the United States publishes *United States Treaties and Other International Agreements* (cited as UST) (Washington, DC: USGPO, 1950–), which is the cumulative collection of *Treaties and Other International Acts Series* (cited as TIAS) (Washington, DC: USGPO, 1946) and is the current official collection of US treaties and agreements. TIAS is the first US official publication of new treaties and agreements—slip treaties—and is later bound in UST. It combines and continues the numbering of the Treaty Series and Executive Agreement Series. The United Kingdom publishes *Treaty Series* (cited as TS) (London: HMSO, 1892) and also used to publish treaties in a series called *British and Foreign State Papers* (London: HMSO, 1812). Among other countries that publish a treaty series are Australia (*Australian Treaty Series* (ATS)), Canada (*Canada Treaty Series* (CTS)), and the Netherlands (*Tractatenblad* (Trb 'year', 'nr', eg Trb 1994, 12)). This list is not exhaustive. When conducting research, one must inquire into the existence and availability of a treaty series in the country in question.

Many states also maintain government websites that publish either the full text of treaties, indexes to treaties, or both. For example, Australia maintains the *Australian Treaties Library*,[4] a website that contains the full text of Australia's multilateral and bilateral treaties and their current status. The website is updated by the Department of Foreign Affairs and Trade. The *Verdragenbank*, published by the Netherlands Ministry of Foreign Affairs, contains information on treaties published in the official treaty series *Tractatenblad* as well as on treaties for which the Netherlands is the depositary.[5] The UK's Foreign and Commonwealth Office maintains an official website with links to the full texts of treaties involving the United Kingdom listed by subject grouping (eg Investment Promotion and Protection Agreements (IPPAs)), and within each group alphabetically by country, and by signature date.[6] The database of Switzerland's Federal Department of Foreign Affairs contains information on all the international treaties that are either in force or signed by Switzerland, together with information on other important treaties and non-binding instruments.[7] In the United States, a useful website for treaty texts includes one maintained by the US Department of State Office of the Assistant Legal Adviser for Treaty Affairs.

[3] JE Roberts (ed), *A Guide to Official Gazettes and their Contents* (1985).

[4] <http://www.austlii.edu.au/au/other/dfat/> accessed 15 May 2009.

[5] <http://www.minbuza.nl/verdragen/> accessed 15 May 2009.

[6] <http://www.fco.gov.uk/en/about-the-fco/publications/treaties/treaty-texts/ippas-investment-promotion/> accessed 23 August 2009.

[7] <http://www.eda.admin.ch/eda/en/home/topics/intla/intrea/dbintr.html> accessed 15 May 2009.

This website serves as the principal US government repository for US treaties and other international agreements.[8] The text of treaties,[9] published as Senate Treaty Documents, may be accessed through the Library of Congress' THOMAS website.[10]

Some other governmental websites sites include: Belgium's *Federal Public Service Treaties*,[11] Canada's *Treaty Information*,[12] France's *Base Pacte*,[13] and India's Ministry of External Affairs *Bilateral Documents*.[14]

As with the official print treaty series, the availability of official websites containing investment treaty texts and their legal status should be researched in each case: ministries of foreign affairs or trade and commerce may be good a starting point of the search.

(ii) International organization sources

Certain international organizations also are depositories of investment treaty texts. These include the United Nations, the United Nations Conference on Trade and Development (UNCTAD), the International Centre for Settlement of Investment Disputes (ICSID), and the Organization of American States (OAS), among others. Each is examined in turn below.

The United Nations The United Nations Treaty Collection (UNTS) is a collection of treaties and international agreements concluded since 1946. They are registered or filed with the Secretariat and then recorded and published pursuant to Article 102 of the Charter. The UNTS includes the texts of treaties in their authentic language(s), along with translations into English and French, as appropriate. The collection currently contains over 50,000 treaties and a similar number of related subsequent actions. The United Nations Treaty Collection, which has been published in hard copy in over 2,100 volumes, also continues to be the largest single collection of treaties on the internet.[15]

[8] <http://www.state.gov/s/l/treaty/> accessed 15 May 2009.

[9] The US legal system distinguishes between international treaties and agreements. The former are concluded in accordance with Article II section 2 of the US Constitution, which gives the President the power 'by and with the *advice and consent* of the *Senate* to *make treaties*, provided *two-thirds of the Senators present concur*'. Article VI states that the Constitution and 'the laws of the United States which shall be made in pursuance thereof; and all treaties made, or which shall be made, under the authority of the United States, shall be the supreme law of the land'. The latter type consists of two kinds of agreements: *executive-congressional agreements*, entered by the President in accordance with legislation enacted by Congress, and *presidential agreements*, entered by the President in reliance on his constitutional powers.

[10] <http://thomas.loc.gov/home/treaties/trhelp.htm> accessed 15 May 2009.

[11] <http://www.diplomatie.be/en/treaties/default.asp> accessed 15 May 2009.

[12] <http://www.treaty-accord.gc.ca/Section.asp?Page=TS> accessed 15 May 2009.

[13] <http://www.doc.diplomatie.gouv.fr/pacte/index.html> accessed 15 May 2009.

[14] <http://meaindia.nic.in/> accessed 15 May 2009.

[15] <http://untreaty.un.org> accessed 15 May 2009.

United Nations Conference on Trade and Development (UNCTAD) UNCTAD's *Compendium of International Investment Instruments* (fourteen volumes as of 2009) is a compilation of the legal texts of all the existing bilateral, regional, interregional, and multilateral instruments on international investment, as well as prototype instruments. It is available both in print and in online version.[16] In particular, UNCTAD's website 'Investment Instruments OnLine' is an extremely valuable and accessible source for the texts of individual bilateral investment treaties. The UNCTAD database is searchable by keywords, country/region, by the categories (multilateral, regional, bilateral, non-governmental, and prototype instruments) and date.[17] Details of the bilateral investment treaties of 177 economies are provided in the UNCTAD maintained rubric 'Country-specific Lists of BITs'.[18]

International Centre for Settlement of Investment Disputes (ICSID) Since the early 1970s, ICSID, an affiliate of the World Bank, has collected and published the texts of bilateral investment treaties. Most have been included in a multivolume collection of investment treaties entitled *Investment Promotion and Protection Treaties* (compiled by the International Centre for Settlement of Investment Disputes. London; New York: Oceana Publications, c1983–). Also, lists of bilateral investment treaties were published in 1989 and 1992 in the ICSID Review—Foreign Investment Law Journal. ICSID also maintains a webpage that provides a chronological list of BITs concluded through the end of 1996 and an alphabetical list of signatories that indicates the treaties which that State has concluded. The data contained in both lists, which include signature and (where applicable) entry into force dates, are based on information provided to ICSID by foreign governments.[19]

Organization of American States (OAS) The website supported by the OAS contains complete information of every trade- and investment-related bilateral or multilateral legal instrument concluded by a member state of the OAS.[20]

Energy Charter Treaty The Energy Charter Secretariat, located in Brussels, Belgium, maintains a website containing the text of the 1994 Energy Charter Treaty and its related documents.[21]

[16] Available in pdf format at <http://www.unctad.org/Templates/Page.asp?intItemID=2323&lang=1> accessed 22 August 2009.

[17] <http://www.unctadxi.org/templates/DocSearch____780.aspx> accessed 15 May 2009.

[18] <http://www.unctad.org/Templates/Page.asp?intItemID=2344&lang=1> accessed 15 May 2009.

[19] <http://www.worldbank.org/icsid/treaties/intro.htm> accessed 15 May 2009.

[20] <http://www.sice.oas.org/agreements_e.asp> accessed 15 May 2009.

[21] <http://www.encharter.org/> accessed 15 May 2009.

(iii) Unofficial and non-governmental sources of investment treaty texts

One can also tap a variety of unofficial and non-governmental sources to locate investment treaty texts. These include: (1) the Electronic Information System for International Law (EISIL), which was developed and maintained by the American Society of International Law (ASIL) and contains specific references to BITs and other international investment agreements;[22] and (2) the International Treaty Arbitration (ITA). ITA maintains a useful website providing access to all publicly available investment treaty awards, information and resources relating to investment treaties and investment treaty arbitration, and useful links to resources on BITs, Free Trade/Sectoral Agreements with Investment Protections, and Model BITs.[23] Also, there is (3) InvestmentClaims.com, an online resource providing access to all relevant foreign investment law instruments and jurisprudence, which also includes references to international investment agreements;[24] and (4) NAFTAClaims.com, which provides information about NAFTA investor–state dispute settlement and contains copies of important NAFTA legal documents.[25]

(b) The language of treaty texts

While the basic source for interpreting an investment treaty is the text of the treaty itself, often the treaty is embodied in two or more separate texts, each in the official language or languages of the parties to the treaty. Almost invariably, when parties to a treaty have different official languages, the official text of the treaty is in those different languages. Moreover, the treaty text itself normally states that the treaty is done in the specified languages and that the different texts are 'equally authentic'.[26] Under Article 33 of the Vienna Convention on the Law of Treaties (VCLT), '[w]hen a treaty has been authenticated in two or more languages, the text is equally authoritative in each language, unless the treaty provides or the parties agree that, in case of divergence, a particular text shall prevail'. It further provides in Article 33(3) that '[t]he terms of the treaty are presumed to have the same meaning in each authentic text'.

Despite the skill and efforts of translators, one occasionally finds differences between the versions of specific treaty provisions, a factor that greatly complicates

[22] <http://www.eisil.org/index.php?sid=346890273&cat=483&t=sub_pages> accessed 15 May 2009.
[23] <http://ita.law.uvic.ca/investmenttreaties.htm> accessed 15 May 2009.
[24] <http://www.investmentclaims.com/iii.html> accessed 15 May 2009.
[25] <http://www.naftaclaims.com/> accessed 15 May 2009.
[26] For example, Art 2206 of the North American Free Trade Agreement states: 'The English, French and Spanish texts of this Agreement are equally authentic.'

treaty interpretation and application. As a guide in resolving such conflicts, Article 33(4) of the Vienna Convention stipulates:

> Except where a particular text prevails in accordance with paragraph 1, when a comparison of the authentic texts discloses a difference of meaning which the application of articles 31 and 32 does not remove, the meaning which best reconciles the texts, having regard to the object and purpose of the treaty, shall be adopted.

An example of such an interpretational problem and its resolution is found in the case of *Berschader v Russia*.[27] In that case, an investment arbitration tribunal had to interpret a Russia–Belgium BIT written in the Russian and French languages, each of which was equally authentic by the terms of the treaty. In order to establish its jurisdiction over the dispute, the tribunal had to determine whether the claimant's financial contribution to the construction of a building for the Russian Supreme Court was an 'investment' under the BIT. The Russian language version, in Article 1.2 of the BIT, employed the term *kapitalovlozhenie* as the noun form of the word 'investment' and the term *vlozhit* as the verb form 'to invest'. The French text used the words *investissement* and *investir*. Russia argued that the meaning of *kapitalovlozhenie* was restricted to capital investments contributed to the charter capital of a joint venture and that, although such interpretation was narrower in scope than the French term '*investissement*', the tribunal should adopt a narrower interpretation to best carry out the object and purposes of the BIT, as required by Article 33 of the VCLT.

The tribunal found that such a narrow interpretation could not be supported and dismissed Russia's arguments on several grounds. First, the tribunal found that Russian–English legal and economic dictionaries translated the term *kapitalovlozhenie* as *investment*. Second, it took note of BITs concluded by Russia in which the contracting parties agreed that the Russian and English were equally authentic languages and in which the term *kapitalovlozhenie* was translated as *investment*. Based on this analysis, the tribunal concluded that 'while those terms may sometimes be used in the Russian language in the more limited sense of "contributions to the charter capital of a joint venture," they are in fact also frequently used in a broader sense corresponding exactly to the English terms "investment" and "invest"'.[28] Furthermore, the tribunal also took note of the French version of the Russia–Belgium BIT, which according to that treaty's Protocol is equally authoritative as the Russian version. Since the French text uses the words *investissement* and *investir*, the tribunal concluded that the ordinary meaning of the words is identical to that of the English words *investment* and *to invest*.[29]

[27] *Berschader v Russia* SCC Case No 080/2004 (Award) (21 April 2006) (Belgium–Russia BIT). This and many other BITs arbitral awards discussed in this book are available at *Investment Treaty Arbitration*<http://ita.law.uvic.ca/alphabetical_list.htm> accessed 15 May 2009. Investment treaty texts are available on line at *UNCTAD: Investment Treaties Online* <http://www.unctadxi.org/templates/DocSearch.aspx?id=779> accessed 15 May 2009.
[28] *Berschader v Russia* SCC Case No 080/2004 (Award) (21 April 2006) (Belgium–Russia BIT) ¶ 109.
[29] ibid ¶ 110.

6.4 'Ordinary Meaning' of Treaty Terms

The first principle stated in Article 31(1) of the VCLT is that 'a treaty shall be interpreted in good faith in accordance with the *ordinary meaning* to be given to the terms of the treaty'.[30] Accordingly, the first step in interpretation is to establish the ordinary meaning of an investment treaty provision. To accomplish this, those engaged in the task of interpretation ordinarily refer to recognized dictionaries. For example, in the ICSID case of *MTD v Chile*, the tribunal interpreted the 'fair and equitable' standard of treatment by looking to a dictionary to determine the ordinary meaning of the terms 'fair' and 'equitable'.[31]

Difficult interpretational problem are rarely settled conclusively by this first step. For example, in interpreting the word 'fair and equitable treatment' in a bilateral investment treaty, the tribunal in *Saluka Investment BV (Netherlands) v The Czech Republic* observed that the '"ordinary meaning" of "fair and equitable treatment" can only be defined by terms of almost equal vagueness'.[32] After referring to the interpretational approaches of previous tribunals, the tribunal in *Saluka* concluded with respect to ordinary meaning:

> In MTD, the tribunal stated that: 'In their ordinary meaning, the terms "fair" and "equitable" [...] mean "just", "evenhanded", "unbiased", "legitimate". On the basis of *such and similar definitions, one cannot say much more than the tribunal did in S.D. Myers* by stating that an infringement of the standard requires "treatment in such an unjust or arbitrary manner that the treatment rises to the level that is unacceptable from the international perspective." This is probably *as far as one can get by looking at the "ordinary meaning"* of the terms of Article 3.1 of the Treaty.'[33] (emphasis added)

Thus, an inquiry into 'the ordinary meaning' of a treaty term may not always yield conclusive results. In such a case, one would have to rely on other principles of treaty interpretation to determine the meaning of a treaty term.

6.5 'Context' of Treaty Terms and 'Object and Purpose' of the Treaty

According to Article 31(1) of the Vienna Convention, the ordinary meaning of the terms of the treaty is to be given 'in their context' and 'in the light of [the treaty's] object and purposes'. Thus, the interpretation of an investment treaty requires a determination of the 'context' of the treaty terms and the treaty's object and purpose. Article 31(2) provides that the context of the terms of a treaty consist of the treaty text, including the preamble and annexes, any agreement relating to the treaty made by the parties in connection with the conclusion of the treaty, and any instrument made by one or more parties in connection with the conclusion of the treaty that was accepted by the other parties as an instrument related to the treaty. Thus, diplomatic correspondence between two states with respect to a bilateral investment treaty could be considered part of the context of the treaty terms and, therefore, useful for interpretation.

[30] See eg the *Admissions* case, ICJ Rep 1950, p 8; I Brownlie, *Principles of Public International Law* (6th edn, 2003) 604.

[31] In their ordinary meaning, the terms 'fair' and 'equitable' used in Art 3(1)62 of the BIT mean 'just', 'even-handed', 'unbiased', 'legitimate'. *MTD Equity Sdn. Bhd. & MTD Chile SA v Chile*, ICSID Case No ARB/01/7 (Award) (25 May 2004) ¶ 113.

[32] *Saluka Investments BV (The Netherlands) v The Czech Republic* (Partial Award) (17 March 2006) ¶ 297.

[33] ibid.

Investment arbitration tribunals often refer to the context of a treaty term and to the object and purpose of an investment treaty to interpret a specific treaty provision. For example, in considering the context within which Argentina and the United States included the fair and equitable treatment standard in their BIT, and its object and purpose, the *LG&E* tribunal[34] referred to the Preamble of that BIT. In that Preamble, the two countries agreed that 'fair and equitable treatment of investment is desirable in order to maintain a stable framework for investment and maximum effective use of economic resources'.[35] As a result, the tribunal concluded that:

> In entering the Bilateral Treaty as a whole, the parties desired to 'promote greater economic cooperation' and 'stimulate the flow of private capital and the economic development of the parties'. In light of these stated objectives, this Tribunal must conclude that stability of the legal and business framework is an essential element of fair and equitable treatment in this case, provided that they do not pose any danger for the existence of the host State itself.[36]

In *Saluka*, the tribunal made a clear distinction between the context of the treaty terms and the object and purposes of the treaty itself. It also distinguished the immediate context, which included the language used in the treaty regarding the level of treatment each state was to accord to investors from other states, from the 'broader context', which included the other provisions of the treaty.[37] In determining the treaty's object and purpose, the *Saluka* tribunal looked to the title and preamble of the treaty and found its purpose was not only to protect investment but, more generally, to promote investment and intensify economic relations between the two states. This finding led the tribunal to take a balanced approach in interpreting the term 'fair and equitable' treatment. The tribunal chose this approach because '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'.[38]

[34] *LG&E Energy Corp et al v The Argentine Republic*, ICSID Case No ARB/02/1 (Decision on Liability) (26 September 2006).

[35] ibid ¶ 124.

[36] ibid.

[37] *Saluka Investments BV (The Netherlands) v The Czech Republic* (Partial Award) (17 March 2006) ¶ 298.

[38] ibid ¶ 300.

Thus, an examination of the context of the terms and the object and purpose of a treaty itself may assist in the interpretation of a treaty term when its ordinary meaning is elusive. At the same time, as the tribunal in *Plama v Bulgaria* noted, one should be mindful of the warning of Sir Ian Sinclair that 'the risk that the placing of undue emphasis on the "object and purpose" of a treaty will encourage teleological methods of interpretation [which], in some of its more extreme forms, will even deny the relevance of the intentions of the parties'.[39]

6.6 'Subsequent Agreement' and 'Subsequent Practice'

In addition to context, Article 31(3) of the Vienna Convention requires that the interpretation of a treaty term take into account subsequent agreements between the parties regarding the interpretation and application of the treaty as well as any 'subsequent practice in the application of the treaty which establishes the agreement of the parties regarding its interpretation'.

Since the contracting parties may agree on an investment treaty provision's interpretation in subsequent agreements and practice, investment arbitration tribunals and others engaged in treaty interpretation should refer to such agreements in interpreting treaty provisions. This is especially pertinent in the context of NAFTA's Chapter 11 arbitrations. Under NAFTA's Article 1131(2), the NAFTA Free Trade Commission (FTC) has the authority to issue interpretations of NAFTA provisions that are binding on NAFTA-based arbitration tribunals.[40] As of January 2009, the FTC had issued several statements concerning the interpretation of some Chapter 11 provisions,[41]

[39] I Sinclair, *The Vienna Convention on the Law of Treaties* (2nd edn, 1984) 130; *Plama Consortium Limited v Bulgaria*, ICSID Case No ARB/03/24 (Decision on Jurisdiction) (8 February 2005) ¶ 193 (Energy Charter Treaty).

[40] The text of Art 1131(2) reads: '2. If the Commission submits to the Tribunal an agreed interpretation, the *interpretation shall be binding* on the Tribunal. If the Commission fails to submit an agreed interpretation or fails to submit an agreed interpretation within such 60 day period, the Tribunal shall decide the issue of interpretation of the exception' (emphasis added). The North American Free Trade Agreement of 1992 (1993) 32 ILM 289, 605 (NAFTA).

