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법학 전문박사 학위논문

A Standard Public Order Treaty
Carve-out as a Means for Balancing
Regulatory Interests in International
Investment Agreements

규제권을 위한 조정 수단으로의 공공 질서
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Abstract

A Standard Public Order Treaty Carve-out as a Means for Balancing Regulatory Interests in International Investment Agreements

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Since the start of the BIT program, the purpose of BITs was predominantly motivated by the sole objective of providing foreign investment protection mostly for the benefit of the capital-exporting, developed countries. The capital-importing, developing countries entered into BITs to attract foreign investment without a comprehensive awareness of the legal ramifications of BITs.

However, the conclusion of FTAs with investment chapters such as the NAFTA expanded the narrowly conceived BIT goal of investment protection to include other purposes like investment promotion and liberalization. Prior to the NAFTA, carving out policy space in international investment agreements (IIAs) was not a real concern until the NAFTA experience demonstrated that investor-State arbitrations could be initiated not only against the developing States, but also against the developed States. Moreover, the ICSID cases against Argentina have been instrumental in bringing attention to the need of host States to exercise regulatory power.

These experiences helped to create an understanding for both the developed and developing States that a significant legal consequence of concluding IIAs is that their sovereign right to regulate various aspects of public interest might result in a breach of the IIA.

The objective of this research is to fill a meaningful gap in international investment law to enable States to better exercise their sovereign right to regulate by using the public order clause in the non-precluded measures provision of the U.S.-Argentina BIT as a starting point. The questions asked in this study include whether a public order carve-out for public interest matters is emerging and, if so, whether the public order carve-out can equip host States with the flexibility needed to exercise their regulatory authority.

This research makes the discovery that the concept of public order is undefined in international investment law making it difficult for investment tribunals to interpret the public order carve-out in a consistent and predictable manner. On one level, the notion of the right to regulate is being incorporated in the most current versions of IIAs without an appreciation of how it should apply in international investment law despite the lessons exemplified in the ICSID arbitrations against Argentina. On another level, BITs have been designed to usually only contain substantive obligations. Although the recent trend of IIAs is to include some variation of a general exceptions provision to limit the scope of the substantive obligations, the practice remains largely inconsistent and borrowed from the WTO/GATS jurisprudence. However, this research concludes that the inclusion of a standard public order carve-out specifically aimed at preserving the regulatory space of States should become a fixed feature of future investment

treaties to better address the growing aggregate community interests of IIA stakeholders. This ultimately requires that the base values and concerns of the participants in international investment law be evaluated.

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Keywords: public order, standard carve-out, IIA exceptions, right to regulate, investment protection, necessity defense

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Chapter 1: Introduction

I. Trends of International Investment Agreements

A. Changes in BIT/IIA Perspective

The purpose of bilateral investment treaties (BITs) is to provide foreign investment protection. Before the making of the European BIT program with the conclusion of the Germany-Pakistan BIT in 1959, protection of foreign investment was partially addressed under Friendship, Commerce and Navigation (FCN) treaties. However, FCN treaties lacked the characteristics to persuade developing countries that they could provide investor protection guarantees and an effective dispute settlement mechanism because they also covered non-commercial areas such as consular relations, immigration, religious and individual rights while also containing protectionist policies.¹ However, the Germany-Pakistan BIT set itself apart from the typical FCN treaties available during the post-WWII era by providing many substantive investment protection provisions that still resonate in modern international investment agreements (IIAs) and by also introducing the State-to-State dispute settlement mechanism which allowed disputes to be submitted either before the ICJ (International Court of Justice) or an arbitration tribunal. Since the conclusion of the first BIT, about 20 BITs

¹ K. Scott Gudgeon, *United States Bilateral Investment Treaties: Comments on their Origin, Purposes, and General Treatment Standards*, 4 INT'L TAX & BUS. LAW. 105, 108-9 (1986). See R. DOAK BISHOP, JAMES CRAWFORD & W. MICHAEL REISMAN, FOREIGN INVESTMENT DISPUTES: CASES, MATERIALS AND COMMENTARY 32 (Kluwer Law Int'l 2005); JESWALD W. SALACUSE, THE THREE LAWS OF INTERNATIONAL INVESTMENT: NATIONAL, CONTRACTUAL, AND INTERNATIONAL FRAMEWORKS FOR FOREIGN CAPITAL 340 (Oxford Univ. Press 2013); JAN OLE VOSS, THE IMPACT OF INVESTMENT TREATIES ON CONTRACTS BETWEEN HOST STATES AND FOREIGN INVESTORS 51 (Martinus Nijhoff 2011).

were concluded every year from the 1960s to the 1980s.² During this timeframe, many of the BITs were negotiated between a developed and developing country and/or a transition economy. Unlike Europe, however, the United States was not quick to abandon its FCN treaty program believing it to be capable of establishing commercial relationships with developing countries.³ Moreover, as a strong supporter of the Hull Rule, the United States feared that the European BIT model would replace the expropriation standard provided under customary international law to the disadvantage of U.S. nationals.

By the late 1960s and the early 1970s, two major developments affecting Europe and the United States revealed that the international legal system did not foster an international investment climate which was favorable to either the developing or developed countries. From the European perspective, some developing countries targeted investments owned by investors from the former colonial powers of Europe by implementing expropriation policies that contradicted the established international law principles advocated by developed countries.⁴ Meanwhile, the United States had difficulty appealing to the developing countries using

² See Guzman et al., *Competing for Capital: The Diffusion of Bilateral Investment Treaties, 1960-2000*, 2008 U. ILL. L. REV. 265, 269-70 (2006).

³ Gudgeon, *supra* note 1, at 108; KENNETH J. VANDEVELDE, *U.S. INTERNATIONAL INVESTMENT AGREEMENTS* 23 (Oxford Univ. Press 2009).

⁴ Patrick Juillard, OECD, *Bilateral Investment Treaties in the Context of Investment Law*, in *Investment Compact Regional Roundtable on Bilateral Investment Treaties for the Protection and Promotion of Foreign Investment in South East Europe* (May 28-29, 2001), <http://www.oecd.org/investment/internationalinvestmentagreements/1894794.pdf>. See also Gudgeon, *supra* note 1, at 110.

a broad economic instrument like a FCN treaty. The United States was slow to embrace bilateral arrangements, but a decision was made in 1981 under the Reagan administration that the U.S. government could better promote its foreign policy including the Hull Rule to developing countries by entering into European-style BITs that contain only the essential investment protection provisions.⁵

The negotiating pattern changed during the 1990s as developing countries concluded more BITs with other developing countries and transition economies than with developed countries.⁶ During the golden years of the BITs from the 1990s to the 2000s, about 160 BITs were concluded annually.⁷ The proliferation of BITs gained momentum during this era as developing countries incorporated BITs into their national economic development schemes for the promotion of FDI.⁸ The culmination of the U.S. BIT program may have been realized when the NAFTA was concluded in 1993. Under the NAFTA, the initial goal of the BIT expanded from investment protection to also cover investment promotion and market liberalization. Perhaps more strikingly, these goals were no longer limited to the bilateral economic arrangements offered in BITs, but placed within the

⁵ Guzman et al., *supra* note 2, at 271.

