

THESIS, ANTITHESIS AND SYNTHESIS: INVESTOR PROTECTION IN BITS, WTO AND FTAS

MICHAEL EWING-CHOW*

I INTRODUCTION

Prior to the advent of the World Trade Organization ('WTO'),¹ individual states either wanting to protect the investments of their citizens abroad or seeking to attract foreign investments entered into bilateral investment treaties ('BITs'). Though it has yet to be proved that entry into such investment treaties directly correlates to an increase in foreign investment, it is estimated that well over 2000 of these BITs exist.² Their proliferation is perhaps attributable to the belief in the need for investor protection. This belief first arose in the post-colonial era from the need of home states to conclude investment treaties to protect their multinational corporations from host states.³ This occurred in response to host states justifying the nationalisation of foreign-owned property by invoking the Calvo doctrine. According to the Calvo doctrine, the applicable standard of protection for foreign investment is the national standard of treatment under the laws of the host state.⁴ The belief in BITs resurfaced again in the 1990s, when the triumph of capitalism over socialism led to the liberal economic idea that

* Assistant Professor, National University of Singapore, LLB (NUS), LLM (Harvard), Advocate & Solicitor, Singapore. The writer would like to thank Ng Wuay Teck for his significant contributions to this paper.

1 Established pursuant to the *Marrakesh Agreement Establishing the World Trade Organization*, opened for signature 15 April 1994, 1867 UNTS 3 (entered into force 1 January 1995) ('WTO Agreement').

2 According to the United Nations Conference on Trade and Development, there were 2392 such treaties in force by 2004: see United Nations Conference on Trade and Development, 'Foreign Investment Database – Bilateral Investment and Double Taxation Treaties (Cumulative)' (2004) <<http://stats.unctad.org/FDI/TableView/tableView.aspx?ReportId=7>> at 10 August 2007.

3 In this paper, 'home state' refers to the country of origin of a foreign investor, while 'host state' refers to the country in which the foreign investment takes place.

4 This doctrine is associated with Carlos Calvo, who was an eminent Latin American jurist and diplomat. Home states thought that the laws of a host state offered an inferior level of protection to foreign investors because the national laws of a host state would inevitably permit any nationalisation of foreign investment by the host state. Investment treaties concluded with host states allowed home states to define the standards of protection that would apply to their investments in the host states. This allowed home states to impose their own, supposedly more robust, domestic standards of investment protection.

inflows of foreign investment were good for the host economy.⁵ States concluded treaties offering substantial investment protection to foreign investors in the hope that this would provide a more favourable investment climate, which would consequently attract greater inflows of foreign investment.⁶ These BITs have resulted in a complex network of rules created on a bilateral basis.

The advent of the WTO in 1995 provided the Organisation for Economic Cooperation and Development ('OECD') with the confidence to try for a multilateral version of these BITs in an effort to harmonise the rules. However, the proposed OECD Multilateral Agreement on Investment ('MAI') came to a standstill because OECD member states could not come to agreement on its terms. Later, the WTO's Doha Development Agenda ('DDA') proposed to look at investment protection, potentially portending greater WTO involvement in investment protection; but the investment talks within the Doha Round have since been suspended with uncertain prospects for revival.

As a result, the main growth in international investor protection agreements can be found in the recent proliferation of free trade agreements ('FTAs') containing substantive investment chapters. In this paper, BITs and FTAs with investment chapters are collectively referred to as 'investment treaties'. Examples of FTAs containing substantive investment chapters include the *United States-Singapore Free Trade Agreement* ('US-Singapore FTA')⁷ the *North American Free Trade Agreement*⁸ ('NAFTA') and the *Singapore-Australia Free Trade Agreement* ('Singapore-Australia FTA').⁹ Yet, by entering into bilateral or regional investment treaties in addition to the multilateral trading regime, potentially different regimes are created governing the protection afforded to foreign investors in a state which is a Member of the WTO but which has also entered into an investment treaty, whether in the form of a BIT or a FTA.

This is underscored by the fact that the majority of countries in the world are also Members of the WTO.¹⁰ While the *Agreement on Trade-Related Investment Measures* ('TRIMS')¹¹ of the WTO deals directly with foreign investment, it offers a 'thin' form of investor protection. Its coverage is not comprehensive as it mainly restricts trade discriminatory practices such as performance requirements, specifically those measures which are 'inconsistent with the provisions of Article III [on national treatment] and Article XI [on quantitative restrictions] of [the *General Agreement on Tariffs and Trade* ('GATT')]¹²'.¹³ However, the WTO

5 Host states believed that foreign investment could create new employment, lead to the building and upgrading of infrastructure, and allow for the diffusion of technology and management skills to locals, all of which would benefit the host economy.

6 For a comprehensive outline of the history of investment treaties, see M Sornarajah, *The International Law on Foreign Investment* (2nd ed, 2004) 18–30, 37–65.

7 42 ILM 1026 (entered into force 15 January 2003).

8 32 ILM 296 (entered into force 1 January 2004).

9 [2003] ATS 16, (entered into force 28 July 2003).

10 There are 151 member states in the WTO, the latest to join being Tonga on 27 July January 2007.

11 *WTO Agreement*, above n 1, annex 1A (*Agreement on Trade-Related Investment Measures*) 1868 UNTS 186.

12 *WTO Agreement*, above n 1, annex 1A (*General Agreement on Tariffs and Trade*) 1867 UNTS 190.

13 *Ibid* art 2(2).

also provides rules on trade in goods and services which may be applicable to some aspects of foreign investment. Rules on trade in services are particularly pertinent because among the four modes of supply of services, mode three, or supply through commercial presence,¹⁴ directly relates to investment in services.

The interaction of these WTO rules with the ‘thicker’ form of investor protection found in BITs and FTAs, particularly FTAs which contain substantive chapters on trade in services in addition to investment chapters,¹⁵ merits a closer investigation. This paper looks at three possible ways in which a state’s obligations under a BIT or an investment chapter of a FTA can interact with its obligations under the WTO, and, if existent, the services chapter of the same FTA, so as to produce unexpected consequences. Part II considers the possibility of a particular state measure being re-litigated in multiple forums. Part III examines the use of WTO rules and obligations in services chapters, which are used to obtain advantages in addition to the rights provided under investment law. Finally, Part IV explores the possibility of WTO law being directly applicable to investment treaties.

II FIRST CONSEQUENCE: RE-LITIGATION OF THE SAME MEASURE

The *GATT*, *General Agreement on Trade in Services* (*GATS*)¹⁶ and the services chapter of a FTA impose obligations such as market access, most-favoured nation (‘MFN’) treatment and national treatment on their member states. If a member state accedes to an investment treaty, that treaty may potentially become an additional source of liability for a measure which has already incurred liability under WTO rules or a FTA services chapter. For instance, measures constituting breaches of national treatment, MFN or market access under *GATT*, *GATS* or a FTA services chapter can potentially incur liability under investment treaties via the MFN, national treatment and even expropriation provisions. This means that, due to a single measure it undertakes, a state can be found to have breached its obligations under not just WTO rules and the FTA services chapter but also under the investment treaty.

The phenomenon of a single state measure being litigated under more than one regime has already been manifested recently in the soft drinks dispute between the United States and Mexico. Mexico subjected soft drinks using non-cane sugar sweeteners such as high-fructose corn syrup (‘HFCS’) and beet sugar to a 20 per cent tax on their transfer and importation, and taxes on specific services, such as

14 See *WTO Agreement*, above n 1, annex 1B (*General Agreement on Trade in Services*) 1869 UNTS 183 (*GATS*). Article I:2(c) of the *GATS* defines mode three as ‘the supply of a service ... by a service supplier of one Member, through commercial presence in the territory of any other Member’. Article XXVIII(d) defines ‘commercial presence’ as:

any type of business or professional establishment, including through

- (i) the constitution, acquisition or maintenance of a juridical person, or
- (ii) the creation or maintenance of a branch or a representative office, within the territory of a Member for the purpose of supplying a service.

15 Examples include the US–Australia FTA, the US–Chile FTA and the US–Singapore FTA.

16 See *GATS*, above n 14.

the transfer of soft drinks and bookkeeping requirements. Under *GATT*, the tax was held, in *Mexico – Soft Drinks*,¹⁷ to constitute an indirect tax on US imports of beet sugar and HFCS, which was inconsistent with *GATT*'s national treatment requirements.¹⁸

The Panel found that the tax measures were inconsistent with the first sentence of *GATT* Article III:2 because these drinks were subject to internal taxes in excess of taxes imposed on like domestic products, such as soft drinks sweetened with cane sugar. This taxing practice is prohibited under Article III:2. The Panel also found that the 'the dissimilar taxation imposed on 'directly competitive or substitutable imports (HFCS) and domestic products (cane sugar)'¹⁹ was applied in a way that afforded protection to domestic production, contrary to the second sentence of Article III:2.²⁰ The Panel concluded that Mexico acted inconsistently with Article III:4 in respect of non-cane sugar sweeteners, such as HFCS, by using the tax measures and bookkeeping requirements to accord them less favourable treatment than the treatment accorded to like domestic products, such as cane sugar.