[41] The Statement of Interpretation of Certain Chapter 11 Provisions of 31 July 2001 addressed two important issues: access to documents and the scope of minimum standard of treatment. In addressing the former issue, the FTC took the view that nothing in NAFTA imposes a general duty of confidentiality on the disputing parties to a Chapter 11 arbitration. Further, subject to the application of Art 1137(4), nothing in NAFTA precludes the parties from providing public access to documents submitted to, or issued by, a Chapter 11 tribunal. In addressing the latter issue, the FTC adopted the interpretation that (1) NAFTA's Art 1105(1) requires that the customary international law minimum standard of treatment of aliens also be the minimum standard of treatment afforded to the investments of another party; (2) the concepts of 'fair and equitable treatment' and 'full protection and security' do not require treatment in addition to or beyond what is required by the customary international law minimum standard for the treatment of aliens; and (3) a determination that there has been a breach of another provision of NAFTA, or of a separate international agreement, does not establish that there has been a breach of Art 1105(1). Statement on Interpretation of Certain Chapter 11 Provisions, 31 July 2001.

non-disputing party participation,[42] and notice of intent to submit a claim to arbitration.[43] It is worth noting the distinction in legal character between the FTC's Statement on Interpretation of Certain Chapter 11 Provisions and the Statements of the NAFTA Free Trade Commission on the operation of Chapter 11. The former was adopted 'in order to *clarify* and *reaffirm* the *meaning* of certain of Chapter 11 provisions',[44] whereas the latter was adopted 'in order to enhance the transparency and efficiency of Chapter 11 and *provide guidance* to investors and to Tribunals constituted under Section B of the Chapter'.[45] This distinction is especially important in the light of Article 31(3)(a) of the Vienna Convention, since the Statement on Interpretation of Certain Chapter 11 Provisions may be construed to constitute a subsequent agreement between the parties regarding the proper interpretation of Article 1105, and thus under the Vienna Convention must be taken into account in interpreting a treaty's terms. On the other hand, the Statements of the NAFTA Free Trade Commission on the operation of Chapter 11 represent mere 'recommendations' and thus lack binding character.[46]

[42] The Commission's Recommendation on Non-Disputing Party Participation made clear that no NAFTA provision limits a Chapter 11 tribunal's discretion to accept written submissions from a non-disputing party. It also recommended that tribunals adopt the procedures agreed by NAFTA parties with respect to such submissions. Recommendation on Non-disputing Party Participation, 7 October 2004.

[43] The FTC determined that the approved form for notices of intent to submit a claim to arbitration, if properly completed, would satisfy the requirements of Art 1119 of NAFTA and clarify the basis of a claim. The FTC also recommended that disputing investors use it. Recommendation on the Format of Notices of Intent, 7 October 2004.

[44] Statement on Interpretation of Certain Chapter 11 Provisions, 31 July 2001 (emphasis added).

[45] Statements of the NAFTA Free Trade Commission on the Operation of Chapter 11 (emphasis added).

[46] The FTC's Statement on Interpretation of Certain Chapter 11 Provisions has elicited strong criticism regarding both its nature (whether it was 'an amendment' and the FTC had thus overstepped its powers under NAFTA or whether it was 'a subsequent agreement' and the FTC thus acted within the treaty's limits) and its content (whether the words 'international law' in NAFTA's Art 1105 meant only 'customary international law') on the part of commentators and international tribunals. Subsequent decisions followed the FTC interpretation. For more details, see T Weiler, 'NAFTA Article 1105 and the Free Trade Commission; Just Sour Grapes, or Something More Serious?' (2001) 29 Int'l Business Lawyer 496; P Dumberry, 'The Quest to Define "Fair and Equitable Treatment" for Investors under International Law: The Case of the NAFTA Chapter 11 Pope and Talbot Awards' (2002) 3 J of World Investment 4, 674–6; C Schreuer, 'Fair and Equitable Treatment in Arbitral Practice' (2005) 6 J of World Investment 3, 663; T Westcott, 'Recent Practice on Fair and Equitable Treatment' (2007) 8 J of World Investment 3, 413; *Second opinion* of Christopher Greenwood of 16 August 2001, ¶ 77 in *Loewen Group, Inc and Raymond L Loewen v United States*, ICSID Case No ARB(AF)/98/3; *Second opinion* of Robert Jennings of 18 September 2001, Part I in *Methanex v United States*, UNCITRAL (NAFTA) <http://ita.law.uvic.ca/documents/MethanexResubAmendStateClaimAppend.pdf> accessed 15 May 2009; *Pope & Talbot Inc v The Government of Canada* (Award on Damages) (31 May 2002) UNCITRAL (NAFTA) ¶ 47; *Mondev International Ltd v United States of America*, ICSID Case No ARB(AF)/99/2 (Award) (11 October 2002) (NAFTA) ¶ 120–2.

6.7 'Relevant Rules of International Law Applicable between the Parties'

Article 31(3)(c) of the Vienna Convention requires that, along with the context, subsequent agreements, and practice, treaty interpretation will also take into account any relevant rules of international law applicable to the relations between the parties. The importance of this provision is that it permits reference to other sources of international law for guidance in interpreting an unclear or deliberately ambiguous term. An example of such a situation is the ICSID case of *LG&E v Argentina*,[47] where the tribunal had to decide claims arising out of what was asserted to be an indirect expropriation. The tribunal noted that in order to find an indirect expropriation it first had to define the concept, a task that was complicated by the fact that '[g]enerally, bilateral treaties do not define what constitutes an expropriation—they just make an express reference to "expropriation" and add the language "any other action that has equivalent effects"'.[48] The US–Argentina BIT, which was the treaty that the tribunal had to apply, followed a similar pattern: 'Likewise, Article IV of the [US–Argentina] Bilateral Treaty does not define the term "expropriation" and does not establish which measures, actions or conduct would constitute acts "tantamount to expropriation."'[49] To interpret the BIT, the tribunal therefore found it necessary to look to international law, provisions of other BITs,[50] decisions of other international investment tribunals,[51] and writings of publicists.[52] Its reference to such sources of international law allowed the tribunal to define indirect expropriation and to determine that the respondent's actions did not fall within the scope of the US–Argentina BIT's expropriation clause, which protected against 'any action that has the equivalent effects' of expropriation.

In order to interpret the NAFTA provisions in *SD Myers, Inc v Canada*,[53] the tribunal found it necessary 'to review the other international agreements to which the Parties adhere'.[54] Accordingly, it analysed the Canada–USA Transboundary Agreement on Hazardous Waste (Transboundary Agreement) and the North American Agreement on Environmental Co-operation (NAAEC) to assist in determining of the scope of a state's freedom under NAFTA to regulate the cross-border movement of toxic wastes. The tribunal found guidance in Article 11 of the Transboundary Agreement, which 'does not give a party ... absolute freedom to exclude the import or export of hazardous waste simply by enacting whatever national laws it chooses'.[55] It also pointed out that the NAAEC and

[47] *LG&E Energy Corp et al v The Argentine Republic*, ICSID Case No ARB/02/1 (Decision on Liability) (26 September 2006). [48] ibid ¶ 185.
[49] ibid. [50] ibid ¶ 188. [51] ibid ¶¶ 191–5. [52] ibid 196.
[53] *SD Myers, Inc v Canada* (First Partial Award) (13 November 2000) UNCITRAL (NAFTA). *Investment Treaty Arbitration*. [54] ibid ¶ 204.
[55] ibid ¶ 208.

the international agreements affirmed in the NAAEC suggested that specific provisions of the NAFTA should be interpreted in the light of the general principle that 'where a state can achieve its chosen level of environmental protection through a variety of equally effective and reasonable means, it is obliged to adopt the alternative that is most consistent with open trade'.[56] Although the tribunal acknowledged the possible relevance of the Basel Convention on the Control of Transboundary Movements of Hazardous Waste and Their Disposal of 1989, it refrained from applying it because at the time of the dispute the United States, unlike Canada, was not a party to that treaty.[57] As a result, the tribunal's reference to the applicable treaties between the United States and Canada was a key factor in its interpretation of Article 1102 of NAFTA and its subsequent finding that Canada's regulatory measures were in breach of its obligations.

At the same time, the application of the Vienna Convention's Article 31(3)(c) to the interpretation of investment treaties requires a careful and balanced approach in order to avoid unjustifiably including the same rules of international customary law that the contracting states sought to avoid by making a treaty. States have often decided to conclude an investment treaty either for substantive reasons, such as giving investors higher standards of protection than that afforded by customary international law, or for procedural reasons, such as avoiding the methodological problems associated with establishing the customary international norm's constitutive elements—'general practice' and *opinio juris sive necessitatis*—which is often a contentious process.

On the other hand, in some cases contracting states may specifically intend to link an investment treaty's substantive provisions with the rules of international customary law. For example, paragraph 1 of Article 5 of the US–Uruguay BIT of 2005 provides that each contracting party will grant covered investments treatment consonant with customary international law, including fair and equitable treatment and full protection and security. Paragraph 2 of that Article clarifies that 'paragraph 1 prescribes the customary international law minimum standard of treatment of aliens as *the minimum standard of treatment* to be afforded to covered investments' and that '"*full protection and security*" requires each Party to provide the level of police protection required under customary international law'.[58] Such language clearly demonstrates the intent of the parties

[56] ibid ¶¶ 220–1.
[57] Still the tribunal made this observation:

> Even if the Basel Convention were to have been ratified by the NAFTA Parties, it should not be presumed that CANADA would have been able to use it to justify the breach of a specific NAFTA provision because ... *where a party has a choice among equally effective and reasonably available alternatives for complying... with a Basel Convention obligation, it is obliged to choose the alternative that is... least inconsistent... with the NAFTA.* If one such alternative were to involve no inconsistency with the Basel Convention, clearly this should be followed.

ibid ¶ 215. [58] Article 5(2).

to incorporate the requirements of international customary law into the interpretation of the terms *'the minimum standard of treatment'* and *'full protection and security'* as it existed at the time of the conclusion of that treaty and as it has evolved over time.[59]

In general, then, the application of Article 31(3)(c) of the Vienna Convention to the interpretation of investment treaties should proceed carefully and with due regard to the intentions of the contracting states.

6.8 Special Meanings Intended by the Parties

The Vienna Convention's Article 31(4) provides that a special meaning shall be given to a treaty term if it can be established that such was the contracting parties' intention. Thus, for example, the tribunal in *Parkerings-Compagniet AS v Lithuania*[60] had to decide whether 'fair and *reasonable* treatment' had the same meaning as 'fair and equitable treatment', and whether the former holds the respondent state to a stricter standard of conduct than the more commonly found fair and equitable treatment standard. The tribunal concluded that:

> The standard of 'fair and equitable treatment' has been interpreted broadly by Tribunals and, as a result, a difference of interpretation between the terms 'fair' and 'reasonable' is insignificant. The Claimant did not show any evidence which could demonstrate that, when signing the BIT, the Republic of Lithuania and the Kingdom of Norway intended to give a different protection to their investors than the protection granted by the 'fair and equitable' standard.[61]

One may therefore infer from this statement that the proponent of the special meaning has the burden of proving that the asserted special meaning was intended by the contracting parties to the treaty.

6.9 Supplementary Means of Interpretation

Article 32 of the Vienna Convention allows recourse to supplementary means of interpretation,

[59] See eg ¶¶ 107–8, 124 of *Mondev*, where Mexico and Canada were found to have expressly accepted the point that the 'minimum standard of treatment' adopted in NAFTA's Art 1105 'existed in 1994, ... had developed to that time ... [and] has evolved and can evolve'. *Mondev International Ltd v United States of America*, ICSID Case No ARB(AF)/99/2 (Award) (11 October 2002) (NAFTA).

[60] *Parkerings-Compagniet AS v Lithuania*, ICSID Case No ARB/05/8 (Award) (11 September 2007) (Norway–Lithuania BIT).

[61] ibid ¶ 277.

> including the preparatory work of the treaty and the circumstances of its conclusion, in order to confirm the meaning resulting from application of article 31, or to determine the meaning when the interpretation according to article 31:
>
> (a) leaves the meaning ambiguous or obscure, or
>
> (b) leads to a result which is manifestly absurd or obscure.

An illustration of recourse to supplementary material in treaty interpretation is found in *Plama Consortium Limited v Bulgaria*,[62] in which the claimant, a Cypriot company, sought to establish ICSID jurisdiction on the basis of the Energy Charter Treaty and the 1987 BIT between Cyprus and Bulgaria. The tribunal affirmed ICSID jurisdiction under the Energy Charter Treaty and also considered whether it had jurisdiction under the Bulgaria–Cyprus BIT. This BIT contained a very limited international dispute settlement offer that, in essence, provided that only the measure of compensation for expropriation could be submitted to an UNCITRAL arbitration. It contained no offer of ICSID arbitration. The BIT did, however, have a most-favoured-nation clause. Since other BITs concluded by Bulgaria provide for ICSID arbitration, the claimant relied upon the most-favoured-nation clause to take advantage of the ICSID dispute settlement mechanism included in the other BITs. The investor argued that (1) the claimant *Plama Consortium Limited* qualified as an investor under the Bulgaria–Cyprus BIT; (2) the Bulgaria–Cyprus BIT contained an MFN provision; (3) the MFN provision in the Bulgaria–Cyprus BIT applied to all aspects of investor 'treatment'; and (4) 'treatment' covers settlement of disputed provisions in other BITs to which Bulgaria is a contracting party. As a result, the tribunal had to decide whether the term 'treatment' in the MFN provision of the BIT included or excluded dispute settlement provisions contained in other BITs to which Bulgaria was a contracting party.

The tribunal found that neither the ordinary meaning of the term 'treatment', nor its context, nor the object and purpose of the treaty provided legally sufficient guidance to conclude that the contracting states to the Bulgaria–Cyprus BIT intended the MFN provision to incorporate agreements to arbitrate in other treaties to which Bulgaria was a contracting party.[63] Nor did it find any guidance in the provisions of paragraphs 2, 3, and 4 of Article 31 of the Vienna Convention, since there were no facts or circumstances that indicated their application to the issues at hand.[64] Lacking both specific textual support in the treaty and related documents to base a conclusion on regarding the scope of the MFN clause, the tribunal turned to the negotiating history of the Bulgaria–Cyprus BIT. There, the tribunal found a sufficient basis to infer that the contracting

[62] *Plama Consortium Ltd v Bulgaria*, ICSID Case No ARB/03/24 (Decision on Jurisdiction) (8 February 2005) (Energy Charter Treaty).

[63] ibid ¶¶ 189–93.

[64] ibid ¶ 194.

parties did not consider the MFN provision to extend to dispute settlement provisions in other BITs.[65] Although the parties were unable to produce actual preparatory work for the BIT, as authorized in Article 32 of the Vienna Convention, the tribunal did find assistance in two facts relating to Bulgaria's general negotiating behaviour. The first fact was that at the time Bulgaria concluded the BIT with Cyprus, 'Bulgaria was under a communist regime that favored bilateral investment treaties with limited protections for foreign investors and with very limited dispute resolution provisions'.[66] The second was that in 1998, after the end of communism, Bulgaria and Cyprus specifically sought to negotiate a revision to the dispute settlement provisions of the 1987 BIT. The negotiations failed. The *Plama* tribunal 'inferred from these negotiations that the Contracting Parties to the BIT themselves did not consider that the MFN provision extends to dispute settlement provisions in other BITs'.[67] Thus, when faced with an inconclusive textual basis for interpreting the investment treaty, the tribunal resorted to facts outside the treaty and to its negotiating history as supplementary means of interpretation to determine the contracting parties' intention at the time they concluded their BIT in 1987.

Despite the nearly 3,000 investment treaties that have been negotiated over the last six decades, for various reasons obtaining useful negotiating history to assist in interpreting a treaty can be difficult, if not impossible. The recorded negotiating history and preparatory work may be scant or lost, or contracting states may be unwilling to provide the record to litigants, since such material, once released, may be used against the state that released it.[68]

One important preparatory document that is often publicly available, as was discussed in Chapter 4.7, is the 'model' or 'prototype' treaty prepared by many capital-exporting countries to conduct BIT negotiations. While no arbitration cases seem to have referred to such prototypes of models yet, these documents may be used to interpret or illuminate the meaning of provisions in the BITs for which they were used. In studying investment treaties, a model BIT may not only provide a historical perspective but could also conceivably be used to interpret unclear treaty text. Under Article 32 of the Vienna Convention, if the meaning of the text is ambiguous or obscure, recourse may be had to 'the

[65] ibid ¶ 195. [66] ibid ¶ 196. [67] ibid ¶ 195.

[68] For example, in *Pope & Talbot Inc v Canada*, Canada initially refused to reveal the *travaux preparatoires* that led to the adoption of NAFTA's Art 1105. The tribunal criticized that incident, stating that 'having the documents would have made [tribunal's] earlier interpretations of Article 1105 less difficult and more focused on the issues before it. In this sense, the failure of Canada to provide the documents when requested ... was unfortunate. Forcing the Tribunal to chase after the documents as it did is not acceptable' (ibid ¶ 39). When Canada finally acceded only partially to the tribunal's request, the tribunal observed that '[i]t is almost certain that the documents provided ... are not all that exists, yet no effort was made by Canada to let the Tribunal know what, if anything, has been withheld' (ibid ¶ 40). Accordingly, the tribunal concluded that '[t]his incident's injury to the [NAFTA] Chapter 11 process will surely linger' (ibid ¶ 41). See also *Pope & Talbot Inc v The Government of Canada* (Award on Damages) (31 May 2002) UNCITRAL (NAFTA).

preparatory work of the treaty' to interpret its text. Model or prototype treaties would certainly constitute 'preparatory work' within the meaning of that Article.

6.10 Arbitration and Judicial Decisions

International law contains no doctrine of binding precedent making the decisions of an international judicial or arbitral body in one case binding upon international judicial or arbitral bodies deciding similar, future cases.[69] Article 59 of the Statute of the International Court of Justice specifically states that '[t]he decision of the Court has no binding force except between the parties and in respect of that particular case'.[70] Similarly, Article 1136(1) of NAFTA, in virtually identical language, makes clear that decisions of investment arbitral tribunals under Chapter 11 do not constitute binding precedent for the future. The treaty states: 'An award made by a Tribunal shall have no binding force except between the disputing parties and in respect of the particular case.'[71] Neither the ICSID Convention nor individual investment treaties contain a similarly specific prohibition, but neither do they expressly recognize that investment arbitration awards constitute precedent.[72]

On the other hand, Article 38(d) of the Statute of the International Court of Justice, in defining the sources of international law, recognizes 'judicial decisions and the teachings of the most highly qualified publicists of the various nations as subsidiary means for the determination of rules of law'.[73] Thus, in applying international law, international courts and tribunals may refer to previous judicial decisions and arbitral decisions to determine the applicable rules of international law. In international investment arbitration, counsel for the parties regularly cite prior cases in support of their positions, and tribunals, while reaffirming that they are not bound by previous arbitral decisions and awards, nonetheless regularly refer to earlier awards and decisions in interpreting investment treaty provisions and deciding investment disputes. Various factors have supported this trend. First, the vague and general language of many investment treaties, and the fact that treaties employ common legal

[69] G Kaufmann-Kohler, 'Arbitral Precedent: Dream, Necessity or Excuse?' (2007) 23 Arbitration Int'l 357.

[70] Statute of the International Court of Justice (1945), 3 Bevans 1179; 59 Stat 1031; TS 993; (1945) 39 AJIL Supp 215.

[71] The North American Free Trade Agreement of 1992, (1993) 32 ILM 289, 605 (NAFTA).

[72] Article 53(1) of the ICSID Convention states: 'The award shall be binding on the parties.' Schreuer suggests that this provision may be interpreted as 'excluding the applicability of the principle of binding precedent to successive ICSID cases'. He also notes that there is nothing in the preparatory work of the Convention suggesting that the doctrine of precedent should be applied to ICSID arbitration. C Schreuer, 'A Doctrine of Precedent?' in P Muchlinksi et al, *The Oxford Handbook of International Investment Law* (2008) 1190.

[73] Statute of the International Court of Justice (1945), 3 Bevans 1179; 59 Stat 1031; TS 993; (1945) 39 AJIL Supp 215 Art 38(1)(d).

concepts and phrases, naturally leads lawyers and tribunals to refer to decisions in other cases to determine how such provisions should be interpreted. Second, the recognized goal of international investment law is to establish a predictable, stable legal framework for investments, which causes tribunals to pay attention to previous decisions on similar issues. Third, tribunals, like courts, are motivated by the underlying moral consideration that 'like cases should be decided alike', unless a strong reason exists to distinguish the current case from previous ones.

