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I. Introduction

With newly emerging issues in legal scholarship regarding the effective protection of human rights, the role of human rights in investment treaty arbitration has become exceedingly important.[1] However, beyond reflecting an academic interest, or even a certain pro-human rights ideology, the question of this role is a pragmatic international issue, which arose in the framework of a number of well-known investment law arbitrations.[2] These proceedings generally have involved investors alleging breach of an investment treaty by the host state, arising from state action or policies intended to protect or promote the human rights of the host states' population.[3]

From an international law standpoint, such situations raise

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[1] For a collection of papers on this question, see generally RÉMI BACHAND & STÉPHANIE ROUSSEAU, INT'L CTR. FOR HUMAN RIGHTS AND DEMOCRATIC DEV., INTERNATIONAL INVESTMENT AND HUMAN RIGHTS: POLITICAL AND LEGAL ISSUES 1 (2003), *available at* http://www.dd-rd.ca/site/_PDF/publications/globalization/bachandRousseauEng.pdf; PIERRE-MARIE DUPUY, ERNST-ULRICH PETERSMANN & FRANCESCO FRANCIONI, HUMAN RIGHTS IN INTERNATIONAL INVESTMENT LAW AND ARBITRATION (2009); LUKE ERIC PETERSON, INT'L CTR. FOR HUMAN RIGHTS AND DEMOCRATIC DEV., HUMAN RIGHTS AND BILATERAL INVESTMENT TREATIES–MAPPING THE ROLE OF HUMAN RIGHTS LAW WITHIN INVESTOR STATE ARBITRATION 8 (2009); Marc Jacob, *International Investments Agreements and Human Rights*, *in* I.N.E.F. RESEARCH PAPER SERIES: HUMAN RIGHTS, CORPORATE RESPONSIBILITIES AND SUSTAINABLE DEVELOPMENT 6 (Mar. 2010), *available at* http://www.humanrights-business.org/files/international_investment_agreements_and_human_rights.pdf; Ursula Kriebaum, *Privatizing Human Rights: The Interface Between International Investment Protection and Human Rights*, *in* THE LAW OF INTERNATIONAL RELATIONS: LIBER AMICORUM HANSPETER NEUHOLD 165-189 (Ursula Kreibaum & August Reinisch eds., 2007); Laura Liberti, *Investissements et droits de l'homme*, *in* NEW ASPECTS OF INTERNATIONAL INVESTMENT Law 791 (P. Kahn & T. Wälde eds., 2007); Bruno Simma & Theodore Kill, *Harmonizing Investment Protection and International Human Rights: First Steps Towards a Methodology*, *in* INTERNATIONAL INVESTMENT LAW OF THE 21ST CENTURY 678 (Christina Binder et al. eds., 2009).

[2] *See, e.g.*, Suez, Sociedad General de Aguas de Barcelona S.A. v. Arg., ICSID Case No. ARB/03/19, Decision on Liability (July 30, 2010), *available at* http://italaw.com/documents/SuezVivendiAWGDecisiononLiability.pdf; Aguas del Tunari S.A. v. Republic of Bol., ICSID Case No. ARB/02/3, Decision on Respondents Objections to Arbitration (Oct. 21, 2005), *available at* http://icsid.worldbank.org/ICSID/Frontserlet?requesttype=GenCase; Metalclad Corp.v. Mex., ICSID Case No. ARB (AF)/97/1, Award, (Aug. 30, 2000), *available at* http://naftaclaims.com/Disputes/Mexico/MetalcladFinalAward.pdf.

[3] In these cases, the activities of investors appeared to threaten and even damage the human rights of the population, especially in relation to the population's need for sanitation and water. *See, e.g.*, Suez v. Argentina, ICSID Case No. ARB/03/19; Aguas del Tunari v. Bol., ICSID Case No. ARB/02/3; Metalclad Corp. v. Mex., ICSID Case No. ARB(AF)/97/1.

certain legal questions regarding: (1) the responsibility of the investor for breach of human rights committed in the frame of investment activities; (2) the responsibility of the home state for demonstrating lack of diligence—i.e., failing to fight human rights abuses by its own investors;[4] and (3) the responsibility of the host state for breaching its obligations under investment and/or human rights law.[5]

However, if one examines the same issue from the perspective of contemporary investment law, most of these questions become irrelevant. Indeed, it is common knowledge among investment lawyers that investment treaties—bilateral (BIT) or multilateral (MIT)—place no obligation on investors or on their respective home states.[6] In principle, investment treaties create obligations only for the host state.[7] Furthermore, conventional references to

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4 For instance, Francioni contends that the home state may be held responsible for the activities of the investor for the pollution of the environment as well as the violation of human rights. *See* Francesco Francioni, *Exporting Environmental Hazard through Multinational Enterprises: Can the State of Origin be Held Responsible?*, *in* INTERNATIONAL RESPONSIBILITY FOR ENVIRONMENTAL HARM 279-80 (Francesco Francioni & Tullio Scovazzi eds., 1991) [hereinafter Francioni, *Exporting*]; *see also* Francesco Francioni, *Alternative Perspectives on International Responsibility for Human Rights Violations by Multinational Corporations*, *in* ECONOMIC GLOBALISATION AND HUMAN RIGHTS 245, 297 (Wolfgang Benedek, Koen De Feyter & Frabrizio Marella eds., 2007) [hereinafter Francioni, *Alternative*]; Robert McCorquodale, *Spreading Weeds Beyond their Garden: Extraterritorial Responsibility of States for Violations of Human Rights by Corporate Nationals*, 100 AM. SOC'Y INT'L L. PROC. 95, 96 (2006); Dinan Shelton, *Protecting Human Rights in a Globalized World*, 25 B.C. INT'L & COMP. L. REV. 273, 273-74 (2002); Vassilis P. Tzevelekos, *In Search of Alternative Solutions: Can the State of Origin be Held Internationally Responsible for Investors, Human Rights Abuses That Are Not Attributable to It*, 35 BROOK. J. INT'L L. 155, 157 (2010).

5 *See* Francioni, *Alternative*, *supra* note 4, at 288-97 (analyzing situations where investment-arbitration implicates human rights law).

6 *See* JESWALD W. SALACUSE, THE LAW OF INVESTMENT TREATIES 194 (2009).

7 *See* *Investment Treaty Arbitration: Protecting and Promoting Foreign Investments*, ALLEN & OVERY, L.L.P. 3 (2010), *available at* http://www.allenovery.com/AOWeb/binaries/50590.pdf ("BITs create legal obligations owed by the Host State to the foreign investor" and "allow foreign investors to enforce these obligations directly against the host state."); *see also* Frances Aldson, *Biwater v. Tanzania: Do Corporations have Human Rights and Substantive Development Obligations Stemming from Private Sector Involvement in Natural Resource Provision?*, 18 ENV. LIABILITY 58, 62 (2010), *available at* http://soas.academia.edu/FrancesAldson/Papers/259939/Biwater_v_Tanzania_Do_corporations_have_human_rights_and_sustainable_development_obligations_stemming_from_private_sector_involvement_in_natural_resource_provision.

human rights in such treaties are rather unusual.[8] Among the rare investment treaties that do so, human rights are addressed in two different ways. First, certain treaty clauses, such as Article 1114(1) of the North American Free Trade Agreement (NAFTA), allow a host state under its respective regimes to enact measures aimed at protecting human rights.[9] However, such measures are only allowed to the extent that they are consistent with the terms of the investment treaty.[10] Second, other treaty clauses provide that the provisions of the investment treaty do not limit the regulatory power of states regarding the protection of human rights. Article 10(1) of the Canadian BIT Model provides such an example;[11] however, this remains an exception.[12] Most investment conventions are silent on the issue of human rights. Arbitrators are expected to deal with this gap following their usual reasoning and means of interpretation within the limits of their jurisdiction.[13]

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8 *See e.g.*, Aldson, *supra* note 7, at 62 (setting out elements of a BIT as protection against expropriation, fair and equitable treatment, etc.; however, human rights obligations were not among them).

9 *See, e.g.*, North American Free Trade Agreement, U.S.-Can.-Mex., art. 1114(1), Dec. 17, 1992, 32 I.L.M. 289 (1993) [hereinafter NAFTA].

10 *See id.* Nothing in this Chapter [11] shall be construed to prevent a Party from adopting, maintaining or enforcing any measure *otherwise consistent with this Chapter* that it considers appropriate to ensure that investment activity in its territory is undertaken in a manner sensitive to environmental concern. *Id.* (emphasis added).

11 The Canadian Model BIT provides that:

> Subject to the requirement that such measures are not applied in a manner that would constitute arbitrary or unjustifiable discrimination between investments or between investors, or a disguised restriction on international trade or investment, nothing in this Agreement shall be construed to prevent a Party from adopting or enforcing measures necessary: (a) to protect human, animal or plant life or health.

Model Agreement for the Promotion and Protection of Investments, art. 10(1) (2004) (Can.), *available at* http://italaw.com/documents/Canadian2004-FIPA-model-en.pdf.

12 Though shelved for the moment, the 2007 Norwegian Draft Model BIT provides that a joint committee is set up for purposes, which among others "where relevant, discuss issues related to corporate social responsibility, the preservation of the environment, public health and safety, the goal of sustainable development, anticorruption, employment and human rights." Model Agreement Between the Kingdom of Norway and . . . for the Promotion and Protection of Investments, art. 23(3)(viii) (2007) (Nor.).

13 *See generally* SALACUSE, *supra* note 6 (discussing how neither BIT nor MIT places a particular obligation on the states).

In light of these characteristics, it is easy to understand that arbitration tribunals lack the competence to rule on the responsibility of the investor for human rights law violations. In investment treaty arbitration, arbitral jurisdiction stems from investment treaties[14] and is, therefore, controlled by the content of the treaties.[15] Investment arbitration cannot rule over claims other than those related to investment law.[16] Nonetheless, the principle that investment disputes (i.e., their legal basis, claims, and the respective judicial competence) can only be "investment" in substance does not mean that the law of international investment is not "humanized" enough, nor that there is no place for its further "humanization."[17]

This paper will attempt to demonstrate that traditionally, investment law has always left room—whether silently or indirectly—for states to dispose of the necessary margin to effectively regulate various sectors of policy at the domestic level in a way that is compatible with investment treaty obligations. From this perspective, excluding human rights due to its distinctive "lexicon," the law of international investments allows host states to comply with human rights obligations and, more generally, to develop human rights policies.[18]

It is important to note that the rights granted to investors by

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14 Though beyond the scope of this article, it is worth noting that jurisdiction can also flow from an arbitration clause inserted in a contract between a host state and an investor or from a unilateral offer provided in a domestic investment law. *See generally* Emmanuel Gaillard, *Investment Treaty Arbitration and Jurisdiction over Contract Claims-The SGS Cases Considered*, *in* INTERNATIONAL INVESTMENT LAW AND ARBITRATION: LEADING CASES FROM THE ICSID, NAFTA, BILATERAL TREATIES AND CUSTOMARY INTERNATIONAL LAW 325 (Todd Weiler ed., 2005).

15 *See* Aldson, *supra* note 7, at 58 (explaining that the formation of the treaties themselves often dictates the jurisdiction of any ensuing arbitration).

16 *But see* Susan D. Franck, *The Legitimacy Crisis in Investment Treaty Arbitration: Privatizing Public International Law Through Inconsistent Decisions*, 73 FORDHAM L. REV. 1521, 1523-24 (2005) (predicting that with the inclusion of public international law rights, international arbitration will eventually absorb investment arbitration).

17 On this concept, see M. T. Kamminga, *Humanisation of International Law*, *in* CHANGING PERCEPTIONS OF SOVEREIGNTY AND HUMAN RIGHTS: ESSAYS IN HONOUR OF CEES FLINTERMAN 29 (I. Boerefijn & J. Goldschmidt eds., 2008) and THEODORE MERON, THE HUMANIZATION OF INTERNATIONAL LAW (Martinus Nijhoff ed., 2006).

18 *Id.*

investment treaties are not absolute rights.[19] If the home state's class of investors are granted rights on a general policy level, the same cannot be said in relation to individual investors in each case.[20] At a casuistic jurisdictional level, investors are granted the right to challenge a state measure aimed at protecting the public and general interest, such as the protection or promotion of human rights, which harms the individual investor's interest in such a way that it entails a breach of the treaty.[21] The negative impact of a state measure on an investor does not automatically entitle her to treaty protection.[22] Rather, arbitration tribunals determine on a case-by-case basis whether the investor is entitled to conventional protection.[23] Naturally, in the normative frame of treaty provisions, such endeavors require that the interests of the investor be balanced against public and general interests. As illustrated by the genesis of international investment law, both of these interests are equal parts of the investment law regime.[24] Therefore, to some

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19 General treatment standards under investment treaties include both absolute and relative standards. *See* SALACUSE, *supra* note 6, at 206. Among the "absolute standards" is full protection and security. *Id.* Even so, the ICSID tribunal in *Técnicas Medioambientales Tecmed S.A. v. United Mexican States* concluded that this guarantee was not absolute. *See* Ryan Suda, *The Effect of Bilateral Investment Treaties on Human Rights Enforcement and Realization, in* TRANSNATIONAL CORPORATIONS AND HUMAN RIGHTS 104 (Oliver De Schutter ed., 2006); Técnicas Medioambientales Tecmed, S.A. v. United Mexican States, ICSID Case No. ARB(AF)/00/2, Award, (May 29, 2003), *available at* http://italaw.com/documents/Tecnicas_011.pdf.

20 *See, e.g.*, Suda, *supra* note 19, at 104. ("[T]he guarantee of full protection and security is not absolute and does not impose strict liability upon the State that grants it [in cases where individual investors bring claims.]") (quoting Técnicas Medioambientales Tecmed S.A. v. United Mexican States, ICSID Case No. ARB(AF)/00/2, Award (May 29, 2003)).

21 *See* Kriebaum, *supra* note 1, at 177 ("[An] investor may use BIT provisions to challenge human rights-inspired regulations that interfere with its investment.").

22 For example, in *Tecmed* the investor claimed additional protection under the treaty, alleging that the Government of Mexico had breached its duty of "full protection and security" by failing to prevent "adverse social demonstrations" at the investor's hazardous waste treatment facility. Técnicas Medioambientales Tecmed, S.A. v. United Mexican States, ICSID Case No. ARB(AF)/00/2, Award, ¶ 175 (May 29, 2003), *available at* http://italaw.com/documents/Tecnicas_011.pdf. The tribunal decided the investor was not entitled to additional protection because there was "not sufficient evidence supporting the allegation." *Id.*

23 *See id.*

24 *See, e.g.*, Lars Markert, *The Crucial Question of Future Investment Treaties, in* INTERNATIONAL INVESTMENT LAW AND EU LAW 166 (Marc Bungenberg et al. eds.,

extent, the regime of international investment law is arguably schizophrenic. It aims at protecting and promoting both the interests of the investor as well as public and general interest.[25] In cases of conflict between these two respective interests, a balance must be struck.

Thereby, while balancing the interests of the investor against general interests (that is, human rights), arbitrators not only harmonizes two potentially conflicting regimes of international law (investment law and human rights law), but, in substance, also highlight the human dimension of investment law.

In this context, the aim of this article is neither to stigmatize an incomplete system, which appears on its surface inconsiderate of human rights, nor to sketch an ideal system regulating international investment operations in such a way that would impose international human right norms on investment arbitration.

Rather, the primary aim is to demonstrate that human rights preoccupations have always been part of the investment regime and that the "toolbox" of investment arbitrators traditionally contains a number of tools that are specially designed to take into account public and general interest. Hence, the object of this paper is to investigate under which conditions a non-discriminatory measure enacted by a host state—with the aim of protecting or promoting human rights [26] —may breach an investment agreement.[27] By doing so, this article will demonstrate

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2011).

25 *See, e.g.*, PETERSON, *supra* note 1, at 34 (predicting that had the tribunal in *Tecmed v. Mexico* found the government authorities acted unreasonably, it "would have had to wrestle with the balance to be struck between the right to public protest and the obligation to provide protection and security for foreign investment projects").

26 Considering this article focuses on the investment law system, the relevant human rights norms are not considered in detail. For such a detailed presentation, see REMI BACHAND, MARTIN GALLIE & STEPHANIE ROUSSEAU, *Droits de l'investissement et droits humains dans les Amériques*, *in* 49 ANNUAIRE FRANÇAIS DE DROIT INTERNATIONAL 575, 577-89 (2003). Furthermore, the reference to "human rights" is used in a broad sense; it is intended to include the right of the first and second generations, as well as the rights to development and environmental protection. *See id.*

27 The "measures" dealt with here cover measures addressing an investor in particular, as well as measures having a general scope of application. When needed, a distinction will be made between them. In addition, they refer to the state as a whole and, therefore, concern the relevant practice of all the organs of the host state. Considering its topic, this article focuses on investor-state arbitration and not on

that such state measures rarely breach an investment treaty.

Investment treaty provisions that could be affected by municipal practice over human rights are varied.[28] However, the limited scope of the study renders it necessary to narrow the analysis and focus only on two provisions which, in light of relevant case law, are proven to be the most important—the fair and equitable treatment clause (FET) and the prohibition of indirect expropriation.[29] As explained in detail below, the keys to balancing public and general interest against the interests of investors—in relation to the FET and the indirect expropriation prohibition—are, respectively, the principles of legitimate expectations and distinct-investment-backed expectations.[30]

Demonstrating that investment law is already "humanized" does not, however, mean that there is no space for a more direct "humanization." Hence, the second aim of this paper is to suggest that in addition to the indirect effectiveness of human rights protection by the public and general interest, general international law also authorizes investment arbitrators to refer directly to human rights norms. Investment arbitration may resort to international human rights law for two reasons: (1) to maximize the legitimacy of a decision, striking the balance in favour of public and general interest; or (2) to shift from what has previously been described as a conflict of interests (between the investor and the public and general interests) to a proper normative conflict (between the rules of international law that establish human rights obligations for the state and obligations vis-a-vis the investor).[31]

Starting with the second goal, Part II of this paper will focus

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interstate arbitration, which is also mentioned in most investment treaties. Only the former directly concerns the settlement of a dispute in relation with an investment operation.

28 *See* MONIQUE SASSON, SUBSTANTIVE LAW IN INVESTMENT TREATY ARBITRATION: THE UNSETTLED RELATIONSHIP BETWEEN INTERNATIONAL AND MUNICIPAL LAW 4 (2010).

29 For a discussion of the other provisions, see Suda, supra note 19, at 104.

30 Int'l Thunderbird Gaming Corp. v. United Mexican States, NAFTA Arb. Trib., Dissent, ¶ 27 (Jan. 26, 2006) (identifying both legitimate expectations and investment-backed expectations as the most important factors in balancing public interest against investor interest).

31 *See* Vienna Convention on the Law of Treaties, art. 31(3)(c), May 23, 1969, 115 U.N.T.S. 331, ¶ 17.

on general international law by first briefly addressing the question of its applicability in investment disputes, followed by a review of the means available under international law to investment arbitration, thus allowing tribunals to explicitly rely on international human rights norms. Faithful to the premises set in the introduction, this part will conclude by arguing that given the nature and the consequent limitations, in the jurisdiction of investment arbitration tribunals, there is a tendency to give a limited role to international human rights norms.

