Striking a fair balance between foreign investor protection and host states’ right to regulate

A review of the international investment law awards of 2016 through the lens of the principle of proportionality

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1 Introduction

This master’s thesis investigates whether current international investment law manages to balance foreign investor protection with other rights and interests at stake in an international investment dispute. The investigation takes the form of a case law review of the international investment law awards of 2016, focusing on whether and how the international investment arbitral tribunals use the elements of the principle of proportionality. The analysis is twofold, as it will look at how international investment law tribunals of 2016 apply the principle of proportionality, as well as use the three criteria of the principle of proportionality to understand the legal reasoning of the international investment tribunals.

This chapter will introduce the debate in which this master’s thesis is based; namely that international investment law has been perceived as solely focusing on foreign investor protection and thus separating itself from all other rights and interests, and that the principle of proportionality has been suggested as a solution for the system to become more balanced (section 1.1). The thesis’ research questions and demarcations will also be presented (section 1.2 and 1.3, respectively). Methodological issues will be addressed (section 1.4), and some terminology will be explained (1.5).

1.1 Background

1.1.1 International investment law as a system designed to protect the foreign investor

International investment law is an international legal system that protects the investments of foreigners from the abuse of public power by the host state, which is the country where the investment takes place. Protection is granted to the foreign investor as a third party to an international investment agreement between states. These agreements can be bilateral investment treaties (BITs),¹ or other international treaties with investment provisions (TIPs),² such as the Energy Charter Treaty (ECT) and free trade agreements such as NAFTA³ and CAFTA-DR⁴. Attempts have been made to create an international framework convention for international investments, but none of these have so far been successful.⁵ Foreign investor protection

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¹ There are currently 2 369 BITs in force according to UNCTAD’s investment policy hub, ‘International Investment Agreements Navigator’.
² There are currently 303 TIPs in force according to UNCTAD’s investment policy hub, Ibid.
³ The North American Free Trade Agreement (NAFTA) is between the US, Mexico and Canada.
⁴ The Dominican Republic-Central American Free Trade Agreement (CAFTA-DR) is between Costa Rica, El Salvador, Guatemala, Honduras, Nicaragua and the Dominican Republic.
⁵ The OECD’s draft for a Multilateral Agreement on Investment (MAI) halted in 1998. It was questionable whether an organisation representing capital exporting countries was the right forum to negotiate a global instrument, and all the compromises led many to believe that the investor protection wouldn’t be satisfactory.
nevertheless has global implications, because some aspects are considered part of international custom and may be invoked through diplomatic protection.\textsuperscript{6}

The content of this customary protection has been labelled the minimum standard.\textsuperscript{7} It ascertains that fundamental justice is provided to the foreign investor; the foreign investor shall be treated with fairness in criminal and civil proceedings, not be discriminated against, and especially enjoy a certain protection of its property rights.\textsuperscript{8} In modern international investment agreements, this fundamental protection is secured through clauses that regulate the conditions for expropriation and clauses imposing an obligation to provide the investor with fair and equitable treatment.\textsuperscript{9}

In the event of a dispute, most international investment agreements give the foreign investor the possibility of pursuing its rights in an international arbitration process, instead of relying on diplomatic protection or on the host state’s national courts. This is called Investor-State Dispute Settlement (ISDS), and means that the foreign investor and the host state will settle the dispute in an ad hoc arbitral tribunal.\textsuperscript{10}

In sum, international investment law can be described as a system that singles out one type of legal entity (the foreign investor) and one type of rights (that of the investment), and provides the combination a special protection (through ISDS). The system might thus be viewed as separated from other rights and interests by design.

\textsuperscript{6} Prominent cases before modern investment agreements are the \textit{Norwegian shipowners’ claims} case decided by the Permanent Court of Arbitration (PCA) in 1922, the \textit{Chorzow factory} case decided by the Permanent Court of International Justice (PCIJ) in 1928, and the \textit{Barcelona Traction} case decided by the International Court of Justice (ICJ) in 1970.

\textsuperscript{7} The minimum standard was addressed by the president of the American Society of International Law, Elihu Root, in a speech from 1910. Root, ‘The Basis of Protection to Citizens Residing Abroad’, 521–22.

\textsuperscript{8} Dolzer, \textit{Principles of International Investment Law}, 3. The classical example of the obligation to provide criminal justice to foreigners is the \textit{Neer v. Mexico} case from 1926 decided by the US-Mexico General Claims Commission.

\textsuperscript{9} In addition, many international investment agreements contain particular clauses against discrimination, most favourable treatment clauses (MFT), full protection and security clauses (FPS), umbrella clauses, and stabilization clauses.

\textsuperscript{10} There are currently 767 known treaty-based investor-state arbitrations, of which 256 are pending and 495 are concluded, according to the UNCTAD investment policy hub, ‘Investment Dispute Settlement Navigator’.
1.1.2 International investment tribunals seen as enhancing the foreign investor bias

The number of cases decided by international arbitral tribunals has increased in recent years. From 1990 to 2000 a total of 42 arbitrations were initiated and 18 decisions were issued, compared to the decade from 2000 to 2010, where 324 arbitrations were initiated and 271 decisions issued.\(^1\) During this period, mounting criticism towards international investment law has reached the extent that scholars have claimed that international investment law is facing a legitimacy crisis.\(^2\)

One main concern is that some international investment tribunals have interpreted the broadly worded investment agreements in stark favour of the investor. Thereby they have neglected other fundamental rights and interests also at stake in the same dispute, such as human rights or environmental protection.\(^3\) International investment tribunals have also found it to be legitimate for foreign investors to expect that the business environment in which they have invested does not change.\(^4\) The necessity of being able to regulate for the public welfare has on the other hand been stressed both by developed countries seeing their democratic and administrative systems challenged, and by developing countries, emphasising that sustainable development is only possible through the establishment of functioning institutions.\(^5\)

The question of how international investment law combines foreign investor protection and the host state’s ability to regulate and exercise its police powers has not been given one unified answer.\(^6\) The diversity of awards is problematic as such because it undermines predictability and makes the system appear as a forum for the arbitrators’ subjective opinion. In addition, the diversity makes it hard to determine what the current doctrine of international in-

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\(^1\) According to UNCTAD’s investment policy hub, ‘Year | Investment Dispute Settlement Navigator’.


\(^3\) The tribunals in for instance Mealclad v. Mexico declared that it was irrelevant for their decision that the undertaken measure aimed at protecting the environment.

\(^4\) The many cases regarding Argentina’s economic crisis of 2001-2002 have strengthened this concern, as the tribunals did not take Argentina’s interests into account and adopted an unduly broad interpretation of Argentina’s obligations. Henckels, *Proportionality and Deference in Investor-State Arbitration*, 4.


\(^6\) With regard to the fair and equitable treatment standard, the most prominent example is CME v. Czech Republic and Lauder v. Czech Republic, where the two tribunals viewed the same media policy to both be a violation and not a violation of the standard. SGS v. Philippines and SGS v. Pakistan are examples of how the umbrella clause has been interpreted in opposite directions. In all the cases against Argentina, the Argentinean government has argued that the economic crisis 2001-2002 led to a state of necessity, and this defense has been addressed rather differently by the tribunals; see for instance CMS v. Argentina, Continental Casualty v. Argentina and Total v. Argentina.
vestment law is. Looking at the cases from the beginning of this millennium we are presented with a rapidly expanding system of law where it has been uncertain whether the state has a right to regulate or whether investor protection is the only aim of international investment law.

As a consequence of the perceived bias towards the foreign investor, some countries, especially in Latin America, have terminated their BITs. Other countries have disengaged from ongoing negotiations. The widespread public opposition towards the Transatlantic Trade and Investment Partnership (TTIP) negotiations between the EU and the US is also an evident sign of the challenges the investment system is facing.

1.1.3 The principle of proportionality as a suggested tool for creating balance in the system

In recent international investment law literature, the principle of proportionality has gained much attention and it has been proposed as a solution to many of the challenges facing the system.

The principle of proportionality is generally understood to comprise a three- or four pronged test, which the measure under review has to pass. This is (1) an assessment of the legitimacy of the objective of the measure, (2) an analysis of the measure’s suitability to achieve this objective, (3) a determination of whether there exist alternatives, which infringe the right in question to a lesser degree, and (4) a final balancing exercise evaluating the importance of avoiding the interference vis-à-vis the importance of achieving the objective. The two first assessments are often combined in the so-called criterion of suitability. The third test assesses whether the measure is necessary for achieving the objective. The actual balancing undertaken as the final step is often labelled proportionality in the narrow sense or proportionality *stricto sensu*. The principle of proportionality can thus be summarised as encompassing the criteria of suitability, necessity and proportionality in the narrow sense.

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17 Titi, *The Right to Regulate in International Investment Law*, 23.
19 In addition to many articles, two doctoral dissertations have been written on proportionality and international investment law: Bücheler, *Proportionality in Investor-State Arbitration*, and Henckels, *Proportionality and Deference in Investor-State Arbitration*.
International investment law scholars have argued that application of the principle of proportionality will be advantageous in the context of international investment law as it will help the system overcome its isolation and become more balanced. The principle of proportionality is seen as a tool that may help tribunals cope with increased politicization of investment-state arbitration, and make the system pay due regard to human rights. Scholars have also claimed that the use of the principle of proportionality may help investment tribunals in producing “better and more convincing reasoning”, that can “enhance the perception of judicial output legitimacy in hard cases at a time where the regime in question by many is regarded to be at a crossroad”. The principle of proportionality is thus seen as a means to both overcome an excessive emphasis on the rights of the foreign investor and the system’s problem with inconsistency.

Although many view the use of the principle of proportionality as a positive development, serious concerns have also been raised regarding to its application in international investment law. Some international investment law scholars argue that the use of proportionality paves the way for excessive deference on the hand of the tribunals in deciding highly political matters. The use of the principle of proportionality is often considered to make value judgments more explicit, as well as to link the assessment more to the concrete facts of the case and the moral environment in which the dispute takes place. An excessively intense and subjective review may be seen as a negative by-product of this.

1.2 Research questions
This thesis will look at how the principle of proportionality may play a role in international investment law in making the system become more balanced. Chapter 2 will investigate what the three criteria of the principle of proportionality really entail, with the aim of answering what we can and cannot expect from applying the technique.

Chapter 3 presents the legal landscape in which the analysis of the cases of 2016 takes place. With special regard to the clauses of expropriation and the fair and equitable treatment stand-

22 Krommendijk and Morijn, “‘Proportional’ by What Measure(S)?”, 451.
25 Henckels, Proportionality and Deference in Investor-State Arbitration, 28. This mirrors Habermas’ famous critique that optimising legal values will make “the fire wall erected in legal discourse by a deontological understanding of legal norms and principle [to] collapse”, Habermas, Between Facts and Norms, 258–59.
ard, the chapter will display that the doctrine of international investment law in the first decade of this millennium diverged. The focus on the clauses regarding expropriation and fair and equitable treatment in this thesis is due to the fact that they provide the most fundamental protection to foreign investors and also lie at the heart of the cases from 2016. Chapter 3, moreover, highlights some of the concerns raised regarding how investment tribunals at the beginning of this millennium ordered foreign investor protection and host states’ right to regulate; be it an extensive foreign investor protection, giving the host state’s interests priority, or by applying the principle of proportionality. These concerns will be addressed again when the cases of 2016 are summarised in chapter 5, with the aim of discovering whether they still apply to the current doctrine of international investment law.

Chapter 4 provides the actual analysis of the international investment awards of 2016 through the lens of the principle of proportionality. This thesis understands the principle of proportionality as a general technique of legal reasoning that to various degrees may be recognised in all kinds of case law where arguments pull the decision in different directions. This has implications on the analysis of the investment tribunals’ awards of 2016. In addition to undertaking a traditional analysis of how the tribunals explicitly address the principle of proportionality, chapter 4 will investigate the reasoning of the tribunals in the cases of 2016 with the aim of discovering whether and how the elements of the principle of proportionality have been used. The analysis undertaken in chapter 4 thereby reveals important aspects of how the current doctrine of international investment law orders the interests of foreign investor protection and host states’ right to regulate – has it managed to strike a fair balance?

1.3 Demarcations
The apparent lack of legitimacy facing international investment law may be addressed in several ways. One way is to focus on flaws in the system’s design, which resembles commercial arbitration. Such procedural criticism points to the fact that within the institutional framework of Investor-State Dispute Settlement (ISDS) the arbitrators are chosen by the parties, the tribunals’ decisions are final without any possibilities of appeal, and the parties may be

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27 As for instance done by Fauchald with regard to the tribunals’ reasoning more generally, Fauchald, ‘The Legal Reasoning of ICSID Tribunals - An Empirical Analysis’. When establishing a legal concept, it is common to first address cases that explicit refer the concept, then cases where the concept is used without an explicit reference and lastly cases where the concept can be established as a constructed ratio decidendi.

28 Criticism has been targeted both towards whether the arbitrators might have economic benefit in the outcome and whether they are suitable (both professionally and legitimately) to decide such disputes.

29 The issue of lack of appeal has especially been addressed by EU when negotiating new investment agreements such as CETA and TTIP.
granted discretion. This thesis will not address any systemic flaws in international investment law, but instead look at the substantial reasoning of the investment tribunals and thus the content of international investment law doctrine.

Another way of addressing the concern that international investment law is too isolated is through the fragmentation debate, which asks whether similar questions are solved differently in different legal systems. This debate was partly sparked by the Yukos disputes, in which shareholders brought claims to different international courts and tribunals challenging the Russian criminal proceedings with regard to tax evasion, leading the oil company to go bankrupt. Although this thesis frequently will refer to how other courts and tribunals apply the principle of proportionality, this is not addressed as a question of whether international investment law is a self-contained regime.

There are also many political and factual aspects with regard to whether international investment law is perceived as a legitimate system or not, for instance whether the investment tribunals’ assessments historically have been a product of colonialism and whether their awards cause so-called regulatory chill. Some also question whether the grant of protection actually influences whether the foreign investors decide to invest in the host country. This thesis will neither confirm nor challenge these views.

In addition to these radically different perspectives on addressing concerns regarding international investment law, there are also many other ways to view the role of proportionality than the view taken in this thesis. A prominent alternative view is to link the principle of proportionality to the so-called “margin of appreciation” doctrine. In that context, the questions of deference and the intensity of the review are often seen as an integral part of the principle of proportionality. Although these issues are acknowledged in this thesis as central aspect of legal doctrine, they will not be addressed separately.

30 The system’s lack of transparency has been met with extensive critique and this has led UNCITRAL to adopt UNCITRAL Rules on Transparency in Treaty-based Investor-State Arbitration based on the UN Mauritius Convention on Transparency.
31 ECtHR Yukos v. Russia, application number 14902/04, 31 July 2014. In addition many arbitral proceedings were conducted; three before the PCA (Hulley v. Russia, Yukos v. Russia, Veteran v. The Russia), as well as one before the ICC and two before the SCC. For an analysis of the differences see for instance Brabandere, “Yukos Universal Limited (Isle of Man) v The Russian Federation Complementarity or Conflict?”
32 Ville and Siles-Brügge, T.T.I.P., 115.
33 Hallward-Driemeier, ‘Do Bilateral Investment Treaties Attract Foreign Direct Investment?’, 22.
1.4 Methodological clarifications

1.4.1 International investment law as public international law

The Investor-State Dispute Settlement (ISDS) system, in which arbitral tribunals settle investment disputes directly between a foreign investor and the host state, resembles commercial arbitration to a high degree. Despite such similarities, international investment law is concerned with public international law and not private law. This is because the state’s obligations arise from international investment agreements, which are international treaties between states benefiting foreign investors as third parties. International investment agreements are thereby international conventions under the Statute of the International Court of Justice (ICJ) article 38. Most agreements also explicitly contain provisions stating that the investor-state dispute shall be decided in accordance with international law.

The acknowledged method of interpretation of international conventions is established in the Vienna Convention on the Law of Treaties, which was drafted partly as a codification of customary law and partly as a new development of custom. Especially, articles 31 and 32 are considered customary law and are applicable to any international treaty interpretation regardless of whether the involved states are party to the Vienna Convention or not.

For several years, it was unclear whether international investment law arbitral tribunals used the method established in the Vienna Convention. Fauchald undertook a study of the legal reasoning of international investment tribunals in 2008, where he concluded that the way the tribunals use interpretive arguments is far removed from the structure in the Vienna Convention articles 31 through 32 and “it seems appropriate to conclude that ICSID tribunals could do significantly more to align their approaches with those of other tribunals”. Weeramantry, on the other hand, has stated that the number of investment awards that acknowledge the customary status of the Vienna Convention is considerable. The latter also points to the fact that tribunals have used the Vienna Convention in cases where the respondent state was not party

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35 Some international investment agreements contain a so-called umbrella clause that includes contractual obligations into international investment law. The scope of foreign investor protection is thus extended from only acts originating from the state as a sovereign in breach of international obligation to acts undertaken in its private capacity. See Alvik, Contracting with Sovereignty., and Brabandere, Investment Treaty Arbitration as Public International Law, 24–49.

36 In addition to the ICSID Convention Article 42 (1), this is stated in NAFTA Article 1131 (1) and ECT Article 26 (6), as well as in many BITs and special agreements on applicable law, see Krommendijk and Morijn, “Proportional” by What Measure(S)?’, 424. and Dolzer, Principles of International Investment Law, 288.

37 The preamble of the Vienna Convention on the Law of Treaties

38 Gardiner, Treaty Interpretation, 7.


40 Weeramantry, Treaty Interpretation in Investment Arbitration, 28.
to the Convention. Gazzini argues that the question in international investment law is not whether the Vienna Convention applies, but how it applies. The approach taken in this thesis is therefore that international investment agreements are to be interpreted in accordance with the method established in the Vienna Convention, especially articles 31 and 32.

1.4.2 Challenges raised by a patchwork of different investment agreements, arbitral tribunals and awards

This thesis will focus on 19 cases decided by investment tribunals in 2016. Earlier cases will also frequently be invoked. An analysis of decisions from arbitral tribunals faces some particular methodological challenges.

Case law will be the main legal source of this master’s thesis. This might be problematic, as there is no doctrine of precedence in international investment law. Case law is nevertheless the most frequently used source of interpretation by investment tribunals. Today, it is well established that investment tribunals rely on awards passed by other tribunals. Looking at how investment tribunals reason is therefore relevant for establishing the doctrine of international investment law.

International investment disputes are decided by arbitration tribunals put together for that particular dispute. The fact that there is no uniform forum for settling investor-states disputes is a challenge with regard to finding the relevant awards. This issue will be elaborated on further in chapter 4. It is also a challenge that many of the tribunals’ decisions are not public.

There are, however, different institutions that arrange for Investor-State Dispute Settlement (ISDS). The most widely used institution by far is the Centre for Settlement of Investment Disputes (ICSID), established under the World Bank, with 495 known cases in total. The second most used institution is the Permanent Court of Arbitration (PCA), with a total of 98 known cases. The Stockholm Chamber of Commerce (SCC) is the third most used institution for settling international investment disputes, with 37 known cases in total. The fourth and fifth most used institutions are the International Chamber of Commerce (ICC) and the London Court of International Arbitration (LCIA), with only six and five known decided cas-

41 Ibid., 29.
42 Gazzini, Interpretation of International Investment Treaties, 4.
44 Dolzer, Principles of International Investment Law, 19.
45 ‘Arbitral Rules | Investment Dispute Settlement Navigator’.
46 Ibid.
47 Ibid.
Cases from the Iran-US Claims Tribunal are entirely excluded from this thesis because the tribunal’s jurisdiction essentially concerns contractual claims. An additional challenge is that the legal basis, meaning the international investment agreement establishing the foreign investor’s rights, varies from dispute to dispute. Since the tribunals’ assessments must be based on the specific investment agreement relevant for the dispute, variations will have implications on the tribunals’ reasoning. But, because many of the clauses resemble each other, this thesis will, like most international investment law literature, compare the cases without taking too much notice of the differences that might exist between the wordings in the underlying investment agreements. This approach must, however, not be mistaken for an indifference towards the fact that every international investment agreement is an individually negotiated international treaty where the specific intentions by the parties are of significant importance when solving disputes arising under it.

The procedural rules regulating the disputes are mostly those of the ICSID convention. The UN Commission on International Trade Law (UNCITRAL) has also provided procedural rules for international investment arbitration. Since this thesis does not focus on the procedural aspects of international investment law, this will not be elaborated any further.

1.4.3 Legal theory

The case law review undertaken in this thesis is made on the basis of a thorough theoretical analysis of the principle of proportionality. This analysis primarily draws on the work of the German legal scholar Robert Alexy. In the 1980’s, he developed a principle-theory where he distinguishes between rules and principles. Where rules are definitive and determine the outcome of a case in an all or nothing manner, principles are *prima facie* reasons for determining the outcome and must be optimised to the greatest extent possible by using the principle of proportionality. Although this thesis does not agree with Alexy’s qualitative distinction be-

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48 Ibid.
51 Ibid., 60,67.
tween rules and principles, his elaboration on the principle of proportionality will form the
basis of chapter 2.