The growth in investor–state arbitration in recent years has led to a significant expansion in the jurisprudence of investment treaties. The commonality of language and provisions among investment treaties makes an understanding of judicial and arbitration decisions important to the interpretation and application of investment treaties. The sources for locating such decisions include: ICSID's website,[74] the Permanent Court of International Arbitration's website,[75] InvestmentClaims.com,[76] *Investment Treaty Arbitration* (edited by Professor Andrew Newcombe),[77] and NAFTA Claims.[78] The NAFTA Chapter 11 awards and briefs can be also retrieved from governmental websites of the United States,[79] Canada,[80] and Mexico.[81] On the other hand, principles of confidentiality, which to a greater or lesser extent apply to all investor–state arbitrations, may prevent the publication of important arbitral decisions and related documents in specific cases. Thus, unfortunately, unlike most well-administered national judicial systems, it is likely that some important arbitral decisions interpreting key treaty provisions are kept private and so are not part of investment treaty jurisprudence because the parties to the dispute or their counsel sought this result.[82]

6.11 Scholarly Commentary on Investment Treaties

The writing of scholars and practitioners are another source of assistance in interpreting investment treaties. As noted above, Article 38 of the Statute of the International Court of Justice specifies the use of 'teachings of the most highly qualified publicists of the various nations as subsidiary means for the

74 <http://icsid.worldbank.org/ICSID/FrontServlet?requestType=CasesRH&actionVal=ShowHome&pageName=Cases_Home> accessed 22 August 2009.
75 <http://www.pca-cpa.org> accessed 15 May 2009.
76 <http://www.investmentclaims.com/iii.html> accessed 15 May 2009.
77 <http://ita.law.uvic.ca/investmenttreaties.htm> accessed 15 May 2009.
78 <http://www.naftaclaims.com> accessed 15 May 2009.
79 <http://www.state.gov/s/l/c3433.htm> accessed 15 May 2009.
80 <http://www.dfait-maeci.gc.ca/tna-nac/nafta-en.asp> accessed 15 May 2009.
81 <http://www.economia.gob.mx/?NLanguage=en&P=5500> accessed 22 August 2009.
82 Even ICSID, which is the most open of the arbitral institutions, is prevented by Art 48(5) of the ICSID Convention from publishing awards without the consent of the parties.

determination of rules of law'. Both counsel and tribunals in investor–state arbitrations routinely refer to such works in analysing the meaning of treaty terms in specific cases. The amount of doctrinal literature is vast and growing quickly. A selective bibliography of some of these works may be found at the end of this volume. Other useful bibliographies include ICSID's Bibliography on Bilateral Investment Treaties and International Investment Law[83] and the Peace Palace Library's Bibliography on New Aspects of International Investment Law.[84]

83 <http://icsid.worldbank.org/ICSID/FrontServlet> accessed 15 May 2009.
84 The Bibliography on New Aspects of International Investment Law was originally compiled in 2004 and is updated regularly with new titles. <http://www.ppl.nl/bibliographies/all/?bibliography=investment> accessed 22 August 2009.

nationals of a Member State in the territory of another Member State shall be prohibited' and that

> Freedom of establishment shall include the right to take up and pursue activities as self-employed persons and to set up and manage undertakings in particular companies or firms within the meaning of the second paragraph of Article 48, under the conditions laid down for its own nationals by the law of the country where such establishment is effected, subject to the provisions of the chapter relating to capital.

Article 48 states that '[c]ompanies or firms formed in accordance with the law of a Member State and having their registered office, central administration or principal place of business within the Community shall, for the purposes of this Chapter, be treated in the same way as natural persons who are nationals of Member States', thereby guaranteeing such firms national treatment. Furthermore, under the treaty, investors from other EU member states have the right to transfer capital and earnings freely and are guaranteed national treatment on expropriation. Indeed, Article 56 of the EU Treaty specifically prohibits restrictions on the movement of capital and payments between member states and between member states and third countries. Finally, any violation of these rights can be adjudicated by the European Court of Justice. The Court may hear cases related to the violation of treaty rights directly or overturn national court decisions found inconsistent with the treaty. The EU Treaty authorizes the European Commission to reduce barriers to investment among EU members and from third countries, a task that the Commission has pursued quite energetically.[38]

Although no other investment treaty has gone so far to create an 'open door' for investments from treaty partners as has the European Union, the EU Treaty may stand as a model for countries that desire increased economic integration through the treaty-making process.

[38] For example, in June 1997, the European Commission issued an interpretative Communication clarifying the scope of EU Treaty provisions on capital movements and the right of establishment. It took this initiative because certain member states had imposed limits on the number of voting shares that investors from other member states could acquire in privatization operations. The Communication stresses that free movement of capital and freedom of establishment constitute fundamental and directly applicable freedoms established by the EU Treaty. Nationals of other member states should, therefore, be free to acquire controlling stakes, exercise the voting rights attached to these stakes, and manage domestic companies under the same conditions that a member state has prescribed for its own nationals. *Communication of the European Commission on Certain Legal Aspects Concerning Intra-EU Investment*, Official J C 220, 19/07/1997 15–18. In April 2001, the Commission reaffirmed the validity of its interpretative Communication on investment.

9

General Treatment Standards

9.1 The Nature of Investment and Investor Treatment

In order to protect foreign investors against the political risk resulting from placing their assets under a host country's jurisdiction, investment treaties stipulate obligations regarding the 'treatment' that host countries must give to investors and their investments. Although the treaties do not usually define the meaning of 'treatment', that term in its ordinary dictionary sense includes the 'actions and behaviour that one person takes towards another person'. In other words, by entering into an investment treaty, a state makes promises about the actions and behaviours it will take towards investments and investors of treaty partners.[1] The treaty provisions on investor and investment treatment are intended to restrain host country government behaviour and impose a discipline on governmental actions. To achieve this goal, treaties define a standard to which host countries must conform in their treatment of investors and investments. State actions that fail to meet the defined standard constitute treaty violations that engage the offending state's international responsibility and render it potentially liable to pay compensation for the injury it has caused.

Investment treaties normally contain treatment provisions with respect to numerous matters that investors consider important. One may categorize the various treatment standards included in treaties as 'general' or 'specific'. General standards of treatment apply to all facets of an investment's activities in the host country. These include host government commitments to grant investors and investments 'fair and equitable treatment', 'full protection and security', and 'treatment in accordance with international law'. Specific treatment standards concern particular matters relating to an investment, such as monetary transfers,

[1] In the ICSID case of *Suez, Sociedad General de Aguas de Barcelona SA, and Vivendi Universal SA v The Argentine Republic*, ICSID Case No ARB/O3/19, the tribunal defined 'treatment' as follows: 'The word "treatment" is not defined in the treaty text. However, the ordinary meaning of that term within the context of investment includes the rights and privileges granted and the obligations and burdens imposed by a Contracting State on investments made by investors covered by the treaty.' *Suez, Sociedad General de Aguas de Barcelona SA, and Vivendi Universal SA v The Argentine Republic* ICSID Case No ARB/O3/19 (Decision on Jurisdiction) (3 August 2006) ¶55.

expropriation, and investor rights in times of war, revolution, or civil disturbance.[2] This chapter is concerned with general treatment standards, while succeeding chapters will discuss individual, specific treatment standards.

It should be noted that while investment treaties specify standards for state behaviour towards investors, they generally do not impose standards for the behaviour of investors towards the host country or its government. Presumably, the reason for this is the assumption by treaty negotiators that host country laws and legal institutions are sufficient to ensure proper investor behaviour.

9.2 General Treatment Standards in General

General treatment standards consist of two types: (a) *absolute standards*, which are not contingent upon specified factors, happenings, or government behaviour towards other investors or persons; and (b) *relative standards*, which are dependent upon the host government's treatment of other investments or investors. Examples of absolute standards include guarantees of full protection and security, fair and equitable treatment, or treatment in accordance with the minimum standard of international law. Examples of relative standards are most-favoured-nation treatment and national treatment. Whereas the latter type of standard requires a comparator for its application,[3] the former does not.

The present chapter discusses the absolute and relative general treatment standards used most frequently in international investment treaties. These include full protection and security, fair and equitable treatment, minimum treatment according to international law, most-favoured-nation treatment, and national treatment. That these standards exist in one form or another in most investment treaties gives the treaties a strong similarity—indeed, some would say a significant commonality. It must also be acknowledged, however, that not all treaties include all of these general standards and that significant differences exist in the way individual treaties articulate them. For example, particular treaties may grant investments 'complete protection and security', 'full protection and security', 'full legal protection and security', or simply 'protection and security'. Moreover, some treaties may articulate specific treatments standards as independent commitments, while others may link them to or condition them on another standard. For example, while many early US BITs simply required host countries to grant investors 'full protection and security', the 2005 US–Uruguay BIT specifies that 'full protection and security' requires each party to provide

[2] UNCTAD, *Bilateral Investment Treaties 1995–2006: Trends in Investment Rulemaking* (2007) 28.

[3] TJ Grierson-Weiller and IA Laird, 'Standards of Treatment' in P Muchlinski et al, *The Oxford Handbook of International Investment Law* (2008) 262.

'the level of police protection required under customary international law'.[4] As a result of these differences, the degree of protection afforded individual investments may vary significantly among treaties. Consequently, persons interpreting investment treaty provisions should give careful attention to the differing ways individual treaty texts articulate their protections. At the same time, it should be emphasized that treatment standards are almost always expressed in general and even vague terms and thus render the task of applying them to concrete, complex fact situations, like those that usually arise in investment disputes, even more difficult.

9.3 Protection and Security

(a) In general

In virtually all investment treaties, contracting parties promise to give some degree of 'protection' and 'security' to the investors and investments of other contracting parties. The precise formulation of that promise varies among treaties. For example, the first BIT ever concluded, the agreement between Germany and Pakistan in 1959, provided that investments by nationals or companies of either party are to 'enjoy *protection and security* in the territory of the other party'.[5] On the other hand, Article 4(1) of the Germany–Argentina BIT of 1991 states that investments should enjoy 'full legal protection and full legal security',[6] and Article IV(2) of the Ecuador-El Salvador BIT of 1994 provides for 'full legal protection' for the investments of either party's nationals.[7] Article 3 of the China–Qatar BIT of 1999 merely states that the contracting party investments and the activities associated with those investments 'shall be accorded fair and equitable treatment and shall *enjoy protection* in the territory of the other Contracting Party'.[8] Despite the generality and vagueness of these

[4] Treaty between the United States of America and the Oriental Republic of Uruguay Concerning the Encouragement and Reciprocal Protection of Investment (November 2005), Art 5(2)(B).

[5] Treaty between the Federal Republic of Germany and Pakistan for the Promotion and Protection of Investments (25 November 1959) (1963) UNTS No 6575, Art 3.

[6] Artikel 4:

(1) Kapitalanlagen von Staatsangehoerigen oder Gesellschaften einer Vertragspartei geniessen im Hohheitsgebiet der abderen Vertragspartei vollen rechtlichen Schutz und volle rechtliche Sicherheit.

[7] ARTICULO IV 'Protección de inversiones':

(2) Cada Parte Contratante, una vez que haya admitido en su territorio inversiones de inversionistas de la otra Parte Contratante, concederá plena protección legal a tales inversiones y les acordará un tratamiento no menos favorable que el otorgado a las inversiones de sus propios inversionistas nacionales o de inversionistas de terceros Estados.

[8] Agreement between the Government of the People's Republic of China and the Government of the State of Qatar Concerning the Encouragement and Reciprocal Protection of Investments (April 1999), Art 3.1.

provisions, they do seem to imply that the host state has an obligation to take measures to protect covered investors and investments from certain negative actions that may affect them.[9] Beyond this basic observation, treaty provisions on full protection and security do little to answer three difficult but essential questions:

1. Against whom is the host state to protect covered investors and investments?
2. Against what actions is the host state to protect investors and their investments?
3. Precisely what measures must a host state take in order to meet its treaty obligations?

To answer these questions, one must consider the historical origins of this standard, which has now become a common feature of investment treaties.

(b) Historical origins of the term

The origin of the terms 'full protection and security', 'constant protection and security', or simply 'protection and security' appears to lie in the bilateral commercial treaties that many countries concluded in the nineteenth and early twentieth centuries. One example is the friendship, commerce, and navigation (FCN) treaties made by the United States during that period.[10] Of the twenty-two commercial treaties concluded by the United States before 1920, fourteen contained reference to 'special protection' and the remaining eight required 'full and perfect protection' of persons' private property.[11] As an illustration, Article 3 of the 1850 FCN treaty between the United States and Brunei provided that His Highness the Sultan 'engages that such Citizens of the United States of America shall as far as lies within his power, within his dominions enjoy *full and complete protection and security* for themselves and for any property which they may acquire' (emphasis added).[12] The bilateral treaties of other countries also employed this term.[13]

Arbitral decisions, judicial decisions, and other forms of international practice have given meaning to the term 'protection and security' over the years. Indeed,

[9] R Dolzer and C Schreuer, *Principles of International Investment Law* (2008) 149.
[10] K Vandevelde, 'The Bilateral Investment Treaty Program of the United States' (1988) 21 Cornell Int'l L J 203, 204.
[11] R Wilson, 'Property-protection Provisions in United States Commercial Treaties' (1951) 45 AJIL 84, 92–6.
[12] Treaty of Friendship, Commerce and Navigation with Brunei (entered into force 11 July 1853) 10 Stat 909; Treaty Series 331.
[13] See eg the bilateral treaty between Italy and Venezuela, stating that 'citizens of each state should enjoy in the territory of the other "the fullest measure of protection and security of person and property, and should have in this respect the same rights and privileges accorded to nationals"'. Quoted in the *Sambiaggio* case, Italy–Venezuela Mixed Claims Commission, UN Reports of International Arbitral Awards, vol 10, p 512.

it is only through jurisprudence that one can fully understand the content of this standard. Most cases involved actions by third persons, such as mobs, revolutionaries, or insurgents, who had physically damaged investments covered under the treaty. Injured investors sought compensation from the host government on the grounds that the government had not taken sufficient measures to protect the investment or the investor. For example, in the *Sambiaggio* case,[14] the Italy-Venezuela Mixed Claims Commission in 1903 had to adjudicate whether Venezuela was monetarily liable to Italian nationals for damage resulting from the acts of revolutionaries operating in Venezuelan territory. Article 4 of the Italy–Venezuela Treaty of 1861 stated that each state's citizens should enjoy 'the fullest measure of protection and security of person and property, and should have in this respect the same rights and privileges accorded to nationals' of the territory. The umpire in the case declared that he 'accepts the rule that if in any case of reclamation submitted to him it is alleged and proved that Venezuelan authorities failed to exercise due diligence to prevent damages from being inflicted by revolutionists, that country should be held responsible'.[15] He ultimately denied Italy's claims that the treaty imposed strict liability.

Probably the most authoritative case interpreting the FCN treaty provisions on protection and security was a 1989 decision of a chamber of the International Court of Justice in the *ELSI* case.[16] In that case, the United States brought a claim against Italy under the US–Italy FCN treaty for injuries incurred by Raytheon, a US company, with respect to its subsidiary in Sicily. A factory of Raytheon's subsidiary in Palermo was taken over by workers and then requisitioned by the mayor in order to forestall its closure by the investor for economic reasons. The United States alleged that such actions violated Italy's obligation to give US investors 'the most constant protection and security', as required by Article V(1) of the FCN treaty. The United States did not contend, however, that the obligation constituted a guarantee resulting in strict liability. Instead, it pointed to the 'well-established aspect of the international standard of treatment ... that States must use "due diligence" to prevent wrongful injuries to the person or property of aliens within their territory'. The ICJ Chamber found that the Italian government had taken adequate measures to protect the investor and its property, stating that '[t]he reference in Article V to the provision of "constant protection and security" cannot be construed as the giving of a warranty that property shall never in any circumstances be occupied or disturbed'.[17]

In general, jurisprudence relating to the FCN provisions on protection and security recognizes that this standard requires host countries to take steps to protect investors against physical injury to their persons or properties, whether by government agents or third persons. However, the FCN provision does not make the host state a guarantor of the safety of the investor or its property. It

[14] ibid. [15] ibid 534. [16] *Elettronica Sicula SpA (ELSI)* 1989 ICJ Reports.
[17] ibid ¶108, p 65.

requires only that the host state exercise due diligence in carrying out its obligations under the treaty. As one commentator has observed, the decisions of tribunals and the other sources offer no definition of 'due diligence', but 'obviously no very dogmatic definition would be appropriate, since what is involved is a standard which will vary according to the circumstances'.[18] A host states satisfies its due diligence obligation when it takes all the reasonable measures of protection that a well-administered government would take in a similar situation.[19]

(c) Full protection and security in the modern era

With the development of bilateral and other investment treaties since 1960, the inclusion of provisions granting investors some form of protection and security has become standard. It can thus be found in countless BITs, NAFTA,[20] the Energy Charter Treaty,[21] and the 1987 ASEAN Agreement on the Promotion and Protection of Investment,[22] among others. These provisions have also been the basis of several investor-state arbitrations, and so arbitral tribunals have been forced to interpret and apply them in a new era. In doing so, contemporary tribunals have relied on the jurisprudence interpreting FCNs to a significant extent but have also extended the scope of protection in certain instances.

The first such BIT case was *Asian Agricultural Products Ltd v Sri Lanka (AAPL)*.[23] In *AAPL*, an ICSID tribunal considered the claims of a UK investor in shrimp farming in Sri Lanka which had suffered injuries as a result of the destruction of its facilities by Sri Lankan security forces during an alleged

[18] I Brownlie, *Principles of Public International Law* (1990) 454.

[19] On the meaning of due diligence, tribunals and scholars have often referred to the statement of Professor AV Freeman in his lectures at the Hague Academy of International Law: 'The "due diligence" is nothing more nor less than the reasonable measures of prevention which a well-administered government could be expected to exercise under similar circumstances.' AV Freeman, 'Responsibility of States for the Unlawful Acts of Their Armed Forces' 88 *Receuil des Cours* (1956) 261. See also *Asian Agricultural Products Ltd v Sri Lanka*, ICSID Case No ARB/87/3 (Final Award) (27 June 1990) ¶170.

[20] NAFTA, Art 1105, entitled 'Minimum Standard of Treatment', provides:

1. Each Party shall accord to investments of investors of another Party treatment in accordance with international law, including fair and equitable treatment and full protection and security.

[21] The Energy Charter Treaty, Art 10, entitled 'Promotion, Protection, and Treatment of Investments', provides in part in paragraph 1 that '[s]uch investments shall enjoy the most constant protection and security'.

[22] Article III(2) of the ASEAN Investment Treaty states: 'Investments of nationals or companies of one Contracting Party in the territory of other Contracting Parties shall at all times be accorded fair and equitable treatment and shall enjoy full protection and security in the territory of the host country.' (1988) 27 ILM 612.

[23] *Asian Agricultural Products Ltd v Sri Lanka*, ICSID Case No ARB/87/3 (Final Award) (27 June 1990). The Sri Lanka–United Kingdom Agreement on the Promotion and Protection of Investments (entered into force 18 December 1980) (1980) 19 ILM 886.

operation against rebels. The claimant maintained that the UK–Sri Lanka BIT's provision guaranteeing 'full protection and security' went beyond the minimum standard of customary international law and imposed an unconditional obligation of protection on the host country. Therefore, failure to comply with the obligation entailed 'strict or absolute liability' for the host state once damage to the investor's property was established. In response, Sri Lanka contended that the 'full protection and security' standard incorporates, rather than supplants, the customary international legal standard of responsibility requiring due diligence on the part of states and reasonable justification for the destruction of property, but not imposing strict liability. A central issue throughout the case was the standard of liability to be applied to the Sri Lankan security forces.

The tribunal unanimously rejected the UK investor's contentions that the 'full protection and security' standard imposed 'strict liability' on the host state; however, a majority of the arbitrators did find the Sri Lankan government responsible for the property destruction under the customary international law standard requiring 'due diligence' protection from the host state. The tribunal acknowledged that customary international law contemplated a 'sliding scale of liability related to the standard of due diligence'. This scale would range from the older 'subjective' criteria that take into account the relatively limited existing possibilities of local authorities in a given context to an 'objective' standard of vigilance in assessing the required degree of protection and security with regard to what one should legitimately expect from a reasonably well–organized modern state with respect to the level of security afforded to foreign investors.[24] Applying this reasoning to the facts of the case, the tribunal concluded that the Sri Lankan government could reasonably have used other means than those employed by its troops to exclude suspected rebel elements from the shrimp farm staff. Further, those other actions would have minimized the risk of death and destruction in the counter-insurgency operation. The tribunal also found that the failure to take such precautionary measures was especially significant because such measures fall within the normal exercise of governmental inherent powers. The tribunal concluded that Sri Lanka, both through inaction and omission 'violated its due diligence obligation which requires undertaking all possible measures that could be reasonably expected to prevent the eventual occurrence of killings and property destructions'.[25]

Subsequent cases have found host governments liable for not taking steps to protect an investor's factory from looting by government troops in Zaire, and for not employing measures to prevent the seizure of a hotel by disgruntled employees in Egypt. In the case of *American Manufacturing and Trading, Inc v Zaire (AMT)*,[26] the tribunal rejected Zaire's defence that it should not be liable for the

[24] ibid ¶ 170. [25] ibid ¶ 85(B).

[26] *American Manufacturing and Trading, Inc v Zaire*, ICSID Case No ARB/93/1 (Award) (21 February 1997).

acts of marauding soldiers who looted the investor's factory on at least two consecutive occasions without any intervention by government authorities. The tribunal stated that the protection and security treatment standard constituted an objective obligation 'which must not be inferior to the minimum standard of vigilance and of care required by international law'.[27] It therefore found it unnecessary to discuss whether Zaire was bound by an obligation of result or simply an obligation of conduct, but found it sufficient that Zaire took no measures whatsoever to ensure the protection and security of the investment in question. Consequently, Zaire's failure to take any protective measures to ensure the security of AMT's investment engaged its international responsibility. The tribunal stated:

> the obligation incumbent upon Zaire is *an obligation of vigilance*, in the sense that Zaire as the receiving State of investments made by AMT, an American company, shall take all measures necessary to ensure the full enjoyment of protection and security of its investment and should not be permitted to invoke its own legislation to detract from any such obligation. Zaire must show that it has taken all measure of precaution to protect the investments of AMT on its territory. It has not done so ... [28] (emphasis added)

A similar result is found in *Wena Hotels Ltd v Arab Republic of Egypt*,[29] in which an ICSID tribunal considered a UK investor's claim under the UK–Egypt BIT. The facts of the case concerned the seizure of a hotel by its employees. Relying solely on the standards developed in the *AAPL* and *AMT* cases, the tribunal found Egypt responsible for the failure to accord the investment 'fair and equitable treatment' and 'full protection and security' because it did not take any action to prevent the seizures or to immediately restore control over the hotel to Wena.