⁶ *Id.*

⁷ DANIEL W. DREZNER, *THE SYSTEM WORKED: HOW THE WORLD STOPPED ANOTHER GREAT DEPRESSION* 53 (Oxford Univ. Press 2014). See Guzman et al., *supra* note 2, at 269.

⁸ See UNCTAD, *BILATERAL INVESTMENT TREATIES: 1959-1999*, UNCTAD/ITE/IIA/2 (2000) [hereinafter UNCTAD, BITs], available at <http://unctad.org/en/docs/poiteiad2.en.pdf>.

FTA framework so that detailed investment provisions would be available as a separate investment chapter alongside other chapters on trade. The period after the NAFTA through the 2000s saw an increase in the conclusion of FTAs, which led to the conclusion of FTAs with investment chapters and, more recently, to the conclusion of mega FTAs involving greater regional blocs. In a moderately short period of time, BITs and investment chapters in FTAs influenced the development of the international investment regime.⁹ The number of BITs steadily decreased as investment treaty-making gradually shifted towards regionalism, but the number of investment chapters in bilateral/regional FTAs increased,¹⁰ paving the way for megaregional treaties such as the Trans Pacific Partnership (TPP)¹¹ as well as the Transatlantic Trade and Investment Partnership (TTIP)¹² and Regional Comprehensive Economic Partnership (RCEP) which are currently under negotiations.

By the end of 2015, a total of 3,304 IIAs, comprising of 2,946 BITs and 358 TIPs (treaties with investment provisions) were concluded.¹³ Despite the

⁹ Jeswald W. Salacuse & Nicholas P. Sullivan, *Do BITs Really Work?: An Evaluation of Bilateral Investment Treaties and Their Grand Bargain*, 46 HARV. INT'L L.J. 67 (2005).

¹⁰ UNCTAD, WORLD INVESTMENT REPORT 2012: TOWARDS A NEW GENERATION OF INVESTMENT POLICIES 84, U.N. Doc. UNCTAD/WIR/2012 (July 4, 2012). See, e.g., Jennifer L. Tobin & Marc L. Busch, *A BIT is Better than a Lot: Bilateral Investment Treaties and Preferential Trade Agreements*, 62 WORLD POLITICS 1 (2010) (stating that a BIT between developed and developing countries usually leads to an international trade agreement).

¹¹ Trans Pacific Partnership, Feb. 4, 2016 [hereinafter TPP].

¹² Transatlantic Trade and Investment Partnership (investment chapter draft) [hereinafter TTIP (draft)], available at http://trade.ec.europa.eu/doclib/docs/2015/september/tradoc_153807.pdf.

¹³ See UNCTAD, WORLD INVESTMENT REPORT 2016: INVESTOR NATIONALITY: POLICY

record-setting cumulative number of IIAs, only 31 new IIAs were concluded in 2015.¹⁴ Just as the 2014 World Investment Report predicted that megaregional agreements will have “a major impact” on investment rule-making and worldwide investment patterns once they enter into effect, the 2016 edition of the same report affirms that megaregional agreements could unite a deeply fragmented international investment system by *de facto* multilateralizing international investment law.¹⁵ Alternatively,

CHALLENGES 101, U.N. Doc. UNCTAD/WIR/2016 (June 22, 2016) [hereinafter WIR 2016] (noting that the top contracting State was Brazil which concluded six IIAs, followed by Korea and Japan with four IIAs, and China with three IIAs).

¹⁴ *See id.* (stating that 31 new IIAs were concluded in 2015, of which six were concluded by Brazil, four by Korea and Japan respectively, and three by China).

¹⁵ *Id.* at 185 (citing to UNCTAD, WORLD INVESTMENT REPORT 2014: INVESTING IN THE SDGs: AN ACTION PLAN 118, U.N. Doc. UNCTAD/WIR/2014 (June 24, 2014) [hereinafter WIR 2014]). For the fragmentation debate, *see* Anne van Aaken, *Fragmentation of International Law: The Case of International Investment Law*, in 17 FINNISH YEARBOOK OF INT’L LAW 91 (Jan Klabbers & Katja Creutz eds., 2008) (arguing that the fragmentation issue should be viewed from the perspective that the international investment regime needs to evolve for compatibility with other areas of international law including human rights law, multilateral environmental treaties, and WTO law); John F. Coyle, *The Treaty of Friendship, Commerce and Navigation in the Modern Era*, 51 COL. J. TRANSNAT’L L. 302, 345-47 (2013) (proposing that a modern version of the FCN treaty model could address the problem of fragmentation in international investment law better than specialized investment treaties). *Cf.* STEPHAN W. SCHILL, THE MULTILATERALIZATION OF INTERNATIONAL INVESTMENT LAW 361 (Cambridge Univ. Press 2009) (contending that investment tribunals produce jurisprudence that “put into practice a system that behaves and functions according to multilateral rationales and does not, despite the existence of innumerable bilateral investment relationships, dissolve into infinite fragmentation”); Joost Pauwelyn, *At the Edge of Chaos? Foreign Investment Law as a Complex Adaptive System, How it Emerged and How it Can be Reformed* (2014), available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2271869&download=yes (explaining that although the investment law regime is in a haphazard state of fragmentation, it “may not be one of law’s most pathological sub-field in need of top-to-bottom reform” and instead may offer “an organizational life form more similar to species that have survived evolutionary biology and, in this sense, be a model that other legal regimes may want to copy from”). For the overlap debate, *see* Andreas Ziegler, *Is it Necessary to Avoid Substantive and Procedural Overlaps with Other Agreements in IIAs?*, in IMPROVING INTERNATIONAL INVESTMENT

megaregional agreements may further exacerbate the problem of inconsistencies due to the overlaps between existing IIAs and the newly concluded investment treaties. The overlap of the megaregional FTAs with more than 140 existing international investment agreements has been estimated to create more than 200 new BIT relationships.¹⁶ The proposed EU-Vietnam FTA¹⁷ will overlap with 21 BITs whereas the Canada-EU CETA¹⁸ overlaps with seven BITs,¹⁹ but existing BITs/IIAs will be terminated. This is in contrast to the TPP, which overlaps with 39 IIAs, but does not stipulate anywhere in the treaty that the existing IIAs of the 12 contracting States will be terminated.²⁰

Even though BITs and other IIAs are still evolving and engaging a more diverse group of stakeholders that transcends the relationship between States and foreign investors, the objective rooted since the early BITs that they primarily provide protection of foreign investors and investments has been slow to adapt to the swift changes occurring in international investment law. Prior to the NAFTA, carving out policy space in international

AGREEMENTS 158, 160-73 (Armand de Mestral & Celine Levesque eds., 2013) (stating that the overlapping dispute settlement provisions in international economic agreements like the WTO, regional trade agreements, and IIAs causing the spaghetti bowl effect is not entirely detrimental to efficiency).