Despite lobbying their government to bring the WTO action, concurrently, US sweetener companies also initiated two parallel proceedings against Mexico under *NAFTA* Article 1110 by claiming that the Mexican tax was discriminatory and constituted 'indirect expropriation'.²¹ Both proceedings still continue today and have not been withdrawn despite the success of the US action in the WTO forum. It is probable that this scenario involving litigation of a state measure in several forums may be repeated in the future because of the overlap between treaties. Of the 14 investment cases brought against the US under Chapter 11 (the investment chapter) of *NAFTA* by 2006, at least nine could conceivably have been brought as trade cases to the WTO as well.²²

At present, there is no rule at international law which allows states to avoid incurring liability under two or more different forums. Under general international law, the initiation of arbitration proceedings against the host state by an investor does not preclude the investor's home state from concurrently exercising diplomatic protection and launching WTO dispute settlement proceedings, and vice versa.²³ The WTO agreements do not address the re-litigation of a WTO-inconsistent measure in other forums. While the principle of

17 *Mexico – Tax Measures on Soft Drinks and Other Beverages*, WTO Doc WT/DS308/AB/R, AB-2005-1 (2006) (Report of the Appellate Body) ('*Mexico – Soft Drinks*').

18 The Appellate Body agreed with the Panel's finding in respect of *GATT* Article III:2 and III:4.

19 *Mexico – Tax Measures on Soft Drinks and Other Beverages*, WTO Doc WT/DS308/R (2005) 131 (Report of the Panel).

20 Ibid.

21 See Notice of Intent, *Corn Products International v United Mexican States*, ICSID Case No ARB(AF)/04/1 (28 January 2003) (copy on file with author); Notice of Intent, *Archer Daniels Midland Company and Tate & Lyle Ingredients Americas Inc v United Mexican States*, ICSID Case No ARB(AF)/04/5 (13 October 2003) (copy on file with author).

22 Joost Pauwelyn, 'Trade and Investment Disputes: Complement or Conflict?' (Paper presented at the Annual WTO Conference, British Institute of Comparative and International Law, London, 24 May 2006) 3 <http://www.law.duke.edu/fac/pauwelyn/pdf/NT_trade_and_investments.pdf> at 10 August 2007.

23 Gaetan Verhoosel, 'The Use of Investor-State Arbitration under Bilateral Investment Treaties to Seek Relief for Breaches of WTO Law' (2003) 6 *Journal of International Economic Law* 493, 495.

res judicata exists, its three requirements are not satisfied. For two rulings to be genuinely in conflict, the overlapping proceedings must first involve the same parties; however, disputes under investment treaties are between investors and states, while WTO disputes are solely inter-governmental. Even if the second requirement of the proceedings involving the same subject matter is met, the proceedings will not satisfy the third requirement of involving the same legal claim because claims under WTO rules, FTA services chapters and investment treaties are dissimilar.²⁴

A Measures Taken by States

As a result, some states have taken measures to prevent the incurring of liability for the same measure under both WTO law and investment treaties, as well as under both a FTA services chapter and FTA investment chapter. For example, to prevent re-litigation of the same measure under both WTO law and investment treaty obligations, Article 2005(1) of *NAFTA* explicitly provides that disputes regarding a matter arising under both *NAFTA* and the WTO can be brought to either forum.²⁵ However, Article 2005(6) states that once procedures have been initiated at either forum, the forum selected shall be used to the exclusion of the other.²⁶

The effectiveness of Article 2005 will be tested in two upcoming *NAFTA* claims resulting from the tax measures in *Mexico – Soft Drinks*. It will be interesting to see if the tribunals at the International Centre for the Settlement of Investment Disputes assume jurisdiction over the dispute, since it already has been litigated at the WTO. It is possible that the claimants may argue that their *NAFTA* dispute does not involve the same matter as the WTO dispute because the WTO and *NAFTA* disputes each involve different claimants. Also, the disputes are not based on substantially similar grounds as they involve different legal claims. These arguments are not unlike the arguments used to deny the application of the *res judicata* principle outlined above. To avert this situation, states should consider inserting a similar provision to Article 2005 of *NAFTA*. Further, if states do not wish to expose themselves to potential liability under both forums for a single measure, they should clarify that, *once the same economic interest or investment* is being litigated under one of the forums, litigation in the other forum is precluded even if the claimants and legal claims

24 Joost Pauwelyn, 'Adding Sweeteners to Softwood Lumber: The WTO-NAFTA "Spaghetti Bowl" is Cooking' (2006) 9 *Journal of International Economic Law* 197, 200–1.

25 Article 2005(1) reads:

Subject to paragraphs 2, 3 and 4, disputes regarding any matter arising under both this Agreement and the *General Agreement on Tariffs and Trade*, any agreement negotiated thereunder, or any successor agreement (GATT), may be settled in either forum at the discretion of the complaining Party.

26 Article 2005(6) reads: 'Once dispute settlement procedures have been initiated under Article 2007 or dispute settlement proceedings have been initiated under the GATT, the forum selected shall be used to the exclusion of the other, unless a Party makes a request pursuant to paragraph 3 or 4'.

are dissimilar.²⁷ Of course, it must be conceded that this solution will move the uncertainty to the definition of ‘economic interest’ or ‘investment’, and may not completely solve a *Mexico – Soft Drinks* problem if economic interest or investment is defined narrowly. Nonetheless, this solution may at least provide a semi-effective barrier against a flood of re-litigation.

Similarly, to prevent re-litigation of the same measure under both the services and investment chapters of a FTA, states may want to provide that if the same economic interest or investment is being litigated under one of the chapters, litigation under the other chapter is precluded even if the claimants and legal claims are dissimilar. Some states have taken alternative measures. Article 2 of the *Framework Agreement on the ASEAN Investment Area*²⁸ removes investment in services from the scope of investment disciplines.²⁹ Articles 6.2 and 7.24 of the *Singapore-India Comprehensive Economic Cooperation Agreement*³⁰ (‘CECA’) establish that in case of inconsistencies, precedence is given to the services chapter, while investment disciplines still apply insofar as they affect matters not covered by the services chapter. Under these arrangements, a measure can only potentially breach the provisions in one of the chapters, but never both; thus, preventing re-litigation of the same measure under both chapters. These arrangements are equally viable.

Elsewhere, Article 38 of the *Agreement between the European Free Trade Association States and Singapore*³¹ and Article 26 of the *Agreement between New Zealand and Singapore on a Closer Economic Partnership*³² provide that

27 Marie-France Houde and Katia Yannaca-Small, ‘Relationships between International Investment Agreements’ (OECD Working Paper on International Investment No 2004/1, Organisation for Economic Co-operation and Development Directorate for Financial and Enterprise Affairs, 2004) 13 <<http://www.oecd.org/dataoecd/8/43/31784519.pdf>> at 10 August 2007.

28 Signed 7 October 1998. See ASEAN, *Framework Agreement on the ASEAN Investment Area* (2006), <<http://www.aseansec.org/6466.htm>> at 27 August 2007.

29 Article 2 provides: ‘[t]his Agreement shall cover all direct investments other than; (a) portfolio investments; and (b) matters relating to investments covered by other ASEAN Agreements, such as the ASEAN Framework Agreement on Services’.

30 Signed 29 June 2005 (entered into force 1 August 2005). See Government of India Department of Commerce, *Comprehensive Economic Cooperation Agreement between The Republic of India and the Republic of Singapore* (2006), <http://commerce.nic.in/trade/international_ta_framework_ceca.asp> at 27 August 2007.

31 Entered into force 1 January 2003. See AsianLII, *Agreement between the European Free Trade Association States and Singapore*, <<http://www.asianlii.org/>> at 28 August 2007. EFTA is a free trade area comprising Switzerland, Iceland, Liechtenstein and Norway. Article 38(2) provides: ‘Article 40(1) [which is the national treatment and MFN provision] shall not apply to measures affecting trade in services whether or not a sector concerned is scheduled in Chapter III’. Article 38(3) provides: ‘Article 40(1) shall also not apply to investors of a Party in services sectors and their investments in such sectors. This provision is subject to review after a period of ten years from the date of entry into force of this Agreement, with a view to examining its continued need’.

32 Entered into force 1 January 2001. See CommonLII, *Agreement between New Zealand and Singapore on a Closer Economic Partnership*, <http://www.commonlii.org/sg/other/treaties/2000/1/NZS_agreement.html> at 28 August 2007. Article 26(2) provides: ‘Articles 28, 29 and 30 [which are the MFN and national treatment provisions] shall not apply to any measures affecting investments adopted or maintained pursuant to Part 5 [which is the services chapter] to the extent that they relate to the supply of any specific service through commercial presence as defined in Article 16(n), whether or not they are covered by Annex 2’.

the national treatment and MFN obligations of their investment chapters do not apply to measures affecting commercial presence as governed by their services chapters. This arrangement assumes that the only potential overlaps between the two chapters are in national treatment and MFN. However, this is not the case because, as seen from *Mexico – Soft Drinks*, a measure in breach of national treatment may potentially be seen as ‘expropriatory’ at the same time, which presents another source of overlap.³³ States should, therefore, not emulate this arrangement if they want to preclude re-litigation of the same measure under the two chapters, but instead should opt for the *NAFTA*, *CECA* and *Framework Agreement on the ASEAN Investment Area* approach.