A finding of liability for failure to provide promised protection and security is necessarily fact driven. It must be based on the details of the threat as well as the government's response to that threat. The burden of proving the facts that constitute the threat, the nature and inadequacy of the government's response, and the connection of these factors to the injury suffered by the investor all rest on the claimants. Failure to carry that burden will result in a denial of government liability. For example, in the case of *Técnicas Medioambientales Tecmed, SA v United Mexican States*,[30] a Spanish company that had invested in a Mexican waste disposal facility brought a claim under the Spain–Mexico BIT. It alleged that Mexico had breached its obligation to provide 'full protection and security' from various social movements, disturbances, and demonstrations against the investor's activities. The investor claimed that Mexican authorities had encouraged the community to react adversely to the landfill and its operation. The

[27] ibid § 6.06. [28] ibid § 6.05.

[29] *Wena Hotels Ltd v Arab Republic of Egypt*, ICSID Case No ARB/98/4 (Award on Merits) (8 December 2000).

[30] *Técnicas Medioambientales Tecmed, SA v United Mexican States*, ICSID Case No ARB(AF)/00/2 (Award) (29 May 2003).

investors also asserted that the authorities did not act as quickly, efficiently, and thoroughly as they should have to prevent or terminate the adverse actions of the local population. The tribunal found that the claimant failed to provide sufficient evidence to establish a causal link between the public protests and Mexico's inaction or to show that Mexico acted unreasonably under the circumstances.[31] Like many previous tribunals, the tribunal concluded that 'the guarantee of full protection and security is not absolute and does not impose strict liability upon the State that grants it'.[32]

A lack of evidence led to similar results in *Eureko v Poland*,[33] which involved the alleged harassment and intimidation of the investor's local representatives, as well as in *Noble Ventures v Romania*,[34] which concerned protests and demonstrations by employees.

Traditionally, tribunals have interpreted provisions guaranteeing protection and security as protecting investors and their investments from *physical* injury caused by the actions of host governments, their agents, or third parties. The 2005 US–Uruguay BIT quoted earlier in this chapter appears to adopt this position by making explicit that '"full protection and security" requires each Party to provide the level of police protection required under customary international law'.[35] At the beginning of the twenty-first century, a few cases have sought to expand the term's scope to include protection against allegedly unjustified governmental actions that injure an investor's legal rights but cause no physical injury. The first such case to take this position was *CME Czech Republic v Czech Republic*,[36] a dispute brought under the Netherlands–Czech Republic BIT in which the investor claimed that certain acts and omissions of the Czech Media Council (a quasi-governmental media regulatory body) amounted to a violation of the obligation to provide full protection and security. The tribunal found that the Media Council's conduct was aimed at removing the security and legal protection from the investor's investment and so violated the standard of full protection and security. The tribunal stated: 'The host State is obligated to ensure that neither by amendment of its laws nor by actions of its administrative bodies is the agreed and approved security and protection of the foreign investor's investment withdrawn or devalued.'[37]

The decision in *CME* could be seen as a strong precedent for the expansion of the full protection and security clause to cover non-physical injuries sustained by investors. However, its precedential force would seem to be weakened by two factors. First, in the related case of *Lauder v Czech Republic*,[38] which involved

[31] ibid ¶¶ 176, 177. [32] ibid ¶ 177.

[33] *Eureko v Poland*, ICSID Case No ARB/ 01/11 (Partial Award) (19 August 2005).

[34] *Noble Ventures Inc v Romania* (Award) (12 October 2005).

[35] US–Uruguay BIT, Art 5(2)(B).

[36] *CME Czech Republic BV v Czech Republic* (Partial Award) (13 September 2001).

[37] ibid § 613.

[38] *Lauder v Czech Republic*, Award, 9 ICSID Reports 66 (3 September 2001).

the same parties and the same set of facts as in *CME*, the tribunal found no violation of the full protection and security clause. Second, the *CME* tribunal did not provide a historical analysis of the concept of full protection and security and did not give any clear reason as to why it was departing from the historical interpretation traditionally employed by courts and tribunals and choosing to expand the concept to cover non-physical actions and injuries.

Other cases have nonetheless followed the approach of *CME*. In *Azurix v Argentine Republic*,[39] a 2006 ICSID case, a US investor argued that the limits of 'full protection and security' were not confined to physical protection but also included the kind of protection described in *CME*. The investor alleged that Argentina breached the standard in question by failing to apply the relevant regulatory framework and the concession agreement applicable to the claimant's investment. Argentina thereby destroyed the security provided to those investments. In response, Argentina contested the relevance of the *AAPL* and *AMT* cases on the grounds that they involved physical destruction of the investor's facilities by the armed forces. As for the relevance of *CME*, it pointed out that relying on *CME* was questionable without referring to *Lauder*, where, on the same facts, the tribunal reached the opposite conclusion. As a final argument, in examining its liability Argentina requested the tribunal to consider that during the period under review the country was undergoing the worst economic, social, and institutional crisis in its history.

Relying on *AAPL*, *AMT*, *Wena Hotels*, and *Occidental*,[40] the tribunal concluded that the interrelation between the 'fair and equitable treatment' and 'full protection and security' 'indicates that full protection and security may be breached even if no physical violence or damage occurs'.[41] Focusing on the specific language of the clause in which full protection and security is granted, the tribunal stated:

> The cases referred to above show that full protection and security was understood to go beyond protection and security ensured by the police. It is not only a matter of physical security; the stability afforded by a secure investment environment is as important from an investor's point of view. The Tribunal is aware that in recent free trade agreements signed by the United States, for instance, with Uruguay, full protection and security is understood to be limited to the level of police protection required under customary international law. However, when the terms "protection and security" are qualified by "full" and no other adjective or explanation, they extend, in their ordinary meaning, the content of this standard beyond physical security.[42]

Thus, *Azurix* seems to suggest that the omission of the words 'full' or 'fully', which are included in some investment treaties, restrict the scope of protection to physical security and protection but that the inclusion of those words expands the scope of protection to cover non-physical injuries. On the other hand, in the later case of *Parkerings-Compangiet AS v The Republic of Lithuania*,[43] the tribunal took a different view, stating: 'It is generally accepted that the variation of language between the formulation "protection" and "full protection and security" does not make a difference in the level of protection a state is to provide.'[44]

Another later case, also involving Argentina, justified the expansion of full protection and security to non-physical injuries in a different way. In *Siemens v Argentina*,[45] the investor initiated arbitration under a German–Argentina BIT and alleged, inter alia, that Argentina breached its obligation to accord full protection and security by engaging in conduct that frustrated the contract. The respondent and the claimant had opposing positions on the scope of protection provided by the standard. According to Argentina, 'security' implied only physical security. The investor, however, gave the term a wider meaning, particularly because of the treaty's reference to 'legal security'. Thus, the tribunal had to determine whether 'security' referred solely to physical security or whether it applied in a wider sense. Having noted that the definition of investment included tangible and intangible assets, the tribunal found that 'the obligation to provide full protection and security is wider than "physical" protection and security'. It offered the following reasoning:

> It is difficult to understand how the physical security of an intangible asset would be achieved. In the instant case, 'security' is qualified by 'legal'. In its ordinary meaning 'legal security' has been defined as 'the quality of the legal system which implies certainty in its norms and, consequently, their foreseeable application.' It is clear that in the context of this meaning the Treaty refers to security that is not physical. In fact, one may question given the qualification of the term 'security', whether the Treaty covers physical security at all. Arguably it could be considered to be included under 'full protection', but that is not an issue in these proceedings.[46]

Based on this textual interpretation of the standard, the tribunal concluded that Argentina's initiation of the renegotiation of the contract constituted a violation of

[39] *Azurix v Argentine Republic*, ICSID Case No ARB/01/12 (23 June 2006).

[40] *Occidental Exploration and Production Company v The Republic of Ecuador*, LCIA Case No UN3467 (Final Award) (1 July 2004). The tribunal pointed out the fact that in some BITs fair and equitable treatment and full protection and security appear as a single standard, in others as separate protections. Under the BIT in question, the tribunal observed that, since 'fair and equitable treatment' and 'full protection and security' appeared sequentially, they constituted different obligations. The tribunal subsequently held that:

> the Respondent has breached its obligations to accord fair and equitable treatment under Article II(3)(a) of the Treaty. In the context of this finding the question of whether in addition there has been a breach of full protection and security under this Article becomes moot as a treatment that is not fair and equitable automatically entails an absence of full protection and security of the investment.

[41] ibid ¶ 406.

[42] ibid ¶ 408.

[43] *Parkerings-Compangiet AS v The Republic of Lithuania* ISCID Case No ARB/05/08 (14 August 2007).

[44] ibid ¶ 354, citing N Rubins and S Kinsella, *International Investment, Political Risk and Dispute Resolution* (2005) to justify this proposition.

[45] *Siemens v Argentina*, ICSID Case No ARB/02/8 (Award) (6 February 2007).

[46] ibid § 303.

its obligations under the BIT because it was done for the sole purpose of reducing its costs, was unsupported by any declaration of public interest, and affected the legal security of Siemens' investment. Moreover, the qualifying adjective 'legal' was meant to extend the scope of the full protection and security clause. One may question the tribunal's reasoning regarding the emphasis it placed on the fact that intangible assets are not subject to physical injury. Merely because some assets are subject to physical injury and others are not does not necessarily mean that a treaty's contracting parties intended to depart from the traditional definition and scope of full protection and security. One could equally well conclude from reading the treaty's provisions that the contracting parties only intended to protect assets from physical injury that are capable of physical injury.

At least one award since the *CME* decision has maintained the more traditional approach to interpreting full protection and security. In *Saluka Investments BV (The Netherlands) v The Czech Republic*, the tribunal determined that the Czech Republic did not violate the Czech Republic-Netherlands BIT when it took measures to stop trading in the claimant's securities. Under the BIT, investors were promised 'full security and protection'. In reaching its decision, the tribunal stated: 'The practice of arbitral tribunals seems to indicate however that the "full protection and security clause" is not meant to cover just any kind of impairment of an investor's investment but to protect more specifically the physical integrity of an investment against interference by the use of force.'[47]

In addition to the apparent divergence of views on the scope of the full protection and security clause, it would seem that the treaty provisions and the cases represent two different views about the nature of full protection security. On the one hand, some view it as part of a minimum standard of international law elaborated in customary international law. On the other hand, some view it as an independent, self-contained treaty standard to be interpreted without reference to the limitations of customary international law. Thus, *CME* seemed to view the standard as independent, while *Saluka* tended to view it as a manifestation of traditional customary international law. The NAFTA Free Trade Commission, which is empowered under the NAFTA treaty to make authoritative interpretations of the treaty, has sought to clarify the issue by opting for the traditional approach. In 2001, it issued such an interpretation for the term 'full protection and security' as found in NAFTA Article 1105(1): 'The concepts of "fair and equitable treatment" and "full protection and security" do not require treatment in addition to or beyond that which is required by the customary international law minimum standard of treatment of aliens.'[48]

From this interpretation it can be inferred that, as was the case under customary international law, full protection and security should be limited to physical injuries.

[47] *Saluka Investments BV (The Netherlands) v The Czech Republic* (17 March 2006) ¶484.
[48] NAFTA Free Trade Commission, *Notes of Interpretation of Certain Chapter 11 Provisions* (31 July 2001).

(d) Conclusion

In reviewing the jurisprudence related to the meaning of the term 'full protection and security' and the variations of the term found in investment treaties, one may conclude the following:

1. The core element under this standard is an obligation on the part of a contracting state to exercise due diligence in providing physical protection and security from injurious acts by government agents or third parties to the investor and its investment. The standard imposes an objective obligation that must not be less than the minimum standard of vigilance and care required by international law. Qualifying words such as 'constant' or 'full' that are found in many treaties might strengthen the required standard of 'protection and security' by requiring a standard of 'due diligence' higher than the 'minimum standard' of general international law.
2. The due diligence obligation requires a host state to undertake all measures that could be reasonably expected to prevent damage to foreign investments. Since due diligence means, according to the cases and commentators, 'nothing more nor less than the reasonable measures of prevention which a well-administered government could be expected to exercise under similar circumstances',[49] it would seem that a state's lack of resources or the existence of crisis conditions are not defences to a state's obligation to meet this objective standard. A state may breach its obligation by action, failure to act, omission to act, or by instigation or connivance. Moreover, a state may not absolve itself of international responsibility arising out of a treaty violation by invoking its legislation as a defence.
3. The nature and scope of the protection and security standard under a given treaty depends on its precise wording and its place in the treaty relative to other standards of investment treatment.
4. Certain arbitral cases indicate that protection may be expanded to cover non-physical injuries caused by host states or their instrumentalities. Thus, the host state may be held responsible for the failure to provide 'legal security', which is defined by tribunals as the quality of the legal system and particularly the certainty of its norms and their foreseeable application. Additionally, the interrelationship of 'fair and equitable treatment' and 'full protection and security' might allow for full protection and security to be breached without physical violence or damage; however, the force and durability of this trend is not yet clear or certain.

[49] AV Freeman, 'Responsibility of States for the Unlawful Acts of Their Armed Forces' (1956) 88 *Receuil des Cours* 261.

9.4 Fair and Equitable Treatment

(a) Background

Virtually all investment treaties contain promises by the contracting parties to give 'fair and equitable treatment' to investors and the investments of other contracting parties. Although the precise formulation of these promises of fair and equitable treatment and the conditions attached thereto vary considerably among treaties, fair and equitable treatment is a core concept embedded in nearly all international investment agreements. Indeed, one might say that it represents the 'golden rule' of investment treaties.

While the term 'fair and equitable' is vague and ambiguous on its face and is never defined within the treaties themselves, it is invoked so often in contemporary investor–state arbitrations that one scholar has labelled it 'an almost ubiquitous presence' in investment litigation.[50] Its undefined and potentially elastic nature has made it a favourite of aggrieved investors and their lawyers when seeking compensation for the allegedly injurious acts of host country governments. Indeed, some have claimed that a majority of successful claims in investor-state arbitrations have been based on the fair and equitable clause.[51] As a result of its wide use, tribunals have interpreted and applied the fair and equitable standard in a large number of arbitral cases, and scholars have analysed and commented upon it extensively.

Unlike the full protection and security clause, which dates from the development of friendship, commerce, and navigation treaties in the nineteenth century, the concept of fair and equitable treatment in investment treaties has its origins in the post-World War II era. Whereas the concept of full protection and security was developed within treaties whose fundamental purpose was to facilitate trade, the fair and equitable treatment standard arose within international efforts to foster international investment specifically. These early developments took place at both the multilateral and bilateral levels.

Commentators[52] seem to agree that the fair and equitable treatment standard became part of the international legal landscape with the attempts to establish an International Trade Organization (ITO) through the Havana Charter of 1948 after World War II. In Article 11(2), the Havana Charter provided that the ITO had authority to make recommendations for and promote bilateral or multilateral agreements on measures designed: '(i) to assure *just and equitable treatment* for the enterprise, skills, capital, arts and technology brought from one Member country to another' (emphasis added).[53] The ITO would never become

[50] R Dolzer, 'Fair and Equitable Treatment: A Key Standard in Investment Treaties' (2005) 39 Int'l Lawyer 87.

[51] Dolzer and Schreuer (n 9 above) 119.

[52] UNCTAD, *Fair and Equitable Treatment*, UNCTAD/ITE/IIT/11 (1999) vol 3, p 26.

[53] UNCTAD, *International Investment Instruments: A Compendium* (1996) vol 1, p 4.

a reality due to the failure of certain countries to ratify it,[54] but the concept of just and equitable treatment and fair and equitable treatment persisted in subsequent efforts to shape multilateral frameworks for investment. Such efforts can be seen in the failed 1948 Economic Agreement of Bogota among Latin American States,[55] the private initiative in 1959 known as the Abs-Shawcross Draft Convention on Investment Abroad,[56] and the 1963 OECD Draft Convention on the International Protection of Foreign Property, subsequently revised in 1967.[57]

Although none of these multilateral efforts resulted in an enforceable treaty, their discussion and elaboration of the fair and equitable concept seem to have implanted the idea into the minds of the epistemic community of international lawyers and negotiators, who would become a principal channel for its diffusion and development among countries. Eventually, these ideas found their way into national programmes to negotiate bilateral investment treaties, and through this process the fair and equitable treatment standard has become a principle of international law and a fundamental norm of the emerging global regime for international investment. Indeed, one would say that fair and equitable treatment is, to employ Hans Kelsen's concept from his *Pure Theory of Law* (1934), the *grundnorm* or basic norm of the investment treaty system.

The first country to adopt the fair and equitable concept in treaty practice was the United States. With the expansion of American investment abroad after World War II, the United States negotiated a series of modern friendship, commerce, and navigation (FCN) treaties whose primary goal was to protect US foreign investments by obtaining treaty commitments from other countries on new absolute standards of investment treatment, one of which was 'equitable treatment'. For example, US FCN treaties with Uruguay and Ireland contained the obligation to accord 'equitable' treatment to the capital of nationals and companies of the other party.[58] Subsequent FCN treaties routinely employed the term 'fair and equitable treatment' in their texts.[59]

[54] ibid vol 1, p xx.

[55] Article 22 of the Bogota Agreement included the following provision:

> Foreign capital shall receive equitable treatment. The States therefore agree not to take unjustified, unreasonable or discriminatory measures that would impair the legally acquired rights or interests of nationals of other countries in the enterprises, capital, skills, arts or technology they have supplied.

[56] This draft, prepared under the leadership of Herman Abs (Director-General of the Deutsche Bank) and Lord Shawcross (the UK Attorney General), stipulated in Art 1 that 'each party shall at all times ensure fair and equitable treatment to the property of the nationals of the other Parties'. H Abs and L Shawcross, 'The Proposed Convention to Protect Foreign Investment: A Round Table: Comment on the Draft by the Authors' (1960) 9 J of Public L 119, 119–24.

[57] Article 1 of the Draft stated: 'Each Party shall at all times ensure fair and equitable treatment to the property of the nationals of the other Parties.'

[58] Wilson (n 11 above) 101, 104.

[59] R Wilson, *United States Commercial Treaties and International Law* (1960) 120. The US FCN treaties with Belgium and Luxembourg, France, Greece, Ireland, Israel, Nicaragua, and Pakistan contained the express assurance that foreign persons, properties, enterprises, and other interests

European countries launched their programmes to negotiate bilateral investment treaties around 1960 and the fair and equitable treatment standard would eventually also become a basic feature of those agreements. For example, in the period from the early 1960s to the early 1990s, the fair and equitable treatment standard was incorporated into over 300 BITs. One study of 335 of these treaties found that only 28 did not expressly include the standard and 196 combined the fair and equitable standard with the national treatment and most-favoured-nation treatment standards.[60]

In recent years, the number of capital-exporting countries that have proposed draft BITs for negotiations with their capital-importing counterparts has broadened, so that countries such as Chile and China, not traditionally regarded as capital-exporting states, now have model BITs that incorporate norms of fair and equitable treatment. BITs between developing countries, such as Peru and Thailand, the United Arab Emirates and Malaysia, and Argentina and Chile, as well as those between states in transition and developing countries, such as Bulgaria and Ghana and Russia and the Republic of Korea, are additional evidence of the concept's broad acceptance. There are still deviations in practice, but the inclusion of the fair and equitable standard is clearly a dominant trend in investment treaty-making.[61]

(b) Formulation of the standard

The precise formulation of the fair and equitable standard varies among investment treaties. In some treaties, the standard is given a prominent and independent position at the beginning of the general treatment clauses. A number of French treaties, as well as Belgium-Luxembourg and Swedish agreements, adopt this approach. German BITs, on the other hand, tend to refer to the standard in the admission clause.[62] In still other treaties, the fair and equitable treatment standard is combined with provisions on the protection and security of the investment, as is the case in UK and US treaties. Yet other treaties have combined the clause with provisions prohibiting discriminatory measures, or with national and most-favoured-nation standards.[63] NAFTA includes it as part of the section discussing the protection to be accorded under international law. Thus, Article 1105(1) of NAFTA provides: 'Each Party shall accord to investments of investors of another Party treatment in accordance with international law, including fair and equitable treatment and full protection and security.'

would receive 'equitable' treatment, while other US FCN treaties—including those with Ethiopia, the Federal Republic of Germany, Oman, and the Netherlands—contemplated 'fair and equitable' treatment for a similar set of items in the foreign investment process.