Some basic logic will also be applied as part of the analysis of the principle of proportionality.
This is mainly the conditional sentence “if … then …”, which will be symbolised with “→”.
Using a conditional sentence implies the logical rules of modus ponens (A → B, A, conclusion is B) and modus tollens (A → B, not B, conclusion is not A). The use of this basic logic
aims at more precisely addressing legal reasoning.

1.5 Terminology
Since this thesis does not share Alexy’s categorical distinction between rules and principles,
these terms will not be used in accordance with his theory. This also has implications for the
use of the terms “collision”, “conflict” or “competition”, where the terms will be used indepen-
dently of whether the realisations of the rights in question are mutually exclusive or merely
pull the decision in different directions, so that they may be fulfilled or violated to various
degrees (including the extreme situation of total violation).

Two other terms that will be used somewhat synonymously in this thesis are the host states’
“police power” and their “right to regulate”. Both terms will cover the interest of regulating
for the public benefit as well as using ordinary discretion.

The term “award” is used for the investment tribunal decisions that assess the merits of the
investor-state dispute. The term “case” will, however, also be frequently used and, depending
on the context, these terms will be used as synonyms.

52 Chapter 2 rather argues that both the situations can be solved through the principle of proportionality as a
reason based model. The distinction is that in some legal cases competing reasons seldom apply and when it
applies, the relation between them can be decided rather intuitively, whereas on other cases a more thorough
reasoning is needed, taking account of both the reasons for and against the outcome.
53 According to Kumm, Alexy’s work is “one of the most penetrating, analytically refined, and influential gen-
54 Høgberg, I språkets bilde, 76–77.
55 Alexy distinguishes between “conflicts” between opposing rules and “collisions” between principles.
56 Sometimes the “police power doctrine” is only used with related to expropriation and the “right to regulate”
only with regard to the fair and equitable treatment standard.
2 The principle of proportionality as a semantic structure used when rights and interests collide

2.1 Introduction
This chapter will investigate the principle of proportionality. It will first address the diffusion of the principle of proportionality, establishing that the principle today is considered a general principle of law (section 2.2). Then the different elements of the principle of proportionality will be elaborated, namely the criteria of suitability (section 2.3), necessity (section 2.4) and proportionality in the narrow sense (section 2.5). The process of applying the principle of proportionality in legal cases will be summarised (section 2.6), before the premises for the following analysis of the international investment cases of 2016 will be stated (section 2.7).

The rather technical explanations that will be given in this chapter are helpful for understanding what courts and tribunals do when they decide a case. This chapter thereby establishes the framework upon which the analysis in chapter 4 will be conducted.

2.2 The principle of proportionality as a general principle of law
The growing scholarly interest in the principle of proportionality has mostly taken an inductive approach; focusing on how courts and tribunals actually reason instead of how they should reason.\(^{57}\) This interest has led to investigations of the diffusion of the principle in constitutional systems in different parts of the world, as well as its use in international courts and tribunals. The conclusion of these investigations seems to be that “[a]lready today, this technique possibly constitutes a principle of customary international law across all areas of the law. It is also plausible to classify proportionality as a general principle of law as referred to in Article 38 (2) (c) of the ICJ Statute.”\(^{58}\)

The following presentation will substantiate the statement that the principle of proportionality today should be considered a general principle of law.\(^{59}\)

The use of the principle of proportionality by various constitutional courts is well documented. Stone Sweet and Mathews have tracked the genealogy of the principle from German administrative law (polizeirecht) and documented thoroughly its diffusion into the adjudication

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\(^{57}\) Beatty, The Ultimate Rule of Law, 34.


\(^{59}\) The Statute to ICJ article 38 (1) (c) requires the general principle of law to be “recognized by civilized nations”. A common understanding of this is that the norm must be established through abstraction from national legal systems and be recognized by a generality of states. See for instance Bücheler, Proportionality in Investor-State Arbitration, 32. and Raimondo, General Principles of Law in the Decisions of International Criminal Courts and Tribunals, 1.
of the supreme courts of Canada, New Zealand, South Africa and Israel. Beatty examines how the principle also is used in Hungary, India, and Japan, and that even controversial cases in the US, like Roe v. Wade (1973), are best understood through the lens of the principle of proportionality. This resonates with the observations made by Aleinikoff in his famous article “Constitutional Law in the Age of Balancing”, where he already in 1987 pointed to the widespread use of balancing in the US. The principle of proportionality is today viewed as a global model for constitutional rights.

The principle of proportionality is not only used by national courts. Also those who apply public international law in international courts and tribunals have recognized it as a tool to solve cases where different interests are at play. The principle applies to various circumstances precluding wrongfulness under international public law, like consent, self-defence, counter measures, force majeure and distress, as well as being a fundamental element of humanitarian law.

The most frequently emphasised example of international tribunals using the principle of proportionality is the European Court of Human Rights (ECtHR), which systematically applies the principle of proportionality. The principle is also well established in EU law, both regarding fundamental principles and the four freedoms of movement. The principle of proportionality is also gaining ground in the WTO Appellate Body.

Peters has characterised three different conflicting norm constellations in international law where the principle of proportionality is applied: The first is the horizontal version, where the relationship is between a breach of international law by one state and the countermeasures by another state. The requirement in humanitarian law not to use force beyond what is necessary to defeat the enemy is an example of this. The second is the diagonal version, where the

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60 Stone Sweet and Mathews, ‘Proportionality Balancing and Global Constitutionalism’.
64 Articles 20 to 25 of the ILC Articles on State Responsibility contain six circumstances that preclude wrongfulness; consent, self-defence, counter-measure with regards to an international wrongful act, force majeure, distress and necessity. These articles are commonly deemed to codify customary international law, see for instance Titi, The Right to Regulate in International Investment Law, 236, and Christoffersen, Fair Balance, 35.
65 See Arai-Takahashi, The Margin of Appreciation Doctrine and the Principle of Proportionality in the Jurisprudence of the ECHR.
67 See Andenas and Zleptnig, ‘Proportionality’.
relationship is between national public interests and the particular interests of individuals. Human rights law, as well as international investment law, belongs to this category. The third is the vertical version, between a global public interest and the particular interests of a state. Trade law is often used as an example of this version, where all states’ common interest in global trade stands against individual states’ interest in protection.

The three different elements of the principle of proportionality; suitability, necessity and proportionality in the narrow sense is not necessary undertaken in a strict sense by those who apply the law. Christoffersen has for instance showed that the Canadian Supreme Court undertakes a quite strict assessment of each of the steps, whereas the South African Supreme Court rather places all relevant factors side by side in a none-hierarchical order and thus undertakes a more flexible assessment. Christoffersen’s point is that “the various elements in the proportionality test may be listed vertically and tested one after the other or arranged horizontally and reviewed as part of an overall balance test”. What remains, however, is that the three different elements of proportionality describe types of assessments which can be recognized regardless of how strict they are applied. A more precise presentation of these elements will be given in the following section.

2.3 The criterion of suitability

As established in the above section, all the tree elements that constitute the principle of proportionality are general principles of law widely recognised by courts and tribunals. In the following three sections, the three criteria of suitability, necessity and proportionality in the narrow sense will be thoroughly elaborated. The aim of these sections is to explain what courts and tribunals do when they decide fundamental legal disputes, a technique that scholars have labelled the principle of proportionality. In chapter 4, it will then be investigated to what extent these elements of reasoning may be found in the cases of 2016, thus explaining their reasoning.

This section will look at the criterion of suitability, which assesses whether the challenged measure is suitable to reach a legitimate end pursued by the state. The suitability criterion thus consists of two assessments; (1) an assessment of the legal legitimacy of the state’s pursued objective and (2) an assessment of whether the challenged measure may contribute to achieve this objective.

69 Christoffersen, Fair Balance, 71–73.
70 Ibid., 73.
2.3.1 Establishing a legitimate objective

What is regarded as a legitimate objective depends on the legal system in which the assessment takes place. It is the underlying legal doctrine that must provide an answer as to which objectives the state is allowed to pursue and whether such an objective in theory might legitimate an interference with the right at issue. The legal systems presented in section 2.2 will serve as examples.

Some legal documents contain explicit textual references as to which ends lawfully may limit the protected rights. The rights in the Canadian Charter of Rights and Freedoms are, for instance, limited by a general limitation clause. The clause has been interpreted by the Canadian Supreme Court so as to allow the government to pursue any objective of “sufficient importance” or “pressing need”. In the European Convention on Human Rights (ECHR) the limitations are not expressed in a general clause, but in specific limitation clauses attached to each of the rights and freedoms in articles 8 to 11. The specific limitation clauses list in detail which interests states may pursue when restricting the relevant rights and freedoms. Also the different clauses on the four freedoms in EU/EEA law declare that states may restrict the free transfer of goods, services, capital and manpower to protect certain aspects of public welfare.

Explicit limitation clauses do not always exist, however. As Aharon Barak has put it: “[i]n some cases, a constitution may declare the substance of a right without saying anything explicit about its limitation. The conventional view is that constitutional silence does not make the right absolute and that the right may be limited by law, as long as the limitation is proportional.” The reasons for allowing limitations may be found somewhere else than explicit in the text; like in the interpretation of the right, in conflicting fundamental rights, or in democracy itself or the idea of the rule of law.

This is for instance the case in Norway, where the Norwegian Supreme Court has stated that the constitutional rights obviously are not absolute and need to be limited even when this is not explicitly stated in the wording of the provision. The German Federal Constitutional Court has also allowed for limitations of rights not containing limitation clauses, because the

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71 Grimm, ‘Proportionality in Canadian and German Constitutional Jurisprudence’, 388. A similar general clause is found in article 52 (1) of the EU Charter on Fundamental Rights.
73 For instance the EEA agreement article 13 (free movement of goods), 33 (right to establishment), 28 (free movement of worker) and 39 (services).
75 Ibid., 741.
76 Rt. 2015 s. 93, para 60.
court “… holds that in a democracy the legislature is entitled to pursue any purpose, provided it is not excluded by the constitution.”

In EU/EEA law, the ends that lawfully can lead to restrictions on the four freedoms have been extended to more than those explicitly listed in the text.

As shown in this subsection, the first part of the principle of suitability is to determine whether a legitimate objective exists. It has also been shown that different legal systems might give different answers to this question.

2.3.2 Establishing whether a measure is suitable to reach the legitimate objective

This subsection will look at the next part of the suitability criterion, namely whether the challenged measure is suitable to reach the legitimate objective pursued. This has been described by Barak as a need for a rational connection between the measure and the end “… that is not merely marginal, scant or theoretical.”

Alexy has described suitability as a negative criterion that cuts out unsuitable means. If the measure M is not suitable to furtherance the end required by a legal norm P₁, it is irrelevant for this norm whether the measure is adopted or not. But if M in the circumstances of the case hinders the realisation of another legal norm P₂, M is not irrelevant for the realisation of P₂. To avoid violating a legal norm without achieving the desired objective, the measure should not be adopted. As formulated by Klatt and Meister: “[t]he principle of suitability is an expression of the idea of Pareto-optimality and excludes the adoption of means which obstruct at least one right without promoting any other right or interest.”

The assessment of suitability is a straightforward clarification of whether a conflict between two relevant norms really exists. If the state has chosen to undertake an action that cannot reach the legitimate end they pursue, there is no real conflict between this end and the infringed right; it is only a right that is infringed by an illegitimate measure. In this conflict the outcome is clear, because there are no reasons why the protected right should not prevail over an illegitimate measure.

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77 Grimm, ‘Proportionality in Canadian and German Constitutional Jurisprudence’, 388.
78 Sejersted et al., EOS-rett, 332, 386, 406, 447. Especially the ECJ Cassis de Dijon case from 1979 is well-known for this.
80 Alexy, A Theory of Constitutional Rights, 399.
This could be exemplified with, for instance, a host state that prohibits chemicals to hinder water pollution, with the result that a foreign investor has to close down its production. If the prohibited chemical is not hazardous and therefore does not pollute the water, there is no conflict between the state’s end to hinder water pollution and the interest of the foreign investor to continue its production. It is only a state measure irrelevant for the attainment of the end, on the one hand, and an infringed interest, on the other, and no legitimate conflict exists.

Under EU/EEA law, the assessment of whether the measure in reality is hidden discrimination is well known, and one example can be the EFTA court’s decision in the Kellogg’s case, where the Court found it to be a restriction of import to forbid cereal with additional iron, when brown cheese also has the same additive. The Norwegian government’s aim of protecting the public from adding nutrition did therefore not hold.

Establishing whether a challenged measure is suitable for realising an end is a factual assessment based on evidence. How the assessment is undertaken is, however, part of the underlying legal doctrine. It is for instance very different if the assessment is based on the hindsight-knowledge or what would be considered reasonable at the time the measure was adopted. What is required for a measure to be reasonable can also vary among legal systems. In constitutional courts the assessment will be characterised by the division of power between the legislature, the government and the court. The assessment will thus normally pay due regard both to the knowledge of the administration and the principle of democracy.

In the judgments from the ECtHR, the strengthening of the principle of subsidiarity has led the Court to focus its assessment on reviewing whether the national decision has followed all the required steps of reasoning, rather than reviewing the actual assessment by the national authorities.

In the above, it has been established that the suitability assessment takes place on two levels; namely to establish a legitimate objective and to assess if the objective can be reached by the undertaken measure. The criterion of suitability thus strives to establish whether legitimate rights and interests collide in the situation at hand. Which arguments and reasons courts and tribunals use to undertake this assessment depend, however, on the underlying legal system. The criterion of suitability is thus a semantic structure in which the existence and validity of the arguments are to be found externally.

82 Sejersted et al., EØS-rett, 338.
83 ECHR Protocol 15
2.4 The criterion of necessity

The second element of the principle of proportionality is the criterion of necessity, which asks whether the challenged measure is necessary for the state to obtain the pursued objective. If another measure is available that would realise the pursued objective equally as the challenged measure, but this measure would infringe the affected right to a lesser degree than the challenged measure, the criterion of necessity requires that the state rather perform this measure instead of the challenged one.

Alexy describes necessity in a technical, but illustrative, way:84 A state justifies pursuing the end E by reference to the principle (legal norm) P₁. If there are at least two measures, M₁ and M₂, which are equally suitable in realising E, it is irrelevant for P₁ whether M₁ or M₂ is chosen, since it does not prefer M₁ over M₂. M₂ affects, however, another principle P₂ less intrusively or not at all in comparison to M₁. In relation to P₂ it is thus not irrelevant which measure is adopted, and to optimize the realisation of P₂, M₂ should be chosen. To take account of both P₁ and P₂, the state should undertake M₂ when pursuing its end.

This description of the structure of necessity shows that it is similar to the economic concept of Pareto-optimization; one norm can be improved without detriment to another norm.85 This is not optimization to the highest point, but simply a ban on unnecessary sacrifices of constitutional rights.86

The legal scholar Kai Möller has distinguished between two situations where the state measure is considered unnecessary. In the first situation, the state does more than what is necessary for realising the objective and in the second, the state has a choice between different ways of achieving the objective, and one is less restrictive than the other.87 In the following, both of these situations will be examined; it will be shown that only the first situation is a factual assessment of whether the measure is necessary to reach the aim, and that the second situation is a balancing exercise in line with the last step of the principle of proportionality.

2.4.1 The measure exceeds what is necessary to reach its end

The first situation of necessity, in which the state does more than what is required for achieving the pursued objective, the parts of the measure exceeding the aim resemble the situation of an unsuitable measure.

85 Ibid., 398.
86 Ibid., 399.
This can be illustrated with the European Court of Justice (ECJ) judgment in the *Rau* case. In Belgium, margarine was sold in square packages and butter in round packages. The Belgian government defended the prohibition on selling margarine in other packages than square ones, by claiming that the consumer could be misled to think that the content was butter. ECJ, however, found that consumer protection could be adequately safeguarded by correct labelling on the margarine packages and therefore found that the Belgian measure exceeded what was necessary.\(^88\)

The legal conflict in the *Rau* case was between the need for consumers to understand what they were buying and a restriction on the free exchange of goods, here margarine. When correct labelling would provide the consumer with adequate information, measures exceeding this, such as requiring a specific shape on the packages, would then only infringe the free exchange of goods without any legitimate reasons. This is the same situation as the one described as the suitability criterion; when the measure is irrelevant for one of the principles at stake, no conflict arises.

To return to the example of chemicals being prohibited by a state to prevent water pollution, a measure prohibiting all kinds of a chemical composition even if some of them are not hazardous, this would exceed what would be necessary for preventing water pollution. The prohibition of also the chemicals that are not hazardous would not contribute to the realisation of that state’s objective, and therefore be neither suitable, nor necessary.

This subsection has shown that in the situation where the challenged measure goes beyond what is necessary to achieve the state’s objective, the exceeding parts can be described as unsuitable. It has thereby been shown that the necessity criterion is nothing else than the suitability criterion, under which it is established whether an actual conflict between legally relevant rights and interests exists.

### 2.4.2 A choice between two measures

In the second situation where a measure can be considered unnecessary, the state has a choice between different measures to achieve its end. In this situation, Möller emphasises that a real conflict does exist, but that the traditional formulation of necessity might be too simple when it asks whether there exists a less restrictive, but equally effective means. “The problem is that often there exists an alternative policy which is indeed less restrictive but has some disadvantage.”\(^89\) First, the alternative measure might not be as effective as that undertaken (a total

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\(^88\) Sejersted et al., *EØS-rett*, 341.
\(^89\) Möller, ‘Proportionality’, 714.
ban is e.g. always more effective than only some particular regulations). Second, the alternative measure might require additional resources. Third, the measure might impose a burden on a third party.

In the hazardous chemicals example, the state could upgrade its purification plant to clean the polluted water instead of prohibiting the hazardous chemical. This alternative measure would not infringe upon the foreign investor’s assumed rights, but it would not be as effective as a total ban and it would be costly for the host state. According to Möller, “[t]he proper way to handle such cases must be to assess all the possible policies relative to each other.”\footnote{Ibid., 715.} This means that what is actually done is balancing the need for investor protection with the need for the host state to undertake the desired measure.

Dieter Grimm has seen a different approach taken by the German and Canadian constitutional courts when faced with this second situation of the necessity assessment.\footnote{Grimm, ‘Proportionality in Canadian and German Constitutional Jurisprudence’, 393.} The German Federal Constitutional Court usually concludes that the measures are not equally effective to achieve the pursued end and moves on to perform the balance exercise under the stage of proportionality in the narrow sense. The Canadian Supreme Court, on the other hand, balances the two rights against each other at the stage of necessity. This Canadian approach to a lesser extent draws the attention to the fact that the court is assessing the relationship between different rights and interests, and instead camouflages it as only a factual consideration labelled necessity. Regardless of what it is labelled, what the court actually does is to perform a stricto sensu proportionality assessment.

In the German approach, the fact that a state considers it necessary does not say anything about whether it infringes a right disproportionally. Alexy stresses that the necessity test only enables us to distinguish between $M_1$ and $M_2$, and emphasises that establishing that no better reason exists does not justify that the measure is undertaken.\footnote{Alexy, A Theory of Constitutional Rights, 68.}

The distinction between these two approaches may be further illustrated comparing the jurisprudence under ECtHR and the case law regarding the free movement under EU law. The European Court of Justice does as a main rule not challenge the level of protection that the national states want to pursue.\footnote{Sejersted et al., EØS-rett, 339.} Because the level of protection wanted by the state is respected by the court, the measure will be deemed lawful as long as the conflict is real (meaning that the measure is suitable to reach the states objective and does not exceed its aim so that the...
surplus is not in conflict with the right to free movement).\textsuperscript{94} In for instance the ECJ \textit{Gräbner} case, the court did not assess whether it was appropriate to only allow doctors to perform certain health services when professionals with other educations were allowed to undertake those services in other countries, without this causing any public health problems. Assessing whether the state merely should have required knowledge in those specific health areas instead of a full medicine degree, would have challenged the desired level of protection and instead opened up for the court to strike another balance between the public health and freedom of movement.

This could be contrasted with for instance the ECtHR case \textit{Smith and Grady v. UK}, where the Court found that prohibiting gays in the armed forces was not considered necessary in a democratic society, partly because the eventual problems regarding the maintenance of moral in the armed forces could have been dealt with in a code of conduct that would have interfered with the individuals’ rights to a far less degree.\textsuperscript{95} The UK government’s desired level of protection from disorder, which is explicitly included as a legitimate objective in the limitation clause to ECHR article 8, was thus challenged, and another balance between the interests at stake was struck.

Necessity in this second situation is thus an assessment of the proportionality in the narrow sense, which will be presented in the following section.