¹⁶ WIR 2014, *supra* note 15, at xxv.

¹⁷ EU-Vietnam FTA [awaiting signature].

¹⁸ Canada-European Union Comprehensive Economic and Trade Agreement, Oct. 30, 2016 [hereinafter Canada-EU CETA].

¹⁹ WIR 2016, *supra* note 13, at 112 & 114-15.

²⁰ *Id.*

investment agreements was not a real concern for developed countries. But the NAFTA experience rapidly demonstrated that developed countries like the United States could become a respondent State in an investor-State dispute. In hindsight, the various stages of investment treaty evolution reflect the struggles faced by developed and developing countries to create a balanced framework that meets the “unique expectations and demands”²¹ and “biases and interests”²² of the various stakeholders in international investment law. The progression from FCNs to BITs followed by a movement towards regional FTAs with investment chapters to megaregional agreements also reflect a shift towards a more balanced relationship among the various participants of international investment law. The main stakeholders in the early generation of BITs were the developed, home States and their investors and the developing, host States. Early BITs/FCNs were not investment treaties between equals and was based on an unbalanced power relationship where customary international law principles like the guarantee of a minimum standard of protection and compensation for expropriation were viewed negatively by developing countries as poverty-maintaining restrictions that ignored the needs of their countries.²³ Without genuine concern for the sustainable economic prosperity of the developing countries, the investment climate of the time privileged developed countries that had the advanced skills to monetize the

²¹ Christopher M. Ryan, *Meeting Expectations: Assessing the Long-Term Legitimacy and Stability of International Investment Law*, 29 U. PA. J. INT’L L. 725, 726 (2008).

²² Rebecca M. Bratspies, *Rethinking Decisionmaking in International Environmental Law: A Process-Oriented Inquiry into Sustainable Development* 32 YALE J. INT’L L. 369, 375 (2007).

²³ Salacuse & Sullivan, *supra* note 9, at 68-69.

natural resources of the developing countries. However, recently concluded megaregional agreements and other modern IIAs reflect public policies inputted by an increased variety of stakeholders that include international organizations, academics, civil society organizations, foreign investors, host States, and home States. The cooperative effort of this diverse group of stakeholders form the basis of the ongoing IIA reform efforts so that modern IIAs may continue to provide standards of protection, promotion, and liberalization while also preserving the domestic regulatory space of host States. The international investment law-making process should not merely be restricted to legal instruments such as court decisions and treaties, but acknowledge the social, economic, and political factors that affect stakeholders like the developed and developing countries and private investors and other stakeholders such as civil societies, academia, and individuals.²⁴

The widespread proliferation of IIAs currently engages most countries to at least one investment treaty, but the level of investment treaty participation does not correlate with general satisfaction towards the international investment law regime.²⁵ The effectiveness of BITs as a promoter of foreign direct investment is certainly one area of concern,²⁶ but

²⁴ See Bratspies, *supra* note 22, at 369. See also Myres S. McDougal, Harold D. Lasswell, & Michael Reisman, *The World Constitutive Process of Authoritative Decision*, 19 J. LEGAL EDUC. 253, 253-58 (1967).

²⁵ UNCTAD, WORLD INVESTMENT REPORT 2015: REFORMING INTERNATIONAL INVESTMENT GOVERNANCE 124, U.N. Doc. UNCTAD/WIR/2015 (June 24, 2015) [hereinafter WIR 2015].

²⁶ See generally Mary Hallward-Driemeier, *Do Bilateral Investment Treaties Attract FDI? Only a Bit... And They Could Bite* (World Bank Policy Research Working Paper No. 3121, 2003), available at

more significantly, the proper role of investment tribunals in adjudicating the policy space of host States has garnered serious attention in the last decade or so. From 2005 to 2008, the ICSID tribunals ordered Argentina to pay more than \$450 million plus interest for having implemented emergency measures during its financial crisis that unilaterally changed the terms of the investment between the government and foreign investors.²⁷ As will be discussed in greater detail in Chapter 4, the investor-State dispute settlement (ISDS) system was criticized by developed and developing countries for transgressing into the regulatory space of a host State because the cost of implementing policy measures for the maintenance of public order was deemed too costly.²⁸ The NAFTA arbitration experience is no better with U.S. investors being accused of exerting influence to make the environmental laws of Canada less burdensome for themselves. Canada has been sued the most among the NAFTA countries and ordered to pay U.S. investors under six occasions due to its environmental legislations.²⁹ One of the largest

http://papers.ssrn.com/sol3/papers.cfm?abstract_id=636541 (questioning whether BITs have increased FDI flows to signatory countries); *see also* Susan Rose-Ackerman & Jennifer Tobin, *Foreign Direct Investment and the Business Environment in Developing Countries: The Impact of Bilateral Investment Treaties* (Yale Law & Economics Research Paper No. 293, 2005), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=557121&rec=1&srcabs=636541&alg=1&pos=1; Susan D. Franck, *Foreign Direct Investment, Investment Treaty Arbitration and the Rule of Law*, 19 MCGEORGE GLOBAL BUS. & DEV. L.J. 337 (2007) (concluding that the exact effect of investor-State dispute on FDI is not discernible).

²⁷ *See, e.g., Argentina Settles Five Investment Treaty Awards*, Nov. 7, 2013, <http://www.allenoverly.com/publications/en-gb/Pages/Argentina-settles-five-investment-treaty-awards.aspx>.

²⁸ WIR 2016, *supra* note 13, at 105 (observing that the U.S.-Argentina BIT continues to attract the most investor-State arbitrations for investment disputes arising out of a bilateral investment treaty).

²⁹ Sunny Freeman, *NAFTA's Chapter 11 Makes Canada Most-Sued Country Under Free*

payout in NAFTA's history occurred in 2010, when Canada paid C\$130 million for expropriating the assets of AbitibiBowater Inc., a forestry giant company incorporated in Delaware.³⁰ One potential concern is that the NAFTA may prevail over policy regulations affecting the environment, health, or safety by preventing countries like Canada from enacting measures for legitimate public concerns.³¹ In 2011, Australia criticized the ISDS system when Philip Morris Asia Limited, a company incorporated in Hong Kong, deliberately engaged in forum shopping to access the ISDS clause under the Australia-Hong Kong BIT so that the investor could demand compensation for Australia's legislation on plain cigarette packaging.³² Australia said that it would reject the ISDS during the TPP negotiations,³³ but has agreed to it in subsequent agreements such as the Korea-Australia FTA and the China-Australia FTA.³⁴ In 2012, Vattenfall, a

Trade Tribunals, HUFFINGTON POST (Jan. 14, 2015) (identifying the , http://www.huffingtonpost.ca/2015/01/14/canada-sued-investor-state-dispute-ccpa_n_6471460.html).