[60] M Khalil, 'Treatment of Foreign Investment in Bilateral Investment Treaties' (1992) 8 ICSID Rev-FILJ 339, 351–5.

[61] S Vasciannie, 'The Fair and Equitable Treatment Standard in International Investment Law and Practice' (1999) 70 BYIL 100, 105, 130.

[62] R Dolzer and M Stevens, *Bilateral Investment Treaties* (1995) 58.

[63] ibid 59.

A treaty that offers fair and equitable treatment and combined national and most-favoured-nation treatment provides foreign investors with both non-contingent and contingent forms of protection. From the perspective of the investor, the fair and equitable component establishes an important fixed reference point because it provides an apparently definite standard that will not vary according to external considerations—its content turns solely on what is fair and reasonable in the circumstances. The fair and equitable standard also prevents discrimination against the beneficiary when discrimination would amount to unfairness or inequity under the circumstances. Simultaneously, national and most-favoured-nation treatment, as contingent standards, protect investments by ensuring equality or non-discrimination in relation to investments by other persons. A foreign investor might believe that even if a state promises protection under national and most-favoured-nation treatment standards that level of protection is insufficient because nationals and investors from the most favoured nation are themselves receiving inadequate protection. In such cases, the fair and equitable treatment standard helps to ensure that the investor will receive a minimum level of protection based on notions of fairness and equity.[64]

(c) The complexities of interpreting and applying the standard

Interpreting the fair and equitable standard and applying it to the kind of complicated fact situations that usually present themselves in investor–state disputes are not easy tasks. Indeed these tasks are complicated by at least three factors. First the term 'fair and equitable' is, one may say without exaggeration, maddeningly vague, frustratingly general, and treacherously elastic. Second, the treaty provisions and the agreements in which the terms are embedded offer no definition for them, nor any real guidance on how to apply them. Third, despite the abundant scholarly commentary on the subject and a growing volume of arbitral decisions, application of the fair and equitable standard is so tied to the facts of the specific cases as to limit the utility of the arbitral decisions and doctrinal analysis.

For persons attempting to apply the treaty standard, one initial question is whether the term 'fair and equitable' embodies a single standard or two distinct standards, one concerning fairness and the other equity. As a matter of practice, the two words are employed as a single standard of treatment. For one thing, most treaty texts and other instruments providing for fair and equitable treatment for investments combine the two words to refer to a single treatment standard—'fair and equitable treatment'. For example, the model BITs prepared by Chile, China, France, Germany, the United States, and the United Kingdom, as well as regional instruments such as NAFTA, the 1993 Treaty Establishing the Common Market for Eastern and Southern Africa (COMESA), and the

[64] UNCTAD, *Fair and Equitable Treatment* (1999) 16.

1994 Energy Charter Treaty, all use the phrase 'fair and equitable treatment' as part of a single concept. An UNCTAD study concluded that this fact points to 'fair and equitable treatment' being a single standard and not two separate standards. Two considerations support this view. First, the consistency with which states have linked the two terms in the verbal formula of 'fair and equitable' treatment supports the view that states believe there is a single standard. The history of the term's use in various efforts to draft a multilateral treaty in the post-World War II era further supports this view. Second, if states intended 'fair and equitable' to refer to two separate standards, they would have made that meaning explicit in the treaty texts. No state has chosen to do so. They could, for example, set out the fairness standard in one treaty provision, and the equity standard in another. The fact that they have not done so indicates that the contracting states intended the phrase 'fair and equitable treatment' to connote a single standard.[65]

One may speculate as to whether a promise in an investment treaty of 'equitable' treatment or 'just and equitable' treatment grants weaker legal protection to investors than a commitment to 'fair and equitable' treatment. However, up to this point there seems to be little basis for making such a distinction. For one thing, a reference to fairness and equity together would seem to afford investors at least as much protection as 'equitable' treatment. Moreover, in view of the similarity in meaning between fairness, on the one hand, and equity, on the other, in the context of investment relations it is difficult to identify ways in which the combination of the two provides greater protection in practice than the equitable standard alone. Similarly, while the term 'just and equitable' treatment occurs in some treaties, it is difficult to determine how this formulation differs in substance from the fair and equitable standard.[66]

(d) Differing concepts of the fair and equitable standard

An examination of treaty practice, jurisprudence, and scholarly commentary reveals two different conceptions of the nature of the fair and equitable standard: (1) that fair and equitable treatment merely reflects the *international minimum standard* required by customary international law; or, (2) that the standard is *autonomous and additional* to general international law. Let us examine each of these views briefly.

(i) Fair and equitable treatment as the international minimum standard

As was discussed in Chapter 3, the traditional position of western governments and commentators has been that states owe aliens and their property a certain

[65] ibid 14. [66] ibid 19.

minimum level of treatment regardless of the treatment each state gives to its own nationals. Treatment short of this required minimum creates state responsibility for any resulting injuries. One view of the fair and equitable treatment standard is that it merely refers to that minimum international standard and does not give investors any additional rights. This position has often been advanced by developing countries, which have sought to limit the scope of the fair and equitable treatment standard. For example, during the negotiations for the Draft United Nations Code of Conduct on Transnational Corporations, it has been claimed that the Group of 77, which is constituted exclusively of developing countries, collectively took the position that the fair and equitable treatment language was equivalent to the international minimum standard.[67]

The treaty practice of certain countries also seems to support this view of fair and equitable treatment. Article 5 of the 2004 US Model BIT, entitled 'Minimum Standard of Treatment', as well as the investment chapters of the recently concluded US Free Trade Agreements go even further and attempt to define a minimum standard of treatment. They provide that:

> 1. Each Party shall accord to covered investments treatment in accordance with customary international law, including fair and equitable treatment and full protection and security.

Paragraph 2 of Article 5 makes clear that the fair and equitable treatment standard does not go beyond the minimum standard:

> 2. For greater certainty, paragraph 1 prescribes the customary international law minimum standard of treatment of aliens as the minimum standard of treatment to be afforded to covered investments. The concepts of 'fair and equitable treatment' and 'full protection and security' do not require treatment in addition to or beyond that which is required by that standard, and do not create additional substantive rights.[68]

Canada has taken a similar approach in its model Foreign Investment Protection and Promotion Agreement.[69]

Certain arbitral decisions have also adopted this concept of fair and equitable treatment. In *Genin v Estonia*,[70] the tribunal considered whether certain actions by Estonia amounted to a violation of its obligation to accord 'fair and equitable treatment' and 'non-discriminatory and non-arbitrary treatment' under the 1994 US–Estonia BIT. The tribunal ultimately dismissed the claim, viewing the fair and equitable treatment standards as incorporating the minimum standard under international law:

[67] P Robinson, 'The June 1985 Reconvened Special Session on the Code' (1985) CTC Reporter No 20, 15.

[68] <http://www.ustr.gov/sites/default/files/U.S.%20model%20BIT.pdf> accessed 24 August 2009.

[69] C Yannaca-Small, *Fair and Equitable Treatment Standard in International Investment Law* (OECD, 2005) 87.

[70] *Alex Genin, Eastern Credit Limited, Inc and AS Baltoil (US) v Republic of Estonia*, ICSID Case No ARB/99/2 (Award) (25 June 2001).

Article II(3)(a) of the [US–Estonia] BIT requires the signatory governments to treat foreign investment in a 'fair and equitable' way. Under international law, this requirement is generally understood to 'provide a basic and general standard which is detached from the host State's domestic law.' While the exact content of this standard is not clear [citing Brownlie], the Tribunal understands it to require an 'international minimum standard' that is separate from domestic law, but that is, indeed, a *minimum* standard.[71]

In *Occidental v Ecuador*,[72] the tribunal asked 'whether the fair and equitable treatment mandated by the Treaty is a more demanding standard than that prescribed by customary international law' and concluded that 'the BIT standard was not different from the minimum standard required under customary international law concerning both the stability and predictability of the legal and business framework of the investment'.[73]

The most significant and explicit adoption of the concept of fair and equitable treatment as a minimum international standard is found in the text of NAFTA and related practice. Article 1105(1) of NAFTA, entitled 'Minimum Standard of Treatment' states: 'Each Party shall accord to investments of investors of another Party treatment in accordance with international law, including fair and equitable treatment and full protection and security.'

Two elements of this text reveal its conceptual basis. The first is its heading, the 'Minimum Standard of Treatment', which is a clear reference to customary international law. The second is the inclusion of the fair and equitable treatment standard in referring to international law ('international law, including fair and equitable treatment'). Both these elements indicate that the NAFTA considers the fair and equitable treatment as part of the minimum standard of treatment under international law, not autonomous from it.[74]

In spite of these indications, some early NAFTA tribunals did not regard the fair and equitable treatment standard in Article 1105(1) as being restricted to customary international law. Instead, the tribunals viewed it as having an additive character. For example, the Partial Award in *SD Myers*[75] stated that the breach of a rule of international law might not be decisive in determining if fair and equitable treatment had been denied. The tribunal said:

In some cases, the breach of a rule of international law by a host Party may not be decisive in determining that a foreign investor has been denied 'fair and equitable treatment', but the fact that a host Party has breached a rule of international law that is specifically designed to protect investors will tend to weigh heavily in favor of finding a breach of Article 1105.[76]

[71] ibid ¶ 367.
[72] *Occidental Exploration and Production Co v Ecuador*, LCIA Case No UN3467 (Award) (1 July 2004).
[73] ibid ¶¶ 188, 190.
[74] C Schreuer, 'Fair and Equitable Treatment in Arbitral Practice' (2005) 6 J of World Investment & Trade 357, 362.
[75] *SD Myers v Government of Canada* (Partial Award) (12 November 2000) (2001) 40 ILM 1408.
[76] ibid ¶ 64.

The tribunal in *Pope & Talbot*[77] was even more explicit. The tribunal discussed the issue of the relationship between Article 1105 of NAFTA and customary international law at some length, and found that the fairness elements in Article 1105 were additional to the requirements imposed by international law. It based this conclusion on the view that the language of Article 1105 grew out of bilateral treaties that had conceived of the fair and equitable standard as extending beyond the minimum international law standard. According to the tribunal, 'the language and evident intention of the BITs makes the discrete (i.e. additive) standards of interpretation the proper one. A contrary reading would do violence to the BIT language.'[78] It followed that 'compliance with the fairness elements must be ascertained free of any threshold that might be applicable to the evaluation of measures under the minimum standard of international law'.[79]

In reaction to these arbitral determinations, the NAFTA Free Trade Commission (FTC), a body composed of representatives of the three states, which has the power to adopt binding interpretations under Article 1131(2) of the treaty, issued the following Note of Interpretation on 31 July 2001:

Minimum Standard of Treatment in Accordance with International Law

1. Article 1105(1) prescribes the customary international law minimum standard of treatment of aliens as the minimum standard of treatment to be afforded to investments of investors of another Party.
2. The concepts of 'fair and equitable treatment' and 'full protection and security' do not require treatment in addition to or beyond that which is required by the customary international law minimum standard of treatment of aliens.
3. A determination that there has been a breach of another provision of the NAFTA, or of a separate international agreement, does not establish that there has been a breach of Article 1105(1).[80]

In a subsequent decision on damages,[81] the tribunal criticized the FTC's power to issue the Interpretation[82] as well as its correctness,[83] but reluctantly accepted the FTC's Interpretation.[84] Later NAFTA tribunals in the *Mondev*,[85]

[77] *Pope & Talbot v Canada* (Award) (10 April 2001) 7 ICSID Reports 102, 105–18.
[78] ibid ¶ 13.
[79] ibid ¶ 111.
[80] Notes of Interpretation of Certain Chapter 11 Provisions (NAFTA Free Trade Commission, 31 July 2001).
[81] *Pope & Talbot v Canada* (Award in Respect of Damages) (31 May 2002) (2002) 41 ILM 1347.
[82] ibid ¶¶ 17–24.
[83] ibid ¶¶ 25–47.
[84] ibid ¶¶ 48–69. See also P Dumberry, 'The Quest to Define "Fair and Equitable Treatment" for Investors under International Law—the Case of the NAFTA Chapter 11 Pope & Talbot Awards' (2004) 3 J of World Investment 4658–91.
[85] *Mondev International Ltd v United States of America* (Award) (11 October 2002).

UPS,[86] *ADF*,[87] and *Loewen*[88] cases relied on the FTC's Notes of Interpretation in applying the fair and equitable standard. Nonetheless, some scholars have argued that the concept of fair and equitable treatment in NAFTA has little application to the interpretation of other investment treaties. The reason is that the NAFTA standard is expressed in a provision entitled 'Minimum Standards of Treatment', which is not widely used in other treaties, and because NAFTA, unlike other treaties, specifically states that the fair and equitable standard falls within the international law minimum treatment standard. Moreover, other treaties have not been subject to an authoritative interpretation like that issued by the FTC.[89]

(ii) Fair and equitable treatment standard as an autonomous standard additional to international law

Many scholars and non-NAFTA tribunals have concluded that the fair and equitable standard, when expressed without qualification or condition, is an autonomous, additional standard whose scope is not limited by the minimum standards required by international law. According to this view, the fair and equitable clause imposes a higher standard of treatment on host states than customary international law does. For example, FA Mann states that:

> The terms 'fair and equitable treatment' envisage conduct which goes far beyond the minimum standard and afford protection to a greater extent and according to a much more objective standard than any previously employed form of words. A tribunal would not be concerned with a minimum, maximum or average standard. It will have to decide whether in all circumstances the conduct in issue is fair and equitable or unfair and inequitable. No standard defined by other words is likely to be material. The terms are to be understood and applied independently and autonomously.[90]

Various arguments support this view. First, if states and investors believed that the fair and equitable standard was entirely interchangeable with the international minimum standard, they could have stated so clearly in their investment treaty texts; instead, most investment instruments do not make an explicit link between the two in the way that the NAFTA has done. Therefore, one may reasonably infer that most contracting states do not believe that fair and equitable treatment is implicitly the same as the international minimum standard. Second, attempts to equate the two standards fail to take into account the significant historical debate between developed, capital-exporting countries and developing capital-importing countries concerning the very existence of the international minimum standard. While developed countries have strongly supported the existence of a minimum international standard, many developing countries have denied its very existence in customary international law. Against this uncertain background, it is difficult to assume that countries participating in investment treaties intended to incorporate the international minimum standard into their treaties without expressly stating so.[91] One may therefore conclude that the fair and equitable standard is autonomous and is not necessarily equivalent to the international minimum standard. Indeed, in view of the various historical challenges to the international minimum standard (as discussed in Chapter 3), and the fact that capital-exporting countries have been the driving force behind the investment treaty movement, it is likely that the fair and equitable treatment provision is intended to be a higher standard of protection than that provided under the disputed international minimum standard. The inclusion of the fair and equitable standard, unknown to customary international law prior to the advent of investment treaties, seems to be intended to provide investors with a basic level of protection in situations where the other substantive provisions of international and national law are inapplicable.[92] Its function in the treaty can thus be seen as filling gaps not covered by other treaty provisions.[93] It also serves to guide the interpretation of other treaty provisions and assure that the general standard of fair and equitable treatment of foreign investment, a fundamental treaty goal, is attained.

These arguments are weakened, however, by the fact that neither the texts of individual BITs nor the available negotiating history demonstrates a clear, mutual intent by the contracting parties to adopt a standard that is higher than that required by customary international law in specific treaties.

Regardless of the different arguments on this issue, it must be admitted that the minimum international standard and the fair and equitable treatment standard overlap significantly with respect to issues like arbitrary treatment, discrimination, and unreasonableness. Moreover, the presence of a provision assuring fair and equitable treatment in an investment instrument does not automatically incorporate the international minimum standard for foreign investors. On the other hand, as at least one tribunal has suggested, the difference between the two standards may for all practical purposes be more apparent than real.[94] Indeed, one might say that for the purpose of applying and interpreting a fair and equitable

86 *United Parcel Service v Canada* (Award on the Merits) (24 May 2007) UNCITRAL (NAFTA). 87 *ADF Group, Inc v United States of America* (Award) (9 January 2003).

88 *Loewen Group, Inc and Raymond L Loewen v United States of America* (Award) (26 June 2003).

89 Dolzer and Schreuer (n 9 above) 126. See also C Schreuer, 'Fair and Equitable Treatment in Arbitral Practice' (2005) 6(3) J of World Investment 360.

90 FA Mann, 'British Treaties for the Promotion and Protection of Investments' (1981) 52 BYIL 24, 1244.

91 UNCTAD, *Fair and Equitable Treatment* (1999) 13.

92 K Vandevelde, *United States Investment Treaties* (1992) 76.

93 Dolzer and Schreuer (n 9 above) 123.

94 *Azurix v Argentine Republic*, ICSID Case No ARB/01/12 (Award) (14 July 2006) ¶ 361. In interpreting Art II.2(a) of the Argentina–US BIT, which provides that '[i]nvestment shall at all times be accorded fair and equitable treatment, shall enjoy full protection and security and shall in no case be accorded treatment less than required by international law', the tribunal stated:

> The purpose of the third sentence is to set a floor, not a ceiling, in order to avoid a possible interpretation of these standards below what is required by international law. While this

clause in an investment treaty that makes no reference to the minimum international standard, the debate is largely irrelevant. When a claimant invokes the fair and equitable provision of a treaty, the central issue for arbitral tribunals is whether the alleged government conduct was unfair and inequitable, not whether it violated some minimum international standard that the treaty does not refer to. The challenge is one of interpreting and applying this vague and general term to a usually highly complex fact situation.

(e) The content of the standard

The application of the fair and equitable standards in most cases is difficult for a variety of reasons. First, investment treaties do not define the term. Thus, arbitrators, government officials, investors' legal counsel, and others who would apply the term must begin interpretation by confronting two words, 'fair' and 'equitable', that because of their vagueness and generality allow for great subjectivity. Second, as a result, the standard created will be highly flexible and may result in a subjective decision-making process that disappointed litigants may consider unprincipled. Third, the fact situations that the term must be applied to are highly complex and in many cases involve troubled relationships between investors and host governments stretching over significant periods of time and involving multiple interactions. Thus, determining whether a particular governmental action violates the fair and equitable standards depends greatly on the facts of the individual case.[95]

In actual practice, it is impossible to anticipate the entire range of state actions that may injure an investor.[96] Some might consider this lack of precision a virtue rather than a shortcoming because it promotes flexibility in the investment process. Like other broad legal principles (such as 'due process of law', a term found in many domestic legal systems), the fair and equitable standard has been and will continue to be elaborated and given specific content through judicial and arbitral practice.[97] Thus, its very vagueness and generality endow it with a flexibility that will permit it to evolve in the light of experience by investors, host countries, and international arbitration tribunals. At the same time, interpreters of the standard must guard against the danger of subjectivity, bias, and lack of discipline in the interpretation process.

conclusion results from the textual analysis of this provision, the Tribunal does not consider that it is of material significance for its application of the standard of fair and equitable treatment to the facts of the case. As it will be explained below, the minimum requirement to satisfy this standard has evolved and the Tribunal considers that its content is substantially similar whether the terms are interpreted in their ordinary meaning, as required by the Vienna Convention, or in accordance with customary international law.

ibid ¶361.

95 *Noble Ventures, Inc v Romania*, ICSID Case No ARB/01/11 (Award) (12 October 2005) 181.

96 Vasciannie (n 61 above) 100, 104, 145.

97 P Weil, 'The State, the Foreign Investor, and International Law: The no Longer Stormy Relationship of Menage a Trois' (2000) 15 ICSID Rev—FILJ 401, 415

Usually, the process of interpreting the fair and equitable clause in most arbitral proceedings begins with a reference to the Vienna Convention on the Law of Treaties, particularly Article 31(1), which provides: '(1) A treaty shall be interpreted in good faith in accordance with the *ordinary meaning* to be given the terms of the treaty *in their context and in light of its object and purpose'* (emphasis added). Thus, three elements are of particular importance in interpreting the fair and equitable standard: (1) the ordinary meaning of the term 'fair and equitable'; (2) the context in which the term 'fair and equitable' is used; and (3) the object and purpose of the investment treaty in question.[98] An inquiry into the ordinary meaning of the words 'fair' and 'equitable' usually yields very little. As the tribunal in Saluka stated after making its own strenuous efforts in this regard:

> The 'ordinary meaning' of the 'fair and equitable treatment' standard can only be defined by terms of almost equal vagueness. In *MTD*, the tribunal stated that: 'In their ordinary meaning, the terms "fair" and "equitable" ... mean "just", "even handed", "unbiased" "legitimate."' On the basis of such and similar definitions, one cannot say more than the tribunal did in *S.D. Meyers* by stating that an infringement of the standard requires 'treatment in such an unjust or arbitrary manner that the treatment rises to a level that is unacceptable from an international perspective'.[99]

The context of the term 'fair and equitable' is the whole treaty in which it is employed. Thus, the term must be interpreted not just as three words plucked from the text but instead must be construed from within the context of the various rights and responsibilities and conditions and limitations to which the contracting parties agreed.