Whether it is because investment arbitrators are not familiar with human rights law or because they believe that sticking to their competency in investment law will increase the legitimacy of their arbitral decisions, international human rights norms to date are generally absent from investment arbitration.[32] Nonetheless, human rights are inevitably an important consideration in investment arbitrations, whether or not the tribunals refer to them by name. As it will be demonstrated, human rights considerations are often disguised under the label of public and general interest.[33]

Part III starts by recalling the schizophrenic "ethos" of international investment law, which aims to simultaneously promote state development and to grant protection to investors. The article then turns toward the tools provided, not by general international law, but by the regime of investment law itself. These tools correspond mainly to the two aforementioned guiding principles of interpretation: legitimate expectations and distinct-investment-backed expectations.[34] These principles function to facilitate balancing public and general state interests and the interests of the investor. After tracing back the administrative law

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32 Investment treaties and free trade agreements offer few instructions as to how such agreements should be reconciled with human rights; therefore, arbitrators have little guidance in factoring those norms into their decisions. *See* PETERSON, *supra* note 1, at 8.

33 *See, e.g.*, Suez, Sociedad General de Aguas de Barcelona S.A. v. Arg., ICSID Case No. ARB/03/19, Decision on Liability (July 30, 2010), *available at* http://italaw.com/documents/SuezVivendiAWGDecisiononLiability.pdf (noting that the case "may raise a variety of complex public and international law questions, including human rights considerations").

34 Int'l Thunderbird Gaming Corp. v. United Mexican States, NAFTA Arb. Trib., (Jan. 26, 2006) *available at* http://www.naftaclaims.com/Disputes/Mexico/Thunderbird/Thunderbird_Dissent.pdf. (explaining that both legitimate expectations and investment-backed expectations are the most important factors in balancing public interest against investor interest).

origins of the former principle and the shaping of the distinct-investment-backed expectations principle by the U.S. Supreme Court in the context of takings, this part of the article will detail their respective functioning mechanisms and highlight their added-value in the context of international investment law.[35]

This article will then focus on examining how, in practice, these principles are given effect in the context of the FET clause and the prohibition of indirect expropriation. In light of the tests of legitimate expectations and distinct-investment-backed expectations, this article will demonstrate that state measures pursuing a human rights objective rarely infringe on the provisions regarding the FET and indirect expropriation. The flexibility of the FET and indirect expropriation provisions—and the idea that the consequent rights they guarantee for the investor are not absolute—allow for states to effectively comply with their human rights obligations and develop human rights policies at the domestic level for the benefit of local populations while still complying with their investment law obligations.[36] For a regime which has been widely accused of being indifferent (if not detrimental) to human rights, the tolerance and flexibility it demonstrates in favour of human rights is a considerable one.

II. Is There A Role for Human Rights Norms in Investment Treaty Arbitration?

The investment regime is open to accommodate rules stemming from other systems, orders, or regimes.[37] This applies in the case of human rights law as well, which may be integrated into investment arbitral case law both as part of the applicable law or as a simple interpretative loan.[38] Section (A) of Part II provides a

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35 One cannot overlook that these principles were originally elaborated within specific domestic contexts and, therefore, cannot be imported as such within the international investment law regime. Their applicability in the field of international investment law thus depends upon a *mutatis mutandis* rationale.

36 *See, e.g.*, PETERSON, *supra* note 1, at 34.

37 *See id.* at 22.

38 *See id.* ("[A]s far back as the 1980s, an investment arbitration tribunal acknowledged that obligations imposed by *other* international treaties [involving human rights, for instance] ratified by a host state may be relevant in defending its treatment of a given foreign investor.").

general framework concerning the question of applicable law.[39] In particular, it points out the interaction between the applicable law and the jurisdiction of arbitral tribunals.[40] The latter tends to limit the applicability of human rights. Section (B) focuses on human rights law and discusses ways through which this law may be introduced into judicial reasoning, and the potential it brings to the investment treaty arbitration process.[41] This section of the article will focus on Article 31(3)(c) of the Vienna Convention on the Law of Treaties (hereinafter VCLT) and the so-called systemic integration method of interpretation that this article introduces.[42] The role of systemic integration is to allow judicial institutions to introduce peripheral norms of international law that are relevant to the norms that concern the case before them into their reasoning.[43] Thus, harmony in international law may be attained.

However, despite the potential of such a method of interpretation, its helpfulness in the field of investment arbitration remains limited. Without undermining the value of an explicit reference to human rights norms for the legitimacy and profundity of judicial reasoning, identical outcomes may be reached even if an investment arbitration tribunal (as it most often does) chooses to abstain from referring expressly to human rights norms.[44] The material philosophy of these rights may be accommodated perfectly well within the concept of public and general interest.

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39 *See infra* pp. 113-18.

40 *See infra* pp. 113-18.

41 *See infra* pp. 118-31.

42 "There shall be taken into account, together with the context . . . any relevant rules of international law applicable in the relations between the parties." *See* Vienna Convention on the Law of Treaties, *supra* note 31, art. 31(3)(c). The International Law Commission argues that "article [31(3)(c)] gives expression to the objective of systemic integration according to which, whatever their subject matter, treaties are a creation of the international legal system and their operation is predicated upon that fact." Rep. of the Int'l Law Comm'n, *Fragmentation of International Law: Difficulties Arising from the Diversification and Expansion of International Law*, 58th Sess., May 1-June 9, July 3-Aug. 11, 2006, ¶¶ 17-23, U.N. Doc. A/CN.4/L.682 (Aug. 11, 2006) [hereinafter Int'l Law Comm'n Report].

43 *See* Int'l Law Comm'n Report, *supra* note 42, at ¶¶ 17-23.

44 *See* Azurix Corp. v. Arg., ICSID Case No. ARB/01/12, Award, ¶ 254 (July 14, 2006), *available at* http://italaw.com/documents/AzurixAwardJuly2006.pdf ("Conflict between a BIT and human rights treaties must be resolved in favor of human rights because the consumers' *public interest* must prevail.") (emphasis added).

This concept is inherent in investment law and authorizes a balancing of the interests of investors in terms at least comparable to the interests that would be applied if an arbitral tribunal chose, by the means of systemic integration, to shift from a conflict of interests into a conflict of norms.[45]

A. Human Rights Law as Part of the Applicable Law

Investment treaties are not closed citadels standing in a vacuum.[46] To determine the responsibility of the host state, arbitral tribunals are entitled to resort to a corpus of rules outside the international investment law system.[47] Nevertheless, it cannot be forgotten that the aim of the investment dispute settlement process is to assess the responsibility of states with respect to their obligations under investment conventions, rather than on other norms of international law, regardless of their importance to society.[48]

This article shows that there is nothing prohibiting the application of human rights law to the settlement of an investor-state dispute. First, it demonstrates that whatever law is chosen by the parties, international law safeguards its applicability. Next, this article explains that the significance of this applicability is restricted by limitations in the jurisdiction of arbitration tribunals.

1. Applicability Safeguarded by International Law

Pursuant to the rules of procedure applicable to the settlement of disputes, it is up to the parties to an investment treaty to select the applicable law.[49] If the parties have not specified which law is

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45 *See* PETERSON *supra* note 1, at 22 ("[A] wide path is open for arbitrators to consider human rights and other international law obligations of states in the course of interpreting the obligations contained in investment protection treaties.").

46 *See* A.F.M. Maniruzzaman, *State Contracts in Contemporary International Law: Monist versus Dualist Controversies*, 12 EUR. J. INT'L L. 309, 320 (2001).

47 *See, e.g., id.*

48 *See* Jacob, *supra* note 1, at 30 (noting that investment tribunals are generally hesitant to deal with competing non-investment obligations and "prefer to disallow human rights arguments . . . rather than engage with the substance of the matter").

49 A distinction is made in arbitration practice between "treaty claims" and "contract claims." For the former, the applicable law is the law chosen by the states party to the investment convention. When it comes to "contract claims," the applicable law is the law determined by the host state together with the investor. *See generally* Yuval Shany, *Contract Claims vs. Treaty Claims: Mapping Conflicts between ICSID

to be applied, it is determined by the applicable rules of procedure.[50] The corpus of applicable law can include the provisions of the investment agreement, the domestic law of the host state party to the dispute and international law.[51] Outside the provisions of the investment agreement, domestic law and international law can be applied either independently or together.[52] Only a few choice-of-law clauses refer solely to international law.[53]

For example, Article 26(6) of the Energy Charter Treaty (ECT) provides that "a tribunal established under paragraph (4) shall decide the issues in dispute in accordance with this Treaty and the

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Decisions on Multisourced Investment Claims, 99 AM. J. INT'L L. 835 (2005) (discussing differences between contract claims and treaty claims in international arbitration and their potential for overlap).

50 *See, e.g.*, Convention on the Settlement of Investment Disputes between States and Nationals of other States, INT'L CTR. FOR SETTLEMENT OF INVESTMENT DISPUTES, art. 42, *available at* http://icsid.worldbank.org/ICSID/StaticFiles/basicdoc/CRR_English-final.pdf [hereinafter ICSID Convention] ("The Tribunal shall decide a dispute in accordance with such rules of law as may be agreed by the parties. In the absence of such agreement, the Tribunal shall apply the law of the Contracting State party to the dispute (including its rule on the conflict of laws) and such rules of international law as may be applicable"); U.N. Comm'n on Int'l Trade L. Arb. Rules, art. 33(1) (2010), *available at* http://www.uncitral.org/pdf/english/texts/arbitration/arb-rules-revised/arb-rules-revised-2010-e.pdf ("The arbitral tribunal shall apply the law designated by the parties as applicable to the substance of the dispute. Failing such designation by the parties, the arbitral tribunal shall apply the law which it determines to be appropriate.").

51 *See* Anthony Parra, *Applicable Law in Investor-State Arbitration, in* CONTEMPORARY ISSUES IN INTERNATIONAL ARBITRATION AND MEDIATION 3 (Arthur Rovine ed., 2008) ("The formula makes it clear that the parties may agree not only that their tribunal will apply a domestic law or international law but also, among other possibilities, combinations of domestic and international law rules.").

52 For a detailed analysis of the applicable law issue, see CHRISTOPH H. SCHREUER, THE ICSID CONVENTION: A COMMENTARY 545-639 (2001). While addressing only Article 42 of the ICSID Convention, the remarks made by the author are generally relevant to this issue. For a detailed analysis of the interaction between national law and international law in the context of Article 42 of the ICSID Convention, see Emmanuel Gaillard & Yas Banifatemi, *The Meaning of 'and' in Article 42(1), Second Sentence, of the Washington Convention: The Role of International Law in the ICSID Choice of Law Process*, 18 ICSID REV. FOREIGN INV. L.J. 375, 376 (2003) ("[I]nternational law may apply either directly, possibly in conjunction with the law of the host State, or indirectly as incorporated into the selected domestic law."). While addressing only the ICSID convention, the interest of this article extends well beyond the ICSID regime. *Id.*

53 *See Antoine Goetz, et al. v. Republic of Burundi*, 15 ICSID REV. FOREIGN INV. L.J. 457, 531 (2000) [hereinafter *Antoine v. Burundi*].

applicable rules and principles of international law."[54]

This type of choice-of-law provision begs the question of the exact norms of international law applicable to the dispute.[55] An answer to this question can be found in the *travaux préparatoires* of Article 42(1) of the ICSID Convention which refers to "such rules of international law as may be agreed by the parties."[56] Pursuant to the report by the Executive Directors, "the term 'international law' as used in this context should be understood in the sense given to it by Article 38(1) of the Statute of the International Court of Justice."[57] In light of this statement, the applicable rules of international law are those contained in treaties, customary law, and general principles of law recognized by civilized nations.[58] As for their content, it is determined on a case-by-case basis.[59] Hence, in this regard, and in the context of an investment dispute involving state practice aiming to protect or

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54 Energy Charter Treaty, art. 26(6), Dec. 17, 1994, 34 I.L.M. 360, 2080 U.N.T.S. 100; *see also* NAFTA, *supra* note 9, art. 1130 ("A tribunal established under this Subchapter shall decide the issues in accordance with this Agreement and applicable rules of international law.").

55 As for the distinction between rules and principles, it can be noted that arbitration practice does not give importance to this distinction, see SCHREUER, *supra* note 52, at 952 (using the terms "rule" and "principle" interchangeably).

56 ICSID Convention, *supra* note 52, art. 42(1).

57 ICSID Report of the Executive Directors, 1 ICSID Rep. 31 (2006), *cited in* SCHREUER, *supra* note 52, at 609. The International Court of Justice Statute provides that:

> 1. 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.
>
> 2. This provision shall not prejudice the power of the Court to decide a case *ex aequo et bono*, if the parties agree thereto.

The Statute of the International Court of Justice, art. 38(1), June 26, 1945, 59 Stat. 1055, 33 U.N.T.S. 993 [hereinafter ICJ Statute].

58 *See* PETERSON, *supra* note 1, at 22.

59 *See* ICJ Statute, *supra* note 57, art. 38.

promote human rights, it is highly probable that human rights law will be applicable.

International law can also come into play whether municipal law is applied alone or together with international law. In both situations, international law plays, with necessary modifications, the same role.[60] It fills potential gaps in the domestic legal order and even rectifies it, if that order is incompatible with the fundamental norms of international law.[61] Thus, if national law is incomplete in terms of human rights protection, or if it fails to satisfy the standards set by international law concerning the so-called fundamental human rights, international law becomes the applicable law[62] to settle the dispute.[63]

It is important to note, however, that in the course of such settlement, the investment-focused jurisdiction of arbitration tribunals tends to limit the significance of the applicability of international law.[64]

2. *Applicability Limited by Arbitrators' Jurisdiction*

Investment treaties generally provide that disputes between an investor and its host state that are subject to arbitration involve the interpretation and the application of these treaties.[65] In other words, the jurisdiction entrusted to arbitral tribunals is limited to determining whether the provisions of an investment agreement have been violated or not. Accordingly, no claim for the breach of

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60 *See* SCHREUER, *supra* note 52, at 580-81, 583-87, 620-27.

61 International law can also be applied as part of domestic law. However, as noted by Schreuer, "[i]t would not be wise to rely on the incorporation of international law into a domestic law chosen by the parties as a general proposition." *Id.* at 582. Indeed, "[t]he status of international law under domestic constitutions varies greatly." *Id.*

62 *See id.* at 590. Schreuer argues that this problem may be better dealt with in terms of mandatory rules of international law than in terms of applicable law. *Id.*

63 *See* PETERSON, *supra* note 1, at 22.

64 *See, e.g.*, Waste Management Inc. v. United Mexican States, ICSID Case No. ARB(AF)/00/3, Final Award, ¶ 85 (Apr. 30, 2004), *available at* http://www.state.gov/documents/organization/34643.pdf ("[T]here is no room for implying into the treaty additional requirements . . . of general international law in the field.").

65 *See, e.g.*, Maniruzzaman, *supra* note 46, at 309 (discussing the issue of whether arbiters' jurisdiction is limited to determining a breach or whether they may consider public international law as well).

any other rule of international law can be brought before an investment arbitration tribunal.[66] The potential role of human rights law, as part of the applicable law in the settlement of disputes, must be analyzed against the background of this well-established jurisdiction. Human rights claims do not have autonomous standing before investment tribunals.[67]

However, in cases where the state has reacted to a systemic or widespread human rights violation committed by an investor, arbitrators may (at least in theory) reach the conclusion that they lack jurisdiction or that they consider it inappropriate to consider the merits of the case, despite officially having jurisdiction.[68] This proposition has been made in literature disseminated in connection with dispute settlement mechanism of the World Trade Organization (WTO):

> As a second way of dealing with predominantly non-WTO disputes, one could argue that in certain extreme cases the dispute no longer genuinely concerns WTO claims (even though such claims could technically be made) but, rather, other rules of international law that the WTO claims are inextricably linked to and that these WTO claims are dependent on to be decided. In such extreme cases it could then be submitted that the history, prior procedures, and substantive content of the dispute indicate that the real issue of the case (i.e., the genuine object of the claim) is related to non-WTO claims as to which a WTO panel does not have jurisdiction. On these grounds, the WTO panel could either decide that it does not have substantive jurisdiction over the dispute or find that it does have jurisdiction but does not consider it appropriate to exercise this jurisdiction.[69]

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66 *See* Gus Van Harten & Martin Loughlin, *Investment Treaty Arbitration as a Species of Global Administrative Law*, 17 EUR. J. INT'L L. 121, 127 (2006) (discussing the system of investment treaty arbitration).

67 *See* PETERSON, *supra* note 1, at 22 (noting that generally investment arbitrators are "not empowered to find that human rights obligations have been breached" unless the human rights laws "form a part of the backdrop against which investment treaty obligations are read and applied").

68 *See* Joost Pauwelyn, *The Role of Public International Law in the WTO: How Far Can We Go?*, 95 AM. J. INT'L L. 535, 558 (2001) (footnotes omitted).

69 *Id.*

Such a hypothesis is theoretically possible,[70] but it is rather unlikely to occur. Furthermore, the fact that sometimes a dispute proves to be highly relevant to human rights should not be the reason for an arbitration tribunal's refusal to exercise jurisdiction.[71] Rather, the tribunal should take this into account and proceed with its determination of whether the investment agreement has been violated.

In its final report on the issue of fragmentation, the International Law Commission (hereinafter ILC) recalled that whatever the scope of the jurisdiction of a judicial body, the exercise of that jurisdiction "is controlled by the normative environment."[72] From the perspective of general international law, the most efficient method for taking this normative environment into account is that of systemic integration.

B. Introducing Human Rights Norms into Investment Arbitration through Interpretation

The rationale of the principle of systemic integration lies in the fact that treaties, whatever their subject matter, do not operate in a vacuum, but rather make part and parcel of the international legal order.[73] "All treaty provisions receive their force and validity from general law, and set up rights and obligations that exist alongside rights and obligations established by other treaty provisions and rules of customary international law." [74] As Lord McNair synthesized, treaties must be "applied and interpreted against the background of the general principles of international law."[75]

Following this rationale, Article 31(3)(c) of the VCLT enables

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70 *See generally* John Barcelo, *Who Decides the Arbitrators' Jurisdiction? Separability and Competence-Competence in Transnational Perspective*, 36 VAND. J. TRANSNAT'L L. 1115, 1121 (2003) (discussing the application of the 'Kompetenz-Kompetenz' principle which, in this situation, implicitly gives the WTO jurisdiction to rule over their competence).

71 *See* United States Diplomatic and Consular Staff in Tehran (U.S. v. Iran), 1980 I.C.J. 3, 20 (May 24) (pointing out that "no provision of the Statute or Rules contemplates that the Court should decline to take cognizance of one aspect of a dispute merely because that dispute has other aspects, however very important").

72 *See* Int'l Law Comm'n Report, *supra* note 42, ¶ 45.

73 *See* Maniruzzaman, *supra* note 46, at 309.

74 Int'l Law Comm'n Report, *supra* note 42, ¶ 414.

75 LORD MCNAIR, THE LAW OF TREATIES 466 (2d ed. 1961).

arbitration tribunals to apply and interpret investment treaties against the background of international human rights law.[76] This article provides that "there should be taken into account, together with the context . . . any relevant rules of international law applicable in the relations between the parties."[77] The role of systemic integration is to authorize judges and arbitrators to escape the narrow confines of applicable law while remaining within their jurisdiction and within the specific legal basis under which a claim was brought before the tribunal.[78] Further, it allows judges and arbitrators to enrich their reasoning by referring to sources of international law that, though extraneous to the respective normative regime, are nevertheless relevant to the judicial issue in question.[79] Article 31(3)(c) of the VCLT broadens the normative horizons of a judge—not her competence. It simply allows her to introduce the normative materials into the judicial analysis that may be useful in delivering her judgment.