\textbf{2.5 The criterion of proportionality in the narrow sense}

Proportionality is well described by Peters as “an appropriate relationship between different things in terms of size, number, and type. Disproportionality is thus a ‘wrong’ relationship.”\textsuperscript{96} Möller similarly argues that realising a fundamental right to the greatest possible extent, means to the “correct extent” in relation to other relevant rights and interests at play.\textsuperscript{97}

This actual undertaking of a balance exercise relating the rights and interests at stake is the last criterion of the principle of proportionality. To distinguish this criterion from the entire concept of the principle of proportionality, this element is often called proportionality in the narrow sense or proportionality \textit{stricto sensu}. This balancing exercise might seem rather mysterious, but the aim of this section is to show that it only describes ordinary legal reasoning.

\textsuperscript{94} Ibid., 409.
\textsuperscript{95} \textit{Smith and Grady v. UK} §§ 101-102
\textsuperscript{96} Peters, ‘Proportionality as a Global Constitutional Principle’, 1.
\textsuperscript{97} Möller, ‘Balancing and the Structure of Constitutional Rights’, 459.
2.5.1 The law of balancing

The legal scholar that most thoroughly has tried to understand what courts do when they assess proportionality in the narrow sense is Alexy. He has described the process in his so-called law of balancing:

The greater the degree of non-satisfaction of, or detriment to, one principle, the greater must be the importance of satisfying the other.\(^98\)

This law of balancing describes an exercise that Alexy breaks down into three stages:

The first stage is a matter of establishing the degree of non-satisfaction of, or detriment to, the first principle. This is followed by a second stage, in which the importance of satisfying the competing principle is established. Finally, the third stage answers the question of whether or not the importance of satisfying the competing principles justifies the detriment to, or non-satisfaction of, the first.\(^99\)

Striking a balance between two principles is thus to argue for the intensity of infringement of principles, and then to compare them. This process is illustrated in the weight formula that gives a mathematical picture of what happens when two competing principles (\(P_i\) and \(P_j\)) are balanced against each other:\(^100\)

\[
W_{i,j} = \frac{W_i \cdot I_i \cdot R_i}{W_j \cdot I_j \cdot R_j}
\]

\(W_{i,j}\) stands for the concrete weight of the principle \(P_i\), namely the weight of \(P_i\) in the circumstances of the case at hand.

\(W_i\) and \(W_j\) are the abstract weight of \(P_i\) and \(P_j\) respectively. The abstract weight is the weight of the principle relative to other principles, but independent of the circumstances of any concrete case. Most legal systems will for instance ascribe a higher abstract weight to the right to life than the right to property.\(^101\)

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I_i and I_j are the intensities of the interference under the concrete circumstances of the case.\textsuperscript{102} This means how much the right is affected by that particular measure (e.g. a total annihilation or only a minor interference). This mirrors the importance of satisfying the principle.

Lastly, R_i and R_j are the reliability of the empirical premises for what the measures in question mean for the realisation of one of the principles and the non-realisation of the other.\textsuperscript{103} The relationship between the empirical reliability of the competing principles follows what Alexy calls the second law of balancing: “[t]he more heavily an interference in a constitutional right weighs, the greater must be the certainty of its underlying premises.\textsuperscript{104}

Alexy then develops a triadic scale where the intensity of the interference with the principle (I_i and I_j, as well as W_i and W_j) is given the degrees of light (l), moderate (m) and strong (s).\textsuperscript{105} To reflect that the power of a principle to determine the outcome increases over-proportionality with the intensity of the interference, these values can be allocated numbers in according with the geometric sequence $2^0$, $2^1$ and $2^2$, namely 1, 2 and 4.\textsuperscript{106} The value of the reliability of the empirical assumptions decreases exponentially when the uncertainty increases in the geometrical sequence $2^0$, $2^{-1}$ and $2^{-2}$.

When the triadic scale is combined with the weight formula, it is possible to determine the outcome of the balancing. When the value of $W_{ij}$ is over 1, $P_i$ takes precedence over $P_j$, and when the value of $W_{ij}$ is below 1, $P_j$ takes precedence over $P_i$. When the value of $W_{ij}$ is 1 a situation of stalemate occurs – the balancing does not determine the outcome of the case and there is a structural discretion on the outcome of the balancing; the law does not determine an outcome and the situation is by definition political.

\begin{footnotesize}
\begin{enumerate}[\textsuperscript{102}]
\item Ibid.
\item Grasping reliability is hard, but Klatt and Meister seem to have found it used in the reasoning of the German Federal Constitutional Court when the court declared section 14(3) of the Aviation Security Act unconstitutional. The challenged provision would allow the German government to shoot down an airplane if they suspect that it is hijacked and thus might be used in a terrorist attack. The intensity of interference with the right to life was undisputedly considered high both for the people in the airplane and the potential victims of a terror attack. “Empirical uncertainties only exist as to whether the conditions required for such interference are met in the individual case, that is whether, for instance, a terrorist attack is given as a matter of fact or whether the radio contact is merely lost.” Ibid., 113, 129. According to Klatt and Meister’s analysis, the difference in reliability for the two groups of right holders made the certain loss of life of those in the airplane trump the more uncertain loss of life of the potential victims of terror.
\item Alexy, \textit{A Theory of Constitutional Rights}, 418.
\item The triadic model can easily be expanded to a double triadic (ll, lm, ls, ml, mm, ms, sl, sm, ss) or even a triple triadic scale, but this only makes the illustration more complicated without bringing much additional value. The intensity of the interference is the same as the importance of satisfying the principle.
\item Alexy, \textit{A Theory of Constitutional Rights}, 103.
\end{enumerate}
\end{footnotesize}
The weight formula highlights that the structure of balancing follows the rules of arithmetic in the same way as subsumption follows the rules of logic. An argument is logically wrong if the conclusion does not logically follow the premises, like when Erasmus Montanus claims that mother Nille is a stone because neither she nor a stone can fly. Simultaneously, an argument is arithmetically wrong if it concludes in favour of the reason that was given the least weight instead of the one given a high weight. If one says that the right to life has higher weight than catching a pickpocket to prevent crime both in abstract and in the particular situation at hand, and nevertheless concludes that it was okay for the police to deadly shoot the pickpocket, the rules of arithmetic are infringed.

The weight formula can be summarised in Alexy’s words, which also introduces the next subsection, which will emphasise how weight is ascribed to different legal norms:

“[The weight formula] identifies what is significant in balancing exercises, namely the degree or intensity of non-satisfaction of, or detriment to, one principle versus the importance of satisfying the other. Those who say that a very intensive infringement can only be justified by a very important satisfaction of an opposing principle are not saying when a very intensive infringement and a very important satisfaction are present. But they are saying what has to be shown in order to justify the conditional preferential statement which is to result from the balancing exercise, namely statements about degrees of infringement and importance. The arguments which can be used to justify such statements have nothing to do with balancing. One can rely on every possible type of legal argument.”

2.5.2 Ascribing weight to the different rights and interests in accordance with the underlying legal doctrine

The criterion of proportionality in the narrow sense has by now been described as a weighing of the reasons supporting one of the legal norms against the reasons supporting the colliding legal norm. However, what matters to determine what is correct or wrong, and thus appropriate or disproportionate, is the actual weight ascribed to the different rights and interests. This

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108 Holberg and Toft, Erasmus Montanus, 78.
109 The rules of arithmetic are, however, not violated if the underlying system ascribes more weight to the prevention of crime than to life, and therefore gives the police a general power to shoot in a situation where pockets are picked. The importance of logic and arithmetic are not to be exaggerated, see for instance Høgberg, I språkets bilde, 82.
110 Alexy, A Theory of Constitutional Rights, 105.
is neither a subjective or utilitarian exercise, nor an impossible exercise because rights and interests are incommensurable. Instead, the standard against which the rights and interests are ascribed weight is the underlying legal doctrine. Whether the outcome of a case is valid, therefore depends on the reasons which are given to support it; meaning if it is possible to provide a correct legal justification for the outcome.

Waldron argues that when comparing different entities, what is actually done is that they are ordered in accordance with each other. Waldron distinguishes between what is an “intuitive” ordering, where we simply see that one of the values takes priority over the other (saving the innocent child takes priority over the preservation of the statue that has fallen over her), and “reasoned” ordering, where we have to argue for establishing which value takes priority. The legal theories of for instance Dworkin, who asks which values trump the argumentation in hard cases, Rawls, who establishes a lexical priority among rights and freedoms and Nozik’s arguments for which rights are side constraints, all provide arguments and reasons for establishing what they perceive as the correct ordering.

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111 With the notion weighing or balancing one value, principle, or consideration against another, Waldron argues that non-lawyers do not understand utilitarian quantification (as some legal scholars seem to think that the notions refer to), “but any form of reasoning or argumentation about the values in question.” “In this sense, the reasoned articulation of our moral principles and priorities inescapably involves what ordinary people might regard as weighing and balancing”. Waldron, ‘Fake Incommensurability’, 819,821.

112 Waldron has clarified this by distinguishing between “strong incommensurability” and “weak incommensurability”. In strong incommensurability, the two considerations of a practical decision-problem are genuinely incomparable; neither of them have stronger weight than the other, nor do they have equal weight. This leads to agony and paralysis in practical discourse because it is not possible to reach a conclusion. Weak incommensurability, on the other hand, is according to Waldron usually expressed by a simple and straightforward priority rule – “… instead of balancing them quantitatively against one another, we are to immediately prefer even the slightest showing on the A side to anything, no matter what it weight, on the B side”. Waldron uses the examples of the theory of trumping by Ronald Dworkin, the theory of side constraints by Robert Nozick, and the idea of lexical priority by John Rawls and shows that the incommensurability in their theories are “weak” because the values can be brought into relation with each other, but it is still a form of incommensurability because there is an ordering among them. Ibid., 815–17.

113 “[t]he question is not the direct comparability of some entities, but the comparability of their importance for the constitution, which of course indirectly leads to their comparability.” Alexy, ‘On Balancing and Subsumption. A Structural Comparison’, 422.

114 Alexy, A Theory of Constitutional Rights, 27.


116 When non-philosophers look at for instance the reasoning of Rawls, they would, according to Waldron, describe it as attempts “to balance the importance of the basic liberties against the importance of social and economic considerations”. When Nozick investigates the prohibition against intentional aggression, self-defense comes up as a difficult issue that require him to think about the various reasons that might weigh in favour of attacking people in certain situations. This can be solved in how we define aggression, but as Waldron remarks: “[a]t a purely verbal level that may be so, but we are not permitted to reach this conclusion until we have actually done the reasoning”. Ibid., 819,821.
Courts and tribunals also decide legal disputes by investigating which reasons shall prevail in the particular situation. Sometimes the wording of a rule rather intuitively determines the outcome, and sometimes the outcome is more difficult to reach and requires thorough argumentation. Balancing is thus nothing else than arguing for or against a concrete order of rights and interests – which is given the metaphor of ascribing weight to them.

This applies also to norms that are considered absolute, because establishing that no other rights and interests are neither relevant nor takes precedence requires reasoning.\textsuperscript{117} Even the fundamental rights held to be most absolute, like the prohibition of torture, have in concrete cases been weighted against competing interests by the ECtHR.\textsuperscript{118} Although the US Supreme Court does not explicitly recognise the principle of proportionality, scholars argue that many of its decisions are best understood within the framework of proportionality.\textsuperscript{119}

Whether the provided arguments are valid or not depend on the legal doctrine in which the dispute is to be solved. The criterion of proportionality in the narrow sense thereby resembles the criteria of suitability and necessity and does not provide any arguments on its own accord.

That a semantic structure as such does not provide any outcomes may be illustrated by the controversial issue of abortion, which has been decided differently by courts using the principle of proportionality.\textsuperscript{120} The outcomes depend on how different countries ascribe different weight to the importance of the foetus life and woman’s right to self-determination, and how these weights might change during the pregnancy.\textsuperscript{121}

Since the structure of proportionality in the narrow sense merely is semantic and does not provide for a theory on the validity of the premises that are put into the structure, it has some

\textsuperscript{117} Ideally, contributive reasons are weighted for and against the result when a legal norm is made. Thus, “rules can be seen as a kind of summarise of the reasons that went into making them”, and the need for an additional balancing when applying it is not necessary. Hage, \textit{Studies in Legal Logic}, 279–80. However, a rule only replaces the reasons that went into it and new situations may demand new considerations. The categorical distinction between rules and principles therefore breaks down. “The true distinction between rules and principles is that rules have greater weight due to the additional impact of formal principles”, like democracy or equality. Möller, ‘Balancing and the Structure of Constitutional Rights’, 455.

\textsuperscript{118} Christoffersen, \textit{Fair Balance}, 83.


\textsuperscript{120} That different legal system may reach different conclusions has been lamented by Krommendijk and Morijn stating that “even if they are highly qualified, [investment] arbitrators are likely intuitively to appreciate human rights arguments from a different, more economical, perspective and will use the methodology of investment law to deal with human rights law. Investment law proportionality may then swallow up human rights law proportionality.” Krommendijk and Morijn, “‘Proportional’ by What Measure(S)?”, 449.

\textsuperscript{121} Beatty, \textit{The Ultimate Rule of Law}, 168.
obvious limitations.\textsuperscript{122} This has made many scholars argue that a theory on proportionality in the narrow sense is less relevant.\textsuperscript{123} The important question on how to ascribe “… a common, particular, quantifiable value to all variables considered especially that of weighing as trade-off and prudential compromise…” remains unanswered.\textsuperscript{124}

\section*{2.6 \textbf{The steps of applying the principle of proportionality to legal cases}}

This section will recap the above sections on the different criteria of the principle of proportionality, by highlighting how the principle of proportionality is applied by using investment law as example.

The principle of proportionality says that if the facts of the case fall under the scope of investment protection and the initial scope is not limited, the established consequences take place (for instance that a measure is not fair and equitable and therefore prohibited, or that the measure amount to expropriation and therefore should be compensated):\textsuperscript{125} S and not L \(\rightarrow\) Q

This means that if the host state’s acts and omissions fall under the initial wide scope of investor protection they are prohibited (or must be compensated) unless they are necessary to satisfy legitimately competing rights and interests, which in the circumstances of the case takes precedence over the principle of investor protection.

Alexy’s description of balancing is that that a legal norm takes precedence over another in some particular circumstances (C: (\(P_1\ P_2\))). This means that the reasons supporting \(P_1\) have greater weight than the reasons supporting the competing \(P_2\).

The conditions for the limit \(L\) to take place, so that the legal principle \(P_1\) does not prevail although the measure falls under the initial scope of protection are thus (1) that the competing interest \(P_2\) is a legitimate objective that the state can pursue under international investment law, (2) that the host state’s measure is suitable and (3) necessary to reach the pursued objective, and (4) that under the circumstances of the case the competing principle \(P_2\) take precedence over \(P_1\) ((\(P_2\ P_1\) C), meaning that according to the weight formula, \(W_{1,2}\) sinks below 1.

\begin{flushleft}
\textsuperscript{122} Alexy, \textit{A Theory of Constitutional Rights}, 28.
\textsuperscript{123} Frøberg, ‘Retslig Prinsippargumentasjon’, 134.
\textsuperscript{124} Torre, ‘Nine Critiques to Alexy’s Theory of Fundamental Rights’, 61.
\textsuperscript{125} Limiting a right is, however, nothing else than defining its content. Torkel Opsahl has given a good description of this mutuality in the context of the Universal Declaration: “To define a right in fact is the same time to limit it: It excludes what it does not cover.” Cited from Christoffersen, \textit{Fair Balance}, 73.
\end{flushleft}
The conditions under which the investor rights take precedence over colliding rights and interests, or vice versa, mostly consist of a wide range of circumstances \( (F_1 \ldots F_n) \). The situation might then be described as \( F_1 \) and \( F_2 \) and \( F_3 \rightarrow Q \).\(^{126}\)

2.7 Premises for analysing the awards of 2016

By now it has been established that the principle of proportionality is a semantic structure rather than being a legal doctrine that can provide answers to material questions. The principle of proportionality does not say anything regarding the validity of the premises included into it – be it which rights and interests are relevant in the dispute, or how a collision of rights and interests is to be solved.\(^ {127}\)

Despite the principle of proportionality merely being a semantic structure for reasoning, it may secure some form of basic rationality. The arithmetic rule illustrated through Alexy’s weight formula makes sure that the reasons given by an arbitral tribunal lead up to the conclusion. Establishing that the perceived collision is real under the criteria of suitability and necessity also has an independent value, because it secures that one is not compromising a legal norm without having a legitimate reason for this. Both of these insights are fundamental premises for the further argumentation in this thesis.

\(^{126}\) Alexy, A Theory of Constitutional Rights, 56.

\(^{127}\) The principle of proportionality is, however, often misunderstood. One prominent example is Tsakyrikis, who has criticised the principle of proportionality for assuming “that conflicts of values can be reduced to issues of intensity or degree and, more importantly, assumes further, that intensity and degree can be measured with a common metric (something like a natural force), and that this process will reveal the solution to the conflict. Thus it pretends to be objective, neutral, and totally extraneous to any moral reasoning.” Tsakyrikis, ‘Proportionality’, 7, 23–24. As presented above, this critique misunderstands the entire concept of the principle of proportionality.
3 International investment law at a turning point

3.1 Introduction

This chapter will look at how the clauses of expropriation and fair and equitable treatment have been interpreted differently regarding the competing interests of foreign investor protection and other rights and interests important to the host state. Some tribunals have seen international investment law as having an isolated aim of protecting the investor, whereas others have opened up for the interests of the host state. Both extremes have led to extensive criticism, and middle way approaches have therefore also been introduced.

Although the manifold arbitral decisions to this conflict of interest seem to be a patchwork of different solutions, they nevertheless show a tendency in international investment law that will be presented in this chapter. The aim of the chapter is to emphasise that international investment law the last decade seems to be at a turning point, where it still is not quite clear how it will evolve. The chapter thus establishes the point of reference from which the analysis of the cases of 2016 will be conducted.

The protection against unlawful expropriation (section 3.2) and the fair and equitable treatment standard (section 3.3) will in the following be presented in the same way. First, a general presentation of the clauses will be given, highlighting the part of the clauses that have been controversial and thus understood in opposing directions. Second, a selection of cases that clearly speaks in favour of the foreign investor will be presented, followed by a selection of cases emphasising the interests of the host state. As a last point, cases introducing the principle of proportionality will be addressed.

After the two clauses have been presented, the chapter turns to the concerns raised with regard these different interpretations, that is where the foreign investor is favoured (section 3.4.1), where the host state is favoured (section 3.4.2), and where the tribunals introduces elements of the principle of proportionality as an alternative (section 3.4.3).

3.2 Expropriation

3.2.1 The controversial distinction between indirect expropriation and regulation

The most fundamental protection granted to the foreign investor as a third party to an international investment agreement, is the protection against unlawful expropriation. Already in the 19th century, the so-called Hull-rule established that there were conditions that had to be met if the host state wanted to expropriate a foreign investor’s property.128 Today, four conditions

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128 Named after the US secretary of State Cordell Hull, who in different disputes with Mexico argued that a lawful expropriation required prompt, adequate and effective compensation, Alvarez, The Public International Law Regime Governing International Investment, 114.
are commonly seen as necessary requirements for an expropriation of a foreign investment to be deemed lawful; it must have (1) a public purpose, (2) be non-discriminatory and (3) undertaken under due process of law, and the foreign investor must be provided (4) prompt, effective and adequate compensation.

A typical example of an expropriation clause may be found in the bilateral investment agreement between Switzerland and Uruguay:

Neither of the Contracting Parties shall take, either directly or indirectly, measures of expropriation, nationalization or any other measure having the same nature or the same effect against investments belonging to investors of the other Contracting Party, unless the measures are taken for the public benefit as established by law, on a non-discriminatory basis, and under due process of law, and provided that provisions be made for effective and adequate compensation. The amount of compensation, interest included, shall be settled in the currency of the country of origin of the investment and paid without delay to the person entitled thereto.129

With regard to this typical expropriation clause, there are three categories of situations that might amount to an expropriation that inter alia has to be compensated; direct expropriation, indirect expropriation, and public regulations equated with indirect expropriation.

The first category is direct expropriation, meaning a situation where the host state has been involved in the investment being taken over by someone else than the foreign investor. This is the classical example of for instance a mining company being nationalised, or a parking slot being expropriated by the state, because the site shall be used for building a school. With regard to the example of a producer of hazardous chemicals from chapter 2, the foreign investor would be subject to direct expropriation if e.g. the factory was taken over by the government.

The second category is one for of indirect expropriation, often known as creeping expropriation. In these situations, the host state might take many different seemingly insignificant steps that in sum make up an expropriation. Maybe the title has not formally been transferred, or the host state has not gained any profit from its actions. Nevertheless, the investor has de facto lost the control over the investment. These situations are covered by the traditional expropriation clause, because without this protection from indirect expropriation, it would be possible

129 Article 5 (1) of the BIT between Uruguay and Switzerland. The Norwegian Draft 2015 Model BIT describes in article 6 (1) similar conditions when it reads that expropriation or nationalisation only are accepted if "(i) for a public purpose, (ii) under due process of law, (iii) in a nondiscriminatory manner, and (iv) against payment of prompt, adequate and effective compensation".
for the host state to circumvent its obligations by not explicitly state its intention. With regard to the chemical producer, an indirect expropriation would take place if the host state step by step took over the control of the production, although this was not done as a formal takeover.