III SECOND CONSEQUENCE: EXTRA AND UNINTENTIONAL RIGHTS FOR INVESTORS

In addition to the previously mentioned initiatives, some states are beginning to take measures to counter undesired expansive trends by arbitration tribunals in some areas of investment law, such as the definition of expropriation, equitable treatment and the ambit of the MFN clause. In relation to all three definitions, States have attempted to make their definitions clearer by providing, for example, more specific guidelines about the content of each concept in their newer investment treaties.

If these measures are effective and are implemented by more and more states, investors may find it increasingly harder to make successful claims under investment law in these areas. To circumvent these developments in investment law, which are unfavourable to their interests, investors may begin to consider suing host states through alternative regimes, such as under WTO law or a FTA services chapter. As a result, states may want to reconsider their commitments under the WTO and the services chapters of their FTAs.

It must be noted that investors have no right of standing in WTO disputes or disputes arising from FTA services chapters because both provide only for inter-state dispute settlement mechanisms.³⁴ This means that the measures described below are only available to private investors, who possess sufficient influence to lobby their governments to initiate state-to-state dispute settlement proceedings at the WTO and under a FTA services chapter.³⁵ Apart from the possibility of

33 In the next part, a possible overlap between a breach of market excess commitments and expropriation is also discussed.

34 Martín Molinuevo, ‘Can Foreign Investors in Services Benefit from WTO Dispute Settlement? Legal Standing and Remedies in WTO and International Arbitration’ (NCCR Trade Regulation Working Paper No 2006/17, Swiss National Centre of Competence in Research, 2006) 14, 27 <<http://www.nccr-trade.org/images/stories/publications/Molinuevo.WTF%20Paper.Final%20Draft.pdf>> at 10 August 2007.

35 See above n 242, 495. Private investors have played significant roles in the preparation, initiation and pursuit of a WTO dispute before. *Japan – Measures Affecting Consumer Photographic Film and Paper*, WTO Doc WT/DS44/R (1998) (Report of the Panel) has been termed the ‘*Kodak – Fuji*’ case to illustrate Kodak’s and Fuji’s industrial interests and involvement in the dispute. Part IV below contemplates the possibility of WTO law being directly applicable to investment treaties. If WTO law can indeed be directly applicable, then investors will be able to claim for breaches of WTO law via investment treaty arbitration.

circumventing unfavourable developments in investment law, recourse to the WTO offers two other advantages over investment arbitration.

First, WTO remedies focus on the removal of inconsistent measures.³⁶ This is a more appealing solution for foreign investors who intend to continue their investment activities in the host state for the long-term because WTO remedies can ensure an appropriate competitive environment in the host state.³⁷ In contrast, investment arbitration only offers the remedy of compensation for damages, and cannot oblige the host state to remove the inconsistent measure causing the investor's loss.³⁸

Second, awards rendered in investment arbitration depend on domestic courts for enforcement. While most investor-to-state arbitration rulings (especially rulings by the International Centre for Settlement of Investment Disputes ('ICSID')) have been honoured by the losing state, it is not inconceivable that in certain situations some domestic courts may delay enforcement or even annul arbitration awards, denying claimants their relief.³⁹ The doctrine of sovereign immunity may also be used to impede enforcement.⁴⁰ On the other hand, under the WTO there is no need to rely on other institutions for the enforcement of rulings.⁴¹ Thus, even if direct investor compensation is not readily available under the WTO regime, investors may be 'incentivised' by these potential

36 See *WTO Agreement*, above n 1, annex 2 (*Understanding on Rules and Procedures Governing the Settlement of Disputes*) 1869 UNTS 401 ('DSU'), arts 3.7, 19. Article 3.7 of the DSU expresses that '[t]he aim of the dispute settlement mechanism is to secure a positive solution to the dispute'. To that end, where a mutually agreed solution between the parties cannot be reached, 'the first objective of the dispute settlement mechanism is usually to secure the withdrawal of the measures concerned if these are found to be inconsistent with the provisions of any of the covered agreements'. Article 19 of the DSU provides: '[w]here a panel of the Appellate Body concludes that a measure is inconsistent with a covered agreement, it shall recommend that the Member concerned bring the measure into conformity with that agreement'.

37 This would be the case, for instance, in service sectors with high entry costs and sunk costs, such as telecommunications, distribution, transport or construction services. Investors in such sectors may see greater relief in the removal of the discriminatory measure because removal may provide them with the possibility of greater earnings in the medium to long-term.

38 Above n 34, 22–4. However, for investors thinking of exiting the host state, compensation will probably be a more useful remedy because, for these investors, it will not really matter whether the inconsistent measure is removed or not.

39 Mark Kantor, 'The Limits of Arbitration' (2004) 1(2) *Transnational Dispute Management* 1, 9.

40 *Convention on the Settlement of Investment Disputes between States and Nationals of Other States*, opened for signature 18 March 1965, 8359 UNTS 159, art 55 (entered into force 14 October 1966): '[n]othing in Article 54 shall be construed as derogating from the law in force in any Contracting State relating to immunity of that State or of any foreign State from execution'.

41 However, it must be pointed out that article 22 of the DSU provides for the suspension of concessions or retaliation as a remedy available to the claimant when the respondent fails to comply with the obligation of bringing its measures into conformity with the WTO agreements. Article 22.3 of the DSU directs that the suspension of concessions be imposed primarily 'with respect to the same sector(s)' as those where the inconsistent measures have been found. The imposition of retaliatory trade sanctions may, theoretically, affect the very same foreign investor that has lobbied for the bringing of the claim because the trade sanctions are imposed against the host state and that foreign investor is based in the host state. This was the situation for the foreign investor in *United States – Measures Affecting the Cross-Border Supply of Gambling and Betting Services*, WTO Doc WT/DS285/AB/R, AB-2005-1 (2005) (Report of the Appellate Body), which is discussed in greater detail below.

advantages to seek an alternative relief, such as a recommendation for compliance via the forum afforded by the WTO.

In any case, even if these two potential advantages are not by themselves significant, if investors are not precluded from taking two bites from the same apple, the possibility of re-litigation to obtain these advantages will be high. I now examine the areas in which recent developments have effected significant change in the legal landscape.

A Expropriation

Generally, there are two main considerations in determining whether a government measure by a host state constitutes an act of indirect expropriation, which has to be compensated for – first, the extent of deprivation of the investor’s property rights; second, whether the government measure is a regulatory measure, which does not amount to an expropriatory act and is, thus, non-compensable.

At international law, the primary consideration for determining if there has been an indirect expropriation is the extent of the adverse impact a government measure has on the foreign investor, specifically the extent of deprivation of his property rights. Allowing for some differences in wording, the majority of arbitral tribunals seem to agree generally on the extent of deprivation required. This is evident in cases such as *SD Myers Inc v Canada*⁴² (*‘SD Myers’*), *Compañía del Desarrollo de Santa Elena SA v Costa Rica*⁴³ (*‘Santa Elena’*), *Técnicas Medioambientales Tecmed SA v Mexico*⁴⁴ (*‘Tecmed’*), *Starrett Housing Corporation v Iran*⁴⁵ (*‘Starrett’*) and *GAMI Investment Inc v Mexico*⁴⁶ (*‘GAMI’*).

42 (2001) 40 ILM 1408. The Tribunal held: ‘An expropriation usually amounts to a lasting removal of the ability of an owner to make use of its economic rights although it may be that, in some contexts and circumstances, it would be appropriate to view a deprivation as amounting to an expropriation, even if it were partial or temporary’: at 1440. Note that in addition to being contained in the *International Legal Materials* (*‘ILM’*), ICSID cases are also published by the University of Cambridge’s Lauterpacht Centre for International Law in *ICSID Reports*; finally links to most cases can be found on the ICSID website <<http://www.worldbank.org/icsid/>> at 27 August 2007.

43 (2000) 39 ILM 1317 (Final Award). The Tribunal held: ‘property has been expropriated when the effect of the measures taken by the state has been to deprive the owner of title, possession or access to the benefit and economic use of his property’: at [77].

44 (2004) 43 ILM 133. The Tribunal held:
[The issue is whether 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 [property] or to its exploitation – had ceased to exist. In other words, if due to the actions of the Respondent, the assets involved have lost their value or economic use for their holder and the extent of the loss: at [115].

45 (Interlocutory Award) (1983) 4 Iran-USCTR 122. Chairman Lagergren held:
it is recognised in international law that measures taken by a State can interfere with property rights to such an extent that these rights are rendered so useless that they must be deemed to have been expropriated, even though the State does not purport to have expropriated them and the legal title to the property formally remains with the original owner: at 154.

46 (2004) 44 ILM 545 (Final Award). The Tribunal held: ‘the affected property must be impaired to such an extent that it must be seen as “taken”’: at [126] (emphasis omitted).

In what has been referred to as the ‘orthodox approach’,⁴⁷ these tribunals hold that an indirect expropriation occurs when the investor is deprived of the fundamental rights of ownership, or effective control of the investment, or, more specifically, the use, benefit, management or enjoyment of all or substantially all of his investment.