However, the advantages offered by the systemic integration method of interpretation are somewhat blurred by the fact that difficulties appear quite often in identifying the norms of international law that may fall under the scope of Article 31(3)(c) of the VCLT. Yet, despite these difficulties, Article 31(3)(c) remains an important tool in the efforts of tribunals to bridge the gap between human rights and investment law. Last but not least, given the function of Article 31(3)(c) within the context of investment arbitration and the fact that the toolbox of investment law contains many of its own instruments to facilitate the tacit introduction of human rights into judicial reasoning, one might question the utility of systemic integration, especially in the context of investment arbitration.

1. *An Imperfect Tool: Difficulties in the Identification of the Human Right Norms Relevant between the Parties*

Both the literature and case law on systemic integration are significantly rich.[80] The limited scope of this study requires a brief

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76 *See* Int'l Law Comm'n Report, *supra* note 42, ¶ 420.

77 Vienna Convention on the Law of Treaties, *supra* note 31, art. 31(3)(c).

78 *See* Int'l Law Comm'n Report, *supra* note 42, ¶¶ 17-23.

79 *See id.* ¶¶ 462-72.

80 *See* Isabelle Van Damme, *Systemic Integration of International Law: Views*

discussion of the issues raised by systemic integration which are the most relevant for the purpose of this article.

Reference to the "rules of international law" in Article 31(3)(c) is generally interpreted as excluding the principles or considerations that may not be firmly established as rules.[81] In addition, the term "rules" encompasses all sources of international law, including treaties, international custom and general principles of international law.[82]

The relevance of an extraneous rule must be determined in light of the circumstances of each case. Here, the problem lies in the vagueness of certain international human rights norms, such as the sphere of application or minimum standards of conduct, which often makes it difficult to determine their effect.[83] Human rights as a body of law is indeed partly composed of imprecise standards.[84] This applies especially in the fields of economic, social, and cultural rights, which are ruled by the logic of "progressive fulfillment" and depend both upon the means that a state possesses and its level of development.[85] These rights are the most relevant rights in the framework of investment treaty arbitration. Conscious of this problem, the U.N. Committee on Economic, Social, and Cultural Rights has issued comments—especially on the substantive implication of the right to water—addressing some of the state measures necessary to ensure fulfillment of its goals.[86]

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from the ILC, the WTO, CTE, and UNESCO, in PROCEEDINGS OF THE CANADIAN COUNCIL ON INTERNATIONAL LAW 34TH ANNUAL CONFERENCE 2005, at 59 (2006); *see also* Benedetto Conforti, *Unité et fragmentation du droit international: "Glissez, mortels, n'appuyez pas!,"* 111 REVUE GÉNÉRALE DE DROIT INT'L PUBLIC 5, 19 (2007); Campbell McLachlan, *The Principle of Systemic Integration and Article 31(3)(c) of the Vienna Convention*, 54 INT'L & COMP. L.Q., 279, 280 (2005).

81 Int'l Law Comm'n Report, *supra* note 42, ¶ 426.

82 *See id.* ¶¶ 462-72.

83 *See* David Kinley & Rachel Chambers, *UN Human Rights Norms for Corporations: The Private Implications of Public International Law*, 6 HUM. RTS. L. REV. 447, 466 (2006) (considering complaints that international norms are vague).

84 *See id.*

85 *See, e.g.*, U.N. Comm. on Econ., Soc. and Cultural Rights, *General Comment No. 19: The Right to Social Security*, U.N. Doc. E/C.12/GC/19, (Feb. 4, 2008) (discussing the need for "progressive fulfilment in economic, social and cultural rights").

86 *See* U.N. Comm. on Econ., Soc. and Cultural Rights, *General Comment No. 15: The Right to Water*, U.N. Doc. E/C.12/2002/11 (Jan. 20, 2003).

Beyond the problem of imprecision within the realm of human rights, which relates to the nature and degree of maturity of human rights law, difficulties in the process of judicial interpretation are also encountered from the side of systemic integration. These problems are mainly caused by the uncertainties surrounding the sphere of application and the meaning given to the text of Article 31(3)(c).[87] However, as will be demonstrated, most of the issues that have been brought to light by legal scholarship are of minor importance within investment law.

The first—and most debated—issue concerns the meaning of the term "parties" in Article 31(3)(c).[88] For the relevant rule of international law to be integrated into judicial reasoning, it has "to be applicable in the relations between the parties."[89] Given the status of general applicability recognized to customary law and the general principles of law, this condition raises no difficulty for such sources.[90] On the other hand, a vivid debate arose, mainly in the framework of the WTO, about the meaning of the term "parties" in the context of conventional norms of international law.[91] Does Article 31(3)(c) refer to all parties to the treaty to be interpreted, or simply to the two parties involved in the dispute? In the *EC–Biotechnical Products* case, a WTO panel considered the term "parties" to refer to the parties to the treaty to be interpreted.[92] Such an understanding has the paradoxical effect of

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87 *See, e.g.*, Demir v. Turkey, App. No. 34503/97, 48 EUR. H.R. REP. 1272 (2009) (illustrating the confusion courts may have in interpreting Art. 31(3)(c) before the European Court of Human Rights).

88 *See* Vassilis Tzevelekos, *The Use of Article 31(3)(C) of the VCLT in the Case Law of the ECtHR: An Effective Anti-Fragmentation Tool or a Selective Loophole for the Reinforcement of Human Rights Teleology—Between Evolution and Systemic Integration*, 31 MICH. J. INT'L L. 621, 653-54 (2010).

89 Ulf Linderfalk, *Who Are 'The Parties'? Article 31, Paragraph 3(c) of the 1969 Vienna Convention and the 'Principle of Systemic Integration' Revisited*, 55 NETH. INT'L L. REV. 343, 345 (2008).

90 *See* Tzevelekos, *supra* note 88, at 653 (citing Duncan French, *Treaty Interpretation and the Incorporation of Extraneous Legal Rules*, 55 INT'L & COMP. L.Q. 281, 307 (2006)).

91 *See id.* at 654-55 (citing JOOST PAUWELYN, CONFLICT OF NORMS IN PUBLIC INTERNATIONAL LAW: HOW WTO LAW RELATES TO OTHER RULES OF INTERNATIONAL LAW 261 (2003)).

92 *See* Appellate Body Report, *European Communities–Measures Affecting the Approval and Marketing of Biotech Products*, WT/DS291-293/INTERIM 299 (Sept. 29,

isolating a broadly ratified treaty from the rest of the conventional rules of international law. The greater its membership, the less likely that all of the states parties will also be parties to other treaties.[93] However, as far as the specific question of investment law is concerned, the dilemma in the interpretation of the term "parties" in Article 31(3)(c) turns out to be of limited practical importance. Since the great majority of investment agreements are BITs, the parties to the dispute are the only parties to the convention.[94] The bilateral nature of conventional investment practice almost annihilates the possibility that in the context of investment arbitration, one state party to the investment treaty would not be party to the international treaty to which the arbitral tribunal resorts via the method of systemic integration.[95]

Another sensitive issue concerns the time factor in the effect to be given to Article 31(3)(c).[96] The question here is whether the relevant rules of international law are only those that existed at the time of the drafting of the treaty or whether the relative normative evolution should be taken into account as well.[97] A look at the *travaux préparatoires* of the VCLT demonstrates that the question of inter-temporality was a rather delicate topic, leading to a clash between the supporters and opponents of the doctrine.[98] In reality,

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2006); *see also* Benn McGrady, *Fragmentation of International Law or "Systemic Integration" of Treaty Regimes: EC Biotech Products and the Proper Interpretation of Article 31(3)(c) of the Vienna Convention on the Law of Treaties*, 42 J. WORLD TRADE 589, 607 (2008).

93 *See* Gabrielle Marceau, *WTO Dispute Settlement and Human Rights*, 13 EUR. J. INT'L L. 782, 790 (2002) (citing David Palmeter & Petros Mavroidis, *The WTO Legal System: Sources of Law*, 92 AM. J. INT'L L. 398 (1998)); Pauwelyn, *supra* note 68, at 575 (suggesting this understanding can be technically rebutted). Article 31(2)(a) of the VCLT, for example, refers to "all the parties," while Article 31(2)(b) mentions "one or more of the parties" as well as "other parties." It could thus be inferred that the use in Article 31(3)(c) of "parties" involves a subset of membership, which is less than the unanimity and more than a few parties. In this sense, it is suggested in the literature dealing with the WTO that it is enough that the non-WTO rule reflects only the "common intention" of the WTO members, by being either agreed upon or tolerated.

94 *See* Pauwelyn, *supra* note 68, at 575.

95 *But see* Energy Charter Treaty, *supra* note 54 (standing as an example of an BIT where the "parties" issue may be raised).

96 Tzevelekos, *supra* note 88, at 633-34.

97 *See id.*

98 *See* DIETRICH RAUSCHNING & RALF GÜNTER WETZEL, THE VIENNA CONVENTION ON THE LAW OF TREATIES 244 (1978).

this question is closely connected to the issue of the "dynamic interpretation" of treaties.[99] Indeed, Article 31(3)(c) serves as the basis for both the dynamic and the systemic integration methods of interpretation.[100] However, in the context of investment law, the doctrinal debates over the temporal dimension of Article 31(3)(c) do not constitute a real problem. Given that the first BITs were concluded in the 1960s[101] and that the explosion in the number of BITs is a rather new phenomenon dating back only to the mid-1980s, it is easy to conclude that the conventional investment practice is mainly posterior (or at least contemporary) to the human rights conventional practice within the UN framework in the aftermath of World War II.[102]

The aim of this above analysis is limited to a simple, general overview of systemic integration. Systemic integration stems from Article 31(3)(c) of the VCLT, which has been considered one of the main tools against the fragmentation of international law.[103] The main asset of this Article is to bridge the gap between different regimes of international law; its main handicap derives both from the nature of the regime of human rights—mainly the vagueness in the semantic field and the effect of certain rights—and the unclear text of Article 31(3)(c).[104] Nonetheless, despite the problems in its effective application, no one can deny that Article 31(3)(c) constitutes a useful weapon in the arsenal of investment arbitration.[105] Thus, when the particular circumstances of a case before an arbitral tribunal raise questions of human rights, it is left

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99 Tzevelekos, *supra* note 88, at 635 (citing Rep. of the Int'l Law Comm'n, 58th Sess., May 1-June 9, July 3-Aug. 11, 2006 ¶ 251(4), (22), U.N. Doc. A/61/10; GAOR, 61st Sess., Supp. No. 10 (2006)).

100 *See* Panos Merkouris, *Debating the Ouroboros of International Law: The Drafting History of Article 31(3)(c)*, 9 INT'L COMMUNITY L. REV. 1, 11 (2007); *see also* Tzevelekos, *supra* note 88, at 630-37.

101 *See* Treaty for the Promotion and Protection of Investments, F.R.G.-Pak., Nov. 25, 1959, 457 U.N.T.S. 6575, 6631 (concluding the first BIT between Germany and Pakistan in 1959 and noticeably not including investment arbitration).

102 *See generally* United Nations Conference on Trade and Development, *Bilateral Investment Treaties 1959-1999*, UNCTAD/ITE/IIA/2 (2000) (tracing the number of and history of bilateral investment treaties).

103 *See* Tzevelekos, *supra* note 88, at 636.

104 *See id.* at 630-37.

105 *See* ISABELLE VAN DAMME, TREATY INTERPRETATION BY THE WTO APPELLATE BODY 366-68 (2009).

to the arbitrators to rely on systemic integration.[106] International law guarantees the applicability of norms that are relevant and useful.[107] Arbitrators are then expected to make use of these norms, within the limits of the tribunal's jurisdiction, in order to reach the judicial outcome that they deem as just and legitimate.[108] What remains to be answered, however, is the precise function of systemic interpretation. In other words, what effect will systemic integration have on the case law of investment tribunals?

2. *The Potential of Systemic Integration in Investment Arbitration*

Although investment arbitration offers certain well-known examples of tribunals resorting to international law in their judicial reasoning,[109] references to the method of systemic integration remain absent to date. What these examples have in common is the objective pursued by the silent application of systemic integration. Resorting to international law does not necessarily reflect the will of tribunals to offer a view of the broader normative environment within which investment law is located, nor does it highlight the systemic bonds that exist between investment law and international law.[110] Rather, arbitral tribunals usually turn towards international law out of necessity.[111] They turn to the source of normative elements as a refuge that, though not forming part of the core of investment law, answers legal questions. Often, in light of the particular facts of each case, these questions cannot be answered by the provisions of the applicable investment law.[112] No matter how important the will of the contracting parties is in the regime of investment law, it does not suffice to cover each and every scenario or legal question of a

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106 *See* Tzevelekos, *supra* note 88, at 647.

107 *See id.*

108 *See id.* at 644.

109 *See, e.g.*, Osvaldo Mazorati, *Enforcement of Treaty Awards and National Constitutions (the Argentinian Cases)*, 7 BUS. L. INT'L 226, 230 (2006) (referencing the international law norms occurring in the so-called "Argentinian cases" in relation to the argument of state of necessity).

110 *See, e.g.*, *id.* (discussing the available international law).

111 *See id.*

112 *See, e.g.*, *id.* at 233-34 (citing the lack of applicable law in the Argentinian cases).

dispute.[113] Investment law is not a self-contained regime. The will of the contracting parties is often lacunar; the only way to resolve disputes and guarantee the effective application of the provisions of investment law is to cover these gaps by resorting to general international law.[114]

Such a method of systemic integration is highly unlikely to concern human rights, however. In the scenario described here, the role of systemic integration is to situate investment law within the general system of international law and to interpret the former in accordance with the systemic premises, logic, and economy of the latter. With no regard to the importance of human rights, these premises constitute just another regime within international law—not the system itself. Hence, despite its usefulness, this specific form of systemic integration does not concern, in principle, human rights.

Nevertheless, an analysis of the effect of systemic integration in regimes of international law, other than investment law, demonstrates that in addition to this first scenario, Article 31(3)(c) of the VCLT has been equally applied in two other instances.[115] The first and most important issue is that of conflict of norms.[116] As these studies suggest, in case of a conflict between international law norms, systemic integration comes into play *ipso facto*.[117] Furthermore, given the expansion in the effect of human rights, host states may relatively easily—and conveniently—sustain that virtually all measures they apply are dictated by the various obligations they have under international law to protect human rights.[118] In the case of civil and political rights, beyond the classic abstention from interfering with human liberties, states are equally expected to adopt positive measures aimed at protecting these liberties.[119] The positive effect of these rights extends well beyond the classic state versus individual effect and

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113 *See, e.g.*, *id.*

114 *See* Tzevelekos, *supra* note 88, at 670.

115 *See id.* at 669.

116 *See id.* at 665-70.

117 *See id.* at 671 (citing Loizidou v. Turkey, 310 Eur. Ct. H.R. (ser. A) at 31 (1995) as an example).

118 *See id.* at 670-73.

119 *Id.* at 639.

moves in the direction of indirect horizontal effect.[120] As far as social and economic rights are concerned, states are expected to equally protect, promote, and progressively fulfill these rights.[121] This very multidimensional nature of human rights protection and promotion requires states to develop policies aimed at progressively offering better living conditions to their citizens.[122] Vast areas of domestic policy (e.g., social policy, tax policy, economic policy, and labor policy) can be linked—if albeit indirectly—to international human rights.[123] Thus, most, if not all, conflicts between the interests of investors and those of host states may be translated into a conflict between the obligations that a host state has under investment law vis-à-vis the investor and the obligations it has vis-à-vis other states (if not the international community, as in the case of obligations *erga omnes*) in the field of the protecting and promoting of human rights.[124]

Systemic integration is, therefore, an option for international investment arbitration in order to introduce into judicial reasoning—through a conflicting norm approach—human rights norms of international law. However, in the case of a conflict of norms, the function of systemic integration is limited to simply drawing out the conflict between norms.[125] It does not offer any solutions for the conflict itself.[126] Even if an investment tribunal opts to a claim brought by an investor against a state from investment law norms to international human rights norms, the tribunal still needs to resolve this conflict.[127] In this case, the systemic integration method of interpretation will have to be complemented by the classic tools for conflict resolution such as

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120 *See id.*

121 *See id.*

122 *See id.* at 644.

123 *See* Tzevelekos, *supra* note 88, at 644-45.

124 *See id.* at 641-45.

125 *See* Nele Matz-Lück, *Harmonization, Systemic Integration, and 'Mutual Supportiveness' as Conflict-Solution Techniques: Different Modes of Interpretation as a Challenge to Negative Effects of Fragmentation*, 2006 FINNISH Y.B. INT'L L. 37, 50 (2006); McGrady, *supra* note 92, at 607; Tzevelekos, *supra* note 88, at 686.

126 *See* Tzevelekos, *supra* note 88, at 686-87.

127 *See, e.g., id.* (discussing how courts will often generalize international law to fill in the blanks).

lex specialis and hierarchy of norms.[128]

Yet, given that the first aim in the case of conflict of norms is reconciliation, arbitrators will be expected to pursue harmonization of conflicting rights via the principle of proportionality (i.e., establishing of priorities in the fulfillment of legal obligations in light of the particular circumstances of the case).[129] However, as it will be demonstrated in Part III, proportionality is also a well-known technique within the regime of investment law, and occupies a central role in balancing the interests of the investor against public and general interest.[130] In short, both in the cases of conflict of norms (through systemic integration) and conflict of interests (the traditional way of reasoning in investment law), the logic is the same.[131] The only major change is the legal etiquette (i.e., legal formalism).[132] Substance, however, remains unaffected.[133]

The third and final function of systemic integration is particularly effective in the case of complementarity of norms.[134] According to this third use of systemic integration, investment arbitrators may apply Article 31(3)(c) of the VCLT to integrate normative elements into their reasoning that are complementary to elements inherent in their own legal regime.[135] This scenario applies equally to the normative elements within the regime of investment law that refer to the protection of the investor as well as the elements that refer to the protection of public and general interest.[136] Hence, systemic integration in the case of

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128 *See generally id.* at 653-54 (discussing how both *lex specialis* and a hierarchy of norms may exist in how courts apply such methodologies).

129 *See* Elizabeth Snodgrass, *Protecting Investors' Legitimate Expectations: Recognizing and Delimiting a General Principle*, 21 ICSID REV. FOREIGN INV. L.J. 1, 46 (2006).

130 *See* discussion *infra* Part III.

131 *See* discussion *infra* Part III.

132 *See* Tzevelekos, *supra* note 88, at 633 (discussing the static nature of systemic integration).

133 *See id.* at 661.

134 *See id.* at 647-65.

135 *See id.* at 647-48.

136 *See generally* R. DOLZER & C. SCHREUER, PRINCIPLES OF INTERNATIONAL INVESTMENT LAW (Oxford Univ. Press 2008) (discussing the standards used to provide fair and equitable treatment and protection and security to the investors as well as taking

complementarity may be applied both to reinforce the rights provided by investment agreements to the investor as well as to limit these rights for the benefit of the public and general interest, the way this concept is defined in light of international human rights law.[137]

Once again, however, the normative elements that would be integrated into judicial reasoning are not sufficient *per se* to draw conclusions about the effect to be given to the relevant provisions of human rights law. The overall end-goal of human rights is on a collision course with the rights of the investor; the only way to strike a balance is to proceed again with a proper and in-depth test of proportionality. This is exactly the subject of Part III. The reference to proportionality brings us back to the scenarios of conflict of norms (via systemic integration) or to conflict of interests (via the classical reasoning followed so far by investment tribunals). As it has already been said, these two options coincide substantively.[138] Their logic, in essence and in nature, are, if not identical, at least similar.[139] The question thus remains: if the hypothesis of this paper is correct and, indeed, the regime of investment law already contains a number of tools which allow introduction of the end-goals of human rights to investment law through the concepts of public and general interest, what is the usefulness or comparative advantage of systemic integration?