³⁰ *Id.* (amount shown in Canadian dollars).

³¹ Joseph E. Stiglitz, *The Broken Promise of NAFTA*, N.Y. TIMES (Jan. 6, 2004), available at http://www.nytimes.com/2004/01/06/opinion/the-broken-promise-of-nafta.html?_r=0 ("NAFTA will stifle regulation, no matter how important for the environment, health or safety").

³² Philip Morris Asia Ltd. v. Australia, UNCITRAL, PCA Case No. 2012-12, Written Notification of Claim (June 27, 2011).

³³ *Australia to Reject Investor-State Dispute Resolution in TPPA*, INVESTMENT TREATY NEWS (Apr. 13, 2012), <http://www.iisd.org/itn/2011/07/12/australias-rejection-of-investor-state-dispute-settlement-four-potential-contributing-factors/>.

³⁴ Korea-Australia FTA, art. 11.16, Apr. 8, 2014. *Cf.* China-Australia FTA, art. 9.4.2, June 17, 2015 (excluding application of most favored nation (MFN) standard on the ISDS provision by stating, "For greater certainty, the [MFN] treatment referred to in this Article does not encompass Investor-State Dispute Settlement procedures or

Swedish state-owned energy company, initiated an arbitration claim against Germany under the Energy Charter Treaty (ECT) to supposedly demand somewhere between four and six billion euros in compensation for adopting a legislation that would phase out Germany's nuclear power plants; the German legislation was enacted in response to the Fukushima disaster.³⁵ In 2012, India announced that it would reject the ISDS system and renegotiate existing IIAs³⁶ to abolish the ISDS mechanism to preserve its public policy.³⁷ In 2016, the Indian government released the revised India Model BIT which requires that local remedies be exhausted before arbitration can be accessed unless the investor can prove that no reasonable relief is available during a five-year period which is to be followed after a six-month cooling-off period.³⁸ Similarly, in 2015, the South African parliament passed the Protection of Investment Act requiring investment disputes brought by both foreigners and nationals to be resolved either under domestic mediation or through its local courts.³⁹ As a response to these situations where host States are being challenged in an international investment tribunal for regulating

mechanisms.”).

³⁵ *Vattenfall v. Germany*, ICSID Case No. ARB/12/12 (May 31, 2012).

³⁶ This renegotiation effort may also affect the Korea-India Comprehensive Economic Partnership Agreement, which was signed on August 7, 2009 and went into effect in both countries in November 2009.

³⁷ Eun-Joo Jung, *India Plans to Abolish ISD Clause in FTAs*, HANKYOREH, Apr. 6, 2012, http://www.hani.co.kr/arti/english_edition/e_international/527103.html.

³⁸ India Model BIT, art. 15.1 (2016), available at http://finmin.nic.in/the_ministry/dept_eco_affairs/investment_division/ModelBIT_Annex.pdf [hereinafter 2016 India Model BIT].

³⁹ Protection of Investment Act 22 of 2015 s. 13.

their public interest, the EU has proposed the creation of an investment court system. The EU-Vietnam FTA (which is expected to go into effect in 2018), the Canada-EU CETA, and the EU proposal to the TTIP (which is under negotiations) each contains an investment court system to replace the current arbitration-based ISDS system. The EU-Vietnam FTA proposal creates an independent investment court system consisting of a permanent tribunal of nine members and an appeal tribunal. Although the number of tribunal members will vary by investment treaty, the basic framework remains the same.⁴⁰ It remains to be seen whether the coming generation of IIAs, in particular, the megaregional agreements providing for an investment court system will further promote the proliferation of investment treaties.

Prior to the era of BITs, foreign investment was governed by customary international law and domestic laws to cover the needs of foreign investors.⁴¹ But the evolution of investment treaties eventually produced a sophisticated generation of IIAs that today represents “the most important source of contemporary international investment law.”⁴² The investment treaty purpose of providing guarantees on the protection and treatment of foreign investment has been essential for preventing expropriatory acts and providing remedies, usually through compensations, in cases of host State intervention in matters affecting foreign investors and their investments.

⁴⁰ EU-Vietnam FTA, *supra* note 17, arts. 12-15.

⁴¹ See generally RUDOLF DOLZER & CHRISTOPH SCHREUER, PRINCIPLES OF INTERNATIONAL INVESTMENT LAW 6 (Oxford Univ. Press 2d ed. 2012); Ryan, *supra* note 21, at 730-31.

⁴² DOLZER & SCHREUER, *supra* note 41, at 13. For a historical account of the treatification process for the international framework on investment, see SALACUSE, *supra* note 1, at 332-363.

While variations exist among the few thousand IIAs, investment treaties usually consist of a three-part structure which includes a definitions section for the technical terms used in the agreement, a section that establishes the substantive standards for investment and investor protection, and lastly, a section that provides the procedural rules for dispute settlement. IIAs are often organized into core provisions that address the scope of application, conditions for the entry of foreign investment, general standards of treatment of foreign investments, monetary transfers, operational conditions of the investment, protection against expropriation, compensation for losses, and dispute settlement mechanism.

Such protective mechanisms were necessary because capital-exporting, developed countries sought from their negotiating partners, which were usually capital-importing, developing countries, a favorable investment climate that would not jeopardize the entry and operation of investments made developed countries.⁴³ Developing countries signed investment treaties to receive the foreign capital that would be needed to advance their national economic goals and, in the long run, this has helped to facilitate market liberalization and modernize the foreign investment laws of those countries. Investment treaties can also contribute to the promotion of investments, although they never obligate a contracting State to require its nationals to make foreign investments in the other contracting State,⁴⁴ by prompting host States to establish a stable legal framework conducive to

⁴³ ANDREW NEWCOMBE & LLUÍS PARADELL, *LAW AND PRACTICE OF INVESTMENT TREATIES: STANDARDS OF TREATMENT* 76 (2009).

⁴⁴ Salacuse & Sullivan, *supra* note 9, at 95.

attracting and maintaining foreign investment.⁴⁵ Although the purpose of modern IIAs also embodies the preservation of the States' right to regulate, current reform efforts should better clarify the standard of review for investment treaty carve-outs that enables States to regulate issues of public interest.⁴⁶

One of the ways that IIAs gain meaning is when an investor-State arbitration is brought before the International Centre for Settlement of Investment Disputes (ICSID), which was established in 1965 and formulated model arbitration clauses for BITs in 1969.⁴⁷ Almost soon after the Second World War, the United States' policy was to avoid military action by peacefully binding countries to investment treaties. U.S. FCN treaties permitted future investment disputes to be adjudicated before the ICJ as long as a treaty existed between the United States and the disputing State.⁴⁸ However, the United States rarely needed to bring an investment dispute before the ICJ⁴⁹ because it was usually successful in negotiating lump-sum settlements, which would then be apportioned to the U.S. claimants

⁴⁵ *Id.*

⁴⁶ See Roberto A. Luzi, *BITs & Economic Crises: Do States Have Carte Blanche?*, in INVESTMENT TREATY ARBITRATION AND INTERNATIONAL LAW (T. J. Grierson Weiler ed., 2008), available at http://apps.americanbar.org/intlaw/fall09/materials/Aguirre%20Luzi_Roberto-State%20of%20Necessity.pdf.