And finally, following the directives of Article 31(1) of the Vienna Convention, the tribunal must take into account the objects and purposes of the treaty. Here, most tribunals turn to the treaty's preamble to understand those objects and purposes. Individual treaties differ in their stated objectives, but while the treaty's title states that its immediate goal is the protection and promotion of investments, treaties' preambles often express far broader goals, such as economic cooperation between the treaty partners, economic development of the contracting parties, or mutual prosperity. As the Saluka tribunal noted, these broad goals lead to the conclusion that the promotion and protection of investment is not the only goal of the treaties and a balanced approach that takes into account these diverse goals must be used in interpreting fair and equitable treatment:

> 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

98 See eg *Saluka Investment BV (Netherlands) v The Czech Republic* (Partial Award) ¶ 297, which adopted a similar tripartite approach.

99 ibid ¶ 297

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.[100]

Thus, it would appear that tribunals should take these broader goals into consideration when interpreting and applying the term 'fair and equitable treatment' and other treaty provisions.

In the end, an analysis of the treaty's text is necessary, but not sufficient, for the interpretation and application of the fair and equitable standard to an investment dispute. Normally, one must also consider decisions of tribunals in other cases to gain a better understanding of a term now found in virtually all investment treaties. Within a relatively short time, numerous arbitral tribunals have applied the fair and equitable standard in numerous investment treaties in diverse situations and in many countries and industries. While these decisions only bind the parties in those specific cases, they also elaborate and give content to what is, by its terms, an imprecise standard. Arbitrators, legal counsel, and government officials all refer to this accumulated jurisprudence when seeking to apply the standard to new situations. Moreover, such cases have been the subject of much doctrinal commentary by scholars, yet another source of information for those seeking to apply the fair and equitable standard to specific situations.

An examination of the cases applying the fair and equitable standard reveals that arbitral tribunals have developed specific criteria, norms, and principles to determine whether host states have given fair and equitable treatment to investors. In general, tribunals have been called upon to determine whether specific governmental actions, such as amending legislation, revising administrative regulations, and modifying contracts in ways that adversely affect an investor's interests, have thereby denied investors fair and equitable treatment. Not all such actions are a violation of the fair and equitable standard. States have a right to regulate persons and activities on their territories and do not cede that right when they sign an investment treaty. Therefore, in interpreting the meaning of fair and equitable treatment with respect to investors, tribunals must balance the legitimate and reasonable expectations of investors with the host country's legitimate regulatory interests.[101]

Among the principles most often relied upon by tribunals when applying the fair and equitable standard is whether the host state has: (1) failed to protect the investor's legitimate expectations; (2) failed to act transparently; (3) acted arbitrarily or subjected the investor to discriminatory treatment; (4) denied the investor access to justice or procedural due process; or (5) acted in bad faith. Let us examine each of these arbitration-based interpretations of the fair and equitable standard in turn. It must also be recognized, however, that these five general principles are not separate and distinct, but often overlap and blend into one another. It should also be noted

[100] ibid ¶ 300. [101] ibid ¶ 306.

that some of these principles, such as the prohibition on arbitrary or discriminatory actions or on measures that are denial of access to justice, are stated in particular treaties as explicit, independent standards in addition to being subsumed within the meaning of fair and equitable treatment.

(i) Failure to protect the investor's legitimate expectations

Investor expectations are fundamental to the investment process. It is the investor's expectations with respect to the risks and rewards of the contemplated investment that have a crucial influence on the investor's decision to invest. States seek to influence these investment decisions through their actions, laws, regulations, and policies. Indeed, the very idea of investment promotion, which is a fundamental goal of virtually all investment treaties, is to create an expectation of profit in the minds of potential investors that will lead them to commit their capital and technology to the country in question. Thus, when a state has created certain expectations through its laws and acts that have led the investor to invest, it is generally considered unfair for the state to take subsequent actions that fundamentally deny or frustrate those expectations.

Respecting legitimate expectations is not only important to be fair to the individual but also important to the effectiveness of a country's economic system. The renowned German sociologist Max Weber emphasized the role of 'calculability' in the development of modern capitalism. He saw the main contribution of the legal system in modern capitalism as making economic life more calculable or predictable.[102] In the economic context, calculability refers to the likelihood that an economic actor will achieve its legitimate economic expectations. Economic activity is negatively affected if calculability is reduced by governmental or other action.

The idea that governing authorities must respect the legitimate expectations they create is supported by various bodies of municipal law. For example, the concept of 'legitimate expectations' is central to European Union law and, in fact, forms a 'general principle of law' that can justify the European Court of Justice overturning offensive national measures.[103] It is also a basic principle of English public law that government entities honour statements of policy or intention, particularly those directed at particular individuals or groups, as part of a general duty of fairness. Such statements may create 'legitimate expectations', either procedural or substantive in nature, the disappointment of which can create a cause of action against the government entities concerned.[104] And in US law, courts have identified claimants' 'investment-backed expectations' as

[102] R Swedberg, 'Max Weber's Contribution to the Economic Sociology of Law' (2006) 2 Annual Rev of L and Social Science 61–81.

[103] De Smith, Woolf, and Jowell, *Judicial Review of Administrative Action* (1995) 867. See eg Cases C-104/89 and 307/90, *Mulder v Council and Commission*, 1992 ECR 1–3061; Case C-152/88, *Sofrimport Sour v Commission*, 1990 ECR 1–2477: and Case 74/74, *CNTA SA v Commission*, 1975 ECR 533.

[104] H Wade and C Forsyth, *Administrative Law* (2000) 498.

being a 'relevant consideration' in determining whether or not public entities have 'taken' property in violation of the Fifth Amendment.[105]

Numerous decisions of arbitral tribunals seeking to interpret and apply the fair and equitable standard have adopted a similar approach. Underlying these cases is the fundamental notion that it is unfair for a state to create certain expectations in the minds of investors through its laws, regulations, and actions; and then, once the investment is made, to change those laws and regulations in ways that significantly frustrate or cancel the expectations that the state itself has been instrumental in creating. Over thirty years ago, Professor Raymond Vernon characterized foreign investments as 'obsolescing bargains'.[106] By this he meant that once an investment was made the host country had the power to change the terms of the investment agreement between the host government and the investor through the use of the former's sovereign authority. In many cases, arbitral tribunals have found such unilateral action not to be fair and equitable and have therefore held host states liable for rendering their bargains with investors obsolete. Governments may change policies in their continuing search for the best options available to discharge their functions. However, to the extent that earlier policies might have created legitimate procedural and substantive expectations for investors, they may not be abandoned without compensating the investor if the result would be so unfair as to amount to an abuse of power.[107]

The state is certainly not responsible for all the imaginable factors that could frustrate an investor's expectations. Thus, changes in a country's natural conditions, such as its weather, political stability, and markets, among a host of other factors that may have induced certain expectation in the investor, are not what the fair and equitable treatment standard is aimed to guard against. Rather, it is directed at actions of the state through its legal and policy framework. An initial step in most investor–state arbitral cases is to focus on the nature of the host country legal order at the time the investment was made. In the case of an allegation that the host country violated the fair and equitable standard, the legal order must be evaluated to determine the reasonable, legitimate expectations that it created in the mind of the investor. The legal order must also be evaluated to determine the extent to which the host government had a legitimate and reasonable right to substantively and procedurally change that legal order. The application of the fair and equitable treatment standard therefore requires an inquiry into the investor's reasonable expectations and the host country's reasonable right to regulate.

[105] See eg *Penn Central Transportation Co and Others v New York City and Others*, 438 US 104; 98 S Ct 2646.

[106] R Vernon, *Sovereignty at Bay: The Multinational Spread of U.S. Enterprises* (1971) 46.

[107] F Vicuna, 'Regulatory Authority and Legitimate Expectations: Balancing the Rights of the State and the Individual under International Law in a Global Society' 5 *International Law Forum Du Droit International* (2003) 188 and 194.

The principle of respecting investors' legitimate expectations is not absolute and does not require the host state to freeze its legal system for the investors' benefit. Such a general stabilization requirement goes beyond what an investor can legitimately expect. It is clear that reasonable evolutions in host state law is part of the environment that investors must contend with. For instance, the adjustment of environmental regulations to internationally accepted standards or the improvement of labour laws to benefit the host state's workforce would not lead to violations of the fair and equitable treatment standard if applied in good faith and without discrimination.

While the concept of legitimate expectations has helped to refine the even vaguer concept of fair and equitable treatment, its application in particular cases is by no means automatic. That application requires tribunals to carefully evaluate numerous factors in individual fact situations. Although previous arbitral decisions are helpful in understanding how to apply the fair and equitable standard in cases involving alleged disappointed legitimate expectations, such decisions are highly fact specific and that specificity complicates the application of the principles to conflicts in other arbitrations. Nonetheless, a few such cases are reviewed for illustrative purposes below. Many of these cases involve licences, permissions, and regulatory frameworks that were changed after an investment had been made.

In the NAFTA case of *International Thunderbird Gaming Corp v United Mexican States*,[108] the claimant company, which was engaged in operating gaming facilities, requested an official opinion from Mexican authorities concerning the legality under Mexican law of a planned investment. Its written request (or *solicitud*), which was submitted to the *Secretaria de Gobernacion* (SEGOB), described Thunderbird's planned investment as concerning 'the commercial exploitation of video game machines for games of skills and ability' and explained that '[i]n these games, chance and wagering or betting is not involved'. In its formal response (or *oficio*), SEGOB referred to the Federal Law of Games and Sweepstakes, which prohibited 'gambling and luck related games' on Mexican territory and also laid out Mexican law regarding the regulation and authorization of gambling establishments. The *oficio* stated that, if the machines used by Thunderbird operated in the form and on the conditions stated in the *solicitud*, SEGOB would be unable to prohibit their use pursuant to Mexican law. Thunderbird subsequently opened a number of gaming facilities in Mexico. However, following a change of government, SEGOB began closing down those facilities and issued a resolution declaring Thunderbird's machines to be prohibited, causing Thunderbird to bring a Chapter Eleven NAFTA claim against Mexico.

Thunderbird based a significant part of its complaint on an argument that the *oficio* had created a 'legitimate expectation' that it would be able to operate its

[108] *International Thunderbird Gaming Corp v United Mexican States* (Award) (26 January 2006).

machines without regulation by SEGOB. The tribunal addressed the 'legitimate expectation' issue in general terms in its award. It said that:

the concept of 'legitimate expectations' relates, within the context of the NAFTA framework, to a situation where a Contracting Party's conduct creates reasonable and justifiable expectations on the part of an investor (or investment) to act in reliance on said conduct, such that a failure by the NAFTA Party to honour those expectations could cause the investor (or investment) to suffer damages.[109]

The tribunal concluded that for the purposes of this test the *oficio* had not generated a legitimate expectation upon which Thunderbird could reasonably rely. In doing so, it pointed out that the information presented in the *solicitud* had been incomplete and inaccurate. Furthermore, it found that the *oficio* had done no more than convey a message to the effect that, if the machines operated in accordance with the representations made in the *solicitud*, SEGOB would not have jurisdiction over them. The tribunal was therefore of the view that Thunderbird could not have reasonably relied to its detriment on the *oficio*. Indeed, Thunderbird had known when it chose to invest in Mexico that gambling was illegal under Mexican law. As a result, it was incumbent on Thunderbird to exercise 'particular caution' in pursuing its business venture.

In *CME v The Czech Republic*,[110] the investor complained that interference with its contractual rights by the Czech Media Council, a quasi-governmental media regulatory body, created a violation of the fair and equitable standard promised under the Netherland–Czech Republic BIT. In an important change, the Council reversed its previous position on the legal situation of the investor as a licence holder, a move that had allowed the investor's local partner to terminate the contract the investment depended upon. The tribunal found that '[t]he Media Council breached its obligation of fair and equitable treatment by evisceration of the arrangements in reliance upon which the foreign investor was induced to invest'.[111] In finding a breach of the obligation of fair and equitable treatment, the tribunal determined that the Media Council intentionally undermined CME's investments because it had both the power and the obligation under Czech law to remedy the partner's unlawful actions in severing the service agreement with CME.[112] It also found that CME had a legitimate expectation of reliance on the investment structure that had been arranged by the Media Council and that the Media Council should not have acted, without a bona fide purpose, to undermine the investor's business.[113]

Although the facts in *Ronald Lauder v The Czech Republic*[114] were the same as in *CME*, the *Lauder* tribunal rejected the investor's claims. In its discussions of

109 ibid ¶ 147.1x(12)
110 *CME v The Czech Republic* (Partial Award) (13 September 2001). 111 ibid ¶ 611.
112 ibid ¶¶ 133, 611. 113 ibid ¶ 611.
114 *Ronald Lauder v The Czech Republic* (Final Award) (3 September 2001) UNCITRAL Arbitration.

the obligations owed under the fair and equitable treatment standard, the tribunal noted that the investor's claim could not be sustained because the Media Council had not reversed any prior express permissions.[115] The implication of this statement is that a reversal of a prior express permission by a state agency could constitute a breach of fair and equitable treatment in that such an express permission would have created a legitimate expectation on the part of the investor.

In *Tecmed*,[116] the dispute concerned the Mexican government's replacement of an unlimited licence with a licence of limited duration for the operation of a landfill in which the claimant had invested. Applying a provision in the Spain–Mexico BIT guaranteeing fair and equitable treatment, the tribunal concluded that the provision required transparency and protection of the investor's basic expectations. It noted in particular that '[t]he foreign investor also expects the host State to act consistently, i.e. without arbitrarily revoking any preexisting decisions or permits issued by the State that were relied upon by the investor to assume its commitments as well as to plan and launch its commercial and business activities'.[117] The tribunal concluded that Mexico's behaviour frustrated the investor's fair expectations. That behaviour was 'characterized by its ambiguity and uncertainty which are prejudicial to the investor in terms of its advance assessment of the legal situation surrounding its investment and the planning of its business activity and its adjustment to preserve its rights'.[118]

The case of *MTD v Republic of Chile*,[119] which involved a BIT between the developing countries of Chile and Malaysia, also raised an issue of fair and equitable treatment. The Malaysian investor had signed an investment contract with Chile's Foreign Investment Commission (FIC) to construct a large planned community. The project was halted after it was discovered that it was not consistent with existing zoning regulations. The tribunal found that Chile had violated the BIT's fair and equitable treatment standard by 'the inconsistency of action between two arms of the same Government vis-à-vis the same investor'.[120] While it was the investor's duty to inform itself of the country's law and policy, 'Chile also has an obligation to act coherently and apply its policies consistently, independently of how diligent an investor is.'[121] The fact that one arm of the Chilean government had approved a project that was against the country's urban zoning policy was a breach of the government's obligation to treat the investor fairly and equitably.

Other cases have held that to establish that government action failed to protect legitimate expectations the investor needs to prove an outright and unjustified

115 ibid ¶ 291.
116 *Tecnicas Medioambientales Teemed SA v The United Mexican States*, ICSID Case No ARB (AF)/00/2 (Award) (29 May 2003). 117 ibid ¶ 154.
118 ibid ¶ 172.
119 *MTD Equity Sdn. Bhd. & MTD Chile SA v Chile*, ICSID Case No ARB/01/7 (Award) (25 May 2004). 120 ibid ¶ 163.
121 ibid ¶ 165.

repudiation of government regulations.[122] Fundamental changes in policy that negatively affect existing contracts are not necessarily violations of fair and equitable treatment.[123]

When an investor makes a contract with a host government, it expects that the government will respect that contract. However, in the realm of investment treaties and investor–state arbitration, whether the fair and equitable treatment clause protects investors against failures to respect those contracts is an extremely difficult issue. The question is equally difficult if the non-performance of a contract between the investor and the host state, or one of its territorial subdivisions or entities, is contrary to the investor's legitimate expectations and so a violation of the fair and equitable treatment standard.[124] The essential question is whether reliance on contractual undertakings is protected by the obligation to provide fair and equitable treatment. If the answer is affirmative, then investors could use the fair and equitable treatment standard as an 'umbrella clause',[125] which would effectively elevate contractual breaches to treaty breaches.[126]

Answering this question is not easy. On the one hand, an investor's contract with the government may be viewed as part of the legal framework of the investor's project and so a failure to respect it would result in a failure to protect the investor's legitimate expectations. On the other hand, the breach of a contract can also be viewed as one of the ordinary business risks of an investment, which would make such risks objectively in the contemplation of the investor when it enters into the agreement. In an effort to balance these two views, one might draw a line between two situations: (1) simple breaches of contract arising out of a host state's financial difficulties or legitimate differences between the parties about contractual terms; and (2) wilful refusals by a government authority to abide by its contractual obligations, abuse of government authority to evade agreements with foreign investors, or actions in bad faith in the course of contractual performance.[127] Only the latter situation would justify a finding of a violation of fair and equitable treatment on the ground that the host government had failed to respect the investor's legitimate expectations.

The tribunal in *Waste Management* seemed to recognize this distinction. One of the investor's claims, based on Article 1105(1) NAFTA, involved the failure of the City of Acapulco to make payments under a concession agreement. The tribunal found that the evidence did not support the conclusion that the city had acted arbitrarily or in a grossly unfair way, since it was in a genuinely difficult financial situation. The tribunal said: '[E]ven the persistent non-payment of debts by a municipality is not to be equated with a violation of Article 1105,

[122] *GAMI Investments, Inc v United Mexican States* (Award) (15 November 2004).
[123] *Eureko BV v Poland* (Partial Award) (19 August 2005).
[124] R Dolzer, 'Fair and Equitable Treatment: A Key Standard in Investment Treaties' (2005) 39 Int'l Lawyer 87, 104.
[125] Chapter 11 discusses the umbrella clause.
[126] C Schreuer, 'Fair and Equitable Treatment in Arbitral Practice' (2005) 6(3) J of World Investment 360, 379.
[127] ibid.

provided that it does not amount to an outright and unjustified repudiation of the transaction and provided that some remedy is open to the creditor to address the problem.'[128]

Other tribunals have indicated that a failure to perform a contract may, under certain circumstances, amount to a violation of the fair and equitable treatment standard. For example, the tribunal in the NAFTA case of *Mondev* stated that 'a governmental prerogative to violate investment contracts would appear to be inconsistent with the principles embodied in Article 1105 and with contemporary standards of national and international law concerning governmental liability for contractual performance'.[129]

Eureko BV v Republic of Poland[130] similarly found that the Polish government's wilful refusal to sell shares to an investor as it had previously agreed 'consciously and overtly, breached the basic expectations of Eureko that are at the basis of its investments' and so treated the investor unfairly and inequitably. It will remain for future tribunals to develop criteria for determining which breaches of contract qualify as ordinary risks because a host government is 'in difficulty' and which breaches are wilful and abusive.

(ii) Failure to act transparently

The failure of a host state to act 'transparently' towards an investor may also constitute a violation of the fair and equitable standard. Transparency is considered an important element of good governance generally, and it is especially important to investors. To make effective investment decisions, investors need to know the applicable legal rules. It is these rules that create an investor's legitimate expectations and facilitate the Weberian concept of calculability. Thus, governments need to be transparent about what rules are in force. Once the investor makes an investment, fairness requires that the government inform the investor of changes in the applicable rules so that the investor may plan and manage operations accordingly. The foregoing suggests that even where an investment treaty does not specifically provide for transparency a fair and equitable treatment clause implicitly requires transparency by the host government.

Governmental transparency clearly affects an investor's legitimate expectations. An investor's legitimate expectations will be based on the host state's legal framework and on any undertakings or representations made by it explicitly or implicitly. As the late Thomas Wälde has pointed out, the principle of protecting legitimate, investment-backed expectations 'is often combined with the principle of transparency: that government administration has to make clear what it wants

[128] *Metalclad Corp v United Mexican States*, ICSID Case No ARB(AF)/97/1 (Award) (30 August 2000) ¶ 115.
[129] *Mondev International Ltd v United States of America*, ICSID Case No ARB(AF)/99/2 (Award) (11 October 2002) ¶ 134. See also *SGS Société Générale de Surveillance SA v Republic of the Philippines*, ICSID Case No ARB/02/6 (Decision on Jurisdiction) (29 January 2004).
[130] *Eureko BV v Republic of Poland* (Partial Award) (19 August 2005).

from the investor and cannot hide behind ambiguity and contradiction itself'.[131] Thus, in many investor–state disputes, one finds that arbitral tribunals have ruled that a violation of fair and equitable treatment has occurred where a host government has both failed to act transparently and to protect the investor's legitimate expectations. For example, in the NAFTA case of *Metalclad Corp v United Mexican States*,[132] the federal government of Mexico and the state government of San Luis Potosi issued construction and operating permits for the investor's landfill project and also assured the investor that it had all the permits it needed. However, the municipality of Guadalcazar refused to grant a construction permit, effectively blocking the project. The tribunal held that the investor was entitled to rely on the representations of the federal officials and therefore Mexico had violated the fair and equitable standard under Article 1105(1) NAFTA. It stated:

> Mexico failed to ensure a transparent and predictable framework for Metalclad's business planning and investment. The totality of these circumstances demonstrates a lack of orderly process and timely disposition in relation to an investor of a Party acting in the expectation that it would be treated fairly and justly in accordance with the NAFTA.[133]

Similarly, many of the arbitral cases discussed earlier in this chapter with respect to the requirement of respecting legitimate investor expectations also made reference to transparency in analysing whether a state had acted fairly and equitably.