One may answer this question by referring to the existing empirical data, which clearly suggests that systemic integration is absent from investment arbitration.[140] Hence, one could conclude that this is proof of the validity of the analysis so far—suggesting that, in reality, systemic integration cannot offer any original solutions and that, in substance, it can only function either as an elliptic substitute or as a complement.[141] The first case concerns the conflict of norms between investment rights and human rights; whereas the second emphasizes the norms of international law

consideration of the public/general interest).

137 *See id.*

138 *See* discussion *infra* Part III.

139 *See* Tzevelekos, *supra* note 88, at 649-51.

140 *See* Campbell McLachlan, *The Principle of Systemic Integration and Article 30(3)(c) of the Vienna Convention*, 54 INT'L & COMP L.Q. 279, 280-82 (2005).

141 *See* discussion *infra* Part III.

complementary to the normative conflicting elements that are traditionally harmonized through the classic interpretative process followed by investment tribunals.[142] However, such an answer ignores the fact that systemic integration is a relatively new technique which has only recently been introduced to the vocabulary of international lawyers by the ILC.[143]

Despite its obvious insufficiencies, systematic integration offers a number of clear advantages.[144] It brings all the useful and necessary normative elements under the same roof.[145] Thus, it covers all normative aspects of a case by analyzing its normative dimensions in depth, increasing the legitimacy of reasoning through the method of comparison, and overall, bridging the regime of investment law with different (potentially conflicting) regimes of international law and tying these regimes around the general system of international law.[146]

Thus, the analysis that follows—presenting the tools that are inherent to the regime of investment law and allowing for balancing the interests of the investor against public and general interest, including human rights—should not be read as an effort to undermine the usefulness of systemic integration. When the latter is not complementary to the mechanism that is analyzed below, it is parallel to it; it simply facilitates shifting from a conflict of interests to a conflict of norms.[147] Conflict in both scenarios remains the key word. The only available solution for any type of conflict is proportionality. In most cases, the application of proportionality leads to a certain degree of harmonization. In other words, in the case of a failure to obtain a balanced, legitimate harmonization, states will have to give priority to one of the two conflicting and mutually exclusive obligations and interests.[148] When this happens, a state will have to suffer all the

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142 *See* McLachlan, *supra* note 140, at 294.

143 *See, e.g.*, *id.*

144 *See* Tzevelekos, *supra* note 88, at 649-51 (listing advantages such as generously providing the court with valuable normative "loans," offering judges an opportunity to appear greatly respectful of general international law, and thereby increasing the legitimacy of judgments).

145 *See id.*

146 *See id.*

147 *See id.* at 665-67.

148 *See id.* at 674 (citing Rep. of the Int'l Law Comm'n, *Draft Resolution:*

consequences for its wrongful conduct under international law.[149] Hence, if restitution is impossible, the state will be expected to compensate and give satisfaction to the victims of the wrongful action in question.[150] However, as already explained, given the limitations in the competence of investment tribunals, the victim can only be an investor.[151] Human rights victims may have standing only before domestic courts or before a specialized, competent international human rights forum.[152]

III. Human Rights as a General Interest Within Investment Treaty Arbitration

Leaving aside Article 31(3)(c)[153] and its undeniable usefulness in protecting human rights values and interests, this section will prove that an equivalent result, a judicial outcome equally respectful of human rights, may be reached without applying the systemic integration method of interpretation. The regime of investment law contains a number of tools, the use of which guarantees that the necessary latitude is given to state authorities so that they may legally interfere with the rights of the investor for the purpose of protection and gradual promotion of human rights.[154] The concept of public and general interest is the key issue. Its content is defined ad hoc on the basis of the circumstances of each case, given the realities and the needs of each society.[155] Public and general interest corresponds to a matrix concept, pertinent to accommodate each and every legitimate

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Responsibility of States for Internationally Wrongful Acts, Annex, U.N. Doc. A/C.6/56/L.20; U.N. GAOR 56th Sess., Supp. No. 10, art. 48(1) (Nov. 12, 2001)).

149 *See* Rep. of the Int'l Law Comm'n, *Draft Resolution: Responsibility of States for Internationally Wrongful Acts*, art.28, U.N. Doc. A/C.6/56/L.20.

150 *See id.*, art. 36-37.

151 *See supra* text accompanying notes 14-18.

152 *See* Tzevelekos, *supra* note 88, at 673-74.

153 *See* Vienna Convention on the Law of Treaties, *supra* note 31.

154 *See* August Reinisch, *The Proliferation of International Dispute Settlement Mechanisms: The Threat of Fragmentation vs. the Promise of a More Effective System?: Some Reflections from the Perspective of Investment Arbitration, in* INTERNATIONAL LAW BETWEEN UNIVERSALISM AND FRAGMENTATION 123 (Isabelle Buffard et al. eds., 2008) (discussing the various tools for enforcing investment law).

155 *See* Tzevelekos, *supra* note 88, at 681 (citing *Bosphorus v. Ireland*, 2005–VI Eur. Ct. H.R. 107).

interest or value of the society, including human rights.[156]

As already explained, the first issue examined is the means that investment law utilizes to encapsulate human rights values within the concept of a public and general interest. The ethos of international investment law is defined here as schizophrenic; it aims to equally promote the development of the local population, represented by the host state, and to protect the interests of the investor. [157] Section (A) will provide an overview of the schizophrenic ethos of investment law. Section (B) then analyzes the tools of conciliation for balancing the public and general interest against the interests of the investor. This section examines the two guiding principles of interpretion, i.e., the legitimate expectations and the distinct-investment-backed expectations [158] and how these two principles are being used to assess the legality of state measures in relation to the FET clause and the prohibition of indirect expropriation. These mechanisms of interpretation described below balance the interests of the investor with human rights interests and assess whether these interests carry such weight that they may legitimately pass over those of the investor.[159] The inalienable condition for such a balancing is that the rights granted by investment agreements to investors are not absolute. It must be determined for each case whether the investor is entitled to conventional protection. [160] This is exactly the function of proportionality that is the overall principle governing the mechanisms analyzed below.

A. The Schizophrenic Ethos of International Investment Law

International investment law is often considered as over-protecting investors to such an extent that it could be re-labeled "investor rights law."[161] This due mainly to the fact that the

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156 *See id.* (using *Bosphorus v. Ireland* as an example of the general interest balancing).

157 *See* Reinisch, *supra* note 154, at 123.

158 *See* discussion *infra* Part III.A.2.b.

159 *See* discussion *infra* Part III.B.2.a.

160 *See supra* text accompanying notes 21-23.

161 *See generally* Jan Paulsson, *Arbitration Without Privity*, 10 ICSID REV. FOREIGN INV. L.J. 232 (1995). Such a perception is due to some of the features of the investment law regime, both substantial and procedural, such as the provision of rights only to investors, their lack of obligations, and "arbitration without privacy." *Id.*

system is judged solely from the viewpoint of the interests of investors.[162] Yet, the interests protected and promoted by international investment law are not only those of investors.[163] Investment law also promotes the interests of the states and of their population.[164] It is from this perspective that the *Amco* tribunal argued that "the Convention [ICSID Convention] is aimed to protect, to the same extent and with the same vigour, the investor and the host State, not forgetting that to protect investment is to protect the general interest of development and of developing countries."[165] The international investment law system is made of this schizophrenic ethos, and its normative substance allows the conciliation of the two objectives of protecting both investor and public interests.[166]

1. *The Internal Duality of Interests*

To be aware of the schizophrenia of the objectives of the international investment system, it is useful to look back at the genesis of the system. Because of the abusive recourse to investment treaty arbitration by a few investors through arbitration without privity, as well as the prejudices surrounding this field, it is argued that one has forgotten that the protection granted to investors aims primarily to promote the development of host states.[167]

a. *The Promotion of State Development as the Primary Objective*

The first paragraph of the Preamble of the ICSID Convention identifies the need for international cooperation to promote the

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162 *See* Int'l Law Comm'n Report, *supra* note 42, ¶ 21 ("[T]he characterizations ['trade law', 'environmental law'] have no normative value *per se* and are only informal labels that describe the instruments from the perspective of different interests or different policy objectives.").

163 *See* Kate Miles, *International Investment Law: Origins, Imperialism and Conceptualizing the Environment*, 21 COLO. J. INT'L ENVTL. L. & POL'Y 1, 2 (2010).

164 *See id.*

165 Amco Asia Corp. v. Republic of Indon., ICSID Case No. ARB/81/01, Award on Jurisdiction, ¶ 23 (Sept. 24 1985), 1 ICSID Rep. 389 (1993).

166 *See* Miles, *supra* note 163, at 2.

167 *See id.*

economic development of the state as its first objective.[168] What does this notion of economic development encompass? To answer this question, one must start with the political context that gave birth to the ICSID Convention.

At the time of the creation of the ICSID Convention, colonized countries were becoming independent and starting to claim their right to development under the banner of the New International Economic Order.[169] Their claim called for sovereignty over natural resources and for solidarity of the former colonized countries towards the newly independent nations.[170] Such demands were motivated by the economic difficulties faced by these countries.[171] Furthermore, it is well-attested that the economic situation of states has a direct impact on their ability to promote human rights, especially social and economic ones.[172] This is the reason why Article 2.1 of the International Covenant on Economic, Social, and Cultural Rights provides:

> Each State Party to the present Covenant undertakes to take steps, individually and through international assistance and co-operation, especially economic and technical, *to the maximum of its available resources*, with a view to achieving progressively the full realization of the rights recognized in the present Covenant by all appropriate means, including particularly the adoption of legislative measures.[173]

Considering this link between human rights and the economic condition of states, development turns into a key tool for effectiveness in the promotion of human rights.[174] Thus, if the system of international investment law aims to promote the

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168 *See* ICSID Convention, *supra* note 52, at pmbl. ¶ 1 ("Considering the need for international cooperation for economic development, and the role of private international investment therein . . . .").

169 *See* Andreas F. Lowenfeld, *The ICSID Convention: Origins and Transformation*, 38 GA. J. INT'L & COMP. L. 47, 54 (2009).

170 *See id.* at 50.

171 *See id.*

172 *See id.*

173 International Covenant on Economic, Social and Cultural Rights, art. 2(1), Dec. 16, 1966, 993 U.N.T.S. 3, 17 (emphasis added).

174 *See id.* at 5.

economic development of states, then it equally pursues, albeit indirectly, human rights objectives, as well.[175]

This conclusion becomes even more obvious considering the evolution of the content of the right to development.[176] This evolution is well symbolized by the semantic passage from "*droit du développement*" to "*droit au développement,*" which highlights the difference between states' right to development and development as an individual right of the human being.[177] Under the latter, development is no longer only "a comprehensive economic, social, cultural and political process . . . ."[178] In terms of Article 1.1 of the General Assembly UN Declaration on the Right to Development:

> [T]he right to development is an inalienable human right by virtue of which every human person and all peoples are entitled to participate in, contribute to, and enjoy economic, social, cultural and political development, in which all human rights and fundamental freedoms can be fully realized.[179]

Hence, to the extent that the human being is considered to be "the central subject of development,"[180] she can be equally viewed as the central subject of international investment law. From this perspective, the protection of investors aims also to promote human rights.

b. *The Protection of the Interests of the Investor as the Secondary Objective*

It appears then that the protection granted to investors by international investment law is a way of favouring development, rather than an objective *per se*.[181] In this sense, the *Joseph Charles*

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175 *See id.*

176 *Id.*

177 PIERRE-MARIE DUPUY, DROIT INTERNATIONAL PUBLIC 715 (8th ed. 2006).

178 Declaration on the Right to Development, U.N. Doc. A/RES/41/128, art. 2(Dec. 4 1986).

179 *Id.* art. 1(1).

180 *Id.* art. 2(1).

181 *See* Joseph Charles Lemire v. Ukr., ICSID Case No. ARB/06/18, Decision on Jurisdiction and Liability, ¶ 273 (Jan. 21, 2010), *available at*

Lemire Tribunal considered:

> The object and purpose of the BIT—the third interpretive criterion—is defined in its Preamble: the parties "desir[e] to promote greater economic cooperation between them, with respect to investment by nationals and companies of one Party in the territory of the other Party" and recognize that the BIT "will stimulate the flow of private capital and the economic development of the Parties." The main purpose of the BIT is thus the stimulation of foreign investment and of the accompanying flow of capital. But this main purpose is not sought in the abstract; it is inserted in a wider context, the economic development for both signatory countries. Economic development is an objective which must benefit all, primarily national citizens and national companies, and secondarily foreign investors. Thus, the object and purpose of the Treaty is not to protect foreign investments per se, but as an aid to the development of the domestic economy.[182]

More specifically, this secondary purpose is an indirect one. The protection granted to investors is a necessary means for encouraging and promoting the investments that are essential for the development of host states.[183]

This need to protect investors from host states is deeply rooted in the historical background of modern international investment law.[184] By the end of the nineteenth century and throughout the twentieth century, investors were dependent on host states, risking being expropriated or discriminated against without being granted any compensation.[185] Such unevenness also finds its origins in the weakness of individuals in relation to state power. There is no room here to retrace the balancing process that took place throughout the twentieth century.[186] The balancing process

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http://italaw.com/documents/Lemirev.Ukraine2010.pdf.

182 *See id.* ¶¶ 271-73.

183 *See id.*

184 *See* Miles, *supra* note 163, at 2-3.

185 *See* Charles Leben, *La théorie du contrat d'état et l'évolution du droit international des investissements*, *in* 302 RECUEIL DES COURS 197, 200 (2003).

186 *Id.* at 197.

occurred by way of the internationalizing of both the dispute settlement mechanism and the applicable law, first through states' contracts and then by way of investment treaties.[187]

The need to balance the relationship between investors and states partly explains why investment agreements usually provide only for the rights of the investor.[188] This need also explains why the instrumental dimension of this objective has been forgotten in the balancing process.[189] The emphasis placed on the protection of investors has led to the belief that such protection is to be absolute, and that arbitration tribunals tend to always rule in favour of investors.[190] However, careful analysis of the relevant arbitral practice indicates that arbitrators are neither agents of the investor nor cash registers of her claims. The liability of the host state is not founded on the basis of the arguments of the claimants, but rather on treaty provisions that by no means confer absolute rights on the investor.[191]

2. *The Internal Tools of Conciliation*

Having concluded that the international investment law regime aims to protect both the public and general interest as well as the interests of investors, this section analyzes the internal tools of reconciling these two conflicting interests. The misleading contention as to which investors are granted absolute rights is mainly due to the broad and vague wording of certain investment treaty provisions (such as the FET and the prohibition of indirect expropriation).[192] These features are deemed to lead to the paralysis of the normative power of host states. If the rights of the investor were absolute, then states could only exercise sovereignty and, more specifically, could only comply with their human rights obligations to the extent that their practice would not affect the

187 *See id.*

188 *See* Miles, *supra* note 163, at 8-9.

189 *Id.*

190 *See id.*

191 *See id.*

192 *See* Christoph H. Schreuer, *Fair and Equitable Treatment (FET): Interactions with Other Standards, in* INVESTMENT PROTECTION AND THE ENERGY CHARTER TREATY 63, 65 (Graham Coop & Clarisse Ribeiro eds., 2008).

status of the investor.[193] Rejecting this logic, this article emphasizes that, in reality, investment rights imply the modulation of the conventional protections granted to the investor. Hence, to administer the provisions of investment agreements, arbitration tribunals increasingly have recourse to the concepts that guide the administration—the legitimate expectations and the distinct-investment-backed expectations.[194]

The first part of this section addresses the issue of the administration of treaty provisions from the perspective of legitimacy, arguing that the legitimacy of the "normative" power of arbitrators stems from the will of states. The second part introduces the guiding principles of interpretation: the legitimate expectations principle and the distinct-investment-backed expectations principle. The study analyzes the function of these principles in domestic and investment law.

a. The Administration of Treaty Provisions

The "international investment law system" is a heterogeneous field where conflicts of interests often arise and involve complicated factual situations.[195] Therefore, the relevant normative framework must be capable of covering the numerous situations that can occur when taking account of their specificities. Given the practical impossibility of dealing with each and every factual situation in the framework of a single treaty, the parties to investment treaties must make a practical decision to provide for broadly-worded provisions.[196] By including these provisions within investment treaties, state-parties tend to delegate a quasi-normative power to arbitrators, putting them in charge of the administration of international investment law.[197] The nature of that role explains why arbitrators are required to be experts competent enough to deal with complex situations involving both legal and economic issues.[198]

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193 *See id.*

194 *Id.*

195 Susan D. Franck, *The Role of International Arbitrators*, 12 ILSA J. INT'L & COMP. L. 499, 512 (2006).

196 *See id.*

197 *See id.*

198 In relation to situations involving human rights law, one can wonder whether he

At the same time, this quasi-normative power is subject to live criticism[199] putting at stake the discretion which arbitrators enjoy in performing their task in a field that is closely connected to the public policy choices of states.[200] In this context, arbitrary decisions have led in the past to the characterization of arbitrators as the agents of the investor, thereby illegitimately paralyzing the regulatory power of states.[201]

As for the overall question of legitimacy, one needs to remember that, at the international level, the traditional source of legitimacy stems from the will of states.[202] Arbitrators draw their legitimacy from the will of the state-parties that empowered them to settle a dispute.[203] In a similar way, the breathing space they enjoy in applying these provisions is only due to the political choice that states made to establish such norms through their various investment agreements.[204] In doing so, states are responsible for the room left to the discretion of arbitrators in the assessment of the legality of measures involving public and general interest. However, discretion is not to be equated to arbitrariness. In between these two concepts lies a gap that is not bridged by arbitration tribunals. The practice of investment tribunals usually demonstrates the cautiousness of arbitrators when exercising their judicial functions.[205] By the means of interpretation, and especially through the two guiding principles analyzed below, arbitrators strike a balance between the interests

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or she has a sufficient knowledge of this field of law. Such a question is all the more relevant since human rights law is partly made of imprecise norms and obligations.

199 Charles N. Brower & Stephan W. Schill, *Is Arbitration A Threat or A Boon to the Legitimacy of International Investment Law?*, 9 CHI. J. INT'L L. 471, 490 (2009).

200 *See id.*

201 *See* Christian Chavagneux, *Lumière sur l'AMI : le test de Dracula l'Observatoire de la mondialisation, in* ALTERNATIVES ECONOMIQUES 75, 92 (Dec. 1998), *available at* http://www.alternatives-economiques.fr/lumiere-ssur-l-ami-le-test-de-dracula-l-observatorie-de-la-mondialisation_fr_art_120_12046.html.

202 *See* Brower & Schill, *supra* note 199, at 473.

203 *Id.*

204 *Id.*

205 *See* Charles Leben, *La liberté normative de l'Etat et la question de l'expropriation indirecte, in* LEBEN (dir.), LE CONTENTIEUX ARBITRAL TRANSNATIONAL RELATIFF A L'INVESTISSEMENT – NOUVEAUX DEVELOPPEMENTS 179, 179-83 (2005) [hereinafter Leben, *La liberté*].

of states (i.e., the interests of local societies) and those of the investor.[206] In doing so, they increasingly have recourse to the two guiding principles of legitimate expectations and of distinct-investment-backed expectations.[207]

b. The Two Guiding Principles of Interpretation: Legitimate Expectations and Distinct-Investment-Backed Expectations

Arbitration tribunals have increasingly referred to investors' legitimate expectations when assessing whether host states are in breach of their conventional obligations, especially in relation to the FET provision and the provision on indirect expropriation.[208] Despite the inchoate and inconsistent arbitration practice, a close analysis reveals that the way arbitrators test the existence and the legitimacy of investors' expectations tends to differ in relation to the types of claim.[209] As far as the FET provision is concerned,[210] they consider the basis of a special commitment or representation granted to the investor.[211] Beyond this common basis, they tend to

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206 *See* Brower & Schill, *supra* note 199, at 496.