⁴⁷ The Chad-Italy BIT was signed on November 6, 1969 and contained the first binding investor-State arbitration provisions.

⁴⁸ KENNETH J. VANDEVELDE, UNITED STATES INVESTMENT TREATIES: POLICY AND PRACTICE 13 (Springer 1992).

⁴⁹ With the exception of the case involving Italy in *Elettronica Sicula (ELSI)* (U.S. v. Italy), 1989 I.C.J. Rep. 15 (July 20).

whenever a host State expropriated the property of U.S. investors.⁵⁰ This similar situation of dominance was also evident in the early European model of international investment protection.⁵¹ But this approach was flawed for a couple of reasons. As previously mentioned, the U.S. FCN treaty program basically failed to engage developing countries since, without a treaty, recourse to the ICJ was not an option for American investors whose property was expropriated by the host State. Assuming that an investment treaty existed between the U.S. and the other State, the U.S. investor had to resort to diplomatic protection to access the ICJ, which would then decide whether or not to hear the case. Moreover, even in the case a judgment was rendered, an additional step requiring the endorsement of the UN Security Council was necessary. This exasperating process was halted by the creation of the investor-State dispute settlement system, which effectively changed the way foreign investors could expect to receive investment protection even though the first case was not heard in the ICSID until seven years after its establishment.⁵² By authorizing private investors to directly sue the host State, the establishment of the ICSID dramatically elevated the importance of BITs.⁵³ Despite the initial lack of response towards the ICSID dispute

⁵⁰ VANDEVELDE, *supra* note 48, at 14.

⁵¹ See Francesco Francioni, *Access to Justice, Denial of Justice and International Investment Law*, 20 EJIL 729, 730 (2009).

⁵² Convention on the Settlement of Investment Disputes Between States and Nationals of Other States, Mar. 18, 1965, 575 U.N.T.S. 159 [hereinafter ICSID Convention].

⁵³ Salacuse & Sullivan, *supra* note 9, at 70 (“For all practical purposes, BIT law has become the fundamental source of international law in the area of foreign investment.”).

settlement mechanism, the majority of investors today prefer to bring claims under ICSID. Of the 70 known ISDS cases initiated by foreign investors in 2015, 80 percent of the claimants are from developed countries and taking the lead are the United Kingdom, Germany, Luxembourg and the Netherlands.⁵⁴

B. Aggregate Community Interests of the IIA Stakeholders

1. Host States

As one of the principal participants in the international investment regime, host States may be brought before an investment tribunal by a foreign investor under the investor-State provision of IIAs. Despite the risk of an arbitration loss and the possibility that investment tribunals may enter into their regulatory space, host States conclude IIAs to demonstrate that they can provide investment protection, security, transparency, stability, and predictability.⁵⁵ However, the need for host States to keep their domestic regulatory space by carving out treaty exceptions such as the public order carve-out is growing in importance. In order for the international investment regime to endure, it is critical that host States are not subjected to large, unanticipated payouts⁵⁶ even if the concept of sovereignty has

⁵⁴ WIR 2016, *supra* note 13, at 104-5 (record number of cases in a single year).

⁵⁵ See Lauge S. Poulsen & Emma Aisbett, *When the Claim Hits: Bilateral Investment Treaties and Bounded Rational Learning* (Crawford School Research Paper No. 5, 2011), available at https://crawford.anu.edu.au/pdf/crwf_ssrn/crwfrp_1105.pdf (revealing through an empirical study that developing states had entered into investment treaties in the 1990s without fully appreciating their risks and effect on domestic economic policies).

⁵⁶ To illustrate, upon finding that Russia had breached the Energy Charter Treaty, the UNCITRAL arbitral tribunal demanded in July 2014 that Russia make a payment of \$50 billion in compensation to the claimants. *E.g.*, Martin D. Brauch, *Yukos v. Russia: Issues and Legal Reasoning Behind U.S.\$50 Billion Awards*,

strayed away from its traditional meaning in many areas of public international law.⁵⁷

Although host States want to attract foreign investment to promote growth and sustainable economic development, they have become selective about how they want to pursue those goals, how much market access to give foreign investors, and how much protection should be afforded to their investments.⁵⁸ Traditional base values considered of significance to host States have related to the maintenance of sovereignty, the guarantee that natural resources will not be extorted or managed in a way to bring harm to the host State, and the assurance that local laborers will be compensated appropriately and acquire improved skills and competencies, and the

INVESTMENT TREATY NEWS (Sep. 4, 2014),
<https://www.iisd.org/itn/2014/09/04/yukos-v-russia-issues-and-legal-reasoning-behind-us50-billion-awards/>.

⁵⁷ Scholars vary on their opinion on whether sovereignty is losing importance in public international law. *E.g.*, John Laughland, *National Sovereignty is More Important than International "Justice"*, BRUSSELS J. (Jan. 26, 2009) (examining sovereignty in the context of international criminal law and stating that "[w]hat used to be the uncontested cornerstone of the international system will have become a dead letter – and even a principle associated with the worst abuses of human rights"), available at <http://www.brusselsjournal.com/node/3759>; Ruti Teitel, *National Sovereignty: A Cornerstone of International Law – and an Obstacle to Protecting Citizens*, LEGAL AFFAIRS (2002) (stating that the "rise of global politics has led to increasing cooperation among nations and to the emergence of a more humble conception of national sovereignty"), available at http://www.legalaffairs.org/issues/September-October-2002/feature_teitel_sepoct2002.msp. *But cf.* Kal Raustiala, *Rethinking the Sovereignty Debate in International Economic Law*, 6 J. INT'L ECON. L. 841, 843 (2003) (arguing that global economic institutions including the WTO "enhance sovereignty").