(iii) Arbitrary and discriminatory actions

Host government actions that are arbitrary and/or discriminatory towards an investor or an investment covered by an investment treaty also violate the fair and equitable treatment standard. The plain meaning of 'fair and equitable treatment' indicates that if there is discrimination on arbitrary grounds or the investment is subject to arbitrary or capricious treatment by the host state, then the fair and equitable standard has been violated. This conclusion flows from the idea that fair and equitable treatment inherently precludes arbitrary actions against investors.[134] Thus, governmental conduct categorized as arbitrary or discriminatory will generally breach the fair and equitable treatment standard. The problem is to determine whether in a specific situation the particular action of a government towards an individual investor within the framework of a relationship that is complex and long-standing is actually discriminatory or arbitrary. Inevitably, states that take questionable actions justify them as rational and necessary to protect the public interest, while the investors whose interests have been injured claim them to be arbitrary and discriminatory.

[131] T Wälde, 'Energy Charter Treaty-based Investment Arbitration' (2004) 5 JWIT 3 387.
[132] *Metalclad Corp v United Mexican States* (Award) (30 August 2000).
[133] ibid ¶ 99. The Award was set aside in part by the Supreme Court of British Columbia.
[134] Vasciannie (n 61 above) 100, 133.

In the *ELSI* case,[135] the International Court of Justice, while not specifically interpreting a fair and equitable treatment clause, did seek to determine what would constitute an 'arbitrary' measure. Its approach may offer some guidance in deciding what government actions are arbitrary under an investment treaty. The Court stated that an act that is illegal under domestic law is not necessarily arbitrary. Indeed, it suggested that even if a domestic court concluded that an act was arbitrary or unreasonable, that finding would not necessarily make the act arbitrary under international law. Arbitrariness, it stated, 'is not so much something opposed to a rule of law, as something opposed to the rule of law.... It is a willful disregard of due process of law, an act which shocks, or at least surprises, a sense of juridical propriety.'[136]

When determining whether an investor had received fair and equitable treatment, arbitration tribunals have focused on what they characterized as arbitrary governmental actions. In some cases, they did so in order to interpret the term 'fair and equitable treatment'; in others, they did so to apply treaty provisions that specifically prohibit arbitrary or discriminatory treatment. In applying NAFTA's fair and equitable treatment standard in *Pope & Talbot*, the tribunal did not emphasize the legitimate expectations of the investor but focused instead on the aggressive and hostile actions of Canada's Softwood Lumber Division (SLD), a government agency, towards the investor. In particular, it found that SLD's denials of reasonable requests by the investor for pertinent information, its threats to the investor's business, and its misleading statements regarding the investor's actions to the Minister, all contributed to a breach of the fair and equitable treatment standard contained in Article 1105(1) NAFTA.[137]

On the other hand, in *Genin*[138] the tribunal considered whether a decision by the Bank of Estonia to withdraw Genin's banking licence amounted to 'arbitrariness' under Article II(3)(b) of the US–Estonia BIT. After examining the totality of the evidence, the tribunal concluded that for Estonia's action to violate the BIT, 'any procedural irregularity that may have been present would have to amount to bad faith, a willful disregard of due process of law or an extreme insufficiency of action'.[139] It found none of these factors present in the case, stating that the withdrawal of the licence was not 'an arbitrary act that violates

[135] *Elettronica Sicula SpA (United States v Italy)* (Judgment) (20 July 1989) ICJ Rep 1989, p 15.
[136] ibid 73–7. In his dissent, Judge Schwebel concurred in the Chamber's concept of what constitutes an arbitrary act in international law but interpreted Article I of the Supplementary Agreement of 1951 as creating an obligation of result (as opposed to an obligation of conduct). He stated that 'failure to correct an arbitrary measure constitutes a violation of the FCN treaty regardless of the existence of local remedies'.
[137] *Pope & Talbot Inc v The Government of Canada* (Award on the Merits Phase II) (10 April 2001) ¶¶ 177–9.
[138] *Genin, Eastern Credit Ltd, Inc and AS Baltoil v Republic of Estonia* (Award) (25 June 2001).
[139] ibid ¶ 371.

the tribunal's "sense of juridical propriety"'. The tribunal also attached importance to the fact that the political and economic transition occurring in Estonia at the time justified heightened scrutiny of the banking sector and that the state's action reflected 'a clear and legitimate public purpose'.[140] Thus, it would seem that to find a government measure arbitrary that country's special circumstances and the reasonableness of the government goals in taking that action must be taken into account.

The importance of the context for judging the arbitrariness of a governmental action is also illustrated in *LG&E Energy*.[141] In *LG&E Energy*, an ICSID tribunal considered whether the measures taken by Argentina during a severe economic and financial crisis and which adversely affected the investors' gas-distribution licences were arbitrary and therefore in violation of the US–Argentine BIT's Article II(2)(b),[142] which prohibits the host state from taking arbitrary or discriminatory measures against an investor. The investor claimed that the standard for an arbitrary act is 'disregard for the rule of law' and that by wilfully repudiating its legal obligations Argentina had followed 'the rule of power, not the rule of law'. Because the BIT did not define the term 'arbitrary', the tribunal looked to international law to define the term and so considered the *ELSI* case, described above. It then examined the BIT text and interpreted the intent of the contracting parties 'prohibiting themselves from implementing measures that affect the investments of nationals of the other Party without engaging in a rational decision-making process'.[143] A 'rational decision-making process', according to the tribunal, would include a consideration by Argentina of the effect of a proposed measure on foreign investments and a balancing of state interests against the burden placed on the investor. After reviewing the process by which Argentina arrived at the measures taken, the tribunal—emphasizing that Argentina was seeking to avert a complete economic collapse—concluded that the measures were not arbitrary because they resulted from reasoned judgment rather than a disregard for the rule of law.

Arbitrary conduct is also often discriminatory against the investor; consequently, the two words 'arbitrary and discriminatory' are often part of a single treaty standard or are considered inherent in the concept of unfair and inequitable treatment. The question of whether a measure is discriminatory also arises in the application of the required standards in treaties of national and most-favoured-nation treatment, both of which are discussed later in this chapter. When investment treaties are meant to prohibit discrimination against foreign investors, a measure is considered discriminatory if its intent is to discriminate or

[140] ibid.
[141] *LG&E Energy Corp v Argentine*, ICSID Case No ARB/02/1 (Decision on Liability) (3 October 2006).
[142] Article II(2)(b) of the 1994 BIT provides: 'Neither Party shall in any way impair by arbitrary or discriminatory measures the management, operation, maintenance, use, enjoyment, acquisition, expansion, or disposal of investments.'
[143] ibid ¶ 158.

if it has a discriminatory *effect*.[144] In determining whether specific actions are discriminatory, and so violate the fair and equitable treatment standard or other specific provisions against discrimination, tribunals often refer to the *ELSI* case. In *ELSI*, the International Court of Justice determined that the elements of a discriminatory measure include: (i) an intentional treatment, (ii) in favour of a national, (iii) against a foreign investor, and (iv) that is not taken under similar circumstances against another national.[145] However, proving these elements to the satisfaction of a tribunal can be difficult. For example, in the *ADF* case,[146] which concerned the US domestic-contents requirements for the government procurement of a construction project, alleged by the claimant to be discriminatory, the tribunal refused to find a violation of fair and equitable treatment. The tribunal noted that the investor had not claimed that other companies in like circumstances had been granted requirements waivers while the investor was denied, that the investor did not allege that the requirements under the project contract had been 'tailored' so that only a particular US company could comply with its specifications, or that the US measures had imposed 'extraordinary costs or other burdens' on the investor that were not imposed on the successful project bidders.[147]

(iv) Denial of justice or due process

Procedural fairness by governmental and judicial authorities when dealing with nationals or foreigners is a basic requirement of the rule of law and a vital element of fair and equitable treatment. The failure to respect procedural fairness is therefore considered a 'denial of justice'. According to Brownlie, the term 'denial of justice' has been employed by claims tribunals in a way that is coextensive with the general notion of state responsibility for harm to aliens. Regardless, it is widely seen as a particular category of deficiencies in host state governmental organs, particularly those involved in the administration of justice.[148] Other commentators have identified at least three different meanings—broad, narrow, and intermediate—of the term 'denial of justice'. In its broadest sense, 'denial of justice' covers all of state responsibility and applies to all kinds of wrongful acts by the state towards an alien. In its narrowest sense, it refers to direct intervention by government authorities in the workings of the judicial system, for example by taking affirmative action to deny an alien access to the courts or to prevent a court from pronouncing its judgment. The intermediate meaning of the term 'denial of justice' is related to the improper administration of civil and criminal justice with respect to a foreigner, including a denial of

[144] K Vandevelde, *United States Investment Treaties: Policy and Practice* (1992) 77.
[145] ibid 61–2.
[146] *ADF Group, Inc v United States of America*, ICSID Case No ARB (AF)/00/1 (Award) (9 January 2003) (NAFTA).
[147] ibid ¶ 191.
[148] I Brownlie, *Principles of Public International Law* (2003) 506.

access to courts, inadequate procedures, and unjust decisions.[149] It has been observed by three leading scholars of international law that 'the term may thus be usefully employed to describe a particular type of international wrong for which no other adequate phrase exists in the language of the law' and that '[t]he tendency of the jurisprudence of international tribunals and of previous codifications of the law of responsibility of States has been to give only a generalized meaning to "denial of justice" and to refrain from establishing a list of those wrongful acts and omissions which would constitute a "denial of justice"'.[150]

The *Third Restatement of the Foreign Relations Law of the United States* takes the position that although the term 'denial of justice' has sometimes been used to refer to any injury done to an alien, it is used more commonly in a narrow sense 'to refer only to injury consisting of, or resulting from, denial of access to courts, or denial of procedural fairness and due process in relation to judicial proceedings, whether criminal or civil'.[151] From the foregoing, it is clear that an actionable failure of justice must be manifest and must constitute a gross deficiency in the administration of justice in the individual case. An error of law by a national court or an incorrect finding of fact by an administrative authority would not constitute such a denial of justice.

A denial of justice may arise out of either procedural or substantive deficiencies. As Freeman has noted, 'steady international practice as well as the overwhelming preponderance of legal authority, recognizes that not only flagrant procedural irregularities and deficiencies may justify diplomatic complaint, but also gross defects in the substance of the judgment itself'.[152]

The US Model BIT of 2004 specifically clarifies that the fair and equitable treatment standard protects against a denial of justice and also guarantees due process. Article 5(2)(a) provides that 'fair and equitable treatment' includes an obligation not to deny justice in any criminal, civil, or administrative adjudicatory proceeding in a way that would violate the principle of due process 'embodied in the principal legal systems of the world'.[153] Free trade agreements signed by the United States also specifically prescribe the inclusion of due process rights as a part of the fair and equitable standard.

The jurisprudence of international tribunals indicates that a state's failure to comply with its duty to grant due process to aliens constitutes a violation of fair and equitable treatment. Both courts and other state agencies may violate this duty. In the field of investor–state arbitration, tribunals have found a denial of justice and a breach of the fair and equitable treatment standard when government or judicial processes affecting investors' interests failed to give the investor

[149] FV Garcia-Amador, L Sohn, and R Baxter, *Recent Codification of the Law of State Responsibility for Injuries to Aliens* (1974) 180. [150] ibid.
[151] *Restatement Third of the Foreign Relations Law of the United States*, § 711, comm a.
[152] A Freeman, *The International Responsibility of States for Denial of Justice* (1938) 309.
[153] <http://www.ustr.gov/sites/default/files/U.S.%20model%20BIT.pdf> accessed 24 August 2009.

proper notification of the hearing or processes, did not invite or allow the investor to participate or appear, or were influenced by bias or prejudice. For example, in *Metalclad* the tribunal found a violation of the fair and equitable treatment under Article 1105(1) of NAFTA because the construction permit requested by the investor 'was denied at a meeting of the Municipal Town Council of which Metalclad received no notice, to which it received no invitation, and at which it was given no opportunity to appear'.[154] Similarly, in *Middle East Cement*,[155] an investor complained that the Egyptian government had seized and auctioned its ship without proper notice. The tribunal determined that the auction procedure applied to the claimant was not 'under due process of law' as required by Article 4 of the Greece–Egypt BIT and specifically found that the notification procedure had been insufficient.[156]

(v) Good faith

If their actions are taken in bad faith, states will fail to meet the minimum international standard and the fair and equitable treatment standard. On the one hand, there is considerable authority indicating that bad faith is *not* an essential element of a violation of the fair and equitable treatment standard. For example, the *Mondev* tribunal stated, '[W]hat is unfair or inequitable need not equate with the outrageous or the egregious. In particular, a State may treat foreign investment unfairly and inequitably without necessarily acting in bad faith.'[157]

The notion of bad faith is particularly concerned with the motivations of a government or public authority when interacting with an investor. While conceptually it would seem that bad faith actions by a government would violate the fair and equitable treatment standard owed an investor, no modern arbitral decision has actually found a state to have acted in bad faith towards an investor under an applicable investment. Three reasons would seem to explain this result. First, it is not necessary to find governmental bad faith in order to establish a breach of the fair and equitable treatment standard. Second, proving a state's bad faith can be an extremely difficult task, since a government can usually offer some public policy justification for its actions. And third, most arbitral tribunals would be loath to make such a finding against a sovereign state, particularly if it could give redress to an injured investor without having to do so.

(f) Conclusion

Based on the existing jurisprudence of investor–state arbitral tribunals, one may conclude that the core of the fair and equitable treatment standard includes the

[154] ibid ¶ 91.
[155] *Middle East Cement Shipping and Handling Co SA v Arab Republic of Egypt*, ICSID Case No ARB/99/6 (Award) (12 April 2002). [156] ibid ¶ 147.
[157] ibid ¶ 116.

above discussed elements. Thus, a state treats an investor fairly and equitably when its actions respect the investor's legitimate expectations, are transparent, are not arbitrary or discriminatory, respect due process and access to justice, and are done in good faith. The foregoing, however, do not constitute an exhaustive list. Claims based on the denial of fair and equitable treatment will continue to be a constant feature of investor–state arbitration, and so the standard will continue to be subject to interpretation and refinement in the years ahead. Moreover, some states have taken to defining the scope of the fair and equitable treatment standard more precisely, and in some cases limiting it, by using more precise definitions in the treaty itself. An example of this approach is the 2005 bilateral investment treaty between the United States and Uruguay. Article 5 of that BIT, entitled 'Minimum Standard of Treatment', stipulates that '[e]ach Party shall accord to covered investments treatment in accordance with customary international law, including fair and equitable treatment and full protection and security'. A footnote to the Article requires that it be interpreted in accordance with Annex A to the treaty, which states a shared understanding of the parties that 'customary international law ... result[s] from a general and consistent practice of States that they follow from a sense of legal obligation'.

In interpreting and applying the fair and equitable treatment clause, tribunals have focused primarily on the behaviour of the respondent state. The reason is that most investment treaties set down standards of behaviour for states, not investors. It is important to recognize, however, that the investor's behaviour may influence a tribunal in applying the fair and equitable standard. For one thing, whether a state has acted fairly and equitably is not an abstract question but one that requires an examination of the way a state behaved in a particular situation. Investor behaviour is very much a part of that situation, and it is therefore a legitimate area of inquiry by a tribunal. Determining whether a state has acted fairly and equitably towards an investor depends to a significant extent on the acts of the investor as well as the state. An investor that has engaged in corrupt business practices, has conducted its operations recklessly or in an unreasonable manner, or has not appropriately evaluated and protected itself against the risks posed by an investment may well have less standing to claim that a state measure was unfair or inequitable than an investor whose operations have been scrupulously honest, well managed, and attentive to risks. As one scholar has written, '[I]f equity means anything it suggests a balancing process and weighing what is right in all the circumstances.'[158]

[158] P Muchlinski, '"Caveat Investor?": The Relevance of the Conduct of the Investor under the Fair and Equitable Treatment Standard' in F Ortino et al (eds), *Investment Treaty Law, Current Issues II* (2007) 209–10.

9.5 Other General Standards of Treatment

Individual investment treaties often stipulate other general treatment standards, most of which would be subsumed within the meanings of either fair and equitable treatment or full protection and security. Thus, alone or in conjunction with such basic standards of treatment, treaties may require treatment that accords with customary international law, an international minimum standard of treatment, that is not arbitrary or discriminatory, or that allows access to justice or due process. All of these treatment standards have been discussed above in connection with the fair and equitable treatment standard.

9.6 National Treatment

(a) Competition and discrimination

Economic and business activity is a competitive process. Economic actors constantly seek to gain advantage over their competitors and to remove advantages that their competitors may have over them. In response to their perceived national interests, governments often seek through their laws, regulations, and administrative actions to: (1) assist their nationals and companies in the competitive process by taking measures that favour their interests and disfavour the interests of others; or (2) to favour certain foreign nationals and companies over other foreign nationals and companies. Government measures may thus have a discriminatory effect on economic activity.

Such discriminatory measures can impede international investment. In encouraging increased foreign investment, investment treaties often seek to remove the competitive disadvantages that may be placed on foreigners by eliminating such discriminatory treatment. Treaties do this by making non-discrimination a standard that host countries must grant to investors and investment from other contracting states.

Non-discriminatory treatment has two dimensions. The first, known as national treatment, requires host states to treat foreign investors and foreign investments no less favourably than their own national investors and investments. The second, known as most-favoured-nation treatment, demands that host countries treat investments and investors covered by the treaty no less favourably than other foreign investors and investments. The purpose of these treatment standards is to place all economic actors in an equal position on the assumption that such equality of treatment will foster competition and economic growth. Most treaties include, in some form, both of these relative treatment standards. This section will discuss national treatment and the following will consider most-favoured-nation treatment.

(b) National treatment in investment treaties

For many countries, agreeing to grant national treatment to foreign investment is often more difficult politically than granting most-favoured-nation treatment. The reason is that national treatment may require difficult changes in existing laws and policies favouring national companies, while most-favoured-nation treatment usually does not. For example, many countries encourage national industries by granting subsidies or other benefits that the country would be unwilling to provide equally to foreigners and thereby undermine the competitive position of those industries. For that reason, the negotiation and drafting of national treatment provisions in investment treaties has often been fraught with difficulty. It is also for this reason that treaties demonstrate a wide variety of formulations in expressing national treatment standards.

Resistance to the national treatment standard was stronger in the early days of the investment treaty movement, when many countries had large state-owned industries to protect. Today, as a result of large-scale privatizations and the resulting shrinkage of the public sector, countries more readily accept national treatment clauses in treaties of one type or another, and a large majority of treaties now include them.[159] On the other hand, as was discussed in Chapter 8, many treaties distinguish between requiring this treatment standard for the admission of an investment and imposing it once an investment has been made. Thus, the Energy Charter Treaty avoids a firm commitment to grant investors national or most-favoured-nation treatment with respect to the making of an investment, but it does commit the contracting parties to granting national treatment or most-favoured-nation treatment, whichever is the more favourable, to investments, once made, and to their associated activities. These 'associated activities' would include the investments' management, maintenance, use, enjoyment, and disposal.[160]

For investment treaties granting national treatment, one must thus make a fundamental distinction between treaties that promise non-discriminatory treatment during the entire investment process and those that limit national treatment to investments after they have been established in the host country. These latter treaties usually provide that each contracting party shall accord protection to 'investment in its territory'[161] or 'investments made in accordance with its laws'.[162] This type of provision allows the host country to deal with competitively threatening foreign investments by simply refusing them the right of establishment while granting that right to those it has admitted into the

[159] UNCTAD, *Bilateral Investment Treaties 1995–2006: Trends in Investment Rulemaking* (2007) 33.

[160] The Energy Charter Treaty, Art 10(7).

[161] Mauritius–Zimbabwe Treaty for the Promotion and Protection of Investment, Art 4.