207 *Id.*

208 *See generally* Chester Brown, *The Protection of Legitimate Expectations as a 'General Principle of Law': Some Preliminary Thoughts*, *in* 6 TRANSNAT'L DISP. MGMT (2009) (explaining that this increasing arbitration practice triggers an inflation in the academic literature about legitimate expectations in international investment law); *see also* Stephen Fietta, *Expropriation and the "Fair and Equitable" Standard: The Developing Role of Investors' "Expectations" in International Investment Arbitration*, 23 J. INT'L ARB. 375, 380 (2006); Francisco Orrego Vicuna, *Regulatory Authority and Legitimate Expectations: Balancing the Rights of the State and the Individual under International Law in a Global Society*, 5 INT'L L. FORUM DU DROIT INT'L 188, 200 (2003); A. von Walter, *The Investor's Expectations in International Investment Arbitration*, 6 TRANSNAT'L DISP. MGMT. 1, 23 (2009).

209 *See* Fietta, *supra* note 208, at 377-78.

210 *See* Int'l Thunderbird Gaming Corp. v. United Mexican States, NAFTA Arb. Trib., Dissent, ¶ 37 (2006), *available at* http://www.naftaclaims.com/Disputes/Mexico/Thunderbird/Thunderbird_Dissent.pdf ("One can observe over the last years a significant growth in the role and scope of the legitimate expectation principle, from an earlier function as a subsidiary interpretative principle to reinforce a particular interpretative approach chosen, to its current role as a self-standing subcategory and independent basis for a claim under the 'fair and equitable standard' as under Art. 1105 of the NAFTA.").

211 *See* Bayindir Insaat Turizm Ticaret Ve Sanayi A.S v. Islamic Republic of Pak., ICSID Case No. ARB/03/29, Decision on Jurisdiction, ¶ 240 (Nov. 14, 2005), *available*

differ in the manner they assess the existence and the legitimacy of expectations.[212] The main divergence relates to hard cases where it may be doubted that any special commitment or representation grounds legitimate expectations. Some arbitration tribunals consider that investors' bear an obligation of diligence, investors having to assess whether the representation at stake can ground a legitimate expectation.[213] On the other hand, other arbitrators opine that doubt plays in favour of investors, therefore their expectations should be considered legitimate.[214] This issue will be

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at http://italaw.com/documents/Bayandiraward.pdf. A few tribunals took account of the host state law and even of policies at the time the investment was made to assess investor's legitimate expectations. *Id. See also* Saluka Investments BV (Neth.) v. The Czech Republic, Partial Award, ¶¶ 301-02 (Perm. Ct. Arb. 2006), *available at* http://www.pca-cpa.org/upload/files/SAL-CZ%20Partial%20Award%20170306.pdf.

212 *See* Saluka Investments BV (Neth.) v. The Czech Republic, Partial Award, ¶¶ 301-02 (Perm. Ct. Arb. 2006), *available at* http://www.pca-cpa.org/upload/files/SAL-CZ%20Partial%20Award%20170306.pdf.

213 *See* Olguin v. Para., ICSID Case No. ARB/98/526, Award, ¶ 75 (Jul. 26, 2001), *available at* http://italaw.com/documents/Olgun-award-en.pdf ("This Tribunal [does] not accept Mr. Olguín's contention that he was induced to make his investment by the bulletins issued by the Central Bank of Paraguay. To the contrary, the Tribunal feels that prudence would have prompted a foreigner arriving in a country that had suffered severe economic problems to be much more conservative in his investments.").

214 *See* Int'l Thunderbird Gaming Corp. v. United Mexican States, Dissent, ¶¶ 32-33,

> [A] legitimate expectation is assumed more readily if an individual investor receives specifically formal assurances that display visibly an official character and if the official(s) perceive or should perceive that the investor intends, reasonably, to rely on such representation. The strongest way to build a legitimate expectation is if both formal and official elements are followed and reinforced by conduct that carries the same message as the investor reads–and can reasonably read–into an interpretative assurance or "comfort letter" . . . [i]f the parties are in an equal position, a much higher degree of due diligence is justified, as for example in inter-state relations under conventional international law, in WTO law or in transnational commercial relations, as usually adjudicated in international commercial arbitration. Strong parties in an equal position can be expected to deploy more expertise and due diligence to minimise ambiguity in their dealings with each other. Nor can the same requirements as in national judicial review of administrative actions be applied as the foreign investor is in a much more vulnerable, exposed position than a national citizen confronting his administration before national courts.

Id.

discussed further in Part IV.[215] If the first line of reasoning is based on the argument that risk is part of an investment operation, the second one relies upon the weakness of the investor in front of host states. Despite these divergences, by basing their reasoning on a state's special representation or commitment, arbitrators rely on the legitimate expectations principle as developed in domestic administrative law.

When it comes to the indirect expropriation provision, arbitration tribunals take account of all the circumstances—and not only a special commitment or representation[216]—to assess the existence and legitimacy of investors' expectations.[217] In doing so, they disagree on the priority that should be given to the relevant circumstances. While some arbitration tribunals emphasize investors' economic expectations,[218] others assess them in light of the overall circumstances, for instance, by looking at whether the investment was made in a highly regulated sector[219] or whether

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215 *See* discussion *infra* Part IV.

216 *See* Fietta, *supra* note 208, at 384. It can be inferred from arbitration practice that a breach of an investor's legitimate expectations based on a specific commitment or representation when any form of neutralization or destruction of the investment has occurred does not entail a breach of the indirect expropriation provision. *Id. But see* Methanex v. United States, NAFTA Arb. Trib., Final Award, ¶ 7 (Aug. 3, 2005) ("as a matter of general international law, a non-discriminatory regulation for a public purpose, which is enacted in accordance with due process and, which affects, inter alias, a foreign investor or investment is not deemed expropriatory and compensable unless specific commitments had been given by the regulating government to the then putative foreign investor contemplating investment that the government would refrain from such regulation").

217 *See* Fietta, *supra* note 208, at 392 (claiming that "this aspect of the *Methanex* tribunal's analysis would have been far more relevant to its analysis of the Article 1105 [NAFTA's FET provision] than to questions of expropriation under Article 1110.").

218 *See* Telenor Mobile Communications A.S. v. Republic of Hung., ICSID Case No. ARB/04/15, Award, ¶ 70 (Sept. 13, 2006), *available at* http://www.iisd.org/pdf/2006/itn_telenor_hungary.pdf ("In considering whether measures taken by government constitute expropriation the determinative factors are the intensity and duration of the economic deprivation suffered by the investor as the result of them").

219 *See* Feldman v. Mex., ICSID Case No. ARB(AF)/99/1, Award on Merits, ¶ 112 (Dec. 16, 2002), *available at* http://italaw.com/documents/feldman_mexico-award-english.pdf ("To paraphrase *Azinian,* not all government regulatory activity that makes it difficult or impossible for an investor to carry out a particular business, change in the law or change in the application of existing laws that makes it uneconomical to continue a particular business, is an expropriation under Article 1110. Governments, in their

expectations were overly optimistic.[220] Beyond the varying importance afforded to these circumstances, arbitrators' consideration traces back to the U.S. principle of distinct-investment-backed expectations[221] as it was elaborated upon in relation to the Fifth Amendment protecting the right to property.[222] From this perspective, it is not surprising that conventional U.S. investment practice introduced the principle of distinct-investment-backed expectations to help assess whether an indirect expropriation provision was breached.[223]

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exercise of regulatory power, frequently change their laws and regulations in response to changing economic circumstances or changing political, economic or social considerations. Those changes may well make certain activities less profitable or even uneconomic to continue.").

220 *See* Waste Management, Inc. v. United Mexican States, ICSID Case No. ARB(AF)/00/3, Final Award, ¶ 177 (Apr. 30, 2004), *available at* http://www.state.gov/documents/organization/34643.pdf ("[I]t is not the function of the international law of expropriation as reflected in Article 1110 to eliminate the normal commercial risks of a foreign investor, or to place on Mexico the burden of compensating for the failure of a business plan which was, in the circumstances, founded on too narrow a client base and dependent for its success on unsustainable assumptions about customer uptake and contractual performance").

221 U.S. CONST. amend. V.

222 *Id.*

223 Treaty Between the Government of the United States of America and the Government of [Country] Concerning the Encouragement and Reciprocal Protection of Investment (2004), Model BIT, Annex B:

> Expropriation The Parties confirm their shared understanding that: 1. Article 6 [Expropriation and Compensation] is intended to reflect customary international law concerning the obligation of States with respect to expropriation. 2. An action or a series of actions by a Party cannot constitute an expropriation unless it interferes with a tangible or intangible property right or property interest in an investment. 3. Article 6 [Expropriation and Compensation] addresses two situations. The first is direct expropriation, where an investment is nationalized or otherwise directly expropriated through formal transfer of title or outright seizure. 4. The second situation addressed by Article 6 [Expropriation and Compensation] is indirect expropriation, where an action or series of actions by a Party has an effect equivalent to direct expropriation without formal transfer of title or outright seizure. (a) The determination of whether an action or series of actions by a Party, in a specific fact situation, constitutes an indirect expropriation, requires a case-by-case, fact-based inquiry that considers, among other factors: (i) the economic impact of the government action, although the fact that an action or series of actions by a Party has an adverse effect on the economic value of an investment, standing alone, does not establish that an indirect expropriation has occurred; (ii) the extent to which the government

Given the recent and inconsistent way that arbitration tribunals refer to the legitimate expectation principle and the distinct-investment-backed expectations principle, this section aims to clarify these principles in light of their domestic law background. The purpose is not to assess arbitration practice, but rather to equip arbitration tribunals with clear and well-developed practices to apply in situations where a human rights state measure is thought to breach investment conventions.

1. The Legitimate Expectations Principle

The concept of legitimate expectations is rooted in municipal law and, more precisely, in administrative law.[224] It is a common concept in many countries in Europe, and the aim is to strike a balance between the state's freedom to regulate and private individuals' or corporations' protection.[225] Beyond any divergences in the definition and function of the principle within each national order,[226] the common core of legitimate expectations obeys the following rationale: a person granted with an individual right cannot be deprived of this right by an administrative measure, unless the measure is justified by a public and general interest.[227] Taking this rationale into account,[228] domestic courts

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> action interferes with *distinct, reasonable investment-backed expectations*; and (iii) the character of the government action. (b) 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 indirect expropriations.

Id. (emphasis added).

224 *See* Fietta, *supra* note 208, at 384.

225 *See* Case 112/77, August Töpfer Co. GmbH v. Comm'n, 1978 E.C.R. 1019, ¶ 19 (1978). The ECJ introduced legitimate expectations into its review of the legality in the 1970s and this Court considers that it "forms part of the Community legal order." *Id.*

226 *See* P.P. Craig, *Legitimate Expectations: A Conceptual Analysis*, 108 LAW Q. REV. 79, 82 (1992); P.P. Craig, *Substantive Legitimate Expectations in Domestic and Community Law*, 55 CAMBRIDGE L. J. 289, 290 (1996).

227 *See* ROBERT THOMAS, LEGITIMATE EXPECTATIONS AND PROPORTIONALITY IN ADMINISTRATIVE LAW 41 (2000) ("This principle of legitimate expectations concerns the relationship between public administration and the individual. It seeks to resolve the basic conflict between the desire to protect the individual's confidence in expectations raised by administrative conduct and the need for administrators to pursue changing policy objectives. The principle means that expectations raised as a result of administrative conduct may have legal consequences. Either the administration must

traditionally apply a two-step test.[229]

First, courts assess whether a person indeed has certain legitimate expectations.[230] Such expectations are established on the basis of an administrative decision, representation, or practice—the form of which is subject to few formal requirements.[231] To qualify as a legitimate expectation, these decisions must be directed at a specific or small group of persons, either a legal entity or natural person. Acts and rules with a general field of application are unlikely to form a justifiable basis of legitimate expectations.[232] *Ultra vires* conduct of the administration may, in principle, give rise to expectations deemed to be protected; however, domestic courts' scrutiny is much higher in relation to them than to *intra vires* conduct.[233] Legitimate expectations cannot arise as a result of a subjective hope. From this perspective, domestic tribunals assess whether it is reasonable to have such expectations in light of the overall circumstances.[234] If the possibility of change is reasonably foreseeable, expectations are not regarded as legitimate as maintaining the same expectations as before. This is especially true in commercial and economic matters, where a high degree of diligence is expected from traders who must:

> [B]e aware of the inherent uncertainties of a situation, and to be well-informed about the possibilities of any change.... To claim a legitimate expectation successfully any interference must have occurred without warning, with immediate effect and

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respect those expectations or provide compelling reasons why the public interest must take priority. The principle therefore concerns the degree to which an individual's expectations may be safeguarded in the face of a change of policy which tends to undermine them.").

228 *See id.* at 58-62 (noting that English law draws a distinction between procedural and substantive expectations).

229 For analysis of the domestic case law, see id. Given the large number of domestic legal systems making use of the legitimate expectation principle, there is no room to detail the relevant domestic caselaw on which this two-step test's introduction is based.

230 *See id.*

231 *See id.*

232 *See* THOMAS, *supra* note 227, at 41.

233 *See id.*

234 *See id.*

> without any transitional measures with a prudent trader could have used to avoid losses.[235]

The second step of judicial reasoning—balancing the legitimate expectations of the person against the particular public and general interest that motivated the breach of the legitimate expectations[236]—is where the classic test of proportionality is applied.[237] If the necessity of protecting this interest outweighs the rights of the person, determined on the basis of her legitimate expectations, then the state measure in question is considered legal and the person is not entitled to protection. In cases with the opposite outcome, the protection due may—depending on the legal system and the conduct on which legitimate expectations are based—consist of in-kind compensation or specific performance.

2. *The Distinct-Investment-Backed Expectations Principle*

To analyze the second guiding principle of interpretation within the regime of investment law, it is necessary to trace the domestic origin of the distinct-investment-backed expectations

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235 *Id.* at 55.

236 *See* Snodgrass, *supra* note 129, at 46.

237 *See id.* Formulating the rationale of the balancing test, Snodgrass posits the following:

> The balance must in the first instance be for the policy-maker to strike; but if the outcome is challenged by way of judicial review, I do not consider that the court's criterion is the bare rationality of the policy-maker's conclusion. While policy is for the policy-maker alone, the fairness of his or her decision not to accommodate reasonable expectations which the policy will thwart remains the court's concern (as of course does the lawfulness of the policy). To postulate this is not to place the judge in the seat of the minister. As the foregoing citations explain, it is the court's task to recognize the constitutional importance of ministerial freedom to formulate and to reformulate policy; but it is equally the court's duty to protect the interests of those individuals whose expectations of different treatment has a legitimacy which in fairness outtops the policy choice which threatens to frustrate it.

R. v. Ministry of Agric., Fisheries and Food, *ex parte* Hamble Fisheries, Ltd. (1995) 2 All E.R. 714, 724.

principle. This principle, first introduced by Michelman,[238] has been developed by the U.S. Supreme Court as one of the applicable criteria for assessing the violation of the Fifth Amendment to the U.S. Constitution protecting the right to property.[239] This principle help strike the balance between the state freedom to regulate and the protection of property.[240] In the 1978 *Penn Central* case, the Supreme Court stated:

> [W]e have frequently observed that whether a particular restriction will be rendered invalid by the government's failure to pay for any losses proximately caused by it depends largely upon the particular circumstances [in that] case. . . . In engaging in these essentially ad hoc, factual inquiries, the Court's decisions have identified several factors that have particular significance. The economic impact of the regulation on the claimant and, particularly, the extent to which the regulation has interfered with distinct-investment-backed expectations are, of course, relevant considerations . . . . So, too, is the character of the governmental action.[241]

Ever since the *Penn Central* judgment, courts refer systematically to the principle of distinct-investment-backed expectations.[242] However, despite the frequent use of the principle, there is an absence of consensus within American case law as to its content, scope of application, and its specific role in relation to other *Penn Central* factors.[243] Although there is no room here to analyze in detail the relevant U.S. case law,[244] it is

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238 Frank Michelman, *Property, Utility, and Fairness: Comments on the Ethical Foundations of Just Compensation Law*, 80 HARV. L. REV. 1165, 1170 (1967).

239 *See id.*

240 *See id.*

241 Penn Cent. Transp. Co. v. City of New York, 438 U.S. 104, 124 (1978).

242 *E.g.*, Lucas v. S.C. Coastal Council, 505 U.S. 1003 (1992); Guggenheim v. City of Goleta, 638 F.3d 1111 (9th Cir. 2011).

243 *See Penn Cent.*, 438 U.S. at 124.

244 For analysis of relevant case law, see J.D. Bremer & R.S. Radford, *Great Expectations: Will* Palazzolo v. Rhode Island *Clarify the Murky Doctrine of Investment-Backed Expectations in Regulatory Takings Law*, 9 N.Y.U. ENVTL L.J. 449, 452 (2001); J.D. Bremer & R.S. Radford, *The (Less?) Murky Doctrine of Investment-Backed Expectations after* Palazzolo, *and the Lower Courts' Disturbing Insistence on Wallowing*

nonetheless necessary to refer to the general trends in the application of the distinct-investment-backed expectations principle by U.S. courts to explain its function and content. This is an essential step towards better understanding how this principle should be used in the context of investment law.

a.) The Content of the Distinct-Investment-Backed Expectations Principle

As to the content of the principle, the state of the regulatory affairs in force at the time the owner entered into the property plays an important role when testing the reasonableness of the owner's expectations.[245] Reasonableness depends on the extent to which state law fostered and protected the expectations at the time they were established.[246] A specific law or a normative environment, especially in highly regulated sectors, may be considered as giving notice to the owner that a state measure may, hypothetically, affect her property in the future.[247] In such a situation, the owner may not have a distinct-investment-backed expectation.[248] By the same token, no state law will support an owner's expectation that she will be authorized to make harmful use of her property without any intervention from the state.[249]

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*in the Pre-*Palazzolo *Muck*, 34 SW. U. L. REV. 351, 359 (2005) [hereinafter Bremer & Radford, *(Less?) Murky Doctrine*]; D.L. Callies, *Regulatory Takings and the Supreme Court: How Perspectives on Property Rights Have Changed From* Penn Central *to* Dolan, *and What State and Federal Courts Are Doing About It*, 28 STETSON L. REV., 523, 617 (1999); J.A. Kupiec, *Returning to Principles of "Fairness and Justice": the Role of Investment-Backed Expectations in Total Regulatory Taking Claims*, 43 B.C. L. REV. 865, 878 (2008).

245 *See* Kupiec, *supra* note 244, at 878.

246 *See id.*

247 *See id.*

248 *See* Concrete Pipe & Prods., Inc. v. Constr. Laborers Pension Trust, 508 U.S. 602, 645 (1993) ("Those who do business in the regulated field cannot object if the legislative scheme is buttressed by subsequent amendments to achieve the legislative end.") (quoting FHA v. The Darlington, Inc., 358 U.S. 84, 91 (1958)). As it may be inferred from the case law of the Court of Federal Claims, which has repeatedly noted that this line of reasoning is most compelling when there is no "preexisting right of use under common law," this solution might reasonably apply when the property interest at issue is one created by the statutory scheme itself. *See, e.g.*, Maritrans Inc. v. United States, 40 Fed. Cl. 790, 798 (1998).