The last category is the most controversial, namely the situation where a host state’s governmental policies cause economic loss for foreign investors. Exercise of political discretion will in many respects have an effect on a foreign investor; like administrative decisions to grant or withdraw permits and concessions, or legislative changes of laws and regulations. Many situations can be imagined under this category with regard to the foreign chemical producer. Maybe a required permit for producing the chemical is withdrawn, or that the chemical itself becomes illegal. Or it can be imagined that the government closes down the factory because it is found asbestos in the buildings.

In these situations it is highly controversial whether the foreign investor must be compensated for the effect of the measure. This can either be seen as a question of whether the measure amounts to indirect expropriation at all, or whether it is expropriation, but excepted from the requirement of inter alia compensation.\textsuperscript{130}

The following three sections will show that there are different approaches regarding this last category of indirect expropriation. One approach strictly emphasises the foreign investor’s interests (section 3.2.2), another approach grants the foreign investor wide political leeway (section 3.2.3), and the last approach tries to find a middle course by the use of the principle of proportionality (section 3.2.4).

3.2.2 Cases favouring the foreign investor’s interests

For a long time, the investment tribunals followed a strict interpretation of the Hull-rule where all kinds of expropriation for whatever purpose had to be followed by prompt, adequate and effective compensation.\textsuperscript{131} But in a developed world in need of functioning institutions and regulations, it gradually became apparent that its rigid form might cause problems for a modern state.\textsuperscript{132}

Despite this gradual shift from a strict emphasis on the Washington-consensus towards an emphasis of the role of institutions in development, there are prominent examples of a strict

\textsuperscript{130} It does not matter which of these approaches are taken, as to define a right is to limit it, see footnotes 125 and 116 above.

\textsuperscript{131} Pellet, ‘Police Power and the State’s Right to Regulate’, 448.

\textsuperscript{132} For a current investigation of the role of sustainable development in international investment law, see Hinderlang and Krajewski, \textit{Shifting Paradigms in International Investment Law}. 
investor friendly approach being taken at the beginning of millennium. Especially two cases from 2000 reveal an understanding of indirect expropriation where every measure that hinders the utilisation of the investment in accordance with the investors’ plans needs to be compensated.133

The first case that solely looked at how the measure affected the foreign investor was *Metalclad v. Mexico*. In this case, the local authorities denied the foreign investor a permit to a hazardous landfill, partly because it changed the regulation of the area to a national area for the protection of rare cactus.134 The tribunal stated that expropriation not only includes “open, deliberate and acknowledged takings of property, such as outright seizure or formal or obligatory transfer of title in favour of the host State, but also covert or incidental interference with the use of property which has the effect of depriving the owner, in whole or in significant part, of the use or reasonable-to-be expected economic benefit of property…”135 The motivation or intent for hindering the utilisation of the area was not deemed important by the tribunal, which deemed the measure tantamount to expropriation.136

Another case illustrating this investor bias is *Santa Elena v. Costa Rica*. This case also regarded a land area that was included into a national park and therefore could not be developed for business purposes.137 With regard to the amount of compensation that was to be granted, the tribunal stated that:

Expropriatory environmental measures – no matter how laudable an beneficiary to the society as a whole – are, in this respect, similar to any other expropriatory measures that a state may take in order to implement its policies: where property is expropriated, even

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133 Additional tribunals have followed a similar approach where the sole effect on the investor has been determined for the outcome, like *Biloune v. Ghana, Southern Pacific Properties v. Egypt*, and *Vivendi II v. Argentina*, see Kriebaum, ‘Regulatory Takings’, 724.

134 The other reason was that the investor had relied on a permit granted by the federal government, and it was deemed unlawful under NAFTA that the local government subsequently denied the investors the same permit.

135 *Metalclad v. Mexico* § 103.

136 *Metalclad v. Mexico* § 111, “tantamount” is the wording according to NAFTA article 1110, but this term is not used in newer international investment agreements.

137 The disputes origins in 1978, when Costa Rica issued an expropriation decree that made the area into a national park to protect sea turtles and thereby hindered the investors’ plans to make the area into a tourist resort and residential community. The assessment might therefore properly falls under the category of direct expropriation and not the category of ordinary regulation. But because the measure was a change in the zoning plan, the citation has wider application. See for instance the ECtHR case *Sporrong and Lönnroth v. Sweden*. 

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for environmental purposes, whether domestic or international, the state’s obligation to pay compensation remains.\textsuperscript{138}

These two cases show a strict favouring of the foreign investor explicitly excluding other concerns from the scope of international investment law. This direction of interpretation reveals an understanding of international investment law as an isolated system disconnected from the surrounding environment.

### 3.2.3 Cases favouring the host state’s interests

At the beginning of this millennium, also another direction emerged regarding the relation of indirect expropriation and regulation. Some tribunals openly acknowledged the host states’ right to undertake ordinary regulations, with the consequence that such measures did not constitute expropriation.\textsuperscript{139} This understanding of indirect expropriation is often understood as an embarking police power doctrine, which tries to reconcile the sovereign right to regulate in the public interests with the obligations towards the foreign investor.\textsuperscript{140}

One prominent example is the \textit{Methanex v. the US} case from 2005. The dispute regarded a Californian ban on a gasoline additive that affected the investor’s business, because Methanex produced an ingredient used in the additive. The tribunal stated that non-discriminatory public regulations are not to be considered expropriation even if they target foreign investors:

\begin{quote}
[A]s a matter of general international law, a non-discriminatory regulation for a public purpose, which is enacted in accordance with due process and, which affects, inter alios, a foreign investor or investment is not deemed expropriatory and compensable unless specific commitments have been given by the regulating government to the then putative foreign investor contemplating investment that the government would refrain from such regulations.\textsuperscript{141}
\end{quote}

Many tribunals, among them \textit{Saluka v. Czech Republic}, have cited the American Law Institute’s statement to emphasise the host states’ ordinary right to regulate:

\begin{flushright}
\textsuperscript{138} Santa Elena v. Costa Rica § 72.
\textsuperscript{139} This development did, however, start before this millennium. Already the 1961 Harvard Draft Convention on International Responsibility of States recognised situations in which non-compensable takings where allowed, like taxation, general change of value and currency, maintenance of public order, health and morality, valid exercise of belligerent rights and normal operations of laws. See Choukroune, \textit{Judging the State in International Trade and Investment Law}, 139.
\textsuperscript{141} Methanex v. the US, Part IV – chapter D, 4.
\end{flushright}
A state is not responsible for loss of property or other economic disadvantage resulting from bona fide general taxation, regulation, forfeiture of crime, or other action of the kind that is commonly accepted as within the police power of states, if it is not discriminatory. 142

These cases show an understanding regarding the tension between indirect expropriation and regulation contrary to the one presented in the previous section. In this direction, bona fide regulations are per se excluded from the definition of expropriation.

3.2.4 The principle of proportionality as a middle way

In the above two sections, it has been shown that the boundary between indirect expropriation and regulations may be viewed in diametrically opposite directions. In this conflict, the principle of proportionality has been introduced as a way to mediate between the two positions. 143

The most well-known case applying the principle of proportionality in an investment law dispute is Tecmed v. Mexico from 2003. The dispute concerned the Mexican authorities’ refusal to renew an operational permit for a hazardous landfill. The tribunal established that it first had to determine if the investor “was radically deprived of the economical use and enjoyment of its investments, as if the rights related thereto – such as the income or benefits related to the landfill or its exploitation – had ceased to exist”. 144 Since the landfill no longer could be used because of the authority’s decision, this condition was fulfilled. 145

The tribunal did, however, not halt its assessment by this conclusion, but deemed it appropriate to also consider the characteristic of the Mexican authorities’ actions. 146 It thus acknowledged that a state is entitled to exercise its sovereign powers within the framework of its police powers without compensating for it. 147

The tribunal emphasised, however, that regulatory administrative actions are not excluded per se from being expropriation, even when they are beneficiary to the society as a whole. 148 Instead, the tribunal stated that it would determine whether the state measures “are proportion-

142 Saluka v. Czech Republic § 260, citing the American Law Institute’s third restatement from 1987. This statement has also been used by Pope & Talbot v. Canada § 99, Feldman v. Mexico §§ 105-106.
143 Kriebaum, ‘Regulatory Takings’, 727.
144 Tecmed v. Mexico § 115.
145 Ibid. § 117.
146 Ibid. § 118.
147 Ibid. § 119.
148 Ibid. § 121.
ate to the public interest presumably protected thereby and to the protection legally granted to investments, taking into account that the significance of such impact has a key role upon deciding the proportionality”.

The tribunal elaborated its view on proportionality by stating that it would determine “whether such measures are reasonable with respect to their goals, the deprivation of economic rights and the legitimate expectations of who suffered such deprivation”. It further claimed that it had to be “a reasonable relationship of proportionality between the charge or weight imposed to the foreign investor and the aim sought to be realized by any expropriatory measure”. Emphasis should be given to the size of the ownership deprivation, if it was compensated or not, and it should be kept in mind that foreign investors often have little or nil participation in the decision-taking and are not entitled to exercise political rights reserved to nationals.

In Tecmed v. Mexico, the tribunal acknowledged both that denial of permit affected the foreign investor and that it was legitimate for the host state to use its administrative powers. These powers, however, did not per se exclude the existence of an expropriation, but were rather subject to review by the tribunal. The tribunal found that the denial of a permit was a result of local opposition lacking scientific evidence that also violated the expectations established by the government in the previous contact with the investor, and therefore constituted expropriations.

Henckels have criticised Tecmed v. Mexico for only performing the last criterion of the principle of proportionality, namely the actual balancing exercise. Other tribunals have similarly only invoked one of the two other elements of the principle of proportionality. The tribunal in S.D. Myers v. Canada did, for instance, focus on the need to investigate the measures reasonableness, and the tribunals in Feldman v. Mexico emphasised the importance of whether the measure was the least restrictive means.

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149 Ibid. § 122.
150 Ibid.
151 Ibid.
152 Ibid.
153 Henckels, ‘Indirect Expropriation and the Right to Regulate’, 232. It is, however, possible to understand the tribunal’s assessment as a focus on the suitability criterion, where it found that the measure would not strengthen the environment but rather was reasoned in public opposition.
154 Feldman v. Mexico §§ 103-105.
155 S.D. Myers v. Canada § 255.
3.3 Fair and equitable treatment

3.3.1 The controversial concept of legitimate expectations

Most international investment agreements require from a host state that it provides a foreign investor with fair and equitable treatment. A rather typical formulation of a fair and equitable treatment clause would be:

Each Contracting Party shall ensure fair and equitable treatment within its territory of the investments of the investors of the other Contracting Party.\(^{156}\)

Filling such a broad wording with content is not necessarily an easy task for investment tribunals and a wide range of different approaches can be traced. Kläger has systemised the case law on the fair and equitable treatment standard between substantive and procedural principles.\(^{157}\) Legitimate expectations and non-discrimination are substantive principles of the standard and fair procedure and transparency procedural principles.

The approach of reformulating the investigation as to what the foreign investor may legitimately expect from a host state is also emphasised by Somarajah.\(^{158}\) This question does, however, only circumvent the real problem, namely what this concept encompasses. In Dolzer’s examination of the standard it seems to encompass the concepts of consistency, transparency, reasonableness, non-discriminatory and good faith, as well as due process, and lack of harassment and coercion seem on the whole to be important elements.\(^{159}\)

Two opposite approaches can be taken with regard to what a foreign investor may legitimately expect from a host state. The first extreme only regards conduct that amounts “to outrage, to bad faith, to wilful neglect of duty, or to an insufficiency of governmental action so far short of international standards that every reasonable and impartial man would readily recognize its insufficiency” for breaching this standard.\(^{160}\) The other extreme opens up for a wide notion of the expectations that prioritise predictability for the foreign investor. Under this approach the foreign investor may legitimately expect that the investment environment, in which the investment was made, is not subject to any changes affecting the investment.

\(^{156}\) Article 3 (2) of the BIT between Uruguay and Switzerland. Another example is the BIT between Argentina and Australia stating that “each Contracting Party shall at all times ensure fair and equitable treatment to investments”.

\(^{157}\) Kläger, ‘Fair and Equitable Treatment’ in International Investment Law, 154.

\(^{158}\) Somarajah, The International Law on Foreign Investment, 354.

\(^{159}\) Dolzer, Principles of International Investment Law, 142–60.

Returning to the example of the foreign investor producing hazardous chemicals that are prohibited by the state, the situation can at its extremes either be seen as infringing the investors' legitimate expectations to continue to produce the chemicals in accordance with the legislation at the time the investment was undertaken, or that the investor must expect that the legislation with regard to environmental protection might change.\textsuperscript{161}

In the following, both awards showing an emphasis on the foreign investor protection (section 3.3.2) and awards where the legitimate expectations are considerably narrower (section 3.3.3) will be presented. The last section will look at cases where elements of the principle of proportionality are introduced in the tribunals' reasoning and to some extent thus mitigate between the two extremes (section 3.3.4).

3.3.2 Cases favouring the foreign investor's interests
When the concept of legitimate expectations was introduced in international investment law, it was given a rather wide scope also encompassing the legal framework in which the investment was made. This means that the legal framework as it existed when the investment was made, by many tribunals have been viewed as decisive for building a legitimate expectation.

In \textit{Tecmed v. Mexico}, the tribunal emphasised that the foreign investor should “know beforehand any and all rules and regulations that will govern its investments, as well as goals of the relevant policies and administrative practices or directives”.\textsuperscript{162} The foreign investors' need for stability and predictability was also stressed in the \textit{Occidental v. Ecuador I} case from 2004, with regard to the change of VAT reimbursement in the petroleum sector. According to the tribunal, “there is certainly an obligation not to alter the legal and business environment in which the investment has been made”.\textsuperscript{163}

This was repeated in \textit{National Grid v. Argentina} from 2008 where the tribunal stated that the treatment by a host state should “not affect the basic expectations that were taken into account by the foreign investor to make the investment”, and in that case the foreign investor had relied on the regulatory framework provided to attract foreign investors.\textsuperscript{164} Many of the other cases regarding Argentina’s economic crisis in 2001-2002 reveal a similar emphasis on the foreigner investor’s interests. The foreign investors were introduced into an investment cli-

\textsuperscript{161} An interesting question that has been relevant in the \textit{Vattenfall v. Germany II} case (not yet decided), is whether there is a difference between new knowledge leading to changes and the situation where the host state merely changes its attitude towards an already known risk.
\textsuperscript{162} \textit{Tecmed v. Mexico} § 154.
\textsuperscript{163} \textit{Occidental v. Ecuador I} § 191.
\textsuperscript{164} \textit{National Grid v. Argentina} §§173, 178.
mate when Argentina privatised a wide range of sectors in the 1990s. The tribunals found it legitimate for the investors to expect that none of these regulations would be subject to changes, and measures such as the devaluation of the Peso was therefore deemed unlawful even in a situation if a financial crisis.\textsuperscript{165}

These cases may be understood as freezing the legal and regulatory framework, thus preventing the host state from undertaking any regulatory changes. An excessive favouring of the foreign investor under the fair and equitable treatment standard might impose huge obligations on the host state, as there are no minimum thresholds and even minor interferences can constitute breaches.

3.3.3 Cases favouring the host state’s interests

The most host state friendly understanding of the fair and equitable treatment standard is to equalise it with the minimum standard as formulated in the Neer case from 1926.\textsuperscript{166} Today, however, most tribunals have found that the content of this standard has evolved concurrently with the development in the rest of the international community. Distinguishing between the minimum standard and an independent standard in international investment agreements is therefore considered only of theoretical exercise without any practical implications.\textsuperscript{167}

Nevertheless, there are tribunals that do not see the legitimate expectation to encompass the absence of changes to the business environment. Instead, the focus has been on the host state’s right to regulate.

From this starting position where the host state is free to both impose new regulations and change existing ones, a legitimate expectation for stability must be based on a specific assurance towards the particular investor. The tribunal in \textit{Total v Argentina} is one of the cases emphasising that in the absence of a stabilisation promise to the foreign investor, changes in the general legislation reflect a legitimate exercise of the government’s police power.\textsuperscript{168} This is also reflected in \textit{EDF v. Romania} from 2009 stating that “except where specific promises or representations are made by the State to the investor, the latter may not rely on a bilateral investment treaty as a kind of insurance policy against the risk of any changes in the host State’s

\textsuperscript{165} CMS v. \textit{Argentina} §§ 276–280.
\textsuperscript{166} As cited above in section 3.3.1.
\textsuperscript{167} \textit{Murphy v. Ecuador} §§ 206, 208, \textit{Mesa v. Canada} § 500. The US, Canada and Mexico have issued a joint declaration stating that the fair and equitable treatment standard under NAFTA article 1105 shall impose any additional obligations than the minimum standard under customary international law. Also with regard to NAFTA did, however, the tribunal in \textit{Mesa v. Canada} find that there were no differences between the two standards.
\textsuperscript{168} \textit{Total v. Argentina}, decision on liability § 164.
legal and economic framework. Such expectations would neither be legitimate nor reasonable.”

And similar in Waste Management v. Mexico stating that in applying the standard “it is relevant that the treatment is in breach of representation made by the host State which were reasonable relied on by the claimant”.170

This view reflects a notion of pacta sunt servanda, where the investor can rely on specific promises by governmental agents. Similarly, it does not mean that a stabilisation clause may be interpreted into the standard of fair and equitable treatment.

3.3.4 Different ways of using the principle of proportionality

Also with regard to the notion of legitimate expectations under the fair and equitable treatment standard, the idea of balancing has been introduced.

In the previously mentioned decision from 2006, Saluka v. Czech Republic, the tribunal specified that the determination of whether the Czech Republic had not treated the bank fairly and equitably under the financial sector debt crisis required “a weighing of the Claimant’s legitimate and reasonable expectations on the one hand and the Respondent’s legitimate regulatory interests on the other”.171

Under the fair and equitable treatment, the notion of balancing and proportionality has been applied in many different ways. In Glamis v. the US the tribunal gave the American authorities much deference when striking the balance between public and private interests affected by new environmental regulations in the mining sector. This was done after the tribunal had assessed whether a reasonable connection between the environmental harm and the proposed remedy existed, and emphasised that the government had investigated whether the measures were the least restrictive before they were introduced.172

Some cases, however, introduce the criterion of proportionality in the narrow sense as a sort of substantive principle that gives the foreign investor an additional protection. A prominent example is the second Occidental v. Ecuador case from 2012, which found that it was a general requirement in international investment law that the foreign investor is treated proportionate.173 The tribunal found that terminating the contract was not a proportionate response to

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169 EFD v Romania § 217.
170 Waste Management v. Mexico § 98.
171 Saluka v. Czech Republic § 306.
172 Glamis v. US § 803.
the claimant’s action, which had been not to notify Ecuador about a subcontractor,\textsuperscript{174} and awarded the largest amount of damages to date; US$1.76 billion plus interest. This substantive notion of proportionality may also be traced in expressions in \textit{LG&E v. Argentina} and \textit{El Paso v. Argentina}.\textsuperscript{175}

The notion of legitimate expectations seen through the lens of the principle of proportionality has the last decade both been a way to mediate between foreign investor protection and the host state’s interest, but also to amplify extreme positions.

\subsection*{3.4 Criticism of previous balances struck between foreign investor protection and the host state’s interests}

The above sections 3.2 and 3.3 have shown that at the beginning of this millennium, international investment arbitral tribunals were rather divided with regard to whether the interests of the foreign investor or the host state should be prioritised, or a middle course should be found.

This section will look at how the international community, and especially international investment scholars, have reacted to the different approaches taken by the arbitral tribunals. This presentation is given to fully enable the understanding of the environment of international investment law in the beginning of this millennium, from which the cases from 2016 are to be understood.

The section will not distinguish explicitly between expropriation and the fair and equitable treatment standard, but merge them into the same review. This is because the underlying conflict between foreign investor protection and the host states’ right to regulate and exercise their police powers is similar under the two clauses. As also noticed by Kläger, the justification for treating them together can also be that reasons invoked to determine whether the two clauses have been breached resemble each other – this is especially so with the notion of legitimate expectations.\textsuperscript{176}

\subsubsection*{3.4.1 Concerns with regard to excessive foreign investor protection}

It was the tribunals’ perceived bias towards the foreign investors’ interests on the expense of the host state that for real made the international community take an interest in international investment law. By imposing extensive obligations on the host state, reactions came from many different perspectives.

\textsuperscript{174} \textit{Occidental v. Ecuador} §§ 442–52, §455.