However, a line of cases has emerged, which has taken a more expansive approach towards expropriation by requiring a lower extent of deprivation. In the *NAFTA* case of *Metalclad Corporation v United Mexican States*⁴⁸ (*Metalclad*), the tribunal stated that expropriation includes ‘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 reasonably-to-be expected economic benefit of the property’.⁴⁹ While the above mentioned orthodox approach requires a deprivation of the fundamental rights of ownership, all that the *Metalclad* approach apparently requires is that the government measure have deprived the investor of a significant part of its anticipated profits, or significantly affected its business plans. A tribunal taking the more orthodox approach would not equate the deprivation of anticipated profits or adverse impact on business as deprivations of fundamental ownership or effective control. This is clear from the decisions in *Azinian v Mexico*⁵⁰ (*Azinian*) and *Feldman v Mexico*⁵¹ (*Feldman*), where the tribunals stated that not all government measures, which may affect investors’ business plans by making it difficult, impossible or uneconomical for an investor to carry out a particular business, is an expropriation. In *Pope & Talbot, Inc v Canada*⁵² (*Pope & Talbot*), the measures diminished the investor’s profits but the tribunal did not deem this sufficient to constitute indirect expropriation.

Under international law, not all deprivations of property are expropriatory. Under the doctrine of regulatory expropriation, or the exercise of a state’s police

47 Andrew Newcombe, ‘The Boundaries of Regulatory Expropriation in International Law’ (2005) 20(1) *ICSID Review: Foreign Investment Law Journal* 1, 10–11.

48 (2001) 40 ILM 36.

49 Ibid [103].

50 (2000) 39 ILM 527. The Tribunal observed: ‘[i]t is a fact of life everywhere that individuals may be disappointed in their dealings with public authorities ... It may be safely assumed that many Mexican parties can be found who had business dealings with governmental entities which were not to their satisfaction’: at [18] (emphasis omitted).

51 (2003) 42 ILM 625. The Tribunal held: ‘not every business problem experienced by a foreign investor is an indirect or creeping expropriation under Article 1110 [of *NAFTA*]’: at 648.

52 United Nations Commission on International Trade Law (*UNCITRAL*), *Interim Award by Arbitral Tribunal* (26 June 2000) <<http://investmentclaims.com/decisions/Pope-Canada-InterimAward-26June2000.pdf>> at 27 August 2007. The Tribunal held:

Even accepting (for the purpose of this analysis) the allegations of the Investor concerning diminished profits, the Tribunal concludes that the degree of interference with the Investment’s operations due to the Export Control Regime does not [give] rise to an expropriation (creeping or otherwise) within the meaning of Article 1110 [of *NAFTA*]: at [102].

powers,⁵³ a state action that otherwise amounts to a compensable deprivation of property may constitute a regulatory measure, or a legitimate and bona fide exercise of sovereign police powers. This action is non-expropriatory and does not impose an obligation on the state to pay compensation.⁵⁴ While some tribunals such as those in *SD Myers*,⁵⁵ *Feldman*,⁵⁶ *Tecmed*⁵⁷ and *Methanex Corporation v United States of America*⁵⁸ ('*Methanex*') have endorsed this doctrine, other tribunals, such as those in *Metalclad*⁵⁹ and *Pope & Talbot*,⁶⁰

53 According to Daniel Clough, the doctrine regards the government as an agent for the advancement of the interests of its society; hence, the legitimate expectations of foreign investors cannot reasonably contemplate that the government would compromise its role as circumstances change over time: Daniel Clough, 'Regulatory Expropriations and Competition under NAFTA' (2005) 6 *Journal of World Investment and Trade* 553, 563.

54 Section 712 of the Restatement (Third) on the Foreign Relations Law of the US (1987) states:
A state is responsible as for an expropriation of property ... when it subjects alien property to taxation, regulation, or other action that is confiscatory, or that prevents, unreasonably interferes with, or unduly delays, effective enjoyment of an alien's property or its removal from the state's territory ... *A state is not responsible for loss of property or for other economic disadvantages resulting from bona fide general taxation, regulation, forfeiture for crime, or other action of the kind that is commonly accepted as within the police power of states*, if it is not discriminatory ... and is not designed to cause the alien to abandon the property to the state or sell it at a distress price. As under United States constitutional law, the line between 'taking' and regulation is sometimes uncertain (emphasis added): The American Law Institute, *Restatement of the Law (Third) – The Foreign Relations Law of the United States* (1987) vol 2, 200–1.

While the Restatement was written by scholars in the US, it purports to reflect objectively international law rather than US policy, and is occasionally consulted by tribunals. Also, according to Article 10(5) of Louis Sohn's and Richard Baxter's 1961 Draft Convention on the International Responsibility of States for Injuries to Aliens:

An uncompensated taking of property of an alien or a deprivation of the use or enjoyment of property of an alien which results ... from the action of the competent authorities of the State in the maintenance of public order, health, or morality ... shall not be considered wrongful, provided ... it is not a clear and discriminatory violation of the law of the State concerned, ... [and] it is not an unreasonable departure from the principles of justice recognized by the principle legal systems of the world: Louis B Sohn and Richard R Baxter, 'Responsibility of States for the Economic Interests of Aliens' (1961) 55 *American Journal of International Law* 545, 554.

The Iran–US Claims Tribunal has also accepted, as a principle of international law, that a state is not responsible for bona fide regulation that falls within the scope of a generally recognised police power: see *Sedco Inc v National Iranian Oil Company* (1986) 25 ILM 629, 640.

55 The Tribunal observed: '[t]he general body of precedent usually does not treat regulatory action as amounting to expropriation. Regulatory conduct by public authorities is unlikely to be the subject of legitimate complaint under [NAFTA's expropriation provision, art 1110], although the Tribunal does not rule out that possibility': *SD Myers Inc v Canada* (2001) 40 ILM 1408, 1440.

56 The Tribunal stated: 'not all regulatory activity that makes the investment uneconomical is an expropriation': *Feldman v Mexico* (2003) 42 ILM 625, 648.

57 The Tribunal said:
a serious urgent situation, crisis, need or social emergency ... [could be] weighed against the deprivation or neutralization of the economic or commercial value of the Claimant's investment ... [to lead to the conclusion that an otherwise expropriatory regulation does] not amount to an expropriation under the [*Agreement on the Reciprocal Promotion and Protection of Investments signed by the Kingdom of Spain and the United Mexican States*] and international law: *Técnicas Medioambientales Tecmed SA v Mexico*, ICSID Case No ARB(AF)/00/2 (2003) (Award) [139].

58 Final Award of the Tribunal on Jurisdiction and Merits (3 August 2005) pt IV – ch D. I elaborate on this case later.

59 The Mexican Local Government had refused the investor a permit to operate a hazardous waste landfill. The State Government also intended to create an ecological preserve in the area.

apparently had the opportunity to consider the application of this doctrine, but ignored it.

In response to the unexpected consequences and uncertainties arising from the arbitral jurisprudence on expropriation provisions, some states, particularly the US, have reflected on their foreign investment policies, especially, on the appropriate balance between investor protection and regulatory space for themselves. These states have recently attempted to rephrase the expropriation provisions in their newly-concluded treaties⁶¹ so that they are interpreted and applied by tribunals in a manner that accords more with their expectations.

The biggest change comes in the form of an annex on expropriation which all the newer US treaties,⁶² such as the *United States-Chile Free Trade Agreement*,⁶³ *US-Singapore FTA*,⁶⁴ *United States-Australia Free Trade Agreement*,⁶⁵ the 2004 United States Model Bilateral Investment Treaty ('US Model BIT'), and some non-US treaties like the 2004 Canadian Model Bilateral Investment Treaty⁶⁷ and the *CECA*,⁶⁸ contain. According to the expropriation annex, Annex B, in the US Model BIT, the determination of whether a measure constitutes an indirect expropriation requires consideration of three factors – the economic impact of the government action,⁶⁹ 'the extent to which the government action interferes with distinct, reasonable investment-backed expectations',⁷⁰ and 'the character of the government action'.⁷¹ Annex B also provides for a rebuttable presumption that

60 The Tribunal did not consider if the export limits imposed by Canada to implement a Canada-US softwood lumber agreement were regulatory measures.

61 To date, no state appears to have amended the expropriation provisions of an existing treaty.

62 Besides the free trade agreements ('FTAs') mentioned here, the US has since December 2003 concluded FTAs containing similar language with other countries and regions such as Central America (Guatemala, El Salvador, Honduras, Nicaragua and Costa Rica), the Dominican Republic, Bahrain and Morocco. Others underway or planned include FTAs with Colombia, Thailand, the entire American hemisphere (FTAA), Malaysia, Oman, Panama, South Korea, the United Arab Emirates and the South African Customs Union: see Office of the United States Trade Representative, *Bilateral Trade Agreements* <http://www.ustr.gov/Trade_Agreements/Bilateral/Section_Index.html> at 11 August 2007.

63 Signed 6 June 2003. See Office of the United States Trade Representative, *United States-Chile Free Trade Agreement*, <http://www.ustr.gov/Trade_Agreements/Bilateral/Chile_FTA/Final_Texts/Section_Index.html> at 28 August 2007.

64 There is no annex on expropriation in the investment chapter, but the exact same provisions are found in the Exchange of Letters on Expropriation (6 May 2003) <http://www.ustr.gov/assets/Trade_Agreements/Bilateral/Singapore_FTA/Final_Texts/asset_upload_file5_8_4058.pdf> at 11 August 2007, which are binding on the two states.

65 Signed 18 May 2004, [2005] ATS 1, annex 11-B (entered into force 1 January 2005).

66 2004 United States Model Bilateral Investment Treaty, <http://www.ustr.gov/Trade_Sectors/Investment/Model_BIT/Section_Index.html> at 28 August 2007, annex B.