249 *See, e.g.*, Goldblatt v. Town of Hempstead, 369 U.S. 590 (1962); Miller v. Schoene, 276 U.S. 272 (1928). As highlighted by case law and literature, at issue is the

Recognizing the importance of notice, lower courts tend to conceptualize and reduce the principle of distinct-investment-backed expectations to the "notice rule:"[250] "[A] landowner who is on constructive notice of the existence of restrictive regulations has no legitimate expectations to put her property to productive use, and therefore cannot maintain a regulatory takings claim."[251]

The U.S. Supreme Court, however, seems reluctant to grant such importance to the notice rule.[252] The Court's current position is consistent with the concurring opinion of Justice O'Connor in the *Palazzolo* case,[253] where special attention was given to the ways through which the reasonableness of a landowner's expectations may be assessed.[254] In Justice O'Connor's opinion,[255]

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distinction between "harm preventing" measures and "benefit conferring" measures. At the core of the matter, there is the fact that as argued by the Restatement: "[P]ractically all human activities unless carried on in a wilderness interfere to some extent with others or involve some risk of interference." RESTATEMENT (SECOND) OF TORTS § 822 cmt. g (1979) (quoted in Lucas v. S.C. Coastal Council, 505 U.S. 1003, 1025 (1992)). By the same token, Sax suggested in *Takings and the Police Power* that "the problem is not one of noxiousness of harm-creating activity at all; rather it is a problem of inconsistency between perfectly innocent and independently desirable uses." J.L. Sax, *Takings and the Police Power*, 74 YALE L.J. 36, 49 (1964). From this angle, defining property as the "end result of a process of competition among inconsistent and contending economic values," he proposed the following rule:

> When economic loss is incurred as a result of government enhancement of its resource position in an enterprise capacity, then compensation is constitutionally required; it is that result which is to be characterized as a taking. But losses, however severe, incurred as a consequence of government acting merely in its arbitral capacity are to be viewed as a non-compensable exercise of the police power.

Id. at 63.

250 The term "notice rule" has been used by D.R. Mandelker to designate the aforementioned doctrine. *See* D.R. Mandelker, *Waiving the Taking Clause: Conflicting Signals from the Supreme Court, in* LAND USE L. & ZONING DIG. 3 (1988).

251 Bremer & Radford, *(Less?) Murky Doctrine*, *supra* note 244, at 355.

252 *See id.* at 353.

253 *See* Palazzolo v. Rhode Island, 533 U.S. 603, 633-35t 378.

254 In fact, the majority opinion endorsed Justice O'Connor's concurrence in *Palazzolo* in the 2002 *Tahoe-Sierra* case. *See* Tahoe-Sierra Pres. Council v. Tahoe Reg'l Planning Agency, 535 U.S. 302, 321 (2002).

255 *Palazzolo*, 533 U.S. at 633-35.

the role given by lower courts to the notice rule when determining distinct-investment-backed expectations has to be moderated.[256] To assess distinct-investment-backed expectations, it is also necessary to take account of the exigencies of equal treatment and fairness.[257] As to equal treatment, an owner is deemed to have a reasonable expectation to use her property in the same way as other similarly situated owners.[258] Concerning fairness, Justice O'Connor leaves the door open for the identification of specific considerations depending on the overall circumstances of the case.[259]

b.) The Significance of the Distinct-Investment-Backed Expectations Principle

Compared to the practice preferred by a number of lower courts in assessing the legality of a taking, Justice O'Connor emphasized that the principle of distinct-investment-backed expectations is just one among other factors to be considered in assessing the legality of state measures interfering with the

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> [T]he state of regulatory affairs at the time of acquisition is not the only factor that may determine the extent of investment-backed expectations. For example, the nature and extent of permitted development under the regulatory regime vis-à-vis the development sought by the claimant may also shape legitimate expectations without vesting any kind of development right in the property owner . . . . Courts [instead] must attend to those circumstances which are probative of what fairness requires in a given case.

Id.

256 *Id.* at 635-36.

257 *See id.* at 632-36.

258 *See id.* at 633-35.

259 It might include:

> 1) [W]hat the government told the landowner about the property before it was purchased and how it reacted to the owner's plans during and immediately after the land use application process; 2) whether the proposed land use is consistent with the general zoning and planning scheme; 3) whether the projected rate of growth for the subject locality suggests that development will be possible; 4) whether the government allowed the landowner to take concrete steps toward the desired use before stepping in and prohibiting it; and 5) whether the property owner is permitted to continue an existing, profitable use of property.

Bremer & Radford, *(Less?) Murky Doctrine, supra* note 244, at 393.

property of an investor.[260] Distinct-investment-backed expectations, although important, are not talismanic under *Penn Central.*[261] The degree of interference with investment-backed expectations is one factor considered, among others, when evaluating whether giving effect to a particular regulation over particular property "goes too far."[262] Therefore, despite the lack of a clear indication from the Supreme Court as to how to weigh the *Penn Central* factors, there must be some balancing of the economic impact of the measure, its fairness, and the distinct-investment-backed expectations of the owner.[263]

The economic impact of the regulation must be measured against the full scope of the claimant's property interest. Under this "parcel-as-a-whole" rule, "where an owner possesses a full 'bundle' of property rights, the destruction of one 'strand' of the bundle is not a taking, because the aggregate must be viewed in its entirety."[264] As for the character of the property right, it may be seen, in light of the *Tahoe-Sierra* case, as a fairness test considering whether the regulatory means are proportionate and equitably tailored to the ends.[265]

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260 *Palazzolo*, 533 U.S. at 633-36.

261 *See* Penn Cent. Transp. Co. v. City of New York, 438 U.S. 104, 124 (1978).

262 *Palazzolo*, 533 U.S. at 634. In the *Pa. Coal* case, Justice Holmes admonished that "if a regulation goes too far it will be recognized as a taking." Pa. Coal Co. v. Mahon, 260 U. S. 393, 415 (1922).

263 *See* Bremer & Radford, *(Less?) Murky Doctrine*, *supra* note 244, at 401-02.

264 Andrus v. Allard, 444 U.S. 51, 66 (1979). As penned by Justice Brennan in *Penn Cent.*:

> Taking jurisprudence does not divide a single parcel into discrete segments and attempt to determine whether rights in a particular segment have been entirely abrogated. In deciding whether a particular governmental action has effected a taking, this Court focuses rather both on the character of the action and on the nature and extent of the interference with rights in the parcel as a whole.

Penn Cent., 438 U.S. at 130-31.

265 *See* Tahoe-Sierra Pres. Council v. Tahoe Reg'l Planning Agency, 535 U.S. 302, 321 (2002).

c.) The Scope of Application of the Distinct-Investment-Backed Expectations Principle

Another question concerning the principle of distinct-investment-backed expectations is that of its scope of application. Since the *Lucas* case,[266] despite disagreements between the Justices[267] and the on-going opposition of many lower courts, the U.S. Supreme Court has consistently held that distinct-investment-backed expectations play a role in the partial takings of lands and in all personal property takings (both partial and total), but not in total takings of lands.[268] For total land takings, the principle helps to determine the relevant property interest against which the loss of economic use is measured—a determination that will decide whether the total or partial land's takings test applies.[269] However, in the case of lands' total takings, the "background principles of the State's law of property and nuisance" may play a role.[270] Justice Scalia, who wrote for the majority of the Court in *Lucas*, explained:

> Where the State seeks to sustain regulation that deprives land of all economically beneficial use, we think it may resist compensation only if the logically antecedent inquiry into the

266 *See* Lucas v. S.C. Coastal Council, 505 U.S. 1003, 1025 (1992).

267 In the view of Justice Kennedy:

> [R]easonable expectations must be understood in light of the whole of our legal tradition. The common law of nuisance is too narrow a confine for the exercise of regulatory power in a complex and interdependent society . . . [t]he State should not be prevented from enacting new regulatory initiatives in response to changing conditions, and courts must consider all reasonable expectations whatever their source.

Id. at 1035.

268 The concept of "total takings" refers to situations where a state deprives—through regulation—the property of all economically beneficial use. For a more in-depth treatment of "total takings," see Robert Meltz, *Takings Law Today: A Primer for the Perplexed*, 34 ECOLOGY L.Q. 307, 329 (2007).

269 "The answer to this difficult question [for the relevant property interest] may lie in how the owner's reasonable expectations have been shaped by the State's law of property—i.e., whether and to what degree the State's law has accorded legal recognition and protection to the particular interest in land with respect to which the takings claimant alleges a diminution in (or elimination) of value." *Lucas*, 505 U.S. at 1016.

270 *Id.* at 1029.

> nature of the owner's estate shows that the proscribed use interests were not part of his title to begin with. . . . [I]n the case of personal property by reason of the State's traditionally high degree of control over commercial dealings, [the property owner] ought to be aware of the possibility that new regulation might even render his property worthless (at least if the property's only economically productive use is sale or manufacture for sale). . . . In the case of land, however, we think the notion pressed by the Council that title is somehow held subject to the "implied limitation" that the State may subsequently eliminate economically valuable use is inconsistent with the historical compact recorded in the Takings Clause that has become part of our constitutional culture. . . . Any limitation so severe cannot be newly legislated or decreed (without compensation), but must inhere in the title itself, in the restrictions that background principles of the State's law of property and nuisance already place upon land ownership.[271]

d.) The Background Principles of the State's Law of Property and Nuisance

So as not to trigger the obligation to compensate lands' total takings, restrictions that completely eliminate any form of productive use of private property "must inhere in the title itself, in the restrictions that background principles of the State's law of property and nuisance already place upon land ownership."[272] Background principles are not used to balance the effect of the measure against its purpose. Rather, they intervene upstream to deny the existence of a property right, which therefore cannot be affected by any type of measure after-the-fact.[273]

With regard to the "background principle of the state of law,"

271 *Id.* at 1027-29 (emphasis added). It may be inferred from Justice Scalia's contention that in case of personal property's taking, no distinction has to be drawn between partial and total takings. In both cases, the owner's legitimate expectations are tested under the distinct-investment-backed expectations principle.

272 *Id.* at 1029.

273 By the same token, the U.S. Supreme Court stated in the *Keystone* case that "since no individual has a right to use his property so as to create a nuisance or otherwise harm others, the State has not 'taken' anything when it asserts its power to enjoin the nuisance-like activity." Keystone Bituminous Coal Ass'n v. DeBenedictis, 480 U.S. 470, 491 (1987).

Justice Scalia argued that it cannot be based on law "newly legislated or decreed."[274] He also argued that "the fact that a particular use has long been engaged in by similarly situated owners ordinarily imports a lack of any common law prohibition" that would absolve the government of takings liability.[275] In the *Palazzolo* case, the majority opinion added that a regulation cannot be a background principle exception merely because it predates the owner's acquisition of title:

> [It] is explained in terms of those common, shared understandings of permissible limitations derived from a State's legal tradition. . . . A regulation or common-law rule cannot be a background principle for some owners but not for others. The determination whether an existing, general law can limit all economic use of property must turn on objective factors, such as the nature of the land use proscribed.[276]

The Court went on to quote *Lucas*: "The 'total taking' inquiry we require today will ordinarily entail . . . analysis of, among other things, the degree of harm to public lands and resources, or adjacent private property, posed by the claimant's proposed activities."[277]

The synthesis of the previous dicta leads to the conclusion that where a land's total taking is identified through the 'parcel as a

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274 *Lucas*, 505 U.S. at 1029.

275 *Id.* at 1031.

276 Palazzolo v. Rhode Island, 533 U.S. 606, 630 (2001).

277 *Lucas*, 505 U.S. at 1030-31.

> On this analysis, the owner of a lake-bed, for example, would not be entitled to compensation when he is denied the requisite permit to engage in a landfilling operation that would have the effect of flooding others' land. Nor the corporate owner of a nuclear generating plant, when it is directed to remove all improvements from its land upon discovery that the plant sits astride an earthquake fault. Such regulatory action may well have the effect of eliminating the land's only economically productive use, but it does not proscribe a productive use that was previously permissible under relevant property and nuisance principles. The use of these properties for what are now expressly prohibited purposes was always unlawful, and (subject to other constitutional limitations) it was open to the State at any point to make the implication of those background principles of nuisance and property law explicit.

Id. at 1029-30.

whole' rule, the assessment of the owner's distinct-investment-backed expectations is not needed.[278] In that case, only background principles of domestic legislation on property and nuisance may come into play to deny the existence of a property right.[279] The background principles of domestic legislation on property and nuisance can be identified especially through two criteria: (1) equal treatment of all owners that find themselves in a similar situation with regard to the relevant common law; and (2) the relevant objective elements surrounding the particular circumstances of a case, such as the harm caused to the general interest.[280]

e.) Synthesis

This analysis leads to the conclusion that, given the subtleties and intricacies of U.S. case law, knowledge of principle is needed to contextualize the way U.S. landowners' expectations are assessed in relation to all the elements taken into account in U.S. practice. Focusing on the case law of the Supreme Court, the main conclusions that may be reached are twofold, concerning the scenarios of both partial and total takings. The distinct-investment-backed expectations principle plays a role to determine the relevant property interests against which the loss of economic use has to be measured. This determination in turn decides whether the total or partial takings test applies.[281]

In the case of partial takings of both personal and land property, a balance must be struck between the three *Penn Central* factors to assess whether the measure at stake is confiscatory (1) economic impact: (2) character of the measure, and (3) distinct-investment backed expectations.[282] As for the third criterion, the state of regulatory affairs, as it is broadly understood, is one of the main criteria used to evaluate distinct-investment-backed expectations.[283] Beyond this normative element, non-

278 *See id.* at 1034.

279 *Id.* at 1031.

280 *See id.* at 1029-32.

281 *See, e.g.*, Palazzolo v. Rhode Island, 533 U.S. 606 (2001); *Lucas*, 505 U.S. 1003.

282 *See* Penn Cent. Transport Co. v. New York City, 438 U.S. 104, 124 (1978).

283 *See, e.g.*, Bremer & Radford, *(Less?) Murky Doctrine*, *supra* note 244, at 491.

discrimination and fairness will also inform owners' expectations.[284] To evaluate fairness, the Court assesses the overall circumstances. As to the equal treatment of owners in similar situations is considered.

In the case of a total taking of personal property, due to the State's traditionally high degree of control in commercial dealings, the distinct-investment-backed expectations principle applies.[285] It does not apply, however, in relation to a total taking of land property.[286] Instead, the "background principles" of domestic legislation on property and "nuisance" may prohibit the particular use of the property at stake.[287] The objective elements of the case, as well as the way all owners in similar situations are treated help to ascertain the existence of such common law rules.[288]

3. The Connection between the Legitimate Expectation Principle and the Distinct-Investment-Backed Expectations Principle

Finally, it is of interest to analyze the way the legitimate expectation principle and the distinct-investment-backed expectations principle are connected in both conceptual and technical ways. From a conceptual perspective, both principles aim to strike a balance between the state's normative freedom and the protection of the person.[289] In a way, the distinct-investment-backed expectations principle has a narrower scope of application than the legitimate expectation principle, in that it only protects owners.[290] Underlying their common aim is fairness.[291] In both cases, these principles attempt to assess—in light of the overall circumstances—whether a person acted with legitimate

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284 *See, e.g.*, *id.*

285 *Lucas*, 505 U.S. at 1027-28.

286 *See, e.g. id.* at 1029-30.

287 *Id.* at 1029.

288 *See id.*

289 *See, e.g.*, Palazzolo v. Rhode Island, 533 U.S. 606, 634 (2001); Bremer & Radford, *(Less?) Murky Doctrine*, *supra* note 244, 516-22.

290 Bremer & Radford, *(Less?) Murky Doctrine*, *supra* note 244, at 454; Kupiec, *supra* note 244, at 885.

291 *See* Bremer & Radford, *(Less?) Murky Doctrine*, *supra* note 244, at 454.

expectations.[292]

From a technical perspective, the main difference lies in the basis of the expectations.[293] Under the legitimate expectation principle, expectations are tested only when a special commitment or representation exists, the legitimacy of which is then assessed in light of the overall circumstances.[294] Under the distinct-investment-backed expectations principle, expectations are assessed in light of the state of the regulatory affair as a whole, as well as the overall circumstances.[295]

At this point, the question arises whether the legitimate expectation principle plays a role in this second test. As a matter of principle, it seems that if an owner was granted a specific commitment or representation, it may be considered as a relevant circumstance when assessing the frustration of distinct-investment-backed expectations.

Equipped with this domestic law toolbox, it is now possible to describe the way the legitimate expectation principle and the distinct-investment-backed expectations principle may help to assess the legality of human rights measures, in the context of international investment arbitration.

B. Assessing The Legality of Human Rights State Measures

It is useful to recall the special "ethos" of investment law, and to emphasize that the way the principles of legitimate expectations and of distinct-investment-backed expectations are used in the context of investment law is conditioned by that very ethos.[296] The analysis that follows tests the validity of this article's hypothesis, which proposes that by applying the two guiding principles of interpretation, arbitral tribunals will only rarely conclude that a human rights state measure violates the FET and the prohibition of indirect expropriation. If this hypothesis is correct, then one may

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292 *See id.* at 358-59; *see, e.g.*, Kupiec, *supra* note 244.

293 *See* Bremer & Radford, *(Less?) Murky Doctrine, supra* note 244, at 357-58.

294 *See id.*

295 *See, e.g.*, Palazzolo v. Rhode Island, 533 U.S. 606, 633-35; *see also* Kupiec, *supra* note 244 at 865-68.

296 *See generally* Reinisch, *supra* note 154, at 183 (describing how ethos of investment law can be a schizophrenic one, both used to protect the interests of the local population and those of the investors).

safely conclude that, indeed, the regime of investment law is flexible enough to permit regulation at the domestic level in favor of human rights without the host state necessarily being in breach of its obligations vis-à-vis the investor.[297]

1. The Fair and Equitable Treatment Provision

There is no precise definition of the FET.[298] Although the general meaning given to that term is the host state's duty to treat investors fairly and equitably, the exact meaning of the obligation is substantially vague and, therefore, open to interpretation.[299] The relevant case law of arbitral tribunals offers a number of elements, which can be analysed in the following five categories: (a) obligation of vigilance and protection; (b) due process, including non-denial of justice and lack of arbitrariness; (c) transparency; (d) good faith (which includes both transparency and lack of arbitrariness); and (e) autonomous elements of fairness.[300] The only safe conclusion that can be drawn from this general categorization is that the FET provision has a wide scope of application.[301]

Given the difficulties in domesticating the FET provision, this paper will proceed by briefly discussing in section (a) the components of the concept which are the most relevant to the question examined therein. Then, in the light of this framework, the article will focus on the function of the principle of legitimate expectations within the framework of the FET and will seek to demonstrate that its application generally allows us to conclude that human rights state measures are unlikely to result in a breach of the FET provision.

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297 *See generally* Lucas v. S.C. Coastal Council, 505 U.S. 1003, 1030-31 (1992).

298 *See* Org. for Econ. Co-operation and Development (OECD), *Fair and Equitable Treatment Standard in International Investment Law* 1 (Org. for Econ. Co-operation and Dev.,Working Papers on International Investment No. 2004/3, 2004).

299 *See id.*

300 *See id.*

301 As noted by Dolzer and Schreuer, "[i]n its diverse manifestations, the standard of fair and equitable treatment may address a variety of governmental actions that affect investments and which more specific rules are unsuitable to address." DOLZER & SCHREUER, *supra* note 136, at 176.

a. The Relevant Normative Background

To assess the relevant normative framework, we must first delineate the situation at stake. An investor may claim that a non-discriminatory measure enacted to protect human rights constitutes an unfair or inequitable treatment, because she sees that measure as infringing on the normative framework regulating her activity.[302] Such a situation is factually linked to the following question: Does a host state generally have the right to modify the normative framework that regulates the activity of investors? Given the terseness of conventional practice, it is useful to begin by examining the relevant arbitral decision.