⁵⁸ See UNCTAD, WORLD INVESTMENT REPORT 2013: GLOBAL VALUE CHAINS: INVESTMENT AND TRADE FOR DEVELOPMENT 96, U.N. Doc. UNCTAD/WIR/2013 (June 25, 2013) [hereinafter WIR 2013] ("While countries remain eager to attract FDI, several have become more selective in their admission procedures.").

prevention of capital flight or a hollowing out effect. When drafting the State's foreign investment law, the legislature of a host State will deliberate on those factors and may also statutorily require a screening process that reviews foreign investment proposals. Recent IIAs have seen an expansion of the role of IIAs to include non-traditional aspects of community life like the preservation of the environment (such as the protection of human, animal or plant life or health and the conservation of exhaustible natural resources) and the creation of jobs under conditions that support labor rights.⁵⁹ Some host States like those in Africa additionally require that foreign investments make contributions that alleviate poverty, create goods and services for the poor, or associate with small- and medium-sized domestic enterprises.⁶⁰ Host States are increasingly requiring that foreign investors conduct themselves in a socially responsible manner and make investments according to the sophisticated demands of the various actors in an intertwined global community. However, this is much easier stated than practiced: domestically, host States have the sovereign right to revoke their foreign investment law including those provisions related to foreign investor and investment protection while, internationally, host States may be brought to international arbitration by private foreign individuals if an IIA obligation has been violated.⁶¹

⁵⁹ *Id.* at 102.

⁶⁰ *Id.* at 43.

⁶¹ See Hi-Taek Shin & Julie A. Kim, *Balancing the Domestic Regulatory Need to Control the Inflow of Foreign Direct Investment Against International Treaty Commitments: A Policy-Oriented Study of the Korean Foreign Investment Promotion Act and the Korea-U.S. FTA*, 19 ASIA PAC. L. REV. 177, 188 (2011).

Historically, countries have been categorized as developing or developed based on their GDP level as compared to other countries. Internationally agreed criteria do not exist even within the WTO,⁶² but one measure may include the international capital flow of the States to determine whether a country is developed or developing.⁶³ A clear capital-exporting, developed State would want to ensure maximum protection of its citizens and therefore favors investment treaties that over-provide investor protection. In contrast, a clear capital-importing, developing State might conclude investment treaties that under-provide investor protection as exemplified by the early Chinese BITs.⁶⁴ But the classification is less relevant today with the rise of States, especially among the Asian countries, taking on the dual role of recipient and provider of foreign investment so that the capital-exporting, developed countries are no longer the sole providers of foreign capital, but also recipients of foreign investments that could become a respondent host State in an investor-State arbitration.⁶⁵ Europe and the

⁶² WTO, UNDERSTANDING THE WTO: LEAST-DEVELOPED COUNTRIES, https://www.wto.org/english/thewto_e/whatis_e/tif_e/org7_e.htm (“There are no WTO definitions of ‘developed’ or ‘developing’ countries.”).

⁶³ Other measures include the Human Development Index produced by the United Nations Development Programme (UNDP), which measures economic measures (such as national income) and social measures (like life expectancy and education). In 2015, the World Bank listed the median per capita (as opposed to the mean income) and household income to rank the countries.

⁶⁴ See, e.g., NEWCOMBE & PARADELL, *supra* note 43, at 56; Nils Eliasson, *Investment Treaty Protection of Chinese Natural Resources Investments*, in BUSINESS DISPUTES IN CHINA 303, 309 (Michael J. Moser ed., Juris 3d ed. 2011); Leon E. Trakman, *Geopolitics, China, and Investor-State Arbitration*, in CHINA IN THE INTERNATIONAL ECONOMIC ORDER 268, 271 (Lisa Toohey et al. eds., 2015).

⁶⁵ E.g., Jeffrey Sachs, *The Context: Foreign Investment and the Changing Global Economic Reality*, in THE EVOLVING INTERNATIONAL INVESTMENT REGIME: EXPECTATIONS, REALITIES, OPTIONS xliii, 1 (José E. Alvarez et al. eds., 2011) (“With

United States are major exporters, but also recipients of substantial FDI. From 2006 to 2013, the United States was the world's largest recipient of FDI⁶⁶ (but lost that position to China for the years 2014 and 2015⁶⁷). Professor Alvarez explains that "irrespective of whether the host of FDI is a developed economy, a poor developing economy, or a State that finds itself somewhere in between," a country that liberalizes its market to foreign investment will share similar economic, political, and national security concerns and that a State's concern for who may enter its borders and under which circumstances does not "change merely because some of those seeking entry offer the prospect of considerable capital."⁶⁸ Hence, the scope of protection offered by IIAs should not be limited to the interests of the private investors from capital-exporting, developed countries that invest in the capital-importing, developing countries. Such an approach disregards the need of host States to incorporate sustainable development goals in IIAs and prevents host States from achieving a balance between their regulatory

the power shifting away from the United States and Europe toward Asia, it seems difficult to argue that Western law will maintain its international dominance going forward.").

⁶⁶ Dept. of Commerce & Pres. Council of Economic Advisers (United States), *Foreign Direct Investment in the United States* (Oct. 2013), https://www.whitehouse.gov/sites/default/files/2013fdi_report_-_final_for_web.pdf.

⁶⁷ See, e.g., People's Republic of China State Council, *China Becomes World's Largest FDI Recipient Amid Mixed Global Outlook*, June 25, 2015, http://english.gov.cn/news/top_news/2015/06/25/content_281475134110982.htm; WIR 2016 45

⁶⁸ JOSÉ E. ALVAREZ, *THE PUBLIC INTERNATIONAL LAW REGIME GOVERNING INTERNATIONAL INVESTMENT* 20-21 (Hague Academy of Int'l L. 2011) [hereinafter ALVAREZ, *PUBLIC INTERNATIONAL LAW*].

interests and investment treaty commitments.

The perspective that a host State holds in regards to foreign investment can be affected by its associations. Unlike the 1950s to the 1970s when IIAs were negotiated outside of the public eye, host States now have to deal with wide public attention especially when negotiating FTAs with investment chapters, which usually garners more public interest than BIT negotiations.⁶⁹ The problem arises when States, especially the capital-importing, developing countries, approach the negotiation of modern IIAs with the obsolete mindset that investment treaties are a straightforward means of achieving economic transition without fully appreciating the complexities and repercussions of concluding IIAs.⁷⁰ For example, although model BITs may help maximize efficiency for the developed countries, a lesser powered host State may get pulled into the demands of the standard contract-like treaty.⁷¹ But the more serious and problematic issue for host States is the ISDS procedure because it entitles foreign investors to directly challenge the domestic laws, especially regulatory public interest measures, of the host State. However, this is a thorny matter for the host State that has

⁶⁹ Jürgen Kurtz, *Building Legitimacy through Interpretation in Investor-State Arbitration: On Consistency, Coherence and the Identification of Applicable Law*, in THE FOUNDATIONS OF INTERNATIONAL INVESTMENT LAW: BRINGING THEORY INTO PRACTICE 257, 261 (Zachary Douglas et al. eds., 2014).

⁷⁰ *See id.* (“The resulting tendency to regard BITs are routine instruments designed to facilitate simply economic transition is even higher for typical capital importers rather than exporters.”).