67 2004 Canadian Model Bilateral Investment Treaty, <http://www.international.gc.ca/tna-nac/what_fipa-en.asp#structure> at 28 August 2007, annex B.13(1).

68 CECA, above n 30, Exchange of Letters with Annexes, annex 3 (29 June 2005).

69 2004 United States Model Bilateral Investment Treaty, above n 66, annex B(4)(a)(i), which states: 'the economic impact of the government action [should be considered], although the fact that an action or series of actions by a Party has an adverse effect on the economic value of an investment, standing alone, does not establish that an indirect expropriation has occurred'.

70 Ibid annex B (4)(a)(ii).

71 Ibid annex B (4)(a)(iii).

regulatory measures that are non-discriminatory, and ‘designed and applied to protect legitimate public welfare objectives, such as public health, safety, and the environment, do not constitute indirect expropriations’,⁷² except in rare circumstances;⁷³ thus, effectively mandating tribunals to consider the doctrine of regulatory measures.

While the effectiveness of these new provisions on expropriation remain untested, it may become harder for investors to succeed in expropriation claims under this new regime. Instead of suing for expropriation under an investment treaty, an investor may consider invoking other alternatives. As can be seen from the *Mexico – Soft Drinks* dispute, a discriminatory tax can potentially be an indirect expropriation and a breach of national treatment under *GATT*, at the same time. This is similar to the interaction of market access commitments under the WTO, the services chapters and the prohibition against expropriation under investment law. For example, if a host state implements a non-discriminatory ban on the operation of gambling services within the state, an investor who operates gambling facilities within the state will attempt to claim for an indirect expropriation against the host state by asserting that it has been deprived of the use, benefit and management of all of its investment due to the ban. However, under the newer treaties, tribunals may be more likely to find the measure to be regulatory and non-compensable, thus denying relief to the investor.

As an alternative claim, it could be argued that there has been a breach of market access commitments under the WTO and a FTA services chapter, assuming the host state has indeed made the requisite commitments not to limit market access to the gambling sector in its services schedule. In *US – Gambling*,⁷⁴ the US imposed a ban prohibiting the cross-border supply of gambling and betting services via three US federal laws, namely the *Wire Act of 1961*,⁷⁵ the *Travel Act of 1961*⁷⁶ and the *Illegal Gambling Business Act of 1970*.⁷⁷ The Appellate Body held that such a ban was effectively a quantitative restriction with a zero quota and, hence, constituted a breach of market access commitments under Articles XVI:2(a) and XVI:2(c) of *GATS*.⁷⁸ Thus, following the alternative claim, the ban would be a *prima facie* breach of market access commitments. Of course, the host state would seek to justify its measures under

72 Ibid annex B (4)(b).

73 Ibid.

74 *United States – Measures Affecting the Cross-Border Supply of Gambling and Betting Services*, WTO Doc WT/DS285/AB/R, AB-2005-1 (2005) (Report of the Appellate Body) (*‘US – Gambling’*).

75 18 USC § 1084 (1961).

76 18 USC § 1952 (1961).

77 18 USC § 1955 (1970).

78 *US – Gambling*, above n 74. *GATS* Articles XVI(2)(a) and XVI(2)(c) read:

In sectors where market-access commitments are undertaken, the measures which a Member shall not maintain or adopt either on the basis of a regional subdivision or on the basis of its entire territory, unless otherwise specified in its Schedule, are defined as: (a) limitations on the number of service suppliers whether in the form of numerical quotas, monopolies, exclusive service suppliers or the requirements of an economic needs test; ... (c) limitations on the total number of service operations or on the total quantity of service output expressed in terms of designated numerical units in the form of quotas or the requirement of an economic needs test.

the general exceptions in *GATS*. In this case, the relevant exception would be the public morals exception under Article XIV(a).⁷⁹

However, it must be pointed out that most of the general exceptions are subject to a strict requirement of ‘necessity’, which is seldom proven to the satisfaction of the WTO Panels by the respondent states. In fact, the ‘necessity test’ has only been satisfied in one case, *EC – Asbestos*,⁸⁰ which was perhaps unique as it dealt with a clearly carcinogenic product. Thus, it seems that a claim for breach of market access rules may, if the doctrine of regulatory measures is followed, be a more viable avenue to pursue as it may be more likely to succeed than a claim for indirect expropriation.

B MFN

The arbitral jurisprudence has stated that the applicability of the MFN clause in investment treaties to procedural rights can be limited by ‘public policy considerations’. Some states have begun to do away with the MFN clause altogether in their newer treaties. This could be the beginning of a trend by states of excluding the application of the MFN clause from expropriation and minimum standard of treatment provisions.

This new practice arose out of the fear created in host states by *Maffezini v Spain* (hereinafter ‘*Maffezini*’).⁸¹ In this case, the Tribunal held that the MFN clause in the primary treaty between Argentina and Spain⁸² applied not just solely to provisions offering substantive protection to investments, but also to provisions dealing with dispute resolution.⁸³ However, the tribunal limited the scope of its decision by stating that the MFN clause should not be used to ‘override public policy considerations that the contracting parties may have envisaged as fundamental conditions for their acceptance of the agreement, particularly if the beneficiary is a private investor’.⁸⁴ The Tribunal listed four situations as non-exhaustive⁸⁵ examples of when the clause should not apply –

79 Other exceptions include the maintenance of public order (art XIV(a)); the protection of human, animal or plant life or health (art XIV(b)); the prevention of deceptive and fraudulent practices (art XIV(c)(i)); the protection of the privacy of individuals (art XIV(c)(ii)); and the equitable or effective imposition or collection of direct taxes (art XIV(d)).

80 *European Communities – Measures Affecting Asbestos and Asbestos-Containing Products* WTO Doc WT/DS135/AB/R, AB-2000-11 (2001) (Report of the Appellate Body) (‘*EC – Asbestos*’).

81 (2001) 40 ILM 1129 (Decision of the Tribunal on Objections to Jurisdiction).

82 *Agreement for the Reciprocal Promotion and Protection of Investments between the Kingdom of Spain and Republic of Argentina*, signed 3 October 1991, 1699 UNTS 202 (entered into force 28 September 1992). Article IV of the bilateral investment treaty (‘BIT’) was the MFN clause. It read: ‘[i]n all matters subject to this Agreement, treatment shall not be less favourable than that extended by each Party to the investments made in its territory by investors of a third country’ (unofficial translation from Spanish text). The original Spanish text reads: ‘En todas las materias regidas por el presente Acuerdo, este tratamiento no será menos favorable que el otorgado por cada Parte a las inversiones realizadas en su territorio por inversores de un tercer país’.

83 (2001) 40 ILM 1129 (Decision of the Tribunal on Objections to Jurisdiction), [54].

84 Ibid [62].

85 The Tribunal indicates that the four enumerated situations are non-exhaustive by stating ‘[o]ther elements of public policy limiting the operation of the [MFN] clause will no doubt be identified by the parties or tribunals’: *ibid* [63].

first, where one of the treaty states conditions its consent to arbitration on the exhaustion of local remedies by investors; second, where there is a ‘fork in the road’ provision which requires investors to make a final and irreversible choice of submission to either the local courts or arbitration; third, where there is an express reference to a specific forum such as ICSID; and fourth, where there are express provisions on a ‘highly institutionalized system of arbitration that incorporates precise rules of procedure’,⁸⁶ such as that of *NAFTA*.⁸⁷ *Maffezini* was subsequently endorsed by the Tribunals in the decision on jurisdiction of *Siemens A.G. v Argentina*⁸⁸ (*Siemens*) and *Tecmed*.⁸⁹

There has been a recent backlash against the *Maffezini* approach. In *Plama Consortium Limited v Bulgaria*⁹⁰ (*Plama*), the primary treaty had provided for a specific, albeit limited, form of dispute settlement.⁹¹ The claimant sought to replace the primary treaty’s form of dispute settlement with ICSID arbitration⁹² which was possible using the primary treaty’s MFN clause.⁹³ The Tribunal decided that the MFN clause could not apply to displace the specific dispute settlement arrangements under the primary treaty.⁹⁴ This conclusion could have

86 Ibid.

87 Ibid. See also Locknie Hsu, ‘MFN and Dispute Settlement: When the Twain Meet’ (2006) 7 *Journal of World Investment and Trade* 25, 28.

88 (2005) 44 ILM 138 (Decision on Jurisdiction). The Tribunal stated that even though the MFN clause in the primary treaty here, which applied to ‘treatment’ of ‘investments’ and ‘activities related to the investments’, was narrower formulation than the MFN clause used in the primary treaty in *Maffezini*, applied to ‘all matters subject to this Agreement’, the MFN clause here was nevertheless sufficiently wide to be applicable to dispute settlement arrangements: at [103]. In fact, the Tribunal appeared to go further than *Maffezini* when it said: ‘[i]n fact, the purpose of the MFN clause is to eliminate the effect of specially negotiated provisions unless they have been excepted’: at [106].