In the *CMS* case, the arbitral tribunal contended that "[t]he [BIT's] Preamble makes it clear, however that one principal objective of the protection envisaged is that fair and equitable treatment is desirable 'to maintain a stable framework for investments and maximum effective use of economic resources.'"[303] With necessary modifications, a similar conclusion may be inferred from the preamble of most investment agreements.[304]

One then has to determine the requirements of stability—especially with regard to the normative expectations. To answer this question, it is appropriate to start with the statement made by the *Tecmed* arbitral tribunal regarding the "basic expectations" of an investor when making an investment.[305] This example constitutes the most developed *obiter dictum* on the issue.

> The foreign investor expects the host State to act in a consistent manner, free from ambiguity, and totally transparent in its relations with the foreign investor. Knowing beforehand any

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302 *See id.* at 134.

303 CMS Gas Transmission Co. v. Argentine Republic, ICSID Case No. ARB/01/08, Final Award, ¶ 80 (May 12, 2005), *available at* http://icsid.worldbank.org/ICSID/FrontServiet?requestType=CasesRH&actionVal=showDoc&docId=DC504_En&caseId=C4.

304 *See id.* ¶ 274.

305 *See* Técnicas Medioambientales Tecmed, S.A. v. United Mexican States, ICSID Case No. ARB(AF)/00/2, Award, ¶ 154 (May 29, 2003), *available at* http://icsid.worldbank.org/ICSID/FrontServiet?requestTypes=casesRH&actionvai=showDoc&docId=DC602_En&caseId=c186.

> and all rules and regulations that will govern its investments, as well as the goals of the relevant policies and administrative practices or directives, the investor is able to plan her investment and comply with such regulations. Any and all State actions conforming to such criteria should relate not only to the guidelines, directives or requirements issued, or the resolutions approved thereunder, but also to the goals underlying such regulations. The foreign investor also expects the host State to act consistently—without arbitrarily revoking any pre-existing decisions or permits issued by the State that were relied upon by the investor to assume its commitments and to plan and launch its commercial and business activities. The investor also expects the State to use the legal instruments governing the actions of the investor or the investment in conformity with the function usually assigned to such instruments and not to deprive the investor of her investment without the required compensation.[306]

Two main conclusions can be inferred from this *obiter dictum.* First, based on the requirement that investors know all of the relevant rules and regulations beforehand, it may be concluded that investors can expect the regulatory framework to be frozen at the time they made their investment.[307] Secondly, it may be deduced that a state cannot arbitrarily revoke a special commitment entered into with an investor.[308]

It is generally accepted that investors' expectations are grounded in the legal order of the host state as it stands at the time when the investor acquires the investment.[309] However, it is less clear whether both stability and transparency[310] require the freezing of the regulatory framework. Such a conclusion would indeed contravene the fundamental principle of domestic legal orders from which states enjoy their normative freedom.[311] If an

306 *See* Técnicas Medioambientales Tecmed, S.A. v. United Mexican States, ICSID Case No. ARB(AF)/00/2, Award, ¶ 154 (May 29, 2003).

307 *See id.* ¶ 186.

308 *See id.* ¶ 77-200.

309 *See* DOLZER & SCHREUER, *supra* note 136, at 134.

310 *See id.* at 133-34. "Transparency means that the legal framework for the investor's operations is readily apparent and that any decisions affecting the investor can be traced to that legal framework." *Id.*

311 *See, e.g., id.* at 134-35.

investor could always successfully bring the host state before an arbitration tribunal for the modification of the normative framework that regulates her activity, the normative freedom of the state would be paralyzed.[312] However, a state may always—while making use of its normative power—commit to freeze the applicable law with regard to a specific investor.[313]

In light of these two remarks, this paper suggests that the assessment of the legality of state measures that affect the legal framework surrounding the activities of investors may only be realized through the principle of legitimate expectations, on the basis of the aforementioned two-step test that this principle introduces.[314] First, an arbitral tribunal will be expected to assess whether the investor has been granted a specific commitment, aiming to freeze the normative framework that regulates her activity.[315] In cases where such a commitment exists and has been legitimately relied upon, the legitimate expectations of the investor, flowing from the commitment, have to be balanced against the public and general interest pursued by the relevant measure infringing such commitment. If the state measure is judged to be proportionate, modification of the normative framework is considered not to violate the FET provision.[316] If, on the other hand, the relevant state measure fails to pass the test of proportionality, then the FET provision is considered breached and

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312 *See* Leben, *La liberté supra* note 205, at 180.

313 In that sense, the *Parkerings-Compagniet* Tribunal stated that:

> It is each State's undeniable right and privilege to exercise its sovereign legislative power. A State has the right to enact, modify or cancel a law at its own discretion. Save for the existence of an agreement, in the form of a stabilization clause or otherwise, there is nothing objectionable about the amendment brought to the regulatory framework existing at the time an investor made its investment.

Parkerings-Compagniet AS v. Republic of Lith., ICSID Case No. ARB/05/08, Award, ¶ 332 (Sept. 11, 2007), *available at* http://icsid.worldbank.org/ICSID/FrontServlet?requestType=CasesRH&actionVal=showDoc&docId=DC682_En&caseId=C252.

314 *See generally* THOMAS, *supra* note 227 (explaining the "two-step" test).

315 *But see* CMS Gas Transmission Co. v. Argentine Republic, ICSID Case No. ARB/01/08, Final Award, ¶ 198.

316 *See, e.g.*, Org. for Econ. Co-operation and Development (OECD), *supra* note 298.

the host state is liable.[317]

The aforementioned reasoning is validated by part of the arbitration practice.[318] The *CMS* tribunal adopted a more nuanced approach with regard to the criteria of stability and predictability than the *Tecmed* tribunal.[319] Indeed, the Tribunal suggested that:

> [I]t is not a question of whether the legal framework might need to be frozen as it can always evolve and be adapted to changing circumstances, but neither is it a question of whether the framework can be dispensed with altogether when specific commitments to the contrary have been made.[320]

In the same manner, the *EDF* tribunal contended that:

> The idea that legitimate expectations, and therefore FET, imply the stability of the legal and business framework, may not be correct if stated in an overly-broad and unqualified formulation. The FET might then mean the virtual freezing of the legal regulation of economic activities, in contrast with the State's normal regulatory power and the evolutionary character of economic life. 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 legal and economic framework. Such expectation would be neither legitimate nor reasonable.[321]

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317 *See, e.g.*, *id.*

318 *See, e.g.*, CMS Gas Transmission Co. v. Argentine Republic, ICSID Case No. ARB/01/08, Final Award, ¶ 80; EDF (Serv.) Ltd. v. Rom., ICSID Case No. ARB/05/13, Award, ¶ 217 (Oct. 8, 2009), *available at* http://italaw.com/documents/EDFAwardandDissent.pdf; Saluka Inv. BV (Neth.) v. The Czech Republic, Partial Award, ¶ 306 (Perm. Ct. Arb. 2006), *available at* http://www.pca-cpa.org/upload/files/SAL-CZ%20Partial%20Award%20170306.pdf..

319 *See* CMS Gas Transmission Company v. Argentine Republic, ICSID Case No. ARB/01/08, Final Award, ¶ 80, *available at* http://icsid.worldbank.org/ICSID/FrontServlet?requestType=CasesRH&actionVal=showDoc&docId=DC504_En&caseId=C4.; EDF (Serv.) Ltd. v. Rom., ICSID Case No. ARB/05/13, Award, ¶ 217.

320 CMS Gas Transmission Co. v. Argentine Republic, ICSID Case No. ARB/01/08, Final Award, ¶ 277.

321 EDF (Serv.) Ltd. v. Rom., ICSID Case No. ARB/05/13, Award, ¶ 217.

However, the *Saluka* tribunal concluded that the breach of a special commitment does not automatically entail the violation of the FET provision.[322] Such a finding "requires a weighing of the Claimant's legitimate and reasonable expectations on the one hand and the Respondent's legitimate regulatory interests on the other."[323] Proceeding with this kind of weighing, arbitrators must assess whether the breach of legitimate expectations was necessary for the achievement of the public and general interest objective.[324] This requires taking into account all the relevant circumstances of the case, as well as the availability to the host state of alternative measures that would equally protect the public and general interest without harming the interests of the investor.[325]

These preliminary conclusions allow assessment of the circumstances under which a state measure enacted to protect human rights may breach the FET provision.

b. *Assessment of the Legality of Human Rights: State Measures*

In order to better explain the reasoning that follows, it is necessary to recall the factual situation at stake. An investor considers that a non-discriminatory measure enacted by the host state pursuant to a human rights objective affects the normative framework regulating her activity and, therefore, breaches her rights under the FET provision.[326]

For the purposes of this analysis, it is useful to distinguish between two possible normative scenarios.[327] As to the first one, the breach of the FET provision is tested against a normative framework that regulates an entire sector of economic activity, and

322 *See* Saluka Investments BV (Neth.) v. Czech Republic, Partial Award, ¶ 500 (Perm. Ct. Arb. 2006).

323 *Id.* at ¶ 306.

324 *See id.* at ¶ 307.

325 For examples of how such weighing is used in the European Court of Justice, see Case 112/80, Firma Anton Dürbeck v. Hauptzollamt Frankfurt am Main-Flughafen, 1981 E.C.R. 1095; Case C-189/89, Spagl v. Hauptzollamt Rosenheim, 1990 E.C.R. I-4539; and THOMAS, *supra* note 227, at 68.

326 *See* DOLZER & SCHREUER, *supra* note 136, at 123.

327 *See id.* at 130-32. (contending that these two normative frameworks may nevertheless overlap).

not specifically the activities of one particular investor.[328] The second scenario refers to domestic norms aiming to regulate the activities of a particular foreign investor—for instance through an authorization, a licence, or a permit.[329] The aim under both scenarios is to determine under which conditions the modification of the normative framework breaches the FET.

Starting then with the first scenario, it has been explained that states enjoy a normative freedom. In this context, they may, in principle, freely regulate a sector of activity since the regulation is applicable to all investors who are active in that sector.[330] An investor cannot expect the new regulation to not apply to her.[331] The general normative framework that regulates her activity is not frozen at the time she makes her investment.[332] Such a freeze can only occur if the state has made a specific commitment that new regulations will not apply to her.[333] Such a specific commitment would create the legitimate expectation that the normative framework regulating her activity is not modified.[334]

As far as the second scenario is concerned (i.e., the norms regulating the activities of a particular foreign investor), these norms constitute the basis of the legitimate expectations of the investor concerned. More specifically, they constitute the basis of two different legitimate expectations: the expectation to exercise the activity she was authorized to develop and the expectation to do so under the conditions decided by the state or agreed upon by the investor herself.[335]

As a guide to determine whether the FET provision has been breached, arbitrators must first identify whether legitimate expectations for the investor were created by the state.[336]

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328 *See id.* at 144-46.

329 *See id.* at 147.

330 *See, e.g., id.*

331 *See, e.g.*, DOLZER & SCHREUER, *supra* note 136, at 134.

332 *See* Parkerings-Compagniet AS v. Republic of Lith., ICSID Case No. ARB/05/08, Award, ¶ 332 (Sept. 11, 2007), *available at* http://icsid.worldbank.org/ICSID/FrontServlet?requestType=CasesRH&actionVal=showDoc&docId=DC682_En&caseId=C252.

333 *See* DOLZER & SCHREUER, *supra* note 136, at 134.

334 *See id.*

335 *See id.* at 144.

336 *See id.* at 134.

However, an arbitration tribunal cannot definitively conclude that a modification of the normative framework, breaching the legitimate expectations, equally violates the FET provision, unless it first applies the test of proportionality.[337] Assessing the infringement of investors' legitimate expectations constitutes only the first step of the reasoning. In the framework of proportionality, arbitrators must also balance the legitimate expectations of the investor against the human rights objective pursued by the state measure in question.[338] To do so, arbitrators must assess whether the measure was necessary in light of the circumstances of the case and whether alternative means for reaching the same public and general interest goal were available to the host state.

As far as the circumstances of the case are concerned, though reality is often difficult to conceptualize, two general categories may be envisaged. The first relates to the future planned human rights policies of the state; the second is linked to an unforeseeable situation calling for a state reaction.[339] Concerning the former, what may generally be argued is that long-term promotion of human rights will rarely justify the infringement of the investor's legitimate expectations.[340] This is so because the promotion of human rights is an on-going process towards a middle/long-term objective.[341] States are free to plan the way they choose to promote human rights.[342]

The absence of urgency leaves both room and time to adapt domestic policy to the expectations of investors. When a state creates legitimate expectations with regard to the regulatory framework, it knows—or at least is expected to know—the human rights consequences of that specific economic or investment policy.[343]

However, in an unpredictable context, when a state enacts

337 *See id.* at 112.

338 *See* DOLZER & SCHREUER, *supra* note 136, at 175-76 (describing the relationship of arbitration to the FET).

339 *See id.* at 128-230.

340 *See id.* at 164.

341 *See id.*

342 *See id.*

343 *See Id.*

measures to protect human rights in a situation threatening their enjoyment by local society, the circumstances are totally different.[344] The state must act with urgency.[345] It is unable to foresee the necessity of enacting special measures to safeguard human rights.[346]

For instance, after a state licence for the production of a medicine has been granted, science may reveal that the product is life-threatening. Then, there is no alternative for the state other than to ban the production of the medicine. In the same vein, if scientific research concludes that a chemical product is dangerous for the environment, what can the state do other than to ban its production? In such cases, the circumstances surrounding the conflict between the investor's and the state's interests and the absence of any other available means for protecting human rights justify, in principle, the infringement of investor's legitimate expectations. This justification, in turn, legalizes the relevant state practice as necessary to protect the public and general interest. Thus, it passes the test of proportionality. The balance of interests, which could through systemic integration be easily elevated in a conflict between norms, is inherent to the principle of legitimate expectations, which itself allows the legitimate limitation of the expectations of an investor under the FET.[347]

In light of the above, one may conclude that an arbitral tribunal, guided by the principle of legitimate expectations, will only rarely judge that a human rights state measure breaches the FET provision. However, no matter how legitimate the human rights purposes pursued by state policy are, the state will be considered responsible for the breach of its obligations towards an investor acting in good faith if it gave promises it knew—or should have known—it could not harmonize with its human rights obligations or policies.[348]

2. *The Indirect Expropriation Provision*

The second right of the investor, tested with regard to its

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344 *See* DOLZER & SCHREUER, *supra* note 136, at 164.

345 *See id.* at 166-67.

346 *See id.* at 167.

347 *See id.* at 133-35.

348 *See id.* at 134.

flexibility to human rights policy, is the right not to be directly and indirectly expropriated.[349] In terms of conventional practice, indirect expropriation occurs when the relevant state practice interfering with the right to property of the investor has the same effect as direct expropriation. Faced with such an unclear definition,[350] arbitral case law appears rather fragmented,[351] as to the criteria of indirect expropriation.[352] To date, several different tests have been suggested for determining the existence of indirect expropriation.[353] The key criteria, whose use vary from one test to the other, are as follows: (1) the weight given to the effect a state measure may have on the property of the investor; and (2) the objective pursued by such a measure.[354]

However, despite the absence of consensus as to the conditions amounting to an indirect expropriation, the conditions of legality of both direct and indirect expropriation are well established—both in customary law and in investment agreements.[355] An indirect expropriation is considered to be legal under the following circumstances: (1) it aims to protect public and general interest; (2) it is done in conformity with the law; (3) it is done in a non-discriminatory way; and, finally, (4) it is compensated.[356] If these conditions are not met, the expropriation is illegal and violates the investment agreement.[357] The state is thereby obligated to

349 *See* Catherine Yannaca-Small, *Indirect Expropriation And The Right To Regulate In International Investment Law* 3 (Org. for Econ. Co-operation and Dev., Working Papers on International Investment No. 2004/4, 2004). In light of the topic here dealt with, the situations of direct expropriation will not be analyzed in this part. Furthermore, no distinction will be made between indirect and creeping expropriation.

350 *See id.* at 3. The aforementioned Annex B, ¶ (4)(a) of the U.S. Model BIT constitutes an exception.

351 *See id.* at 3-4.

352 *See id.* at 21.

353 *See* Yannaca-Small, *supra* note 349, at 18.

354 *See id.* at 18.

355 *See id.* at 3-4. The conditions mentioned here constitute the core of the conditions provided in investment agreements. However, additional conditions may be added in a few treaties. Considering the issues covered in this chapter, no account will be taken of these conventional specificities. Whatever these peculiarities, the conclusions reached are also applicable in the ambit of these treaty provisions.

356 *See id.* at 7.

357 *See* Yannaca-Small, *supra* note 349, at 6-7.

compensate the investor for the loss she has suffered.[358] Interestingly, compensation in the case of expropriation is both a condition of legality of the expropriation and a means for the reparation of its violation.[359]

In addition to the previous questions, there is a third issue concerning the distinction between expropriation and regulation.[360] It is sometimes suggested that non-discriminatory regulatory measures, no matter their effect, do not constitute an indirect expropriation; and, therefore, the regulations are legal without compensation to be owed.[361] The distinction between expropriation and regulation reflects the idea that these two concepts obey different criteria of identification. The difference is deemed to arise from the regulatory purpose of the measure.[362] A state's human rights measures fall into this category of regulatory measures.[363] They involve the regulation of a general field of activity or are focused on a specific investor.[364] Hence, the focus of this article cannot be different than regulatory measures.

Given the silence of investment agreements in this regard, as well as the inconsistencies in the case law of arbitral tribunals,[365] it is useful to present the tests that have been applied in order to conclude whether a regulatory measure enacted by the host state amounts to an indirect expropriation. Accordingly, this paper will discuss the following three methods: (1) the "sole effect" doctrine, focusing on the effect of such measure on investment; (2) the "police power" doctrine, based on the objective pursued by the

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358 *See id.* at 8.

359 *See* Responsibility of States for Internationally Wrongful Acts, G.A. Res. 56/83(1), U.N. Doc. A/56/49, at 9 (Dec. 12, 2001).

360 *See* Yannaca-Small, *supra* note 349, at 9-10.

361 *See id.* at 4-5.

362 *See id.* at 15.

363 *See id.* at 11.

364 *See id.* at 8.

365 *See* Yannaca-Small, *supra* note 349, at 3. In this respect, the U.S. Model BIT constitutes an exception. Following Annex B, ¶ (4)(b), "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 indirect expropriations." Treaty Between the Government of the United States of America and the Government of [Country] Concerning the Encouragement and Reciprocal Protection of Investment, *supra* note 223, at Annex B, ¶ (4)(b).

measure in question; and (3) the "proportionality test" doctrine which reconciles the two previous tests by balancing the objective pursued by the state measure with the effect this measure has on investment. In doing so, this paper will demonstrate that beyond the dogma of *obiter dicta*, tribunals tend to apply, at least implicitly, a proportionality test that comes close to the aforementioned reasoning of the U.S. Supreme Court.[366]

As a result, Part III.B.2.a. argues that the interpretative tools created by the Supreme Court help to clarify and further develop the approach of investment arbitration tribunals to the issue of indirect expropriation. On this basis, analysis will then turn towards the legality of human rights state measures with regard to the prohibition of indirect expropriation. Once again, consistent with its premises, this article will demonstrate that by using the available mechanisms of interpretation developed by the U.S. Supreme Court, arbitration tribunals will rarely come to the conclusion that a non-compensated measure pursuing a human rights objective is in breach of the provision on indirect expropriation in Part III.B.2.b.

a. Methods for Concluding Whether Regulatory Measures Amount to Indirect Expropriation

Under the sole effect doctrine, arbitration tribunals only explicitly take account of the effect of the measure.[367] This doctrine is applied in three different ways.[368]

Following the first one—the most favourable to the investor—a state measure amounts to an expropriation if it affects significantly the value of the investment. As an example, the *Metalclad* tribunal stated that:

> Thus, expropriation under NAFTA includes not only 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,

366 *See* Yannaca-Small, *supra* note 349 at 18, 22.