\textsuperscript{176} Kläger, ‘Fair and Equitable Treatment’ in \textit{International Investment Law}, 297.
Much of the academic criticism towards the emphasis on the foreign investor raises the concern that tribunals’ decisions might lead to violations of (or at least the risk of neglecting) other fundamental rights such as human rights, including labour rights and access to water, as well as environmental protection and development.\(^{177}\) 37 academics from all over the world therefore joined forces in 2011 and drafted the Osgood Hall Statement, where they essentially called for an end to the investment regime.\(^{178}\) The scholars especially raised concern about the damage done on public welfare by the investment regime, because it overly prioritised the protection of property and economic interests of transnational corporations over the right to regulate of the state and the right to self-determination of peoples.\(^{179}\) International investment law was thus seen as a threat to the important development that took place within the international community.\(^{180}\) As mentioned in the introduction chapter, many states reacted towards this perceived investor biased interpretation by withdrawing from the system.

As a means to overcome the perceived flaws in the system, the UN Conference on Trade and Development (UNCTAD) launched in 2012 an investment policy framework (updated in 2015). The policy framework addresses the concern that by only emphasising the protection of foreign investors, the traditional investment law paralyzes the host states from undertaking necessary (and rather ordinary) actions. The framework therefore highlights how proper negotiated international investment agreements instead can promote sustainable development.\(^{181}\)

Also among typical capital exporting countries, the concern that the investment system would infringe substantially their political leeway, has led to a development in international investment agreements.\(^{182}\) For instance, the US Model BIT from 2012 entails clauses specifically directed towards the contracting parties’ right to regulate to protect the environment and la-

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180 For instance was the United Nations Guiding Principles on Business and Human Rights (UNGP), also called the Ruggie-principles, adopted in 2011. The UNGP requires that the business community respect human rights.


182 Already in 2004, the US adopted a new Model BIT in which the content and ideology shifted from a single minded quest to protect US investors overseas to a more cautious attitude. This currently emulating wave has been described by Alvarez to emphasise “welfare economics”, where development thinking is “more open to local solutions, a greater diversity of institutions, and multiple plans involving Government to achieve a range of public goods”.

bour rights.\textsuperscript{183} It also entails an annex clarifying the distinction between indirect expropriation and ordinary regulatory measures:

Except in rare circumstances, non-discriminatory regulatory actions by a Party that are designed and applied to protect legitimate public welfare objectives, such as public health, safety, and the environment do not constitute direct expropriations.\textsuperscript{184}

The annex to the Model BIT also emphasises what should be taken into account when determining whether an indirect expropriation has occurred, namely (1) the economic impact of the measure, (2) the investor’s distinct, reasonable investment-backed expectation, and (3) the character of the governmental actions.\textsuperscript{185} Similar developments are also present in the free trade agreement between EU and Canada (CETA),\textsuperscript{186} and the 2015 draft to a Norwegian Model BIT.\textsuperscript{187}

That international investment law was developing in a direction isolating itself from all other rights and interests has been a very serious concern. The extensive criticism and steps taken to overcome the full separation from other rights and interests show that without turning the development away from this direction, the system would face even more challenges regarding its legitimacy. Since law to a certain degree depends on it being recognised, the whole existence of international investment law thus could have been threatened.

3.4.2 Concerns with regard to giving the host state’s interests priority
The other direction, where the host states interests are being favoured, has also been met with criticism. Placing too much emphasis on the host state’s interests has been criticised by international investment law scholars, as it might undermine the investor protection that the system was supposed to secure. The concern is mainly that the balance explicitly struck in international investment agreements are stirred up when the host state is granted a too wide leeway, and that this to a certain extent violates the notion of \textit{pacta sunt servanda}.\textsuperscript{188}

Ranjan has argued that a public purpose, according to the most international investments, is a criterion for determining whether indirect expropriation is lawful and not its existence per

\textsuperscript{183} The 2012 US Model BIT article 12 and 13.
\textsuperscript{184} The 2012 US Model BIT annex B article 4 (b).
\textsuperscript{185} The 2012 US Model BIT annex B article 4 (a).
\textsuperscript{186} CETA annex 11 to the investment chapter, article 2 and 3.
\textsuperscript{187} Draft 2015 Norwegian Model BIT article 6.
\textsuperscript{188} In the meaning that the host states cannot opt out of its obligations towards protecting foreign investments.
Ignoring this leads to a paradoxical situation where what according to the wording of the expropriation clause constitutes indirect expropriation, suddenly is not expropriation at all.

A similar concern is stated by Kriebaum when she points out that when allowing the host state a wide police power, the foreign investor will have to bear the economic burden of nearly every realisations of a public interest through regulatory measures. Although indirect expropriation is part of most expropriation clauses, they “will largely be deprived of their function to protect foreign investors against regulatory measures by States”.190

Büchler has also warned against including other interests without having explicit textual support, because it “raises serious concerns regarding the rule of law, the threat of judicial law-making, and the uncertainty on what rights and interest enter the analysis”.191

The main concern regarding extensive leeway for the host state seems to be that the pendulum swings too much to the other direction and thus undermines the entire system of investor protection, as the investor needs predictability. A concern is also that it is not for the arbitral tribunals to amend the system on their own initiative; if the system as such is flawed, the states should step up and take responsibility instead of allowing investment tribunals to expand their powers.

3.4.3 Concerns regarding the use of the principle of proportionality

International tribunals have attempted to consolidate the two extreme positions through the principle of proportionality. The references to proportionality or balancing seem to mean three different things. First, it might be a reference to all the three criteria of the principle of proportionality. Second, it might be a label on a conclusion where the interests of both the foreign investor and the host state are mitigated based on the facts of the concrete case. Third, it seems to be used as substantive principle providing arguments for foreign investor protection.

In the following, the different concerns raised towards the principle of proportionality will be addressed separately to facilitate better understanding of what the criticism targets.

3.4.3.1 Flawed application

Many international investment scholars are concerned that the investment tribunals seem to apply the principle of proportionality in a rather flawed manner. Leonhardsen, for instance,

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189 Ranjan, ‘Using the Public Law Concept of Proportionality to Balance Investment Protection with Regulation in International Investment Law’, 869.
190 Kriebaum, ‘Regulatory Takings’, 727.
concludes in his analysis that the current use of the principle “sometimes seemed less solid than over-eager”.192

Henckels has also emphasised the flawed methodology by the international investment arbitral tribunals. When analysing the award Tecmed v. Mexico, she found that the tribunal skipped the first two parts of the structure, namely the assessment of suitability and necessity, and went straight to assess whether the measure where strict proportionate or not.193 This is according Henckels problematic because “it lends itself to concerns of subjectivity, failure to assess relevant considerations, and lack of appreciation for the context of the decision taken”.194

These concerns might reflect the notion that arbitrators traditionally have not been recruited from public international law or national administrative and constitutional law, which are more familiar with the principle of proportionality, but from commercial law. International investment law thus have needed to go through some children’s diseases to be comfortable with the technique.

3.4.3.2 Investment tribunals unsuitable to apply the principle of proportionality
Another type of criticism is directed against the idea of incorporating the principle of proportionality to international investment law. Where some scholars see it as strength that proportionality is open towards different political theories and substantive preferences,195 Ranjan finds investment tribunals not suited “to adopt a method of review that would require them to weight and balance complex value-laden regulatory objectives”.196

The level of review adopted by the tribunals is closely acquainted to this concern, which means how thorough they review the host states’ judgments. Henckels have pointed out that it is desirable that tribunals adopts a sensitive approach to the standard of review “that takes into account the desirability of regulatory autonomy, decision-making by proximate decision-makers and issues of relative institutional competence and expertise”.197

194 Ibid.
196 Ranjan, ‘Using the Public Law Concept of Proportionality to Balance Investment Protection with Regulation in International Investment Law’, 862.
It might cause problems to emphasise the circumstances of the particular case when assessing whether a measure violates the obligations established in international investment agreements. Such an approach might raise the impression that laws are not predictable. With regard to international investment law, this concern might, however, originate in divergent interpretations by investment tribunals. Up till 2012, a consistent legal doctrine seemed to be lacking in international investment law.

3.4.3.3 The introduction of new arguments by systemic integration

Concerns have been raised towards some investment arbitral tribunals applying the principle of proportionality by reference to the technique used by other international courts and tribunals, like the ECtHR and WTO bodies, when interpreting similar clauses. The source of applying the principle of proportionality in these cases is thus through systemic integration under the Vienna Convention article 31 (3) (c).198

Bücheler has pointed out that tribunals should be cautious by applying the technique of another international system synonymous in international investment law, because of the different wording of the underlying international treaties.199 Alvarez, on the other hand, sees a high risk of borrowing the system that the tribunals look to wrong.200

If the principle of proportionality is seen as a semantic structure, this concern is not well targeted, because the tribunals only import an empty technique that then has to be filled with arguments from international investment law doctrine. This can be illustrated by the statement from the annulment committee in Continental Casualty v. Argentina, that the original tribunal had only looked to how the criterion of necessity was to be understood: “The tribunal was clearly not purporting to apply that body of law, but merely took it into account as relevant to determining the correct interpretation and application of Article XI of the BIT.”201

The concern raised by Bücheler and Alvarez may, however, also be understood in a another way, namely with regard to cases where it seems that the principle of proportionality as such is a door opener for new arguments and reasons that originally was not part of international investment law. Bücheler seems to have this in mind when he criticises the tribunal in Tecmed v. Mexico for introducing a right to regulate similar as that found under the ECHR property


200 The statement is particularly targeted at the tribunal in the Continental Casualty v. Argentina case, where Alvarez was of the opinion that the tribunal did not take account of the full WTO legal system in its assessment of necessity, Alvarez, ‘Beware’, 30.

201 Continental Casualty v. Argentina, Annulment proceeding, § 133.
protection. This also seems to be the reason for Alvarez to criticise that not the entirety of WTO law being taken into account when applied by the tribunals in *Continental Casualty v. Argentina*.

The concerns may then be understood more formally, namely whether investment tribunals are authorised to look to how other international courts interpret similar clauses. The question is thus whether the similar clause is “applicable between the parties” as required by Vienna Convention article 31 (3) (c). The established position seems to be that not all the parties to a free trade agreement also must be parties to the treaty that shall be integrated. In addition, Simma and Kill have argued that it might not even be necessary that both the parties to the dispute also must be party to the other treaty, as long as the respondent host state is. This understanding seems to have support in the practice from investment tribunals. Gazzini has emphasized that in *Glamis v. US*, for instance, both the tribunal and the respondent noticed the participation of the United States to the UNESCO World Heritage Convention, but not that of the non-disputing party. The similar can be noticed in *Al Warraq v. Indonesia*, where Indonesia’s participation in the ICCPR was emphasized, but not that of Saudi Arabia. An additional argument to this position is that the dispute is not between two states, but between a private investor and a host state – the home state’s international obligations is therefore less relevant. The problem in *Tecmed v. Mexico*, however, is that Mexico in any case is not a member of the ECHR.

### 3.4.3.4 The principle of proportionality as a substantive principle

Another concern regarding the introduction of the principle of proportionality in international investment law is that it is misunderstood by the tribunals and so applied in unconventional situations. Sabahi and Duggal, for instance, emphasise that proportionality is normally used in a situation where the individual is subject to the exercise of state power. Applying it in a contractual situation, as the tribunal in *Occidental v. Ecuador*, is problematic as the contractual right is established through a negotiated bargain.

The introduction of proportionality as a general requirement under international investment agreements is then to fill it with a substantive content that protects the investor from disadvantageous economic agreements.

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204 Gazzini, *Interpretation of International Investment Treaties*, 220.

3.4.3.5 An interim response: the importance of distinguishing between the principle of proportionality and the underlying doctrine

Much of the criticism presented in the above sections targets how investment tribunals have changed the content of the doctrine of international investment law through their application of the principle of proportionality. The principle of proportionality is then seemed as a substantive test of injustice, which they can fill with nearly whatever content they find best.

This thesis takes the view that the principle of proportionality does not provide any arguments on its own, as explained in chapter 2. In the following, it will therefore be distinguished between the semantic structure of the principle of proportionality and how the doctrine of international investment law relates colliding rights and interests.

3.5 Premises for analysing the awards of 2016

This chapter has established the second premise for this thesis, namely that international investment law in the beginning of this millennium seemed to be at a turning point. By 2012 it still seemed open whether the system would continue to merely have the protection of the foreign investor in focus, or was taking a definite turn towards a more host state friendly approach. This chapter has also shown that the confusion regarding the content of investment law to some extent is linked to the investment tribunals’ application of the principle of proportionality.

The following analysis of the awards from 2016 will explore the current stand of international investment law regarding the much disputed content of the expropriation clause and the fair and equitable treatment standard. Analysing the cases through the criteria of the principle of proportionality makes it possible to reveal how this technique either has matured on the investment tribunals or still gives rise for concerns. Both of these questions will be evaluated in chapter 5.
4 Applying the principle of proportionality on the investment cases of 2016

4.1 Introduction

This chapter will analyse the international investment law cases of 2016 through the lens of the principle of proportionality as it was presented in chapter 2.

The chapter has two aims. First, it will test whether the different elements of the principle of proportionality can be found in the reasoning of the international investment law tribunals of 2016. Second, by letting the three criteria of the principle of proportionality guide the investigation, the chapter will seek to unveil the content of the international investment law doctrine as of 2016.

The chapter will start by presenting the cases of 2016 (section 4.2). Then the structure of the chapter will follow the previous presentation of the principle of proportionality (section 4.3); namely the criteria of suitability (section 4.4), necessity (section 4.5) and proportionality in the narrow sense (section 4.6). In the last section, some observations will be made with regard to the interplay between the three criteria of the principle of proportionality, as well as the interplay between assessing whether an expropriation has taken place and the fair and equitable treatment standard has been breached (section 4.7).

4.2 The cases of 2016 in a nutshell

4.2.1 The selection of cases

The following analysis is based on 19 awards from 2016.206 By focusing on awards where the actual material dispute is decided, the analysis excludes procedural decisions such as decisions on jurisdictions and annulment proceedings.

The 19 awards have been found through searches on the database of italaw.com,207 the UN Conference on Trade and Development’s (UNCTAD) policy hub,208 as well as the databases of the most invoked institutions for investor-state dispute settlement, the Centre for Settlement of Investment Disputes (ICSID) and the Permanent Court of Arbitration (PCA).209

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207 ‘Search Results | Italaw’.

208 ‘Year | Investment Dispute Settlement Navigator’.

209 ‘Advanced Search | ICSID’ and ‘Case Results | PCA’.
The search gave 51 results, but not all of these cases were relevant for the analysis undertaken. The first reason for this is that 21 of the cases were not accessible for the analysis, due to language or confidentiality; six awards were only available in French or Spanish, and additional 15 were not public.

The second reason is that 11 of the cases did not engage with the material content of the dispute, although they were labelled awards. The tribunals in three cases concluded that they did not have jurisdiction of the dispute. In two cases, the tribunals found an abuse of process by the claimants. Additional two cases were only the formal ending of cases after the disputes had been finally settled out of arbitration. The tribunals in three cases only revised the amount of previously awarded damages, and the last case only established the costs of the dispute after the claims were dismissed in an earlier award.

There were then 19 cases in which the investment arbitral tribunals actually engaged in a material assessment of the claims. Of the 19 cases, six of the cases where decided by a tribunal under the Permanent Court of Arbitration (PCA) and 13 under the International Centre for Settlement of Investment Disputes (ICSID). The two cases against Canada, Windstream v. Canada and Mesa v. Canada, were disputes under the NAFTA agreement. Corona v. Dominican Republic and Pac Rim v. El Salvador concerned disputed under CAFTA-DR. The remaining 15 cases were all about different bilateral investment agreements. None of them were about the sectorial Energy Charter Treaty (ECT).

4.2.2 The facts of the cases
All of the 19 cases of 2016 assessed whether an unlawful expropriation had taken place and/or if the requirement for fair and equitable treatment had been breached. In addition to these...
clauses, some tribunals also addressed other issues like the most favourable treatment clauses, full protection and security clauses and umbrella clauses. These clauses were, however, mostly raised by the claimant as additional claims and they were often treated superficially by the tribunals.

This section will provide an overview of the factual circumstances of the cases of 2016. It will be structured according to the situation and not according to the underlying provision in the investment agreements; namely expropriation and fair and equitable treatment. There are three reasons for this. First, the tribunals sometimes assessed the same facts under both of the provisions. Second, different tribunals sometimes focus their assessment of rather similar situations under different provisions. Third, the controversial collision of investor protection and other rights and interests also important to the host state is equally relevant under both provisions.

4.2.2.1 Nationalisation
Of the 19 cases of 2016, five were about Venezuela’s nationalisation of different industries under president Hugo Chavez.

The two cases Crystallex (Canada) v. Venezuela and Rusoro (Canada) v. Venezuela were about the gold sector. Two cases concerned nationalisation of the production of components used in the oil and gas industry. The foreign investor in Tenaris (Luxemburg and Portugal) v. Venezuela produced stainless steel pipes and operated iron plants in Venezuela, and the investor in Saint-Gobain (France) v. Venezuela operated a plant that designed and produced ceramic proppants from bauxite used as part of hydraulic fracturing. The last case, Vestey (the UK) v. Venezuela, was about the land reform aiming at eliminating idle land.

In the first part of the tribunals’ assessments, they established whether an expropriation had taken place. In Rusoro and Tenaris the measures were a formal expropriation of the investments and the result was therefore rather clear. In Vestey the tribunal first had to establish that the investor had the ownership to the land taken. Since the investor owned the cattle farms that were declared state property, the tribunal found this to be a blunt nationalisation of the farms. In Crystallex the question was whether the accumulation of measures was a creeping expropriation, and in Saint-Gobain the question was whether the de facto control of the plants by the government amounted to expropriation. After an assessment of the

221 Crystallex v. Venezuela § 674.
222 Saint-Gobain v. Venezuela § 474.
facts, the tribunals concluded that the measures in reality were nationalisation of the mining plants. As described in chapter 3, these two cases exemplify the classical situation of indirect expropriation.

Since all the tribunals found that Venezuela had expropriated the foreign investors’ investments, the decisive question was whether the expropriations were lawful; meaning whether the measures had a public purpose, were non-discriminatory, undertaken under a due process, and were compensated. None of the investors had been granted compensation by Venezuela and the tribunals therefore found a breach of all the relevant BITs. The Rusoro case stands out, because the investor was in fact offered compensation, but the offer was deemed insufficient by the tribunal. The tribunals in the Tenaris and Vestey cases, in addition to lack of compensation, found that the due process guarantees were breached.

4.2.2.2 Denial of permit
Three of the cases were about mining permits not being granted. In the already mentioned case Crystallex v. Venezuela, one of the measures constituting creeping expropriation was Venezuela’s denial of a mining permit reasoned in global warming and environmental issues.

In Copper Mesa (Canada) v. Ecuador the Ecuadorian government halted the process of a mining permit because the claimant had not carried out a proper consultation with all affected parties. This lack of consultation was due to many years of conflict in the area between anti- and pro-miners. The tribunal found the challenged measures not to constitute ordinary regulatory measures, but arbitrary conduct by the host state. The tribunal especially emphasised two problems connected to the host state’s conduct, leading to a violation of the BIT. First, that Ecuador should have undertaken measures that would enable the investor to fulfil the required consultation, and second, the government should not have sided with the anti-miners by making it illegal for the claimant to undertake the required consultations.

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223 Between Venezuela and Canada, Luxemburg, Portugal, France, and the UK.
224 Rusoro v. Venezuela § 408.
226 Crystallex v. Venezuela §§ 590, 674.
227 This was relevant for the tribunal’s conclusion both regarding expropriation and the fair and equitable treatment standard.
228 Copper Mesa v. Ecuador § 6.84.
Also *Pac Rim Cayman (the US) v. El Salvador* concerned the denial of a mining permission due to a failure to undertake the necessary consultations required by El Salvadorian law.\(^{229}\)

The main question for the tribunal was how national law was to be understood, meaning the scope of who had to be consulted. The award therefore stands out, as it mainly focused on national law and how international tribunals should relate to this.\(^{230}\)

### 4.2.2.3 Termination of contracts

Five of the cases from 2016 were about a termination of contracts by the host state and whether this violated the investor’s right under an international investment agreement.

Most of the cases assessed the termination from the angle of expropriation. In *Garanti Koza (the UK) v. Turkmenistan* the contract was about the building of 28 bridges, and *Ickale Insaat (Turkey) v. Turkmenistan* concerned real estate development and infrastructure projects. In *Almås (Norway) v. Poland*, the dispute was about a lease agreement for a farm.

Two cases started the assessment from the angle of the fair and equitable treatment standard, which then later also was relevant for the expropriation assessment. In *Flemingo (India) v. Poland*, the challenged termination regarded a lease agreement for retail stores at an airport that was terminated in relation to modernisation plans at the airport. The challenged termination in *Urbaser (the US) v. Argentina* concerned a water and sewage service concession terminated in 2006, in the aftermath of Argentina’s economic crisis in 2001-2002.

The tribunals in *Almås*, *Garanti Koza*, *Ickale Insaat* and *Urbaser* found that the host states had terminated the contracts as a direct result of contractual breaches by the investors.\(^{231}\) The measures were therefore valid exercises of contractual rights that did not violate international investment agreements.