89 The Tribunal approved the *Maffezini* ruling but effectively added a fifth exception to the four enumerated in *Maffezini*, by holding that there are certain matters that ‘due to their significance and importance, go to the core of matters that must be deemed to be specifically negotiated by the Contracting Parties’ and ‘cannot therefore be impaired by the principle contained in the most-favoured nation clause’. The Tribunal held that ‘the time dimension of the application of [the BIT’s] substantive provisions’ was one such ‘core’ item. Thus, an MFN clause could not be invoked to give the basic treaty retroactive effect: *Técnicas Medioambientales Tecmed SA v Mexico*, (2004) 43 ILM 133, [69].

90 (2005) 44 ILM 717 (Decision on Jurisdiction).

91 The *Plama* tribunal pointed out that the dispute settlement provision of the primary treaty, art 4 of the *Agreement between the Government of the People’s Republic of Bulgaria and the Government of the Republic of Cyprus on Mutual Encouragement and Protection of Investments* (*Bulgaria–Cyprus BIT*), limited Bulgaria’s consent to arbitration to ad hoc UNCITRAL arbitration ‘with regard to the amount of compensation’ due to an investor only after the merits of the investor’s claims had first been adjudicated ‘through the regular administrative and legal procedure[s] of [Bulgaria]’. For the *Bulgaria–Cyprus BIT* see <http://www.unctad.org/sections/dite/ia/docs/bits/bulgaria_cyprus.PDF> at 4 September 2007.

92 The *Plama* tribunal pointed out that the dispute resolution provisions of other BITs signed by Bulgaria, such as the *Agreement between the Government of the Republic of Finland and the Government of the Republic of Bulgaria on the Promotion and Protection of Investments* (*Bulgaria–Finland BIT*), provide for ICSID arbitration of a broader class of investment disputes. For the *Bulgaria–Finland BIT* see <http://www.unctad.org/sections/dite/ia/docs/bits/finland_bulgaria_eng_fn.pdf> at 4 September 2007.

93 The MFN clause, article 3(1) of the *Bulgaria–Cyprus BIT*, reads: ‘[e]ach Contracting Party shall apply to the investments in its territory by investors of the other Contracting Party a treatment which is not less favourable than that accorded to investments by investors of third states’.

94 The Tribunal explained that

been reached under the *Maffezini* framework because the dispute settlement provision would have been sufficiently specific to fall within the third exception precluding the application of the MFN clause. However, the *Plama* tribunal deliberately started from a different footing.⁹⁵ The Tribunal opined that where a MFN clause is silent on its applicability to dispute settlement, ‘one cannot reason *a contrario* that the dispute settlement provisions must be deemed to be incorporated’.⁹⁶ The Tribunal then proposed its own starting point: ‘a MFN provision in a basic treaty [should] not incorporate by reference dispute settlement provisions ... set forth in another treaty, unless the MFN provision in the basic treaty leaves no doubt that the Contracting Parties intended to incorporate [the other treaty’s provisions].’⁹⁷ Like the approach of the tribunal in *Maffezini*, the emphasis of the *Plama* tribunal remains on giving effect to the intention of the states.

Despite the lack of further clarification of its exact requirements, it appears that under the apparently more conservative ‘no doubt’ test of *Plama*, MFN clauses are unlikely to be applied to dispute settlement as readily as under the *Maffezini* approach. However, the three most recent decisions on the subject, namely *Cammuzzi International S.A. v Argentina*⁹⁸ (*‘Cammuzzi’*), *Gas Natural S.D.G., S.A. v Argentina*⁹⁹ (*‘Gas Natural’*) and the final award of *Siemens*,¹⁰⁰

‘[w]hen concluding a multilateral or bilateral investment treaty with specific dispute resolution provisions, states cannot be expected to leave those provisions to future (partial) replacement by different dispute resolution provisions through the operation of an MFN provision, unless the States have explicitly agreed thereto’: *Plama Consortium Limited v Bulgaria* (2005) 44 ILM 717 (Decision on Jurisdiction) [212].

- 95 Dana H Freyer and David Herlihy, ‘Most-Favored-Nation Treatment and Dispute Settlement in Investment Arbitration: Just How “Favored” is “Most-Favored”?’ (2005) 20(1) *ICSID Review: Foreign Investment Law Journal* 58, 77.125.
- 96 *Plama Consortium Limited v Bulgaria* (2005) 44 ILM 717 (Decision on Jurisdiction) [203]. The Tribunal noted that it ‘was puzzled as to what the origin of [*Maffezini*’s] “public policy considerations” [was]’: at [221]. The Tribunal observed that the potential exceptions to *Maffezini*’s approach would ‘take away much of the breadth of the preceding observations made by the tribunal in [that case]’: at [221].
- 97 *Ibid* [223].
- 98 ICSID Case No ARB/03/7 (2005) (Decision of the Arbitration Tribunal on Exceptions to Jurisdiction). Although the MFN clause in the primary treaty did not explicitly refer to dispute settlement, the Tribunal, nonetheless, gave the clause the same effect accorded to the MFN clauses in *Maffezini* and *Siemens*. The Tribunal held that ‘[c]onsistent with the most-favoured nation clause (in article 4 of the *Agreement between the Republic of Argentina and the Belgian–Luxembourgish Economic Union for the Reciprocal Promotion and Protection of Investment*, (*‘Luxembourg–Argentina BIT’*)), invoked by *Cammuzzi* and applicable in the present case ... the Claimant may resort directly to arbitration, without having to comply with [the 18 month waiting period in the *Luxembourg–Argentina BIT*]’: at [34(iii)] (citing unofficial translation of the decision in Freyer and Herlihy, above n 95, 79). The Tribunal did not consider the ‘no doubt’ test adopted in *Plama*.
- 99 ICSID Case No ARB/03/10 (2005) (Decision of the Tribunal on Preliminary Questions of Jurisdiction). The Tribunal held: ‘[u]nless it appears clearly that the state parties to a BIT or the parties to a particular investment agreement settled on a different method for resolution of disputes that may arise, most-favoured-nation provisions in BITS should be understood to be applicable to dispute settlement’: at [49]. This is an adoption of the *Maffezini* starting point.
- 100 (2005) 44 ILM 138 (Final Award). The Tribunal distinguished *Plama* as a situation where the Tribunal faced extensions of the MFN clause to situations widely different from the facts considered by the tribunals in the present case, and in *Maffezini* or *Gas Natural*. According to the Tribunal :

have all sided with the *Maffezini* approach. While the *Maffezini* approach appears to be in the ascendency, the arbitral jurisprudence on this issue cannot yet be deemed as settled. Given this, some states have taken more concrete measures to ensure that MFN clauses operate according to their expectations as far as possible in the following ways.

First, some states have pre-empted unwanted extensions of the MFN standard by determining, beforehand, if the MFN clause is to apply to dispute settlement. States ensure that their MFN clauses expressly include or exclude dispute settlement provisions to remove all uncertainty.

Second, some states insert what some negotiators call a ‘disappearing footnote’, such as the disappearing footnote in the draft of the Free Trade Area of the Americas (‘FTAA’), which expressly explains whether a MFN clause includes or excludes dispute settlement.¹⁰¹ The footnote is subsequently removed from the final treaty text, but remains in the negotiating history of the treaty for future reference.¹⁰²

Third, some states provide for specific dispute settlement arrangements in their treaties. Specific arrangements are less likely to be overridden via the MFN clause as they will probably fall under one of the four exceptions of the *Maffezini* approach.

Fourth, some states, like Australia and India, have, respectively, in the *Singapore-Australia FTA* and *CECA*, elected to omit the MFN clause altogether, as they did with the minimum standards provision.

However, even if the ‘MFN door’ is being shut in certain areas under the investment treaty regime, the door remains ajar in the context of the WTO rules because *GATS* still mandates MFN treatment from Members without those limitations which have been created under investment law. Article II of *GATS*,

In *Plama*, there was no ICSID clause in the basic treaty. There had never been any question that the parties to these proceedings agreed to ICSID jurisdiction and the issue was avoidance, through the MFN clause, of a procedural requirement that Argentina has consistently dispensed within the investment treaties it has concluded since 1994: at [68].

101 This technique was highlighted by the tribunal in *Plama*: see *Plama Consortium Limited v Bulgaria* (2005) 44 ILM 717 (Decision on Jurisdiction) [202]. Footnote 13 to the Third Draft Agreement of the Free Trade Area of the Americas (21 November 2003) reads:

Note: One delegation proposes the following footnote to be included in the negotiating history as a reflection of the Parties’ shared understanding of the Most-Favored-Nation Article and the *Maffezini* case. This footnote would be deleted in the final text of the Agreement:

The Parties note the recent decision of the arbitral tribunal in the *Maffezini (Arg) v Kingdom of Spain*, which found an unusually broad most favored nation clause in an Argentina–Spain agreement to encompass international dispute resolution procedures. See Decision on Jurisdiction §§ 38–64 (January 25, 2000), reprinted in (2002) 16 *ICSID Review: Foreign Investment Law Journal* 212. By contrast, the Most-Favored-Nation Article of this Agreement is expressly limited in its scope to matters “with respect to the establishment, acquisition, expansion, management, conduct, operation, and sale or other disposition of investments”. The Parties share the understanding and intent that this clause does not encompass international dispute resolution mechanisms such as those contained in Section C.2.b (Dispute Settlement between a Party and an Investor of Another Party) of this Chapter, and therefore could not reasonably lead to a conclusion similar to that of the *Maffezini* case.