367 *See id.* at 15.

368 *See* CHRISTOPHER DUGAN, NOAH D. RUBINS, DON WALLACE & BORZU SABAHI, INVESTOR-STATE ARBITRATION 450 (2008).

> in whole or in significant part, of the use or reasonably-to-be-expected economic benefit of property even if not necessarily to the obvious benefit of the host State.[369]

Per the second, a state measure is considered to amount to an expropriation if it deprives the investor of control of her investment. In that sense and referring to the *Pope and Talbot* case,[370] the *Feldman* tribunal contended that:

> [H]ere, as in *Pope & Talbot,* the regulatory action (enforcement of longstanding provisions of Mexican law) has not deprived the Claimant of control of the investment, CEMSA, interfered directly in the internal operations of CEMSA or displaced the Claimant as the controlling shareholder. The Claimant is free to pursue other continuing lines of export trading, such as exporting alcoholic beverages, photographic supplies, or other products for which he can obtain from Mexico the invoices required under Article 4, although he is effectively precluded from exporting cigarettes. Thus, this Tribunal believes there has been no "taking" under this standard articulated in *Pope & Talbot*, in the present case.[371]

Finally, the third trend in the application of the sole effect doctrine bases its reasoning on the destruction of the value of the investment, with no regard for the degree of control left to the investor.[372] Following that trend, the *Tecmed* tribunal declared that:

> To establish whether the Resolution is a measure equivalent to an expropriation under the terms of Section 5(1) of the Agreement, it must be first determined if the Claimant, due to

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369 Metalclad Corp.v. Mex., ICSID Case No. ARB (AF)/97/1, Award, ¶ 130, (Aug. 30, 2000), *available at* http://naftaclaims.com/Disputes/Mexico/MetalcladFinalAward.pdf.

370 Pope & Talbot Inc. v. Government of Can., NAFTA Arb. Trib., Final Awards, ¶ 100 (Nov. 26, 2002).

371 Feldman v. Mex., ICSID Case No. ARB(AF)/99/1, Award on Merits, ¶ 112 (Dec. 16, 2002), *available at* http://italaw.com/documents/feldman_mexico-award-english.pdf.

372 *See* Yannaca-Small, *supra* note 349, at 12.

> the Resolution, 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 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. Those assets and rights of any real substance. Upon determining the degree to which the investor is deprived of its goods or rights, whether such deprivation should be compensated and whether it amounts or not to a *de facto* expropriation is also determined. Thus, the effects of the actions or behaviour under analysis are not irrelevant to determine whether the action or behaviour is an expropriation.[373]

Beyond the dogma of *obiter dicta*, the second and third approaches of the sole effect doctrine do not appear to be more protective of investors than the most balanced and used version of the police power doctrine. Under this version and beyond the rigoristic trend illustrated by the *Methanex* award,[374] a state measure pursuing the realisation of public and general interest that affects the investment does not amount to an expropriation except in extreme situations. Thus, in the *EnCana* case, the arbitration tribunal stated that:

> In the absence of a specific commitment from the host State, the foreign investor has neither the right nor any legitimate expectation that the tax regime will not change, perhaps to its disadvantage, during the period of the investment. Of its nature all taxations reduce the economic benefits an enterprise would otherwise derive from the investment; it will only be in an extreme case that a tax which is general in its incidence could be judged as equivalent in its effect to an expropriation of the enterprise which is taxed.[375]

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373 Técnicas Medioambientales Tecmed, S.A. v. United Mexican States, ICSID Case No. ARB(AF)/00/2, Award, ¶ 115 (May 29, 2003), *available at* http://italaw.com/documents/Tecnicas_011.pdf.

374 *See* Methanex v. United States, NAFTA Arb. Trib., Final Award, ¶ 7 (Aug. 3, 2005).

375 EnCana Corp. (Can.) v. Republic of Ecuador, London Court of International Arbitration, Case No. UN3481, Awards, ¶ 169 (Feb. 3, 2006).

From the perspective of the police power doctrine, this solution seems similar to the one reached by arbitration tribunals in the aforementioned *Feldman* and *Tecmed* cases: a state measure pursuing the public and general interest amounts to an expropriation only in extreme situations—the loss of control or complete destruction of the investment's value.[376]

Beyond the dogma of doctrines, this test can be conceptualized as a technique of interpretation that strikes a balance between public and general interests and the interests of the investor. In practice, the investor bears the brunt of satisfying public and general interest to the point of annihilating his investment.[377] At that point, society assumes the consequences of such satisfaction.[378]

In addition to being at the core of the aforementioned case law,

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376 In that sense, the *Feldman* tribunal made it clear that:

> [N]ot all government regulatory activity that makes it difficult or impossible for an investor to carry out a particular business, change in the law or change in the application of existing laws that makes it uneconomical to continue a particular business, is an expropriation under Article 1110. Governments, in their exercise of regulatory power, frequently change their laws and regulations in response to changing economic circumstances or changing political, economic or social considerations. Those changes may well make certain activities less profitable or even uneconomic to continue.

Feldman v. Mex., ICSID Case No. ARB(AF)/99/1, Award on Merits, ¶ 112 (Dec. 16, 2002), *available at* http://italaw.com/documents/feldman_mexico-award-english.pdf.

377 *See* Yannaca-Small, *supra* note 349, at 18-19.

378 Following this approach, the aforementioned distinction between regulation and expropriation can be discussed. As asked by Judge Higgins: "Is not the State in both cases (that is, either by a taking for a public purpose, or by regulating) purporting to act in the common good. And in each case has the owner of the property not suffered loss?" *Id.* In fact, the author shares the view expressed by Judge Higgins, arguing that the difference between expropriation and regulation based on public purpose is hardly viable intellectually. In this regard, the conclusions reached by Judge Higgins in the context of international law are equally pertinent also for investment law: "A regulation that amounted (by virtue of its scope and effect) to a taking, would need to be 'for a public purpose' (in the sense of in general, rather than for a private, interest). And just compensation would be due. At the same time interferences with property for economic and financial regulatory purposes are tolerated to a significant extent." Rosalyn Higgins, *The Taking of Property by the State: Recent Developments in International Law*, *in* 3 RECUEIL DES COURS 259, 331 (1982).

this technique of interpretation is explicit in the test of proportionality used by some arbitration tribunals.[379] A detailed description of this test can be found in the *Tecmed* case:

> After establishing that regulatory actions and measures will not be initially excluded from the definition of expropriatory acts, in addition to the negative financial impact of such actions or measures, the Arbitral Tribunal will consider, in order to determine if they are to be characterized as expropriatory, whether such actions or measures are proportional 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. Although the analysis starts at the due deference owing to the State when defining the issues that affect its public policy or the interests of society as a whole, as well as the actions that will be implemented to protect such values, such situation does not prevent the Arbitral Tribunal . . . from examining the actions of the State . . . to 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. There must be a reasonable relationship of proportionality between the charge or weight imposed to the foreign investor and the aim sought to be realized by any expropriatory measure. To value such charge or weight, it is very important to measure the size of the ownership deprivation caused by the action of the state and whether such deprivation was compensated or not... it should be also considered that the foreign investor has a reduced or nil participation in the taking of the decisions that affect it.[380]

Under the proportionality test, arbitrators take into account the objectives pursued by the measure, its effect, and the legitimate expectations of the investor.[381] In this sense, it appears to be very

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379 *See* Yannaca-Small, *supra* note 349, at 18.

380 Técnicas Medioambientales Tecmed, S.A. v. United Mexican States, ICSID Case No. ARB(AF)/00/2, Award, ¶ 122 (May 29, 2003), *available at* http://italaw.com/documents/Tecnicas_011.pdf.

381 *See* Yannaca-Small, *supra* note 349, at 21.

similar to the test mentioned in the U.S. BIT model[382] and applied by the U.S. Supreme Court in relation to takings. Given this similarity, the proportionality test needs to be elaborated further in arbitration practice.[383] It is on the basis of the aforementioned U.S. Supreme Court reasoning that, this paper demonstrates that a noncompensated and nondiscriminatory human rights measure—enacted in good faith and in conformity with the law—will rarely be in breach of the provision on indirect expropriation.

b. *Assessment of the Legality of Human Rights State Measures*

The question is here considered when a state measure has the effect of fully depriving the investor of her investment.[384] From this perspective and per U.S. Supreme Court caselaw, this section will follow the legal reasoning of this Court concerning takings.[385] Therefore, with regard to personal property, the expectations of investors must be assessed especially on the basis of the distinct-investment-backed expectations principle. As for land property, the assessment must be made on the basis of the principles which, in the context of the law applicable to investment arbitration, amount to the "background principles of the State's law of property and nuisance" of the United States.[386]

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382 *See id.* at 3.

383 *See id.* at 22.

384 *See id.* at 15. The focus is put on total taking cases and not on partial takings. This focus is justified by the fact that mainstream arbitration practice considers that partial deprivations are not constitutive of an indirect expropriation.

385 *See id.* at 10-15.

386 Treaty Between the Government of the United States of America and the Government of [Country] Concerning the Encouragement and Reciprocal Protection of Investment, *supra* note 223, ¶ 177. This recourse to the "total taking reasoning" developed by the U.S. Supreme Court in relation to lands takings is led by respect for the judicial body's hierarchy in the United States. However, it can be noted that the use of the distinct-investment-backed expectations principle in this situation would reinforce the conclusions reached in this paper. This is so because this principle enlarges the scope of the laws—not only the background principles—which can have the effect, under the condition of an equal treatment of owners, to limit owner's expectations. Furthermore, the U.S. Supreme Court case law tends to highlight the application which can be made of the aforementioned Annex B of the 2004 US BIT Model. In case of total takings, the reference it makes to the distinct-investment-backed expectations tends to put the focus on the background principles. *See* Yannaca-Small, *supra* note 349, at 3

Starting with the personal property of the investor, one should first recall the elements referred to by the U.S. Supreme Court when assessing the takings of such property:[387] (1) the effect of the measure; (2) its character; and (3) the distinct-investment-backed expectations of the owner.[388] The effect of the measure is assessed against the full scope of the claimant's property interest. As for character, the Supreme Court considers whether the regulatory means are proportionate and equitably tailored to the ends.[389] Lastly, the distinct-investment-backed expectations of the owner are assessed with regard to: (a) the notice rule (the state of the regulatory affair in force at the time the person entered into her property); (b) the use of personal property by owners in a similar situation; and (c) specific considerations connected to the overall circumstances of the case.[390]

In the framework of a bona fide state measure which pursues a human rights objective and which, de facto, fully deprives an investor of her property, the distinct-investment-backed expectations principle is the key factor. As for non-discrimination, in the framework of this scenario, all investors in the same situation will be treated equally. Turning to the notice rule, given that human rights norms have been in force since the aftermath of World War II and that investors typically develop an activity in a highly regulated sector, it can be considered that this "human rights normative environment" gives investors notice that a state measure may be enacted which would affect their investment.[391] Lastly, in relation to fairness and the overall circumstances surrounding the case, the existence of a specific commitment or representation may affect the outcome of the test.

In fact, what comes into play here is the legitimate

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387 *See* Penn Cent. Transp. Co. v. City of New York, 438 U.S. 104, 124 (1978).

388 *See id.*

389 *See id.* at 124.

390 *See id.* at 124.

391 *See* Yannaca-Small, *supra* note 349, at 18. Nevertheless, one may consider that under the "character factor" and in relation to the aforementioned analysis of the proportionality test, a state measure enacted for the promotion of a long-term human rights objective and which has the effect of fully depriving an investor of its investment will not pass the *Penn Central* test. On the contrary, it will do so in the cases—the most frequent ones in arbitration practice—where the state measure is enacted to protect a human rights interest in an unforeseeable situation.

expectations created for the investor by a special commitment of the state, promising not to modify the regulatory framework concerning the activity of the investor. But, as previously explained, neither the existence of legitimate expectations nor the mere fact that these have been violated suffices for establishing the liability of the host state. Under the principle of the legitimate expectations, such an infringement has—at the second step of the test—to be balanced against the purpose pursued by the measure in question.

According to the argument concerning the FET clause, the application of proportionality will lead to the conclusion that the infringement of the legitimate expectations of the investor is not justified for measures aiming at the long-term promotion of human rights.[392] If a specific commitment was given by the host state to the investor and the state measure in question is found to pursue a long-term human rights objective, the expropriation will have to be compensated in order to be legal. On the other hand, in principle, the protective measures regarding an unforeseeable situation will pass the balancing test, especially in cases where the enactment of a human rights measure becomes necessary due to the illegal conduct of the investor.[393] Thus, the balancing process that is inherent to the principle of legitimate expectations further reduces the already narrowly defined situations where a state measure enacted pursuant to human rights objectives will be found to breach an investment agreement.[394]

Turning now to land property of an investor, the distinct-investment-backed expectations principle does not apply.[395] As a consequence, a human rights measure that fully deprives the investor of her investment will be presumed to constitute an unlawful expropriation if it is not compensated.[396]

It is suggested here that such a presumption could be rebutted in most situations by assessing the expectations of the investor on the basis of the principles applicable in investment law and equated to the U.S. background principles of the State's law of

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392 *See* Lucas v. S.C. Coastal Council, 505 U.S. 1003, 1025 (1992).

393 *See* Yannaca-Small, *supra* note 349, at 11.

394 *See id.*

395 *Lucas*, 505 U.S. at 1066.

396 *See id.* at 1049; *see* Agins v. Tiburon, 447 U.S. 255, 260-62 (1980).

property and nuisance.[397] Specifically, it is necessary to recall that, according to the relevant U.S. case law, the function of these background principles is not that of balancing the expropriatory effect of the measure in question with its public and general interest purpose.[398] These background principles intervene upstream to deny the existence of a property right which, consequently, cannot be affected by any type of measure.[399]

As Justice Scalia commented in *Lucas*, a background principle cannot be based on law that is "newly legislated or decreed"[400]—it must predate the entry into property. According to the view expressed by the Supreme Court in *Palazzolo*, these background principles are explained in terms of the common, shared understandings of permissible limitations derived from a State's legal tradition.[401] A regulation or common law rule cannot be a background principle for some owners but not for others. The determination of whether an existing, general law can limit all economic use of property must turn on objective factors, such as the nature of the land use proscribed.[402]

Hence, if one relies on U.S. caselaw, one concludes that a state measure enacted to pursue a human rights objective cannot constitute a background principle per se. However, it is contended that the "national and international human rights law background" does so.[403] Thus, relying on human rights law, the assessment of whether the state measure in question has the power to legally limit all economic use of investment without compensation should mainly turn on one objective factor: the nuisance generated by the investment.[404]

An investor cannot expect to cause nuisances affecting human rights without triggering a reaction from the state. This is true

397 *See Lucas*, 505 U.S. at 1029.

398 *See id.* at 1018.

399 *See generally id.* (showing that a governmental land-use regulation that denies the property owner any economically viable use is deemed a taking of the affected property).

400 *Id.* at 1029.

401 *See* Palazzolo v. Rhode Island, 533 U.S. 606, 636 (2001).

402 *See Lucas*, 505 U.S. at 1013.

403 *Id.* at 1035.

404 *See id.*

whatever the responsibility of the investor in the nuisance may be. Obviously this affects an investor who consciously causes such a nuisance due to the illegal nature of her activity or the violation of the rules regulating a lawful business.[405] It also affects those innocent investors whose investments turn out to be harmful.[406] These innocent investors often invest in sensitive sectors of scientific discoveries related to health and the environment.[407] Thus, investors must be conscious of the fact that they operate in a sector of activity whose regulation may be changed in order to answer potential nuisances.[408] In these situations of a nuisance caused by investments, a state measure enacted to protect human rights that fully deprives an investor of her investment should not be considered as violating the provision on indirect expropriation, even if it is not compensated.[409]

It appears that whatever the nature of the property right, there will be very few situations where a human rights state measure will be considered an expropriation requiring compensation to be legal.

Thus, in relation to the outcome of the analysis of the FET, one can conclude that a state measure which pursues a human rights objective will rarely be in breach of investment agreements. Beyond the techniques of interpretation referred to in this section (i.e., the legitimate expectation principle and the distinct-investment-backed expectation principle), it is the aforementioned schizophrenic ethos of the investment law regime that leaves space and requires the balancing of investors and the public and general

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405 *See id.* at 1031.

406 *See Lucas*, 505 U.S. at 1025.

407 *See id.* at 1053.

408 *See id.* at 1030. Furthermore, it has to be remembered that "risk" is part of the definition of "investment."

409 *See id.* This conclusion would not be affected by the existence of a state specific commitment not to modify the normative framework. As for the "guilty investor," if she was granted with a license or a permit or she operates in a freezing normative framework on the basis of a specific commitment, the legitimate expectations thus created are obviously annihilated by their unlawful behaviour. They were indeed not granted with the legitimate expectation to cause nuisance in relation to human rights. Regarding innocent investors, it has been analyzed in relation with the FET provision, that the application of the legitimate expectations principle led to the conclusion that a state measure aiming to protect human rights in an unpredictable and emergency context will pass the balancing test.

interests.[410]

IV. Conclusion

This article aimed at analyzing the situations where a non-discriminatory state measure pursuing a human rights objective may be found in breach of a host state's investment obligation in the context of investment treaty arbitration.

This article argues that when facing this legal question, while arbitrators are entitled to apply human rights norms, they are in no way entitled to assess their violation, as their jurisdiction is only to assess the breach of investment treaties. From this perspective, specific jurisdictional limits affect the applicability of human rights norms.

Beyond applicable law, this article contends that human rights can come into play in the interpretation process, whether through an external or an internal approach. Externally, human rights norms can be taken into account by way of systemic integration. As far as the internal approach is concerned, human rights objectives form part of general and public interest, a concept that is crucial in the framework of the investment law regime.

Being schizophrenic, this regime contains normative tools to strike the balance between the interests of investor and human rights objectives. First of all, treaty provisions do not grant absolute rights to investors.[411] Secondly, the investment law regime contains guiding principles which strike this balance—the legitimate expectations and distinct-investment-backed expectations principles.[412] On the basis of their domestic law origin, the operation of these principles was clarified and elaborated on in the context of investment treaty arbitration. Making use of this investment law tool-box, this article demonstrates that a nondiscriminatory state measure pursuing a human rights objective will rarely be viewed as violating the FET provision or as constituting indirect expropriation.[413]

Through an analysis of the technical tools available to arbitrators in the context of investment law disputes, this article

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410 *See* Yannaca-Small, *supra* note 349, at 2-3.

411 *See id.* at 17.

412 *Id.*

413 *See id.* at 9.

shows that even within the confines of the specific and limited jurisdiction of arbitration tribunals, there is ample room for consideration of human rights related issues. From a utilitarian perspective, this article invites the promoters of human rights to move beyond semantic activism focusing on the literal absence of human rights in investment law treaties and underlying their criticism of the regime as a whole. Rather, these promoters should adopt a more constructive approach by looking within the regime itself to see how its tools can be used to promote human rights, regardless of the semantics used. Indeed, to reverse the famous aphorism, not only must justice be seen to be done, but it must be actually done to be seen.