*Flemingo v. Poland* was the only case where the tribunal found a breach of the host state’s international obligations when the contract was terminated. Although there was a condition under the lease agreement to adjust the amount of the bank guarantees to the increased rent and submit a certified copy of the relevant insurance policies in due time, the tribunal found that the current breach could not justify a termination with immediate effect. The documents

\(^{229}\) *Pac Rim Cayman v. El Salvador* § 8.29.

\(^{230}\) The tribunal dismissed the investor’s claims for three reasons (given different weight by the three arbitrators). First, the tribunal found that the investor had previous relied on the government’s interpretation, second, it granted the national authorities deference to interpret their own legislation and lastly, it also supported a teleological interpretation by the host state in the investor’s disfavour.

\(^{231}\) *Almås v. Poland* § 251, *Garanti Koza v. Turkmenistan* § 366, *Ickale Insaat v. Turkmenistan* § 355 (the termination was at least not politically motivated), and *Urbaser v. Argentina* §§ 947, 1008.
had been submitted one day after the deadline and the termination took place the same day although the guarantee would replace the old guarantee two weeks later.\textsuperscript{232} Because all the lease agreements at the airport were to be terminated in accordance with a governmental decree issued for the purpose of upgrading the airport, the tribunal found that the conduct towards Flemingo’s was an abuse of the contract to circumvent the requirement in the decree to compensate the lessees.\textsuperscript{233}

4.2.2.4 Regulatory changes

Four of the cases of 2016 were about regulations affecting the foreign investor. These cases directly touched upon the collision of interests between foreign investor protection and the host states’ right to regulate.

In \textit{Philp Morris (Switzerland) v. Uruguay} the host state introduced restrictive regulations on the marketing of tobacco packages for the purpose of promoting public health. The first regulation was a requirement that 80\% of the cigarette packages should be covered by warnings of the danger of tobacco. The second regulation was that each tobacco brand only was allowed to have one cigarette variant (single presentation) to avoid the widespread misunderstanding that some cigarette variants are healthier than others (like “light”, “gold” etc.). The tribunal found that these regulations were ordinary regulations being neither expropriation nor breaching the fair and equitable treatment standard.\textsuperscript{234}

In \textit{Murphy (the US) v. Ecuador}, the increased oil price made the Ecuadorian government amend its laws to participate in the extraordinary income. The decisive question for the tribunal was whether this fundamentally changed the conditions for the oil and gas sector, by changing the contracts from service contracts to participation contracts. The tribunal found that Ecuador could impose a burden on the companies to share 50 \% of its increased income with the state, as the first regulation required.\textsuperscript{235} The requirement to share 99 \% of the income was, however, a violation of the fundamental risk distribution in the oil and gas sector that changed the framework to service contracts.\textsuperscript{236}

Moreover, one of the questions in the previous mentioned case \textit{Rusoro v. Venezuela} was whether the government could regulate the illegal (up until now unregulated) swap marked and demand that a percentage of the gold was sold to the state, or if these measures breached

\textsuperscript{232} \textit{Flemingo v. Poland} § 553.
\textsuperscript{233} Ibid. § 554.
\textsuperscript{234} \textit{Philip Morris v. Uruguay} § 305.
\textsuperscript{235} \textit{Murphy v. Ecuador} § 280.
\textsuperscript{236} Ibid. § 282.
the fair and equitable treatment standard. Lastly, one aspect of the Urbaser v. Argentina case was that the economic crisis of 2001-2002 led Argentina to order the investor not to charge low-income users for water and sewage systems, simultaneously as the 1:1 conversion between the Peso and USD financially injured the investor. Both the regulations undertaken by Venezuela and Argentina respectively were considered acceptable regulations by the investment tribunals.\(^{237}\)

4.2.2.5 Policy changes
In especially three of the cases from 2016, the dispute concerned political decisions taken by the host state.

Two cases were about the building of renewable energy sources in the province of Ontario in Canada. In Mesa (the US) v. Canada, the tribunal assessed whether the Canadian policy to not go further with a renewable project because it prioritised another and more comprehensive program was a result of unfair and arbitrary conduct by the government. The tribunal found that the decisions were taken on the basis of reasonable and rational considerations and thus were not arbitrary.\(^{238}\) In Windstream (the US) v. Canada, on the other hand, the tribunal found that the political decision to halt an offshore wind project was not mainly based on the need for better scientific support of the project, but rather the effects upon electricity costs and the public opposition that might influence the upcoming election.\(^{239}\)

In MNSS (Netherlands) v. Montenegro the tribunal focused on whether the government followed a reasonable policy when it did not save a privatised steel mill from bankruptcy after the European bank crisis in 2008.\(^{240}\) Montenegro also granted the union at the steel mill a loan when the workers were striking towards the investor’s personnel policy. This governmental conduct was unsuccessfully challenged by the investor.\(^{241}\)

4.2.2.6 Miscellaneous
Two of the cases from 2016 do not fit into any of the above categories. The first is Corona (the US) v. Dominican Republic where the investor claimed it was denied justice under the fair and equitable treatment standard. The tribunal found that it is only in situations where the host state’s legal system as a whole has failed to accord justice to the investor that the interna-

\(^{237}\) Rusoro v. Venezuela § 533 and Urbaser v. Argentina § 682.
\(^{238}\) Mesa v. Canada § 630.
\(^{239}\) Windstream v. Canada § 377.
\(^{240}\) MNSS v. Montenegro § 340.
\(^{241}\) Ibid. § 345.
tional standard is breached.\textsuperscript{242} When the investor had not initiated any court proceedings, the clause was far from being violated.\textsuperscript{243}

The second case, \textit{Allard (Canada) v. Barbados}, was about an attraction park in Barbados, where the investor challenged the host state’s omissions with regarding to environmental protection affecting the park. The tribunal found that it could not be established that Allard had any legitimate expectations towards the conduct of Barbados, because he had not relied on any specific representation by governmental authorities. Instead the tribunal found that the investor was driven by enthusiasm and did not even wait for the authority’s approval of the attraction plans.\textsuperscript{244}

\textbf{4.3 Using the principle of proportionality to analyse the cases of 2016}

The following three sections will look at how the three criteria of the principle of proportionality are used in the international investment awards of 2016. As was shown in chapter 2, the principle of proportionality is a fundamental technique for legal reasoning that is used to various degrees in case law of different legal systems. It is a semantic structure that describes the reasoning courts and tribunals undertake when different arguments stand against each other and drag the decision in different directions.

Some scholars seem to argue that the principle of proportionality needs a legal source to justify its use in international investment law. This has raised a debate among scholars on whether the principle of proportionality is so commonly used by courts and tribunals of today that it must be recognised as a general principle of law.\textsuperscript{245} Others have pointed to the problems that might arise when the principle of proportionality is applied through systemic integration from for instance the legal doctrine of European Court of Human Rights.\textsuperscript{246} Such systemic integration is considered problematic due to the fact that the two systems might have different aims. In addition it might violate the host state’s sovereignty since the respondent state might not have recognised the legal system that is to be integrated into the international investment agreement.\textsuperscript{247}

The presentation of the principle of proportionality in chapter 2 has, however, shown that the principle of proportionality is a rhetorical technique that is not in need of justification. It is

\begin{itemize}
\item \textsuperscript{242} \textit{Corona v. Dominican Republic} § 254.
\item \textsuperscript{243} Ibid. § 264.
\item \textsuperscript{244} \textit{Allard v. Barbados} § 226.
\item \textsuperscript{245} See for instance Stone Sweet, ‘Investor-State Arbitration’, and section 2.2.
\item \textsuperscript{246} Leonhardsen, ‘Looking for Legitimacy’, 21.
\item \textsuperscript{247} Xiuli, ‘The Application of the Principle of Proportionality in Tecmed v. Mexico’, 635.
\end{itemize}
rather a description of the reasoning that takes place. The following three sections will investi-
gate and structure how this description fits the reasoning in current international investment
awards. Do the tribunals acknowledge that different reasons collide in investment disputes, or
do they bluntly refuse other rights and interests than those of the investor? Do they investigate
whether this conflict is real? And lastly, do they reason for an ordering among the different
arguments to decide the dispute?

The analysis will show that the element of suitability frequently can be recognised in the rea-
soning of international investment tribunals. The criterion of necessity, on the other hand, is
much less frequent, which might be due to the degree of review of the governmental measure
not being so intense.\textsuperscript{248} The criterion of proportionality is sometimes explicitly stated in the
awards of 2016, but the analysis will strive to disclose the reasoning behind – namely how the
doctrine of international investment law orders the different rights and interests at stake in an
investor-state dispute.

The following three sections will be structured according to the criteria of the principle of
proportionality and not primarily with regard to the assessments of expropriation or the fair
and equitable treatment standard. This is because the main focus of this thesis is how interna-
tional arbitral tribunals relate different rights and interests within international investment
law. As will be shown in section 4.7, the assessments under the two clauses seem, however, to
merge.

\section{4.4 The criterion of suitability}
The criterion of suitability is the first criterion of the principle of proportionality. It is an as-
scription of whether a challenged governmental measure has contributed to the fulfilment of a
legitimate objective. As was established in section 2.3, this is in reality two different assess-
ment, namely whether the pursued objective is legitimate (section 4.4.1) and then an assess-
ment of whether the measure is suitable to fulfil this objective (section 4.4.2).

\subsection{4.4.1 Legitimate objectives in the cases of 2016}
With regard to international investment law, the question of whether the host state pursues a
legitimate objective is relevant in two different ways. The first is with regard to direct expro-
priation and situations in which the measure must be seen as being a de facto expropriation
(indirect expropriation),\textsuperscript{249} as these expropriations must be undertaken for a public purpose to
be lawful. The second situation is where the investment is infringed by regulations and politi-

\textsuperscript{248} This thesis demarcates from especially investigating the level of deference in international investment law
and thus also the entire debate on the so-called margin of appreciation, see section 1.3.

\textsuperscript{249} The two first categories of expropriation presented in section 3.2.1.
cal discretion, and the question arises whether such conduct might be expropriation or a breach of the fair and equitable treatment standard.

With regard to the first situation, the cases of 2016 have acknowledged a wide range of objectives to be legitimate public purposes. An illustrative example is *Rusoro v. Venezuela*, where it was for the host state to decide the aim of the economic policy and thus to turn the mining sector from a capitalist model to socialism. In *Vestey v. Venezuela*, it was also considered legitimate to remove idle land and redistribute it to secure access to food and food self-sufficiency.

With regard to the second situation, it is evident that the investment tribunals in the cases of 2016 acknowledge the emerging police power doctrine, also understood as the host states’ right to regulate without breaching international investment agreements. All of the investment arbitral tribunal awards analysed, acknowledged that the host state may regulate for the public good – thereby opening up for right and interests other than that of the foreign investor to be taken into account in international investment law.

The legitimacy of the particular public rights and interests pursued was as a main rule not thoroughly questioned by the tribunals. Instead, the tribunal found it to be for the host state to decide which policy they wanted to pursue. In the *Crystallex* case, the tribunal found it to be a legitimate objective to protect the environment and climate, and the tribunal in *MNSS* found it legitimate that the government aimed at securing jobs and enabling lawful strikes. The objective of securing access to water for the population was considered legitimate in *Urbaser v. Venezuela*, as well as the protection of public health by controlling tobacco marketing was considered legitimate regulations.

Not all of the cases concerned interests with a direct link to international acknowledged fundamental rights, like public health, labour rights and access to water. But also in cases where the host state used its power to undertake more ordinary regulatory measures, the tribunals accepted that this would be legitimate under international investment law. This was for instance the case when the host state undertook regulations in the gold sector as part of the fis-

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251 *Vestey v. Venezuela* § 295.
252 E.g. *Copper Mesa v. Ecuador* § 6.60 and *Rusoro v. Venezuela* §§ 525, 531, 536.
253 *Crystallex v. Venezuela* § 591.
255 *Urbaser v. Argentina* § 720.
256 *Philip Morris v. Uruguay* § 305.
cal politics, or changed the regulations on how the revenue from the oil and gas sector should be distributed between the companies and the state.

Many of the awards of 2016 were about terminations of contracts, where an important premise seems to be that a host state legitimately can pursue its contractual rights.

Also with regard to political decisions, like deciding which renewable project should be undertaken or concerns regarding uncertainty regarding the consequences of the measure, the tribunals found this to be legitimate. Host states were also granted the power to legitimately grant or deny permits and concessions, in opposition to a view where companies have rights to permits. In these cases it became, however, evident that there are some limits to what the host state legitimately can pursue under its ordinary police powers. Neither nationalisation nor adherence to political opportunism were considered legitimate in the cases of 2016, and this will be further elaborated in the following section.

This section has shown that other rights and interests than only that of the foreign investor were in fact taken into account by investment tribunals in the cases of 2016. Most of the tribunals did not explicitly refer to a legal source for introducing other rights and interest in international investment law. Instead, the right to regulate was considered a natural part of international investment law, becoming apparent in case law. With international investment agreements being vaguely formulated standards, it might not be surprising that tribunals recognized the immanent tension of investor protection and other fundamental interests like human rights, environmental protection and national sovereignty, which are all part of international public law.

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257 Rusoro v. Venezuela § 537.
258 Murphy v. Ecuador § 276.
261 Nationalisation was not considered legitimate in Crystallex v. Venezuela § 609 and Fleming v. Poland § 554, and political opportunism was not considered legitimate in Winstream v. Canada § 377 and Copper Mesa v. Ecuador § 6.84.
262 This resembles how scholars generally have described how a police power doctrine has evolved, see Titi, The Right to Regulate in International Investment Law, 288. Pellet, ‘Police Power and the State’s Right to Regulate’, 448.
263 See for instance how Barak argues for including other interests into the constitution by referring to conflicting fundamental rights, democracy itself and the idea of rule of law, Barak, ‘Proportionality’, 741.
Some tribunals, however, explicitly referred to a legal source other than previous case law when introducing other objectives into international investment law.\textsuperscript{264} \textit{Urbaser v. Argentina} referred to the choice of law provisions when it stated that investor protection cannot be considered in isolation, but rather was to be viewed as embodied in the host state’s entire legal framework which includes other international obligations, the national constitution and ordinary national laws.\textsuperscript{265}

The \textit{Philip Morris v. Uruguay} case explicitly referred to the Vienna Convention article 31 (3) (c) and stated that the clause should be interpreted in light of customary international law,\textsuperscript{266} where the host state’s right to regulate constituted customary international law.\textsuperscript{267} In the \textit{Philip Morris} case, the tribunal also paid attention to the development in recent investment treaties, such as the 2004 and 2012 US Model BIT, and stated that they reflected the position under general international law.\textsuperscript{268} It was also emphasised by the tribunal that Uruguay, by the undertaking of the measures, was aiming at implementing the WHO Framework Convention on Tobacco Control.\textsuperscript{269}

4.4.2 Assessing whether the measures are suitable to reach the legitimate objective

The cases of 2016 show that the tribunals do not halt their assessments when it is determined that the objective is legitimate, but move on to investigate whether the actual measure undertaken by the host state contributes to the fulfilment of this claimed objective.

In the cases of 2016, this assessment can be divided into two. One group of the tribunals assessed whether the objectives stated by the host state actually were the ones motivating their conduct, or if they were mere empty excuses covering other reasons (section 4.4.2.1). Another angle from which the tribunals looked at the criterion of suitability was to assess whether the challenged measure reasonably could contribute to the fulfilment of the objective (section 4.4.2.2).

\textsuperscript{264} \textit{Almås v. Poland} stands out, because the tribunal’s reasoning with regard to whether the Polish government had violated the BIT between Norway and Poland when terminating a lease agreement was focused on the ILC Articles on State Responsibility. Although the tribunal thus mainly engaged with the question of whether the challenged measure by an agricultural agency was an act of government, the tribunal also addressed the question of whether the termination was an exercise of lawful policy.

\textsuperscript{265} \textit{Urbaser v. Argentina} § 621.

\textsuperscript{266} \textit{Philip Morris v. Uruguay} § 290.

\textsuperscript{267} Ibid. § 295.

\textsuperscript{268} Ibid. § 301.

\textsuperscript{269} See section 3.4.3.3.
4.4.2.1 Other reasons than those stated determining the measure

This section will present the cases of 2016 where a central aspect of the assessment was whether the governmental undertakings in fact were determined by other reasons than those stated. If this were the case, the measure was not pursuing a legitimate aim, but rather covered up other illegitimate objectives.

This assessment was particularly outspoken in two of the cases on termination of contracts. In Almås v. Poland the tribunal asked if the government followed a “hidden agenda” when terminating the contract.\(^{270}\) In Garanti Koza v. Turkmenistan the decisive factor was whether “the reasons given for the termination constituted a legally valid ground for termination according to the provisions of the contract”.\(^{271}\) In neither of these two cases did the tribunal find this to be the case.

There were especially two situations where the tribunals of 2016 found that host states did not pursue the legitimate objective stated to justify the measures. This was, first, when the underlying goal actually was to nationalise the investment and second, when changes in the public opinion led the government to alter its conduct towards the foreign investor.

With regard to nationalisation, Urbaser v. Argentina is an example. In this case, the tribunal found that the renegotiations failed, not because the investor requested a tariff increase or lower quality requirements, as claimed by Argentina, but because of a political shift to restore water and sewage concessions into public hands.\(^{272}\) The renegotiations were aiming at striking a fair deal after Argentina had imposed new conditions upon the investor during the economic crisis. When the negotiations broke down, not because of unreasonable conduct by the investor, but because Argentina sought to nationalise the water and sewage system, this was considered arbitrary by the tribunal.

Also the concern for global warming and environmental issues stated by Venezuela in the Crystallex case was not found to be the actual reason for the denial of the gold mine permit. The tribunal’s assessment of the facts showed that these concerns all of a sudden were considered important, simultaneously as Venezuela was starting a quest to take over the mining industry.\(^{273}\) Nationalisation was therefore deemed to be the real reason for the measure and the conflict between mining and climate change was not real.

\(^{270}\) The so-called Vigtop-test, Almås v. Poland § 254.

\(^{271}\) The so-called Impregilo-test, Garanti Koza v. Turkmenistan § 365.

\(^{272}\) Urbaser v. Argentina § 326.

\(^{273}\) Crystallex v. Venezuela § 614.
In *Flemingo v. Poland*, the tribunal found that the termination of the contract was not based on a legitimate performance of contractual rights, but rather was an attempt to circumvent the requirement to pay compensation under a decree that was especially undertaken in connection with the modernisation plans of the airport.\(^{274}\) The measure was thus aimed at taking over the shop without providing compensation.\(^{275}\)

In two cases the tribunals seem to have emphasised that the political discretion was motivated by a desire to satisfy public opinion. In *Windstream v. Canada*, the investor challenged that the development of an offshore wind park in a lake was halted. The reasons stated by the local authorities were the need for more scientific knowledge on how such projects affected humans and the environment. The tribunals, however, found that no proper scientific investigations were being carried out by the government, and that the reason for the halt rather was the public opposition to the project and with regard for the upcoming election.\(^{276}\)

A similar situation was found by the tribunal in *Copper Mesa v. Ecuador*, where the local authorities sided with the anti-miners and thus did not follow ordinary regulations, but obstructed the investor in consulting the affected groups.

An opposite angle from which to view whether the measure actually fulfilled a legitimate objective was undertaken in the *Philip Morris* case. Here the tribunal dismissed the investor’s claim that Uruguay’s regulations of tobacco marketing were intended to punish the investor.\(^{277}\) The tribunals rather emphasised that the reasons stated by Uruguay were the real reasons behind the measure.\(^{278}\)

The above presentation shows that many of the objectives originally viewed as legitimate by the host state were not considered to be the real reason behind the governmental conduct. The measures could therefore not be justified under the host states’ right to regulate and were consequently viewed as a breach of the underlying international investment agreement.\(^{279}\)

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\(^{274}\) For the fact see section 4.2.2.3.

\(^{275}\) *Flemingo v. Poland* § 554.

\(^{276}\) *Windstream v. Canada* § 377.

\(^{277}\) *Philip Morris v. Uruguay* § 413.

\(^{278}\) Ibid. § 418.

\(^{279}\) In *Urbaser v. Argentina* and *Windstream v. Canada* this was seen as a breach of the fair and equitable treatment standard, and in *Copper Mesa v. Ecuador, Crystallex v. Venezuela* and *Flemingo v. Poland* the conduct breached both the fair and equitable treatment standard and was viewed as expropriation.
4.4.2.2  The reasonableness of the measures

This section will present the cases where the tribunals assessed whether the challenged measures reasonably could contribute to the fulfilment of the legitimate objective.

In *Philip Morris v. Uruguay*, it was disputed whether it was scientifically proven, or at least rational to believe, that the measure adopted by Uruguay would protect public health. The tribunal’s majority emphasised that it would not perform a hindsight review of whether smoking actually had decreased in Uruguay after the regulations were introduced, but only whether it was reasonable to introduce them in the first place. The majority found scientific support for the requirement to cover 80% of the packages with warnings, as well as that each brand only should have one variant of cigarettes in the amicus curia letters from WHO and PAHO. The dissenting arbitrator, however, argued that Uruguay should have undertaken their own assessment of the measures before they were conducted, instead of hastily introducing them without any careful considerations.