102 Hsu, above n 87, 35–6.

the MFN provision, requires that, with respect to measures ‘affecting trade in services’, a state accords to ‘services or service suppliers of [another state] treatment no less favourable’ than it accords to those of any other state.

In its investment treaties with some states, a state may offer more favourable terms and arrangements regarding trade in services to the investors of those states. These investors should be considered ‘like service suppliers’ to service suppliers from other countries outside of these investment treaties and should be treated no more favourably than other service suppliers in other trade treaties with an MFN provision such as the *GATS*.¹⁰³ More favourable terms could include better protection via expropriation provisions, additional dispute settlement options¹⁰⁴ and the minimum standard of treatment provisions offered to other states. In such a situation, investors may rely on the MFN clauses in *GATS*, just as they would with a MFN clause in a primary investment treaty, to argue that they are entitled to import more favourable terms from a secondary investment treaty.

In defence, host states could argue that the regional integration exception in Article V of *GATS* operates to justify the exemption of discriminatory and preferential treatment granted in an investment treaty to like service suppliers from MFN obligations. A state can successfully invoke Article V:1 if it can show that the investment treaty in question has ‘substantial sectoral coverage’ and ‘provides for the absence or elimination of substantially all discrimination ... through: (i) elimination of existing discriminatory measures, and/or (ii) prohibition of new or more discriminatory measures’.

Regarding the first ‘substantial sectoral coverage’ requirement, the footnote to Article V provides: ‘[t]his condition is understood in terms of number of sectors, volume of trade affected and modes of supply. In order to meet this condition, agreements should not provide for the *a priori* exclusion of any mode of supply’. This would probably mean that standalone BITs, which cover only at most supply of services by commercial presence (mode three), cannot be said to have substantial sectoral coverage because the BIT does not cover the remaining three modes of supply. On the other hand, for FTAs, which contain an investment and a services chapter, it is likely that the two chapters can be analysed together such that if the combined effect of both chapters is to substantially cover the requisite service sectors, volume of trade and service modes, the first requirement will be satisfied.¹⁰⁵

Regarding the second requirement of ‘absence or elimination of substantially all discrimination’, opinion is divided between WTO Members over whether the phrase ‘and/or’ requires states to establish both the elimination of existing

103 This is a requirement of the MFN provision in article II of *GATS*, which also requires that treatment be ‘no less favourable’.

104 Offering investors of a country additional dispute settlement options, in the form of international arbitration, represents discriminatory action against other countries not offered such options because it upsets the equality of competitive opportunities for investors: Federico Ortino and Audley Sheppard, ‘International Agreements Covering Foreign Investment in Services: Patterns and Linkages’ in Lorand Bartels and Federico Ortino (eds), *Regional Trade Agreements and the WTO Legal System* (2006) 201, 210.

105 *Ibid* 212.

discriminatory measures *and* the prohibition of new or more discriminatory measures,¹⁰⁶ or merely either.¹⁰⁷ The latter interpretation would mean that the second requirement would be relatively easy to satisfy because all a state would have to do is prohibit new discriminatory measures in its investment treaty. If the former interpretation is adopted, attention would shift to the exact requirements of eliminating ‘substantially all’ discrimination.

In interpreting the term ‘substantially all’, under the regional integration exception under Article XXIV:8 of *GATT*, the only guidance comes from the Appellate Body in *Turkey – Textiles*,¹⁰⁸ which held that ‘substantially all’ trade involves some flexibility, and is not the same as ‘all’ the trade, but considerably more than ‘some’ of the trade.¹⁰⁹ This interpretation does not go very far in resolving the ambiguity. Two possible approaches may be applied to interpret ‘substantially all’. The quantitative approach involves putting a number to the percentage of trade among the FTA members. While arbitrary, this approach allows negotiations to move out of deadlock and provides a clear rule of thumb.¹¹⁰ However, proponents of the other approach, the qualitative approach, dismiss the quantitative approach because it allows for the exclusion of major sectors, which they deem contrary to the spirit of Article XXIV and *GATT*.¹¹¹ Perhaps a combination of both approaches is worth considering – ‘substantially all trade’ is to be determined by a quantitative percentage of trade with an added requirement that no major sector be excluded. Alternatively, a case-by-case approach may be taken, relying on jurisprudential development through the accumulation of a sufficient body of case law to clarify the term.¹¹²

In conclusion, it is likely that WTO Members cannot rely on Article V of *GATS* to avoid a breach of *GATS* or, alternatively, to prevent the MFN clause in *GATS* from applying to more favourable import provisions in a BIT. Whether ‘and/or’ is interpreted to be conjunctive or disjunctive, or however liberally ‘substantially all’ is interpreted, an agreement with such a narrow scope will not be able to meet the standards of any interpretation of Article V. Nevertheless, states may succeed in avoiding a *GATS* breach where a FTA contains substantive investment and services chapters.

106 This would involve interpreting ‘and/or’ in such a way that both components are seen as options to be judged as appropriate against the circumstance of the sector being considered, and not as alternatives to be freely chosen by the parties to the investment treaty.

107 Peter van den Bossche, *The Law and Policy of the World Trade Organization: Text, Cases and Materials* (2005) 664.

108 *Turkey – Restrictions on Imports of Textile and Clothing Products*, WTO Doc WT/DS34/AB/R, AB-1999-5 (1999) (Report of the Appellate Body) (‘*Turkey – Textiles*’).

109 *Ibid* [48].

110 *Committee on Regional Trade Agreements: Communication from Australia*, WTO Doc WT/REG/W/22/Add.1 (1998).

111 *Ibid*; *Working Party Report on EEC – Agreements with Finland*, GATT BISD 29th Supp, 77 (1983) [12].

112 Sungjoon Cho, ‘Breaking the Barrier Between Regionalism and Multilateralism: A New Perspective on Trade Regionalism’ (2001) 42 *Harvard International Law Journal* 419, 443.

C Fair and Equitable Treatment

Article VI:1 of *GATS* requires Members to ‘ensure that all measures of general application affecting trade in services are administered in a reasonable, objective and impartial manner’. While there is no direct case law dealing with this provision, in *EC – Bananas*¹¹³ the Appellate Body held that Article X:3(a) of *GATT*, which is the *GATT* equivalent of Article VI:1 of *GATS*, had ‘identical coverage’ as Article 1.3 of the *Agreement on Import Licensing Procedures*.¹¹⁴ The latter provided that ‘[t]he rules for import licensing procedures shall be neutral in application and administered in a *fair and equitable* manner’.¹¹⁵ Thus, it is possible to read Article VI:1 of *GATS* as equating more or less to the fair and equitable requirement in investment treaties.¹¹⁶ In the future, claims may therefore be made under Article VI:1 as an alternative to the fair and equitable treatment provisions in investment treaties, especially if the newer investment treaties attempt to limit the scope of the fair and equitable standard of treatment in investment law.

Article III of *GATS* contains transparency requirements requiring Members to publish all measures of general application affecting trade in services. Since it is not established that the fair and equitable treatment provisions in investment treaties require host states to ensure transparency for investors, investors might resort to Article III to access measures affecting them.

IV THIRD CONSEQUENCE: DIRECT APPLICABILITY OF WTO LAW TO INVESTMENT TREATIES

The international minimum standard of treatment provisions in some investment treaties, such as Article 1105 of *NAFTA*, provide for ‘treatment in accordance with *international law*’.¹¹⁷ It is possible that this part of the provision should be given an expansive interpretation such that the provision is taken to mean any favourable treatment that can be found in any source of international law, including international agreements such as the WTO agreements.¹¹⁸ The result is that investors may claim that a breach of a standard provided in another

113 *European Communities – Regime for the Importation, Sale and Distribution of Bananas* WTO Doc WT/DS27/AB/R, AB-1997-3 (1997) (Report of the Appellate Body) (*‘EC – Bananas’*).

114 *WTO Agreement*, above n 1, annex 1A (*Agreement on Import Licensing Procedures*) 1868 UNTS 436.

115 *EC – Bananas*, above n 119, [203] (emphasis added). The Appellate Body noted the difference in wording between article 1.3 of the *Agreement on Import Licensing Procedures* and article X:3(a) of *GATT*, but decided that ‘the two phrases [were], for all practical purposes, interchangeable’.

116 Priscilla M F Leung and Guiguo Wang, ‘State Contracts in the Globalized World’ (2006) 7 *Journal of World Investment and Trade* 829, 854.