[162] Russia–Thailand Treaty for the Promotion and Protection of Investment, Art 3.

country. Even after establishment, some treaties make national treatment tentative by making it contingent upon national legislation. Thus, an investment treaty may provide that '[e]ach Contracting Party shall, subject to its laws and regulations, accord to investments of investors of the other Contracting party treatment no less favorable than that which is accorded to investments of its investors'.[163] This provision gives host countries the power to enact laws favouring national investments when their governments judge it important to advance certain national interests. A variation of this approach is to define the aspects of investment activity that will receive national treatment while stating or implying that other aspects will not receive the same treatment. Many treaties, particularly those negotiated by the United States, make clear that national treatment will be granted to investors or investments of parties that are in 'like circumstances' to those of national investors.

On the other hand, many treaties grant full national treatment in the pre- and post- establishment phase. In addition, some treaties grant national treatment to 'investments of the other Party', to 'investors of the other Party', and still others to both. Thus, NAFTA has separate Articles for investors and investments. It provides:

Article 1102: National Treatment

1. Each Party shall accord to investors of another Party treatment no less favorable than that it accords, in like circumstances, to its own investors with respect to the establishment, acquisition, expansion, management, conduct, operation and sale or other disposition of investments.
2. Each Party shall accord to investments of investors of another Party treatment no less favorable than that it accords, in like circumstances, to investments of its own investors with respect to the establishment, acquisition, expansion, management, conduct, operation and sale or other disposition of investments.

While discussions of 'national treatment' often seem to imply that its meaning is constant and uniform across treaties, that is not the case. Because of the many variations that it takes in particular treaty texts, it is essential for those interpreting and applying the national treatment commitments contained in particular treaties to examine carefully the specific language of the text in question.

(c) The application of the national treatment standard

The application of the national treatment standard depends not only on how the standard is articulated in a particular treaty but also on the specific facts of the case in question. Applying national treatment standards in investor–state disputes, like cases involving the fair and equitable standard, is highly fact-specific

[163] Agreement between the Government of the Republic of Indonesia and the Government of the Republic of India for the Promotion and Protection of Investments (8 February 1999), Art 4(3).

and not easily amenable to a mechanistic application of treaty provisions.[164] But, unlike the fair and equitable treatment standard, tribunals in national treatment standard cases appear to have developed a more or less common, three-step analytical approach. This is particularly the case within the context of NAFTA. The first step involves identifying a group of national investors to be compared with the claimant foreign investor. The second step is to compare the relative treatment the two groups have received and evaluate whether the treatment of the claimant is less favourable than that given to the compared group of national investors. The final step is to determine whether the two are, in the words of NAFTA and similar treaties, in 'like circumstances' or whether factors justifying differential treatment exist.[165] The completion of each step requires the answer to a particular question. Let us examine each step in greater detail.

(i) *With whom should the claimant be compared?*

The application of the national treatment standard is inherently a comparative process. The foreign investor is complaining because it has compared the treatment it has received from the host government with that received by someone else and found its treatment wanting. In order to determine the validity of such a claim, a tribunal first has to determine whether the investor has compared itself with an appropriate comparator. For example, suppose that a host country provides subsidized electricity to small farmers but not to a foreign investor operating an aluminium smelter. Would such differential treatment constitute a breach of the national treatment standard? Has the foreign investor selected an appropriate basis of comparison? For one thing, the subsidized small farmer and the aluminium producer are operating in two very different economic sectors: agriculture and heavy industry. For another, the scale and magnitude of the operations of the two economic actors is vastly different. Moreover, the relative costs and benefits of the electricity subsidy are disproportionate because in the production of aluminium electricity is a much higher percentage of total production costs that in a small farm. An arbitral tribunal analysing all of these factors would conclude that it would be inappropriate, for purposes of determining a breach of national treatment, to compare a small farmer with an aluminium smelter.

Several NAFTA cases provide guidance in the determination of an appropriate comparator. In the NAFTA case of *Pope & Talbot*, the tribunal declared that 'as a first step, the treatment accorded a foreign owned investment protected by Article 1102(2) should be compared with that accorded domestic investments in the same business or economic sector'.[166] Applying this principle to

[164] Dolzer and Schreuer (n 9 above) 179.
[165] UNCTAD, *Investor–State Dispute Settlement and Impact on Investment Rulemaking* (2007) 48.
[166] *Pope & Talbot v Canada* (Award) (10 April 2001) 7 ICSID Reports 102 ¶ 78.

specific cases can prove difficult. An individual tribunal may opt for either a broad or narrow approach in delineating the comparator group. For example, in *Feldman v Mexico*, the claimant was a trading company that was engaged, among other things, in purchasing Mexican cigarettes from local retailers and then selling those cigarettes abroad. The company alleged that the Mexican government had granted tax rebates to competing exporters of Mexican cigarettes but had denied the same rebates to the claimant. In determining the basis of comparison, the tribunal stated that the 'universe of firms' to which the claimant was to be compared were those in the business of 'reselling/exporting cigarettes'. Other firms that might also be exporting cigarettes, such as cigarette manufacturers, were not in that group.[167]

In *Occidental v Ecuador*,[168] the host government had originally granted the claimants and other oil producers a rebate on the value-added tax (VAT) they paid on goods purchased for their exploration activities. In 2001, however, Ecuador's tax authorities stopped granting those rebates to the claimant and other oil exploration companies on the grounds that the participation formulas in their government contract already accounted for such rebates. Although all the companies in the oil sector were treated equally with respect to these value-added tax rebates, the tribunal determined that the relevant comparison group for national treatment purposes was not the oil sector but 'local producers in general . . . since the purpose of national treatment is to protect foreign investors as compared to local producers and this cannot be done by addressing exclusively the sector in which that particular activity is undertaken'.[169]

This conclusion could be criticized as being an overly broad interpretation of the national treatment standard in the US–Ecuador BIT, which requires that national investors in the comparison group be 'in like situations.' In interpreting this provision, the tribunal would have done well to ask a fundamental question: What does the national treatment clause seek to protect US investors from? One answer is that the purpose of the clause is to protect the investor from unfair competitive disadvantages and that the claimant in the *Occidental* case was not in competition with all other 'local producers'. The claimant competed only against other oil companies, all of which had been treated similarly, since the VAT rebates had been denied to all. Applying the *Occidental* tribunal's reasoning to the example given earlier in this section, one would conclude that, because the small farmer and the foreign-owned aluminium smelter are both 'local producers', the host government breached the national treatment standard by denying the smelter subsidized electricity.

[167] *Marvin Feldman v Mexico*, ICSID Case No ARB(AF)/99/1 (Award) (16 December 2002) ¶ 171.
[168] *Occidental Exploration and Petroleum Company v The Republic of Ecuador*, London Court of Arbitration Case No UN 3467 (Final Award) (1 July 2004).
[169] ibid ¶ 173.

(ii) What is the nature of the difference in treatment?

The second step in the analysis is to determine whether the treatment of the aggrieved foreign investor differs from that accorded to local investors, and if so, in what way it differs. Most tribunals have concluded that discrimination may be either de jure or de facto. Thus, one needs to look not only at discrimination in the text and application of legal provisions but also treatment that, while not being discriminatory in law, nonetheless has a discriminatory impact. In *SD Meyers v Canada*,[170] a NAFTA case, the tribunal pointed to two factors in particular that need to be evaluated in determining differential treatment: (1) whether the practical effect is to create a disproportionate benefit for nationals over non-nationals; and (2) whether on its face the contested measure appears to favour the host country's nationals over non-nationals protected by the treaty.[171] Arbitral tribunals have also generally held that in order to demonstrate discriminatory treatment an aggrieved investor need not show discriminatory intent on the part of the host country,[172] nor that the host country's discriminatory action was specifically due to the foreign investor's nationality.[173] On the other hand, the existence of a discriminatory intent without some differential impact is insufficient. As the tribunal stated in *SD Meyers*, 'The word "treatment" suggests that practical impact is required to produce a breach of Article 1101, not merely a motive or intent that is in violation of Chapter 11.'[174]

(iii) Is the difference in treatment justified?

Tribunals will often not find a breach of the national treatment standard if the foreign investor and the compared national investors are not in 'like circumstance', 'similar situations', or if there is a justified policy reason for the differential treatment. This requirement gives host country governments room to make regulations in the public interest. The tribunal in *Pope & Talbot* suggested the importance of considering the policy justifications in measures that have a discriminatory effect when it stated that '[d]ifferences in treatment will presumptively violate Article 1102(2) unless they have a reasonable nexus to national policies that (1) do not distinguish, on their face or de facto, between foreign-owned and domestic companies, and (2) do not otherwise unduly undermine the investment liberalizing objectives of NAFTA'.[175] Thus, in the example given earlier in the section, even if a tribunal found that both the

[170] *SD Meyers Inc v Canada* (First Partial Award) (13 November 2000) UNCITRAL (NAFTA). [171] ibid ¶ 252.

[172] ibid ¶ 254, stating: 'Intent is important, but protectionist intent is not necessarily decisive on its own. The existence of an intent to favour nationals over non-nationals would not give rise to a breach of Chapter 1102 of the NAFTA if the measure in question were to produce no adverse effect on the non-national complainant.'

[173] *Thunderbird v Mexico* (Award) (26 January 2006) ¶ 177. [174] ibid ¶ 254.

[175] ibid ¶ 78.

foreign-owned aluminium smelter and local small farmers were local producers, it might nevertheless hold that no breach of national treatment occurred. The reason is that the process of providing subsidized electricity to small farmers does not distinguish on its face between foreigners and nationals, is done for the justified purpose of supporting small-scale agriculture and raising the standard of living of farm families, and does not affect the basic goal of the treaty, which is to promote and protect investment.

The precise boundaries of justified public policy and 'like circumstances' are by no means clear and will no doubt be the subject of continuing litigation and debate in the years ahead.

9.7 Most-Favoured-Nation Treatment

Virtually all investment treaties contain a most-favoured-nation (MFN) provision whose purpose is to prevent host states from treating investors and investments of its treaty partners less favourably than investors from third countries. The provision's aim is to assure non-discrimination among foreign investors. Countries that have been unwilling to grant national treatment in investment treaties out of a concern to protect domestic industries have been more willing to grant MFN treatment, which they view as less threatening to national enterprises and interests.

In some treaties, the MFN treatment commitment is limited to post-establishment investments and does not apply to the process of making investments. Thus, for example, the Energy Charter Treaty avoids a firm commitment to investors regarding MFN treatment when making investments, but does grant national treatment or MFN treatment, whichever is the more favourable, to contracting parties once their investments have been made. MFN treatment under the Energy Charter Treaty covers the investments' associated activities, including their management, maintenance, use, enjoyment, and disposal.[176]

As has been the case for centuries in international economic treaties, the purpose of the MFN clause in investment treaties is to assure equal treatment at the international level so that covered investors and investments receive treatment no less favourable than that which the host country grants investors from any third country. Like provisions on national treatment, MFN clauses are formulated in different ways in different treaties. As a result, the scope of protection that the clause provides and the stipulated exceptions to it vary from treaty to treaty. For example, some treaties grant MFN treatment only to *investments* of a treaty partner, while others grant it to *investors*. Some may specify the particular matters to which MFN treatment applies, for example, 'to the establishment, acquisition, expansion, management, conduct and sale

[176] The Energy Charter Treaty, Art 10(7).

or other disposition of an Investment',[177] while others may state generally that '[i]nvestments by nationals and companies of either Contracting State ... shall not be subjected to treatment less favorable than that accorded to investments by nationals and companies of third states'.[178] As a result of the wide variety of MFN treatment formulations found in investment treaties, persons interpreting them need to focus carefully on the particular language of the treaty in question and should not assume that the nature and scope of protection is uniform among treaties.

A host country may favour an investment or an investor from another country in one of two general ways: (1) by using its legislation, regulations, or administrative acts to grant those investments and/or investors a special benefit not generally granted to foreign investors or investments; and (2) by entering into treaties with third countries assuring their investors and/or investments special benefits or treatment. An example of the first way might be a national law that grants investors from a neighbouring country tax exemptions that are denied to investors from all other countries. An example of the latter way might be a country that makes a bilateral investment agreement promising national treatment to investors and investments from a treaty partner when all other treaties with third countries omit the promised treatment. To set limits on the effects of MFN clauses, most investment treaties contain stated exceptions as to matters, such as customs unions and free trade zones, to which the clause does not apply.

Most of the litigation surrounding MFN treatment clauses in investment treaties involves a situation in which an investor that is covered under a treaty from one country is seeking to take advantages of benefits that the host country has granted by treaty to an investor or investment from a third country. MFN provisions allow a country that was not able to negotiate a desired standard with a treaty partner to nonetheless attain that standard if the treaty partner has granted it to a third country in another treaty. Accordingly, one of the effects of the MFN clause is to increase a country's bargaining power.[179] It achieves this result by allowing the investor to import the standards of protection from other treaties into the treaty applicable to its investment. For example, in the case of *Bayindir v Pakistan*,[180] the claimant, a Turkish construction company, brought an ICSID case against Pakistan under the 1995 bilateral investment treaty between Turkey and Pakistan. That BIT provided that '[e]ach Party shall accord to these investments, once established, treatment no less favourable than that accorded in similar situations to investments of its investors or to investments of investors of any third country, which ever is the most

[177] Brunei–Korea BIT (14 November 2000), Art 3.2.
[178] Malaysia–Chile BIT (11 November 1992), Art 3(1).
[179] UNCTAD, *Bilateral Investment Treaties 1995-2006: Trends in Investment Rulemaking* (2007) 38.
[180] *Bayindir Insaat Turizm Ticaret VeSanayi AS v Islamic Republic of Pakistan*, ICSID Case No ARB/03/29 (Decision on Jurisdiction) (14 November 2005).

favourable'.[181] The Turkey–Pakistan BIT contained no provision specifically guaranteeing Turkish investors fair and equitable treatment; however, Pakistan had made investment treaties with various European countries explicitly promising such treatment. The Turkish claimant argued, and the tribunal eventually agreed, that by virtue of the MFN clause above in the Turkey–Pakistan BIT Pakistan was obligated to treat the claimant fair and equitably.[182]

Similarly, in *MTD Equity Sdn. Bhd. and MTD Chile SA v Republic of Chile*,[183] Malaysian investors, who had been denied the zoning changes necessary to undertake a land development project, successfully argued that the MFN clause in the Malaysia–Chile BIT made the provisions in the Croatia–Chile BIT and the Denmark–Chile BIT applicable. Both those BITs provided that '[w]hen a Contracting Party has admitted an investment in its territory, it shall grant the necessary permits in accordance with its laws and regulations'.[184] The tribunal in *MTD* considered the incorporation of the protections of the Denmark and Croatia BITs into the Malaysia–Chile BIT as consistent with the treaty's purpose, which is to protect investment and create conditions favourable to investments. Moreover, the fact that the Malaysia–Chile BIT specifically excluded certain matters from MFN protection, and that the protections provided in the Denmark and Croatia BITs were not among those excluded matters, also supported the applicability of the Malaysia–Chile MFN clause.[185]

While it is generally agreed that an appropriately drafted MFN clause will import into an investment treaty substantive protective standards, controversy exists as to whether the clause also extends to procedural rights, particularly those relating to dispute settlement in other treaties. The case of *Maffezini v Spain*[186] first provoked this controversial issue. The claimant, an Argentine national who invested in an enterprise in Spain for the production and distribution of chemicals, initiated an ICSID arbitration against Spain under the Spain–Argentina BIT. That BIT required resort to local courts for a period of eighteen months before an investor could invoke international arbitration. Although Maffezini did not have recourse to the Spanish courts as required by the treaty, he argued that he was not required to do so because the Spain–Chile BIT did not contain a similar eighteen-month requirement and, by virtue of the MFN clause in the Spain–Argentina BIT, he was entitled to avail himself of the lesser requirements in the Spain–Chile BIT.

Interpreting the broad MFN clause, which provided that 'in all matters subject to this agreement treatment shall be no less favourable than that extended ... to investors of a third country', the ICSID tribunal concluded that Maffezini was

[181] Agreement between the Republic of Turkey and the Islamic Republic of Pakistan Concerning the Reciprocal Promotion and Protection of Investments (16 March 1995, entered into force 3 September 1997), Art II(2).
[182] ibid ¶ 231.
[183] *MTD Equity Sdn. Bhd. and MTD Chile SA v Republic of Chile*, ICSID Case No ARB/01/7 (Award) (25 May 2004).
[184] ibid ¶ 197.
[185] ibid ¶ 104.
[186] *Maffezini v Spain*, ICSID Case No ARB/97/7 (Award on Jurisdiction) (25 January 2000).

entitled to avail himself of the lighter procedural burden included in the Spain–Chile BIT. Therefore, Maffezini did not have to pursue his claim for eighteen months in Spanish courts before requesting ICSID arbitration. Subsequent cases followed this approach.[187] On the other hand, in *Salini v Jordan*[188] and *Plama Consortium Ltd v Bulgaria*,[189] the tribunals refused to allow the claimants to import dispute resolution provisions from other treaties. The difference in the result in these cases can be explained largely by the fact that the MFN clauses in the latter cases were much narrower in scope than the MFN clause in the former cases.

9.8 Compensation for Breach of General Treatment Standards

An important final question with respect to general treatment standards is what are the consequences for the host country of their breach? Is the host country obligated to pay the investor compensation if it denies the investor full protection, fair and equitable treatment, or national treatment? If so, what is the standard for determining the compensation that the host state must pay? Curiously, no investment treaty specifically addresses these questions or even provides that contracting parties who breach these treatment standards are liable to compensate either the injured investor or its home state. This lack of specificity is particularly curious when one examines investment treaty provisions on expropriation, which make clear that host states must compensate investors for expropriated assets. As will be discussed in Chapter 12,[190] expropriation provisions also specify in some detail the standard by which such compensation is to be determined. While one might argue that the lack of specific provisions discussing general standards of treatment means they are merely hortatory in nature, arbitral tribunals have uniformly held that states are liable to compensate investors for breaches of general treatment standards that result in their injury.[191]

Tribunals have arrived at this conclusion by finding that customary international law applies to the question of liability and compensation. In particular, they have relied on *Chorzów Factory*,[192] discussed in Chapter 3, in which the

[187] eg *Siemens v Argentina*, ICSID Case No ARB/02/8 (Decision on Jurisdiction) (3 August 2004); *Suez, Sociedad General de Aguas de Barcelona SA, and InterAguas ServiciosIntegrales del Agua SA v The Argentine Republic*, ICSID Case No ARB/03/17 (Decision on Jurisdiction) (16 May 2006); *Suez, Sociedad General de Aguas de Barcelona, SA and Vivendi Universal, SA v Argentine Republic*, ICSID Case No ARB/03/19 (Decision on Jurisdiction) (3 August 2006).

[188] *Salini Costruttori SpA and Italstrade SpA v Jordan*, ICSID Case No ARB/02/13 (Decision on Jurisdiction) (9 November 2004).

[189] *Plama Consortium Ltd v Bulgaria*, ICSID Case No ARB/03/24 (Decision on Jurisdiction) (8 February 2005).

[190] See below Ch 12.10.

[191] M Weiniger, 'The Standard of Compensation for Violation of the Fair and Equitable Standard' in F Ortino et al (eds), *Investment Treaty Law: Current Issues II* (2007) 197.

[192] *Factory at Chorzów* (Merits) 1928 PCIJ Series A No 17.

Permanent Court of International Justice stated that, according to customary international law, if a state has committed a wrong it is liable to pay reparations. The amount of such reparations must be sufficient to eliminate the consequences of the illegal act and to place the wronged party in the situation it would have been had the illegal act not taken place. For example, in the case of *MTD v Chile*, the tribunal accepted 'the classic standard enounced by the Permanent Court of Justice in the *Factory at Chorzów*: compensation should "wipe out all the consequences of the illegal act and re-establish the situation which would, in all probability, have existed if that had not been committed"'.[193] Thus having determined the liability of the host state for violating a treaty treatment standard, an arbitral tribunal will next determine the compensation to be paid to the investor by comparing its actual situation after the breach with the situation it would have been in had no breach taken place. Through its decision on the amount of an award to be paid by the offending state, the tribunal will seek to place the injured investor in the same financial position it would have been in had no breach occurred.[194]

The application of this standard to normally complex fact situations presented in investor–state disputes is a difficult process, fraught with many technical complexities. A discussion of those valuation complexities is beyond the scope of this book. It should be noted, however, that a determination of the precise amount to be paid to investors involves issues of causation, proximity, and valuation.

[193] *MTD Equity Sdn. Bhd. & MTD Chile SA v Chile*, ICSID Case No ARB/01/7 (Award) (25 May 2004) ¶238.

[194] *Petrobart Ltd v Kyrgyz Republic*, Arb No 126/2003, Arbitration Institute of the Stockholm Chamber of Commerce (Award) (29 March 2005). In this case, decided under the Energy Charter Treaty, the tribunal stated: 'The Arbitral Tribunal agrees that, in so far as it appears that Petrobart has suffered damage as a result of the Republic's breaches of the Treaty, Petrobart shall so far as possible be placed financially in the position in which it would have found itself, had the breaches not occurred' (ibid 77–8).