In *Mesa v. Canada*, the tribunal repeatedly emphasised that it was reasonable of Canada to pursue another renewable program than the program the investor had applied for. This program would be more beneficial for the local area, like creating jobs, than the cancelled project. Similar considerations were also undertaken in *MNSS v. Montenegro*, where the tribunal stated that there were good reasons for the government to support the steel manufacture by not letting a bank collapse.

None of the tribunals of 2016 found that the challenged measures were unreasonable undertakings by the host states with regard to reaching their aims. This might imply that the tribunals are giving the host states discretion to determine for themselves what would be reasonable and only will intervene when the situations is obvious unreasonable.

4.5  The criterion of necessity

The second criterion under the principle of proportionality is an assessment of whether the measure is necessary for fulfilling the pursued objective. As shown in chapter 2, the criterion of necessity encompasses an assessment resembling that of suitability and one which actually is an assessment of the relationship between the two colliding rights and interests and so resembles the principle of proportionality in the narrow sense.

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281 Philip Morris v. Uruguay, Dissenting opinion § 126.
282 Mesa v. Canada § 566.
283 MNSS v. Montenegro § 340.
In the following, the tribunals’ use of two situations of necessity will be investigated. First, with regard to whether the challenged measure exceeds what is necessary to reach the objective (section 4.5.1) and second, with regard to the situation where the host state has a choice between two or more measures (section 4.5.2).

4.5.1 Assessing whether the measures exceed what is necessary to reach the objective

The classical situation of necessity is where the measure exceeds what is necessary to reach the objective, so that the surplus does not have any legitimate objective, but merely violates the rights of the investor.\(^\text{284}\)

Few cases from 2016 assess the necessity of the challenged measure. Only the tribunal in *Ickale Insaat v. Turkmenistan* explicitly addressed this element of the principle of proportionality by asking whether the seizure of buildings and equipment was too excessive and “went beyond what would be necessary for the purpose of recovering the delay penalties”.\(^\text{285}\) If Turkmenistan’s measure exceeded its legitimate claim, the additional taking would be irrelevant for the eventual conflict and thus amount to expropriation. This was, however, not found to be the case in *Ickale Insaat v. Turkmenistan*.

The dissenting arbitrator in *Philip Morris v. Uruguay* undertook a necessity assessment when he evaluated Uruguay’s single representation regulation under which only one variant of cigarettes per tobacco brand was allowed to avoid the misinformation that some cigarettes are healthier than others. The arbitrator claimed that Uruguay already had regulations in place that would enable it to forbid connotations such as “light” and “gold” and thus reaching the objective of avoiding misinformation. The dissenting arbitrator therefore claimed that the only thing the single presentation regulation could logically prohibit were “things that Uruguay has not said it wishes to forbid, but that its own citizens wish to undertake”, like seasonal packages or different fonts.\(^\text{286}\)

The dissenting arbitrator did thereby not deny that Uruguay could lawfully adopt measures prohibiting tobacco altogether,\(^\text{287}\) but emphasised that this was not at issue in the current arbitration.\(^\text{288}\) Strictly speaking, the measure therefore went beyond the objective stated by Uruguay and was therefore an unjustified interference with the investor’s rights.

\(^{284}\) See section 2.4.1.

\(^{285}\) *Ickale Insaat v. Turkmenistan* § 371.

\(^{286}\) *Philip Morris v. Uruguay*, Dissenting opinion § 177.

\(^{287}\) Ibid. § 178.

\(^{288}\) Ibid. § 179.
4.5.2 State of necessity: a choice between measures

A typical situation for a necessity assessment is where a country is claiming to be under a state of necessity precluding responsibility under international law. In Urbaser v. Argentina, this question was raised with regard to Argentina’s economic crisis of 2001-2002. The tribunals based its assessment on the ILC Articles on State Responsibility and emphasised that a state of necessity cannot be claimed if the host state has other means available, which to a lesser degree would violate the foreign investors’ rights.289

The challenged measure was Argentina’s offer to renegotiate the contract after it had imposed obligations not to charge low-income users of the water and sewage system and derogate the Peso. The claimant argued in favour of three other measures Argentina rather should have undertaken. The tribunal responded to this by stating that the first two alternatives, which were different forms of subsidiaries and tariff regulations, would require more resources from the state in an already pressured situation.290 The third alternative was to abandon all expansion and reconditioning work and this was found by the tribunals to only ease the investor from contractual obligations which had nothing to do with the economic crisis and the public’s access to water. The tribunal concluded that the alternative of renegotiation was the only real alternative available and dismissed the investor’s claim.

In the tribunal’s assessment of the two first measures it investigated whether the alternative measures were equivalent to the challenged measure. The tribunal seems to assume that also the alternative measures would be able to provide water and sewage systems to low-income users, but stressed that it might not have been possible for Argentina to undertake them under its strained economic situation.291 Because these alternatives demanded more of the state in a pressed situation, they were not considered real alternatives for Argentina.

What the tribunal thereby did was to balance the interests of investor protection, which would be mostly regarded under the two alternative measures with the host state’s actual possibility to provide access to water for the population. An exercise usually associated with the criterion of proportionality in the narrow sense.292 It seems that the tribunals gave more weight to the need of securing low-income users access to water and sewage systems, than to those of the investor.

289 Urbaser v. Argentina § 716.
290 Ibid. § 725–8.
291 Ibid. § 725.
292 See section 2.4.2.
The tribunals’ reasoning when assessing the third alternative suggested by the claimant is best understood under the criterion of suitability. The tribunal did not find a real collision if interests in the situation, as the suggested measure was aiming at abandoning the investor’s contractual obligations and had nothing to do with the economic crisis.

4.6 Proportionality in the narrow sense

The last criterion of the principle of proportionality is the actual balancing known as proportionality in the narrow sense.

This section will first present how tribunals directly have referred to balancing and proportionality in the cases of 2016 (section 4.6.1). Having in mind that the proportionate answer merely means a correct answer in opposition to a wrong one, the section moves on to investigate how the tribunals have filled the clauses of expropriation (section 4.6.2) and fair and equitable treatment with content (section 4.6.3). By describing the reasoning in the cases of 2016 through the criterion of proportionality in the narrow sense as understood in chapter 2, these two last sections will investigate whether a more or less fixed doctrine of international investment law by now has been established.

4.6.1 Explicit references to balancing and proportionality

Four of the cases from 2016 explicitly refer to balancing and proportionality with regard to solving the collision of rights and interests at stake.

In Copper Mesa, the tribunal first highlighted that the obligations towards the foreign investor are not absolute and moved on to the balancing exercise: “Under this FET standard, there is a balancing exercise permitted to the host State, weighing the legitimate interests of the foreign investor with the legitimate interests of the host State and others, including (especially) its own citizens and local residents.”

A quite similar statement can be found by the tribunal in the Flemingo case, “as stated in Saluka, the investor’s legitimate and reasonable expectations should be weighed against the host State’s legitimate regulatory interests.”

The most elaborated statement in the cases of 2016 is found in Rusoro v. Venezuela, also with regard to the fair and equitable treatment standard.

In evaluating the State’s conduct, the tribunal must balance the investor’s rights to be protected against improper State conduct, with other legal relevant interests and coun-

293 Copper Mesa v. Ecuador § 6.81. FET is a common abbreviation for fair and equitable treatment.
294 Flemingo v. Poland § 551.
tervailing factors. First among these factors is the principle that legislation and regulation are dynamic, and that States enjoy a sovereign right to amend legislation and to adopt new regulation in the furtherance of public interest. The right to regulate, however, does not authorize States to act in an arbitrary or discriminatory manner, or to disguise measures targeted against a protected investor under the cloak of general legislation.  

With regard to expropriation, a similar reference to a balancing exercise is found with regard to the police power doctrine. The tribunal in the Philip Morris case emphasised that there are certain criteria that the states’ exercise of regulatory power must comply with in order not to constitute indirect expropriation. “Among those most commonly mentioned are that the action must be bona fide for the purpose of protecting the public welfare, must be non-discriminatory and proportionate.”

That some of the tribunals explicitly state that different rights and interests must be balanced against each other, is to some extent a clear acknowledgment of the principle of proportionality. None of the tribunals, however, moved on to explicitly apply the logic of the law of balancing (illustrated by the weight formula) by first arguing for the importance of each interest and then to compare them.

Neither the law of balancing nor the weight formula is, however, to be understood in such a simplistic way. Rather, they provide an abstraction of legal reasoning in actual, practical disputes. What is interesting is thus not necessarily that investment tribunals state that the rights and interests are to be balanced, but how they reason when they actually order them. The next section will therefore investigate how proportionality in the narrow sense can contribute to explaining how the tribunals reason in the cases of 2016.

4.6.2 Expropriation

The classical situation of expropriation is when the host state seizes the foreign investors’ investments. In three of the cases regarding Venezuela, the different tribunals found that the state had deliberately sought to nationalise the mining industry and the oil and gas sector and that this constituted direct expropriation. In Crystallex v. Venezuela, the tribunals concluded that the measures were a creeping expropriation with the intent of taking over and operate

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295 Rusoro v. Venezuela § 525.
296 Philip Morris v. Uruguay § 305.
297 See section 2.5.1.
the gold mine themselves. Also Saint-Gobain v. Venezuela was an example of this classical situation, because the Venezuelan government de facto ran the mine and production.

All these cases regarding Venezuela are clear examples of situations where the balance has been struck in the international investment agreements in the favour of the foreign investor. Regardless of the good intentions of the state, the action is considered to be expropriation and must among other factors be compensated if it shall be considered lawful.

This thesis has, however, mostly been interested in the situation where the challenged measures are regulations or the outcome of an exercise of police powers. At the beginning of this millennium it was uncertain how this situation was to be understood, but it seems to have been clarified by now. According to the cases of 2016, there are two conditions that must be fulfilled if the measure shall amount to expropriation. Firstly, it must fall under the scope of classical expropriation, and secondly it must not fall under the limitation of being an ordinary regulatory measure.

In Copper Mesa v. Ecuador this interplay was illustratively stated with regard to a mining permit not being granted. To amount to expropriation under an international investment agreement, it is required: “(i) that the measure deprive the investor of its investment permanently; (ii) that the resulting deprivation finds no justification as the legitimate exercise of the Respondent’s police or regulatory powers …”.

This reflects the description of the principle of proportionality given in chapter 2 so that if the facts fall under the initial scope of protection S and are not covered by the limitations L, the consequence takes place Q; S and not L ⇒ Q. The sentence seems, however, to be stronger and also apply the other way around. If an expropriation has taken place then the measure falls under the scope of protection and the limit does not apply; Q ⇒ S and not L. The conditions are thus both necessary and sufficient for each other.

The scope of investor protection under the expropriation clause is according to the cases of 2016, whether the measure amount to a “taking”, meaning if the investor was “substantially

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299 Crystallex v. Venezuela §§ 674. The measures were “equivalent to expropriation”, § 708.
300 Saint-Gobain v. Venezuela § 477.
301 See section 3.2.
302 Copper Mesa v. Ecuador § 6.58.
303 See section 2.6.
304 This gives us a biconditional sentence from which it follows that given S and not L ⇒ Q, it is true that not (S and not L) ⇒ not Q, because the conditions are both necessary and sufficient for each other.
deprived” of the investment. The decisive is not whether a formal transfer of title has taken place and the host state does not need to have had an economic benefit of the measure, but whether the investment de facto has been taken. From another angle this means that it is not sufficient that the investor has suffered a loss, although it as such might be huge, if it does not amount to a substantial deprivation of the entire investment.

In *Copper Mesa v. Ecuador*, the permanent taking of the concession amounted to expropriation, and the conduct was not considered a mere regulatory measure. The tribunal therefore concluded that an expropriation had taken place. This is thus the classical situation of a measure falling under the scope of investor protection and simultaneously not being covered by the limitation, S and not L → Q.

The scope of substantial deprivation was, however, not reached in the cases of *Windstream v. Canada*, *Urbaser v. Argentina* and *Philip Morris v. Uruguay*. In *Windstream v. Canada* the contract was still in force and could be re-activated, and in *Philip Morris v. Uruguay* the business was still intact event though regulated. In *Urbaser* the imposed additional requirements under Argentina’s economic crisis affected the investor, but it did not deprive the investor the concession and thus the investment. The situation in all these cases can be described as when not S, then the consequence Q will also not apply (not S → not Q).

The tribunals in *Philip Morris v. Uruguay* also came to the same conclusion from another angle by looking at whether the limitation, meaning the police power doctrine was applicable in the case. The tribunals emphasised that ordinary regulations such as “bona fide general taxation, regulation, forfeiture for crime, or other action of the kind” makes the limit apply. In a situation of L the consequence does not apply regardless of whether the facts fall under the initial scope or not (L → not Q).

All the cases of 2016 might be seen as typical examples of the extreme positions. Either the facts of the case made it both fall under the scope of protection and the limit did not apply, or

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306 *Windstream v. Canada* § 284.
308 *Copper Mesa v. Ecuador* §§ 6.67, 6.66.
309 *Windstream v. Canada* § 290.
310 *Philip Morris v. Uruguay* §§ 276, 283.
311 According to De Morgan’s theorem (not (p and q) ↔ not p or not q) we have that not (S and not L) is equivalent to not S or L. ‘Table of Logical Equivalences’. Since we have established that the relationship is biconditional, we have that not S or L → not Q.
312 *Copper Mesa v. Ecuador* § 6.60.
the facts did not fall under the scope and the measure was a legitimate exercise of the police power. None of the cases were of the situation of S and L.

The assessment of the limit takes place in accordance with the principle of proportionality. In some of the earlier investment cases, there seemed to be a tendency that ordinary regulations could be outbalanced if the foreign investor was affected excessively. The cases of 2016, however, rather seem to suggest that the affect upon the foreign investor mostly is of concern when assessing whether the threshold for the initial scope of protection is reached or not, and that the following assessment of limitation focuses on the measure as such. It thus seems to be that the ordinary regulation has higher abstract weight than foreign investor protection; if the measure is suitable and necessary the limit will apply. Since none of the cases concerned situations where the threshold of the scope was reached and the measure was ordinary regulations, it is hard to tell whether the intensity of the interference under the concrete circumstances of the case might be so that it can outbalance this abstract weight. But it might be reasonable to assert that the intensity then must go beyond only meeting the threshold of the scope.

4.6.3 Fair and equitable treatment

In the cases of 2016, the fair and equitable treatment standard was described in many different ways. It was emphasised that the standard encompasses fundamental principles like due process, acting in good faith towards the investor, and avoiding harassment, coercion and abuse of power. The host state should create a climate of cooperation, providing a stable and predictable legal framework, and avoid inconsistency between different governmental branches. Fair and equitable thus means “just”, “even-handed”, “unbiased” and “legitimate”, containing legitimate expectation, protection against arbitrary and discriminatory treatment, transparency and consistency. These overarching definitions do, however, not necessarily shed light on the actual content of the standard.

313 See section 2.6.
314 Tecmed v. Mexico § 122.
315 See section 2.5.
316 Rusoro v. Venezuela § 524.
317 Urbaser v. Argentina § 628.
318 Rusoro v. Venezuela § 524.
319 Garanti Koza v. Turkmenistan § 381.
320 Flemingo v. Poland § 535.
321 Crystallex v. Venezuela § 543.
Corona v. Dominican Republic is the only case from 2016 that elaborates on the due process requirement under the fair and equitable treatment standard.\textsuperscript{322} The tribunal in Philip Morris v. Uruguay dismissed the investor’s claim that the regulations in fact were punitive. In most of the cases from 2016, the question therefore was whether the host state violated the foreign investor’s legitimate expectations by its conduct.

In all the awards from 2016 the tribunals granted the host states a wide right to regulate, meaning that a foreign investor had to expect that changes might take place and that discretion might be used. In the cases where the tribunals found that the measure really was motivated by an ordinary regulation, the balance was therefore struck in favour of the host state. The situation thus seems to be that when the measure is part of the states right to regulate, it is not a violation of a BIT. To use the same connotations earlier, this means that $L \rightarrow \text{not} \ Q$.

In not all the cases was the measure considered an act of ordinary regulation. This was, for instance, the case when the investor was assured that the discretion would be used in a specific direction. In Crystallex v. Venezuela the tribunal found that a specific letter from the Ministry of Environment gave rise to a legitimate expectation by the investor that the permit would be granted.\textsuperscript{323} When a specific representation is given the foreign investor, it is a requirement that the investor actually relied upon it when undertaken the investment for it to constitute a legitimate expectation.\textsuperscript{324}

Another situation where the circumstances were not seen to establish an ordinary regulation can be found in Murphy v. Ecuador. When the Ecuadorian government required that it should participate in 99% of the companies increased revenue due to increased oil and gas prices, the entire conditions upon which the oil company had invested in Ecuador changed.\textsuperscript{325} The system was thus changed from a system where the companies took all the risk at the beginning of the project and in return took part in the gains from the oil fields (participation contract), to a system where the companies were mere service providers. Such a fundamental change was not in line with the foreign investors legitimate expectations.\textsuperscript{326}

Similar conditions might also be found in Garanti Koza v. Turkmenistan, where one hand of the government entered into a contract establishing how the investor was to be payed, whereas

\textsuperscript{322} Corona v. Dominican Republic § 254.
\textsuperscript{323} Ibid. § 556.
\textsuperscript{325} Murphy v. Ecuador § 281.
\textsuperscript{326} Ibid. § 292.
another required the investor to make invoices according to other premises according to other regulations.\textsuperscript{327}

Whether the measure is part of the host states’ right to regulate thus depends on the principle of proportionality. As was shown in section 2.6, how the balance is to be struck depends on the circumstances of the case. When recurring in case law, some situations might be viewed as established doctrine of international investment law. With regard to international investment case law of 2016, this might for instance be the case when a specific expectation has been established by the government (F\textsubscript{1}) and the investor relied on it (F\textsubscript{2}), then the limit of ordinary regulation does not apply and the fair and equitable treatment standard might be breached.\textsuperscript{328} F\textsubscript{1} might be elaborated even more, so that a specific expectation might be a promise in a letter from a governmental authority, or an intentional distribution of economic risk under a contract. The fact of the case might, however, provide new reasons so that the balance in the particular situation might have to be struck differently at the case to be reviewed.

4.7 The interplay between different assessments

When looking at international investment law cases of 2016, two observations may be of particular interests. One regards the interplay between the three criteria of the principle of proportionality (section 4.7.1) and the other the interplay between expropriation and fair and equitable treatment standard (4.7.2).

4.7.1 The interplay between the three criteria of the principle of proportionality

The interplay between the three criteria of the principle of proportionality becomes evident on many levels. The first is within the criterion of suitability itself, meaning between first defining which objectives are legitimate and then determining whether the measure contributes to its fulfilment. When the investment tribunals of 2016 found that the host state was not undertaking ordinary regulation when motivated by nationalisation and political opportunism, this assessment may be seen both from the angle of illegitimate objectives and from the angle that the stated objective is not real. Under which category the assessment is labelled thus appears rather random.

A recurring issue with regard to the criterion of necessity is that it merely encompasses the assessments under suitability (establishing that the conflict between different rights and interests is real) and proportionality in the narrow sense (where the conflict is solved by relating

\textsuperscript{327} Garanti Koza v. Turkmenistan § 382.

\textsuperscript{328} See section 2.6 where this was described as F\textsubscript{1} and F\textsubscript{2} \(\rightarrow Q\).
the reasons to each other). This interplay becomes evident in the few cases of 2016 applying the criterion of necessity, where the assessments also might be described under the label of suitability or proportionality in the narrow sense.329

The most striking interplay is, however, the one between the criteria of suitability and proportionality in the narrow sense. In the cases of 2016, the balance between foreign investor protection and the host states’ right to regulate seems to have been struck when the tribunals have assessed the sincerity and reasonableness of the measure. If the measure is suitable, it is generally considered proportionate. Here we might recall the explanation from chapter 2, that the relation between two interests might be intuitive (save the child before the statue that has fallen over her). The tribunals in the case of 2016 seem to find the balance intuitive, so that the host state right to regulate will exclude the measure from the scope of investor protection.

The assessment of whether the measure falls within the host states’ right to regulate is therefore important. The actual balancing is thus to a certain extent interwoven with that of suitability. In for instance the case of Flemingo v. Poland one analysis of the case is that the measure of terminating the contract was not based on the contract but rather the illegitimate wish to take over the shop without compensating for it (suitability). Another angle to understand the reasoning was that the minor breach undertaken by the investor should not have so serious consequences. The importance of protecting the investor was high (minor breach led to a high loss) and the importance of protecting the host state low (minor breach, circumvention of the compensation requirement). This is in reality an assessment of the proportionality of the measure.