117 Emphasis added.

118 For the sources of international law see article 38(1) of the *Statute of the International Court of Justice*, 26 June 1945, 33 UNTS 993. Article 38(1) provides:

The Court, whose function is to decide in accordance with international law such disputes as are submitted to it, shall apply: (a) international conventions, whether general or particular, establishing rules expressly recognized by the contesting states; (b) international custom, as evidence of a general practice accepted as law; (c) the general principles of law recognized by civilized nations; (d) subject to the provisions of Article 59, judicial decisions and the teachings of the most highly qualified publicists of the various nations, as subsidiary means for the determination of rules of law.

international agreement, such as a WTO agreement, amounts to a breach of the minimum standard provision in the investment treaty.¹¹⁹ Indeed, the separate, concurring opinion of *SD Myers* appears to support this interpretation, albeit in dicta, when the arbitrator opined:

The interpretation and application of Article 1105 must ... take into account the letter or spirit of widely, though not universally, accepted international agreements like those in the WTO system ... This line of argument ... gives reasonable value and meaning to all of the words of Article 1105 of *NAFTA*. It invites interpreters of Article 1105 to look to the 'state of the art' in international trade agreements to determine the content of the minimum international standard, rather than relying on personal subjective notions of what is 'fair', 'equitable' or 'full protection and security'.¹²⁰

Such an expansive approach towards the international minimum standard of treatment is possible because some arbitral tribunals have displayed an expansionary attitude in defining the elements of standard of treatment. For instance, denial of justice¹²¹ was identified in *LFH Neer (USA) v Mexico*¹²² ('*Neer*') as being part of the standard. The Tribunal held that in order to constitute a denial of justice, a government's conduct must amount to an outrage, bad faith, wilful neglect of duty, or insufficiency of government action so far short of international standards that every reasonable and impartial man would recognise its insufficiency.¹²³

Indeed, *Loewen Group Inc and Raymond L Loewen v United States of America*¹²⁴ ('*Loewen*') demonstrates the potential ramifications of a claim of denial of justice. The case involved a Canadian investor claiming that a civil case ruling against it by a jury in a Mississippi state court, and the consequent requirement that a hefty bond be posted in order to appeal, which the investor could not afford and alleged was excessive, constituted a denial of justice which violated both the international minimum standard of treatment and the standard of fair and equitable treatment. Although the case was dismissed on jurisdictional grounds,¹²⁵ the Tribunal went on to determine, as obiter dicta, that the trial and its verdict breached both standards of treatment.¹²⁶ This dicta clearly indicates that the Tribunal believed itself competent to rule upon the fairness and

119 George S Akpan, 'The Investment Provisions of the United States–Singapore Free Trade Agreement and the NAFTA – Old Wine in a New Skin or Something Else?' (2005) 6 *Journal of World Investment and Trade* 873, 882–3.

120 *SD Myers Inc v Canada* (2001) 40 ILM 1408, 1482, 1485.

121 Even so, the Tribunal conceded that denial of justice was, nevertheless, a vague concept: *ibid* 61.

122 (1926) 4 Reports of International Arbitral Awards 60.

123 *Ibid* 60–1. In this case, denial of justice as an element of the standard of treatment arose in the context of the abuse of the physical security of the alien. It was not grafted into the context of protecting foreign investment property until recently in cases like *Case Concerning Elettronica Sicula S.p.A (ELSI) (United States of America v Italy)* [1989] ICJ Rep 15, which further clarifies that it is not the misapplication of a rule of law which would engage a state's responsibility, but the violation of *the* rule of law. See above n 6, 340.

124 (2003) 42 ILM 811 (Award). The Tribunal held that 'a claim alleging an appropriation in violation of Article 1110 [the expropriation provision] can succeed only if Loewen [the investor] establishes a denial of justice under Article 1105 [the minimum standard of treatment provision]': at [141].

125 *Ibid* [1].

126 *Ibid* [39].

legitimacy of a domestic court ruling after local remedies have been exhausted.¹²⁷ It is unlikely that any state would intend that standard of treatment provisions serve as a means for investors to challenge civil verdicts or legitimate rules of civil procedure, such as the requirement to post a surety bond on appeal, and for an unelected international trade body to review their validity. This would probably constitute an unacceptable ceding of sovereignty for most states.¹²⁸

In *SD Myers*, the Tribunal ruled that a violation of the national treatment standard meant a violation of the minimum standard.¹²⁹ If this is indeed the case, states might wonder if there is actually any point in drafting a national treatment provision if the minimum standard provision already covers it. The Tribunal was later criticised by US State Department lawyers as having misinterpreted the minimum standard provision.¹³⁰

In response to the expansive attitudes of some of the above mentioned *NAFTA* tribunals, the *NAFTA* States, using the Free Trade Commission, issued an interpretation of Article 1105.¹³¹ This interpretation, along with the provisions in more recent treaties, has clarified that a breach of a provision of a separate international agreement does not establish a breach of Article 1105(1), and that ‘international law’ in the minimum standard provision means ‘customary international law’. As affirmed in the post-interpretation case of *Mondev International Ltd v United States of America*,¹³² this will expressly exclude the possibility of importing WTO rules and other international agreements into investment activities via the minimum standard provision because customary international law does not include international agreements.

127 H Hamner Hill, ‘*NAFTA* and Environmental Protection: The First 10 Years’ (2006) 6 *Journal of the Institute of Justice and International Studies* 157, 168.

128 *Ibid* 167.

129 *SD Myers Inc v Canada* (2001) 40 ILM 1408, 1438. The Tribunal held that ‘on the facts of this particular case the breach of Article 1102 [the national treatment provision] essentially establishes a breach of Article 1105 as well’: at 1438. The Tribunal justified its conclusion in part by asserting that the international minimum standard was considered broader in scope than the national treatment obligation, but then refused to rule out the possibility that there could be circumstances in which a denial of national treatment ‘would not necessarily offend’ the minimum standard provision: at 1438.

130 See Mark Clodfelter, ‘US State Department Participation in International Economic Dispute Resolution’ (2001) 42 *South Texas Law Review* 1273, 1282, where he comments that *SD Myers* ‘interpreted Article 1105’s minimum standard of treatment in a way we think is at odds with the provision’.

131 This is allowed for by article 2001, which establishes a Free Trade Commission comprising representatives from each *NAFTA* State. The Commission is empowered to resolve disputes arising from the interpretation or application of *NAFTA*. Article 1131(2) also provides that ‘[a]n interpretation by the [Free Trade] Commission of a provision of this Agreement shall be binding on a Tribunal [which is established by article 1131(1)]’.

132 42 ILM 85 (2003) (Award). The Tribunal held that the interpretation makes it clear that Article 1105(1) refers to a standard existing under customary international law, and not to standards established by other treaties of the three *NAFTA* parties. There is no difficulty in accepting this as an interpretation of the phrase ‘in accordance with international law’. Other treaties potentially concerned have their own systems of implementation. ... If there had been an intention to incorporate by reference extraneous treaty standards in Article 1105 and to make Chapter 11 arbitration applicable to them, some clear indication of this would have been expected. Moreover the phrase ‘Minimum standard of treatment’ has historically been understood as a reference to a minimum standard under customary international law, whatever controversies there may have been over the content of that standard: at [121].

However, this may not be the case for other treaties that are still phrased similarly to Article 1105 of *NAFTA*. For instance, Article II(2) of the *Treaty between the Government of the United States of America and the Government of the Republic of Panama Concerning the Treatment and Protection of Investments*¹³³ states:

Investment of nationals and companies of either Party shall at all times be accorded fair and equitable treatment and shall enjoy full protection and security in the territory of the other Party. The treatment, protection and security of investment shall be in accordance with applicable national laws and *international law*.¹³⁴

Similarly, Article II(3) of the *Treaty between the United States of America and the People's Republic of Bangladesh Concerning the Reciprocal Encouragement and Protection of Investment*¹³⁵ and Article II(2)(a) of the *Treaty between the United States Of America and the Democratic Socialist Republic of Sri Lanka Concerning the Encouragement and Reciprocal Protection of Investment*¹³⁶ contain very similarly worded provisions.

Under these treaties, it still remains possible for investors to argue that breach of international agreements, such as a WTO agreement, constitute a breach of the minimum standard of treatment in accordance with *international law*.¹³⁷ This would mean breaches of WTO law would be covered under the investment treaty, which in turn would mean investors would have standing to sue host states for breaches of WTO law directly. This is because investors would be able to use investment treaty arbitration without the need to lobby their home states to initiate inter-state dispute proceedings under the WTO. Consequently, it would become easier for investors to invoke WTO law to gain additional rights unintended by the host state. Hence, states may want to consider clarifying the exact scope of the minimum standard provision in their treaties.

V CONCLUSION

Foreign investment is a necessary factor of production today as it is a major source of capital for many states. States have, therefore, sought to attract this capital through entry into BITs, FTAs and the WTO. The interaction of each instrument's respective rules and obligations could potentially create opportunities for re-litigation and multiple claims in different forums for a single measure taken by a state. The existence of all the different investment facilitation instruments also creates situations where obligations are carried over from other agreements by a MFN clause or a minimum treatment clause. States should, therefore, be aware of this issue. Where they deem it appropriate states should clarify the textual content of these agreements so as to minimise the unexpected

133 Signed 27 October 1982, (entered into force 30 May 1991). See UNCTAD, <http://www.unctad.org/sections/dite/ia/docs/bits/us_panama_1982.pdf> at 28 August 2007.

134 Emphasis added.

135 Signed 12 March 1986, (entered into force 25 July 1989). See UNCTAD, <http://www.unctad.org/sections/dite/ia/docs/bits/us_bangladesh.pdf> at 28 August 2007.

136 Signed 20 September 1991, (entered into force 1 May 1993). See UNCTAD, <http://www.unctad.org/sections/dite/ia/docs/bits/us_srilanka.pdf> at 28 August 2007.

137 Above n 23, 502–3.

and unintentional consequences of such an interaction. Such clarifications, while not full proof and subject to the interpretations of the particular dispute settlement forum, would doubtless go some way towards avoiding and delimiting an over-inclusive synthesis of overlapping obligations caused by the unexpected interaction between the various rules and obligations.