⁷¹ *Id.* at 262 (“The very notion of a ‘model BIT’ – developed by a capital exporting state in line with *its* preferences to frame the negotiations with a broad range of country partners – is conceptually similar to a standard form contract used by large private concerns in a domestic law context.”).

to foresee all of the non-conforming measures and future contingencies at the time of negotiation. When the host State does not execute this process properly, an investment tribunal may find that the act breaches the IIA even if the act in question could reasonably be viewed as a legitimate exercise of public policy.⁷² This aspect of the ISDS has led the developing countries to argue since the early 2000s that foreign investors should be required to exhaust local remedies as would a domestic investor.⁷³ As previously explained, the exhaustion of local remedies is set forth as a condition precedent in the revised 2016 India Model BIT.

Increasingly recognizing the complex nature of international investment law and the far-reaching implications of accepting the ISDS clause, host States are updating their IIA models to search for a way that would effectively preserve the regulatory space necessary for the maintenance of public order. At least fifty countries and regions spread across Africa, Asia, Europe, Latin America, and North America are already engaged in the IIA reformation process.⁷⁴ One of the more progressive efforts is being made by the European Commission which in May 2015 released a concept paper specifically identifying the right to regulate of host States as one of the major policy areas requiring further improvement in the drafting of the TTIP to ensure that the investment protection guarantees of

⁷² WIR 2013, *supra* note 58, at 101.

⁷³ See UNCTAD, DISPUTE SETTLEMENT: INVESTOR-STATE 82, U.N. Doc. UNCTAD/ITE/IIT/30 (May 2003) [hereinafter UNCTAD, DISPUTE SETTLEMENT], available at http://www.unctad.org/en/docs/iteit30_en.pdf.

⁷⁴ WIR 2015, *supra* note 25, at 108.

IAs do not usurp the regulatory authority of host States.⁷⁵ Moreover, with deeper awareness among host States that entering into IAs to import capital as a way of fulfilling national economic goals overly discounts the intricacies of the international investment law system, model investment treaties are being revised to include provisions related to sustainable development. Although the principle of sustainable development as a normative rule of international investment law has yet to be firmly rooted, UNCTAD released the Investment Policy Framework for Sustainable Development (IPFSD) in 2012 to provide guidelines for achieving growth and sustainable development.⁷⁶ Most of the 18 IAs concluded in 2014 provide for the right to regulate for sustainable development objectives; general exceptions for the protection of human, animal or plant life or health, or the conservation of exhaustible natural resources; a stipulation that health, safety, or environmental standards should not be compromised to attract investment; and/or, an outright statement in the preamble that refers to sustainable development.⁷⁷ The impact of sustainable development provisions should not be overstated but ought to be viewed critically by host States to avoid

⁷⁵ EUROPEAN COMM'N, CONCEPT PAPER ON INVESTMENT IN TTIP AND BEYOND – THE PATH FOR REFORM (May 5, 2015), http://trade.ec.europa.eu/doclib/docs/2015/may/tradoc_153408.PDF.

⁷⁶ Elisabeth Tuerk & Faraz Rojidi, *Towards a New Generation of Investment Policies: UNCTAD's Investment Policy Framework for Sustainable Development*, INVESTMENT TREATY NEWS (Oct. 30, 2012), <https://www.iisd.org/itn/2012/10/30/towards-a-new-generation-of-investment-policies-unctads-investment-policy-framework-for-sustainable-development/>. See also UNCTAD, INVESTMENT POLICY FRAMEWORK FOR SUSTAINABLE DEVELOPMENT 57 (July 4, 2012) [hereinafter UNCTAD, SUSTAINABLE DEVELOPMENT FRAMEWORK].

⁷⁷ WIR 2015, *supra* note 25, at 112.

another generation of investment treaties that provide a balancing tool for host States but, in fact, are ineffective or unreliable. Host States must therefore recognize that sustainable development provisions “do not in themselves guarantee a positive development impact of the investment” because the investment environment and regulatory framework of a host State are among the important variables that will have a major role in determining how much of the positive development impacts of investment can be reaped while reducing the risks of safeguarding public interests.⁷⁸

2. Home States

The goal of a home State is to secure a favorable investment climate in the host State for its citizens. The home State approaches this by persuading the other contracting State to implement policies that promote and liberalize foreign investment. When IIA negotiations take place, a contracting State assumes the role of either host or home State and is, at least in theory, equally obligated under the investment treaty. Whereas the first BIT generation provided considerable leeway to investment tribunals when interpreting treaties, the newer IIAs reflect a rebalancing of power by including provisions that specify treaty obligations in greater detail, clarify the applicable review standard, and create exceptions aimed at preserving the regulatory public interest of the contracting States. Unlike the European IIAs which “tended to be laconic instruments, free of elucidations,” the United States has since NAFTA preferred “lengthy BITs and interpretive statements in an apparent attempt to better safeguard host State interests.”⁷⁹

⁷⁸ *Id.* at 105.

⁷⁹ CATHARINE TITI, *THE RIGHT TO REGULATE IN INTERNATIONAL INVESTMENT LAW* 43 (Nomos/Hart 2014).

For example, the minimum standard of treatment provision in the 2004 and 2012 U.S. Model BITs ensures that the contracting parties have a shared understanding of the customary international law principle of minimum standard. The fair and equitable treatment (FET) and full protection and security provisions are clarified in the Australia-Chile FTA (2008) to “not require treatment in addition to or beyond that which is required by that standard, and do not create additional substantive rights.”⁸⁰ Each concept is distinctly considered to explain what is meant by the phrase “fair and equitable treatment” and “full protection and security.”⁸¹ Such clarifications and specifications in IIAs enable the contracting States to have a more direct role in shaping the decision-making process by lessening the interpretive authority of international arbitration tribunals while also reducing the risk that arbitrators will “draw on analogies with which they are familiar (such as private international law analogies) or sympathetic (such as analogies between investor rights and human rights).”⁸² Moreover, unlike the past when the capital-exporting countries were the main providers of foreign capital, home States engage in this rebalancing of power because they have also emerged as recipients of foreign investments that can be brought to

⁸⁰ Australia-Chile FTA, art. 10.5.2, July 30, 2008. See also art. 5.2 of the 2004 and 2012 U.S. Model BITs.

⁸¹ *Ids.*

⁸² Anthea Roberts, *Clash of Paradigms: Actors and Analogies Shaping the Investment Treaty System*, 107 AM. J. INT’L L. 45, 80 (2013). See also JONATHAN BONNITCHA, *SUBSTANTIVE PROTECTION UNDER INVESTMENT TREATIES: A LEGAL AND ECONOMIC ANALYSIS* 46 (Cambridge Univ. Press 2014) (describing the criticism that tribunal members with expertise in commercial law may fail to bring in a balanced perspective).

investor-State arbitration under the ISDS mechanism in their capacity as a host State.