To a certain degree the tribunals’ approach resembles that of the European Court of Justice (ECJ) and the EFTA Court with regard to free movement. Harbo includes the criterion of proportionality in the narrow sense to his analysis of the ECJ’ reasoning, but stresses that the Court only engages with this last stage if the parties demand it or if it is a fundamental right that is at stake.330 It is thus a safety valve for particular cases, but in most ordinary cases the focus of the assessment lies on the criteria of suitability and necessity. This seem also to be the case in current international investment law, where the balance is struck in accordance with the host states’ desired level of regulation for the public welfare, but that it might exist a safety valve for cases where the foreign investor is particularly infringed.

329 See section 4.5.
4.7.2 The interplay between expropriation and the fair and equitable treatment standard

The analysis of the cases of 2016 has also shown that in situations where the host state has an interest in regulating and exercising discretion for the public benefit, there is an interplay between the assessments of expropriation and the fair and equitable treatment.\textsuperscript{331} This relationship is for instance shown when the tribunals assess the collision of rights and interests at stake under the fair and equitable treatment standard, and then let the conclusion have direct consequences for whether an expropriation has taken place. In for instance \textit{Copper Mesa v. Ecuador}, the tribunals started their assessment with the expropriation clause and stated that the host state’s measure was arbitrary as would be shown in the later fair and equitable treatment standard.\textsuperscript{332} The tribunal in \textit{Flemingo v. Poland} started its assessment with the fair and equitable treatment standard, and then referred to its conclusion when it later assessed the expropriation clause.\textsuperscript{333}

The main difference between the two assessments seems to be that the scope of protection is wider under the fair and equitable treatment standard since it is not a requirement that the measure substantively deprive the foreign investor its investment. The consequences of a breach of the expropriation clause and the fair and equitable treatment standard also might be different.\textsuperscript{334} The situation where the measure does not infringe the foreign investor as it is an ordinary exercise governmental acts and omissions for the public benefit seems, however, to be similar under the two clauses. Under expropriation this is often referred to as the doctrine of police power and under the fair and equitable treatment standard as a right to regulate, but in accordance to the analysis in this chapter the content seems to be rather similar.

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\textsuperscript{331} The fair and equitable treatment standard might have additional aspects, like protection against discrimination, lack of due process, harassment, and similar with direct expropriation.

\textsuperscript{332} \textit{Copper Mesa v. Ecuador} § 6.66.

\textsuperscript{333} \textit{Flemingo v. Poland} § 597.

\textsuperscript{334} But this thesis has not focused on how compensation and damages are calculated.
5 Has a fair balance been stuck in the case law of 2016?

5.1 Introduction
This thesis takes the view that international investment law appears to be a more balanced system in 2016 than it was at the beginning of this millennium (section 5.4). This is due to the legal doctrine of international investment law to a greater extent taking account of both the interest of the foreign investor and those of the host state in a presumably adequate manner.335

To draw this conclusion, this chapter will engage with the previous criticism against the system presented in the chapter 3,336 and evaluate if these concerns still apply. This will first be done in relation to how the elements of the principle of proportionality are applied in the cases of 2016 (section 5.2). Then, with regard to how the balance actually has been struck between foreign investor protection and the host state’s interest in regulating for the public good as it appears in the cases of 2016 (section 5.3).

5.2 The principle of proportionality in the cases of 2016
This section engages with the use of the principle of proportionality in the reasoning of the international investment tribunals of 2016. It summarises how the tribunals themselves openly applied the technique when solving investment disputes (section 5.2.1), but also how the legal reasoning constituting the semantic structure of the principle of proportionality may be found in the investment cases of 2016 (section 5.2.2). Lastly, the section will engage with the concern that letting investment tribunals undertake a proportionality assessment opens up for subjective and unjustified reasoning (section 5.2.3).

5.2.1 Directly applied by the tribunals
The tribunal awards that started to use the principle of proportionality at the beginning of this millennium were criticised for doing it rather flawed and unsystematically.337 It still seems to be the case that even the tribunals that explicitly refer to the principle of proportionality, do not necessarily undertake a full-fledged review of all the three elements.

The main observation is, however, that the tribunals seldom refer to the criteria in their reasoning. The criterion of suitability is never explicitly mentioned.338 The tribunal in Urbaser v. Argentina is the only case that openly addressed the criterion of necessity in its reasoning, framing it as a requirement that the state should not have other means available that would

335 The analysis of 2016 has especially not revealed any examples where the host state’s interests were bluntly neglected.
336 See section 3.4.
337 See section 3.4.3.1.
338 Although it was addressed as not having a hidden agenda in Almås v. Poland § 254.
both take account of the need of Argentina and its population and the investor’s interest in performing a contract protected as an investment. Some tribunals explicitly refer to balancing and proportionality, for instance *Copper Mesa v. Ecuador* and *Flemingo v. Poland*. These direct references seem to be targeted at the criterion of proportionality in the narrow sense, and not a way of integrating the entire proportionality principle.

The international investment tribunals do therefore not systematically engage in the full technique of the principle of proportionality, like for instance the European Court of Human Rights (ECtHR) and the European Court of Justice (ECJ) do.

5.2.2 The use of the different elements in the tribunals’ reasoning
The other angle is by testing whether the tribunals’ reasoning can be explained through the semantic structure of proportionality, as this was explored in chapter 4. Although the tribunals seldom address the principle of proportionality directly, the elements of this fundamental technique of legal reasoning can be identified in the reasoning of the international investment tribunals of 2016.

Nearly all the tribunals undertook a suitability assessment of the challenged governmental measure. They assessed whether the host state had a legitimate reason for their acts and omissions, and undertook a factual assessment of whether the measure could fulfil this reason. That the tribunals did not explicitly label this assessment as a suitability test is probably because it is as such a fundamental part of legal reasoning – it investigates what kind of reasons are legitimately at play in the dispute.

In their assessment of what was a legitimate objective and how to reach this objective, the tribunals gave the host state much deference in both determining the political ends and how they were to be met. The review of whether the reason actually was real was, however, performed with a rather high intensity. The tribunals thus often initially found the measure as

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339 *Urbaser v. Argentina* § 716.
340 *Copper Mesa v. Ecuador* § 6.84 and *Flemingo v. Poland* § 535.
341 A striking description is given by the tribunal in *Crystalex v. Venezuela* § 585: “Differently put, while the Tribunal will refrain from making findings as to whether or not the concerns expressed by the Ministry were “adequately” addressed by the Claimant, or whether the reasons put forward by the Respondent in denying the Permit were substantively valid, the Tribunal will, in its review of the government conduct, assess whether there have been serious procedural flaws which have resulted in the Permit being arbitrarily denied, or in the investor being treated non-transparently or inconsistently throughout the process and thereafter. It is with this standard of review in mind that the Tribunal examines now the overall process between Crystalex and the Venezuelan authorities.” The tribunal then went on to conclude that the reasons given for the denial of permit (global warming) was not the actual reason, Ibid. § 614.
such legitimate, but nevertheless reached the conclusion that it was not the real motivation for the governmental infringement of the investor.

Also the criterion of necessity can be found in the tribunals’ legal reasoning of 2016, but to a much lesser degree. One reason for this may be that the facts of the disputes made it unnatural to ask whether the host state rather should have done something else than the measure which was found to be suitable. In some situations, like granting permits or terminating a contract, the question often was rather in the form of either a yes or no. Other questions seemed in nature political or administrative, as for instance how to regulate the swap marked in *Rusoro v. Venezuela*, where the tribunal emphasised that the content was for the host state to decide.342

Although the sample of cases is rather small to draw a conclusion, the cases from 2016 nevertheless show reluctance among the tribunals to engage with controversial political questions. The tribunal in for instance *Mesa v. Canada* stated that the manner to which the host state regulates its internal affairs should be given deference.343 Also the tribunal in *Philip Morris v. Uruguay* stated that the host state was given a leeway when making public policy determinations.344 The tribunals of 2016 thus seem to refrain from second guessing governmental decisions and rather respect the governments’ expertise and competence,345 and thus meet the concerns by those stating that investment tribunals are not suitable for making important decisions for society.346

Investigating how the structure of proportionality in the narrow sense might explain the tribunals’ reasoning in the cases of 2016 has in this thesis meant to investigate how the actual balance has been struck between foreign investor protection and the host state’s other interest, - be it protection of human rights, the environment or just ordinary regulations for the public good. In this understanding, the criterion of proportionality in the narrow sense is not reserved for the hard cases where the outcome is uncertain, but can also be a description of the situations where the outcome is more intuitive. How this balance seems to be struck in the cases from 2016 was presented in chapter 4 and will only be briefly summarised in the later section 5.3.

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342 *Rusoro v. Venezuela* § 531.
343 *Mesa v. Canada* § 505.
344 *Philip Morris v. Uruguay* § 398, referring to the so-called margin of appreciation doctrine.
345 See *Crystallex v. Venezuela* § 583.
346 See section 3.4.3.2. This does, however, not say anything about whether the system as such is unsuitable to assess such disputes, due to their composition of arbitrators, transparency etc.
5.2.3 The principle of proportionality is not used as a substantive principle

The use of the principle of proportionality has been met with criticism by investment scholars as it is seen to open up for unjustified and subjective reasoning. The concern is that it might allow for all kinds of arguments to be included in the assessment, and that the investment arbitrators anyway are unsuitable to apply the principle of proportionality.

The first answer with regard to these concerns is that the principle of proportionality as such is not to blame for this, but the eventual flawed reasoning the arbitrators’ perform within the structure. Both the arguments they use and the level of deference they grant the investor must be part of the underlying international investment law doctrine. The advantage, as well as disadvantage, with the principle of proportionality is that instead of hiding the premises and arguments, these becomes transparent and thus are also open for review.

The principle of proportionality may, however, often be mistakenly used as a “substantive principle” that legitimises certain arguments. If flawed reasoning in this way enters international investment law through the principle of proportionality, it will inevitably have consequences for how the principle of proportionality is viewed with regard to international investment law.

An important observation is therefore that it does not seem to be the case that the tribunals of 2016 used the principle of proportionality as a substantive principle that on its own included other rights and interests into international investment law. A reference to the principle of proportionality was not used as a door opener for applying the legal doctrine of for instance ECtHR or WTO into international investment law. It also did not seem to be used as a lever for subjective arguments based on what the tribunals found unjust in various situations. Rather, the analysis in chapter 4 has shown that a uniformed doctrine finally is beginning to merge in international investment law.

5.3 The legal doctrine of international investment law as of 2016

This section will move beyond the principle of proportionality as a plain semantic structure to the legal doctrine that is uncovered when the investment tribunal of 2016’s reasoning is investigated through the technique of the principle of proportionality; meaning to evaluate the balance struck between the colliding rights and interest in investment disputes under the clauses of expropriation and the fair and equitable treatment standard. The section will address the

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347 As was done in *Tecmed v. Mexico* and *Continental Casualty v. Argentina*, see section 3.4.3.3.
348 See section 3.4.3.4. Although *Flemingo v. Poland* may be understood in this direction, see section 4.7.
concerns of a balance (or lack of such) that grants the foreign investor a too excessive protection (section 5.3.1) and a balance that gives the host state unqualified priority (section 5.3.2).

5.3.1 Acknowledging the states' right to regulate
The most fundamental criticism regarding international investment law the last decade is that the system has been perceived to grant the investors a too excessive protection on the expenses of other fundamental rights as well as the ordinary interest of host states’ to regulate for the public benefit.

The examination of the cases of 2016 has, however, shown that the police power doctrine (expropriation) and the right to regulate (the fair and equitable treatment standard), found to be vaguely emerging by Titi in her dissertation from 2013, now seem to be more certain. The system of international investment law as of 2016 thus no longer seems a hindrance per se to welfare regulations, a concern stressed by many scholars in the Osgood Hall Statement in 2011. UNCTAD and many national states have signalised in new draft international investment agreements that a change in the direction of interpretation is desired, and this message has actually being taken into account in the cases of 2016. This shows that the international investment law no longer exclusively look at the interests of the foreign investor.

The analysis in chapter 4 has shown that the host states’ interest in regulating is considered a legitimate objective under the criterion of suitability and that when it actually is the motivating factor for the state’s infringing measure, it will take priority over the investor’s interest.

As a main rule the balance seem to be struck in the interest of the host state’s regulatory freedom.

With regard to the question whether changing laws and regulations as well as the exercise of administrative discretion constitutes indirect expropriation, the answer is no. Even when the challenged measure substantially deprives the investor the investment, the measure is lawful as long as it is not arbitrary or discriminatory. None of the cases of 2016 were illustrations of this, however, because in Copper Mesa v. Ecuador the limit did not apply as the measures were not considered ordinary regulations, and in Phillip Morris v. Uruguay and Windstream v. Canada, the measures did not meet the initial threshold for amounting to expropriation.

349 Titi, The Right to Regulate in International Investment Law, 302.
350 Phillip Morris v. Uruguay § 301: “In the tribunal’s view, these provisions, whether or not introduced ex abundanti cautela, reflect the position under general international law.”
351 Copper Mesa v. Ecuador § 6.60, Phillip Morris v. Uruguay § 295.
352 Or other of the words used to describe the opposite of an ordinary regulation, like harassment, bad faith, lack of due process etc.
Also when assessing the fair and equitable treatment standard, the tribunals acknowledged a right to regulate.\textsuperscript{353} Using the collective term of the foreigner’s legitimate expectation, the tribunals seem to conclude that it must be expected that the host state fulfils its international and constitutional duties,\textsuperscript{354} that it undertakes regulations of different business areas,\textsuperscript{355} and react to changing circumstances.\textsuperscript{356} This is part of the business risk that an investor faces when it establishes in both a developed and a developing country.\textsuperscript{357}

Despite the acknowledgment of the host state’s right to regulate in international investment law, some concerns may apply with regard to international investment law’s emphasis on foreign investor protection. A quantitative observation is that the foreign investor won most of the cases from 2016, in which the merits were assessed. In the 19 examined cases, 12 were decided in favour or partly in favour of the foreign investor,\textsuperscript{358} and the host state was only fully acquitted in 7.\textsuperscript{359}

A reason for this might be that the tribunals engage in a rather intense review of whether the host state’s stated objectives for undertaking the measure were real. Without knowing fully the evidences of the cases, one should be reluctant to second guess the tribunals’ assessments of the facts. It nevertheless seems to be recurrent that the host states are not believed. In two of the cases of 2016, the real reason behind the infringing measure was considered to be the government’s adherence to public opinion.\textsuperscript{360} Although it might have been different if the public opinion was exercised through formal democratic processes, the tribunals’ reasoning seems to emphasize that the exercise of politics is not as such legitimate.

\footnotesize{
\textsuperscript{354} See for instance Urbaser v. Argentina § 622.
\textsuperscript{355} See for instance Rusoro v. Venezuela § 532.
\textsuperscript{356} Murphy v. Ecuador § 276.
\textsuperscript{357} Although the cases of 2016 have erased the previous distinction between the minimum standard of international custom and the independent standard of fair and equitable treatment, the two seem to have met each other on the half way. The legal doctrine of 2016 adapts the evolving standard of what is outrageous to the contemporary view, meaning harassment, bad faith, arbitrary and discriminatory conduct etc. The standard does, however, not impose a freeze of the entire legal and business environment as of the time of the investment, but rather acknowledge the legality of ordinary regulations and execution of administrative discretion. The concern especially raised by the NAFTA parties in their statement of interpretation, thus seems to be taken into account.
\textsuperscript{360} Windstream v. Canada and Copper Mesa v. Ecuador.
}
5.3.2 Still restraints on the host states exercise of powers

Also the acknowledgment of host state’s police power and right to regulate has been met with criticism. Regarding this concern, the first point that must be emphasised is that granting host states a right to regulate has in the cases of 2016 not challenge the fundamental protection from unlawful direct expropriation and measures which in fact are expropriations.\footnote{See for instance all the cases against Venezuela.} Also under the fair and equitable treatment standard, the foreign investor is protected from governmental abuses, such as bad faith, discrimination, lack of due process and harassment. The protection of the host states fundamental rights under international investment agreements are thus not affected when tribunals acknowledge the host states’ right to undertake ordinary regulations – which also might explain why the foreign investors’ claims often succeed in the disputes of 2016.

The cases of 2016 have also shown that when the challenged measure is claimed to be a regulation or exercise of ordinary discretion, the tribunals undertake an assessment of whether this actually is the case. Through especially the criteria of suitability and necessity, the foreign investor is granted protection from an unqualified priority to the host state.

A concern among many international investment law scholars has been the lack of a textual reference for including the host states’ interests in international investment law. With regard to this concern we might remember Barak’s emphasise that legal rights rarely are absolute and that a legal basis for limiting them might for instance be found in conflicting fundamental rights. In the context of international investment law these rights are not listed in the same agreements as the investor protection, but they are nevertheless part of the same system, namely international public law. Human rights, be it access to water or labour standards, are thus relevant, as well as environmental protection.

In his context of national constitutional law, Barak uses the notion of democracy as another reason for allowing rights to be limited even without an explicit textual reference. In the context of international investment law, the notion of sovereignty might resemble this idea, meaning that the public benefit and functioning institutions as such have a value. The development of an acknowledged doctrine of police powers or a so-called right to regulate thus seem to be a valid legal source for limiting/defining the investor protection.

The concern that the host state’s interests have priority may also be addressed under the criterion of proportionality in the narrow sense; the balance is struck in the favour of the host state.
The concern has been framed as a shift of the economic burden of regulation from the host state to the foreign investor. The premise for this view seems, however, to be flawed. Being subject to ordinary regulations, even in the situations when this affects your freedom and impose obligations upon you, are part of life in a modern society.\footnote{Being part of a modern society means for instance to pay tax, be obliged to attend school, have to maintain your buildings so that nobody gets hurt etc.} Also with regard to property protection.\footnote{The distinction between taking of property and regulations affecting the property is for instance emphasized in the Norwegian, German and American national systems, as well as ECHR.} Such regulations are therefore basically not considered an infringement of any fundamental rights. This might be framed as that the abstract weight of the host states’ right to regulate for the public good being higher than the interest of not being subject to regulations. The situation must therefore affect the investor extraordinarily if the intensity of interference in the particular case shall outweigh the interests of the regulation. This was not considered the case in any of the awards from 2016, but might be a safety valve for the foreign investor.\footnote{Although \textit{Flemingo v. Poland} may be understood in this direction, see section 4.7.}

\section*{5.4 Conclusion: Towards a fairer balance in international investment law}

The analysis of the international investment cases of 2016 reveals that international investment law has moved beyond being a legal system that sees itself separated from the rest of international public law to have a more balanced appearance. Instead of only emphasising the interest of the investor, the current doctrine of international investment law also takes account of other rights and interests and gives due weight in determining the outcome of investment disputes.

This thesis has also found that the tribunals perform an intense review of the host states’ intentions, and that public opinion is not considered a legitimate aim for undertaking measures affecting the foreign investor. Both the interests of the host state and that of the investor therefore seem to have been taken into account by the tribunals in the cases of 2016, which support the conclusion that international investment law is heading towards becoming a balanced system of law.

Whether the actual balance struck is considered fair, depends on whether the weight given to the colliding rights and interests are considered appropriate. In a system with a divergent jurisprudence, it might be hard to establish whether the tribunals’ reasoning is in accordance with the underlying legal doctrine. That a more consistent doctrine is evolving in international investment law, will to a greater degree enable a point of reference for evaluating whether the correct balance has been struck.
Another angle for considering the fairness of the balance is a value-based point of view. This means that the moral environment in which the decision has been made might influence whether it is considered correct or not. Take for instance how the question of abortion has been considered differently in different legal systems.\textsuperscript{365} What is considered fair in a private law context and in a public law context might also differ. That international investment law is disconnected from the environment in which both the investment and the measure takes place might make the balance struck seem unfair from either the point of view of the investor or the host state. This is a fundamentally difficult question to solve, and might be a reason for finding the entire system of international investment law flawed.\textsuperscript{366} Another solution, however, may be to investigate and develop theories on how best to order the different rights and interest at stake in international investment law disputes. It is also important that those applying international investment law are sensitive towards these concerns by paying due regard to the national system of review.\textsuperscript{367}

It is therefore too early to conclude on whether international investment law strikes a fair balance between foreign investor protection and host states’ right to regulate. What this thesis has shown, however, is that by taking other rights and interests into account, international investment law has overcome the perceived legitimacy crisis it faced at the beginning of this millennium. Although the principle of proportionality does not as such solve any of the system’s challenges, this thesis has shown that the principle of proportionality is a helpful technique in address important issues that arise when different rights and interests collide. This is because the criteria of suitability and necessity help to address the question of whether a legitimate legal conflict of rights and interests exits and the criterion of proportionality in the narrow sense highlights the reasoning for an order between these rights and interests in the actual dispute at hand.

Despite many challenges still being unanswered, international investment law as of 2016 is a more balanced system of law and thus more in line with what might be expected from an international system of law.

\textsuperscript{365} See section 2.5.2.

\textsuperscript{366} This is the question of whether the setup of the system is fundamental flawed or not, which this thesis has demarcated from, see section 1.3.

\textsuperscript{367} This is the question of deference or the so-called margin of appreciation which thus thesis has demarcated from, see section 1.3.
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