The perspective of the home State may be analogous to the international investment policies of the United States, which is worth mentioning because of the “Americanization of the IIA universe”⁸³ that particularly gained momentum since NAFTA. The perception that the U.S. Model BIT provides the “gold standard”⁸⁴ has led other home States to reflect upon the international investment policies advocated by the United States. Home States in Asia, the Americas, and even some parts of Europe prefer the more comprehensive approach of the U.S. Model BIT because it encourages the contracting States to consider in greater depth during the negotiation process areas that affect liberalization provisions, non-conforming precluded measures clauses, and references to customary international law.⁸⁵ However, the U.S. Model BIT has not been without criticism. Opponents demanded that the scope of certain provisions like those on expropriation, minimum standard of treatment, and the fair and equitable treatment be amended in the 2012 U.S. Model BIT. Critics also argued that the traditional State-State dispute resolution mechanism should be reinstated although this proposal was not included in the 2012 U.S. Model

⁸³ Wolfgang Alschner, *Americanization of the BIT Universe: The Influence of Friendship, Commerce and Navigation (FCN) Treaties on Modern Investment Treaty Law*, 5 GOETTINGEN J. INT’L L. 455, 484-85 (2013).

⁸⁴ Roberts, *supra* note 82, at 82.

⁸⁵ Alschner, *supra* note 83, at 484. *Cf. id.* at 485 (noting that while some European countries are following suit, certain countries like Germany, the Netherlands, and the United Kingdom – coined the “intellectual fathers of the original BIT approach” – still prefer the simplicity offered in European-style BITs).

BIT.⁸⁶

Home States are in a rather unique position within the overall international investment law framework because even though IIAs are concluded between the States, only the host State is bound to a “one-way flow of obligations.”⁸⁷ Suggestions have been made that IIAs should also oblige home States to encourage FDI flows and to better fulfill the goal of promoting foreign investment.⁸⁸ For example, future IIAs could increase the role of the home State by requiring it to give its citizens information about international investment opportunity, technical, and/or financial support, or insurance policies that could ease the burden of investing in a foreign

⁸⁶ See Anthea Roberts, *State-to-State Investment Treaty Arbitration: A Hybrid Theory of Interdependent Rights and Shared Interpretive Authority*, 55 HARV. INT’L L.J. 1 (2014) (arguing that the re-emergence of State-to-State arbitration can open the way to another hybrid form of dispute resolution that can fix some of the existing imbalances in investor-State arbitration); NATHALIE BERNASCONI-OSTERWALDER, IISD, STATE-STATE DISPUTE SETTLEMENT IN INVESTMENT TREATIES (Oct. 2014) (providing recommendations on how State-to-State arbitration can be used for disputes arising out of IIAs). Cf. UNCTAD, WORLD INVESTMENT REPORT 2003: FDI POLICIES FOR DEVELOPMENT: NATIONAL AND INTERNATIONAL PERSPECTIVES 116, 118, U.N. Doc. UNCTAD/WIR/2003 (Sep. 12, 2003) [hereinafter WIR 2003] (expressing skepticism for State-to-State arbitration but discussing a few of its benefits). See GENERALLY UNCTAD, INVESTOR-STATE DISPUTES: PREVENTION AND ALTERNATIVES TO ARBITRATION 93, UNCTAD/DIAE/IA/2009/11 (2010); UNCTAD, INVESTOR-STATE DISPUTE SETTLEMENT: A SEQUEL 43, 47, 157, UNCTAD/DIAE/IA/2013/2 (2014) (providing examples of State-to-State arbitration provisions in IIAs).

⁸⁷ See, e.g., NATHALIE BERNASCONI-OSTERWALDER ET AL., IISD, INVESTMENT TREATIES & WHY THEY MATTER TO SUSTAINABLE DEVELOPMENT: QUESTIONS & ANSWERS 36 (2012).

⁸⁸ See WIR 2003, *supra* note 86, at 155 (“In future IIAs consideration should especially also go to home countries... to encourage FDI flows to developing countries and help increase the benefits from them.”). See also UNCTAD, INTERNATIONAL INVESTMENT AGREEMENTS: KEY ISSUES, UNCTAD/ITE/IIT/2004/10 (Vol. II) (May 16, 2005) [hereinafter UNCTAD, IIA KEY ISSUES]. See, e.g., BERNASCONI-OSTERWALDER ET AL., *supra* note 87, at 36.

country.⁸⁹ Investment treaties may also demand that the home State furnish legal records to verify that the domestic company is compliant or perhaps even agree to providing a forum where redress may be sought for the misconduct of its domestic companies that occur while doing business abroad.⁹⁰ These recommendations are present in Part 6 of the IISD Model Agreement concerning the rights and obligations of home States. Article 29 of the IISD Model Agreement stipulates that “Home [S]tates with the capacity to do so should assist developing and least-developed [S]tates in the promotion and facilitation of foreign investment into such [States], in particular by their own investors....”⁹¹ Article 31 of the IISD Model Agreement on the liability of investors in their own home State requires the following:

Home states shall ensure that their legal systems and rules allow for, or do not prevent or unduly restrict, the bringing of court actions on their merits before domestic courts relating to the civil liability of investors for damages resulting from alleged acts or decisions made by investors in relation to their investments in the territory of other Parties. The host state laws on liability shall apply to such proceedings.⁹²

The objective of increasing the vested interest of the home State even

⁸⁹ UNCTAD, IIA KEY ISSUES, *supra* note 88, at 65. See, e.g., BERNASCONI-OSTERWALDER ET AL., *supra* note 87, at 36.

⁹⁰ See, e.g., BERNASCONI-OSTERWALDER ET AL., *supra* note 87, at 36.

⁹¹ IISD, Model International Agreement on Investment, art. 29 (April 2005) [hereinafter IISD Model Agreement].

⁹² *Id.* art. 31.

after the IIA takes effect may be one direction to consider for the future of international investment law.⁹³ This effort is also evident in the preamble of the IISD Model Agreement, which provides that one aim of the parties would be to “seek[] an overall balance of rights and obligations in international investment between investors, host countries and *home* countries.”⁹⁴ Although not as explicit as the recommendations of the IISD Model Agreement, some IIAs continue to seek the involvement of the home State even after they take effect. For example, the home State is obligated to not demand or penalize its investors regarding transfers as provided in the Canada Model Fair Investment Protection and Promotion Agreement (FIPA) (2004) and NAFTA.⁹⁵ Future IIAs may consider further clarifying the expectations of home States after the IIA goes into effect.

3. Foreign Investors

The goal of the foreign investor is to have its investment protected under the regulatory framework of the host State. As set forth by the tribunal in *Tecmed v. Mexico*:

The foreign investor expects the host State to act in a consistent manner, free from ambiguity and totally transparently in its relations with the foreign investor, so that

⁹³ See Elizabeth Boomer, *Rethinking Rights and Responsibilities in Investor-State Dispute Settlement: Some Model International Investment Agreement Provisions*, in *RESHAPING THE INVESTOR-STATE DISPUTE SETTLEMENT SYSTEM: JOURNEYS FOR THE 21ST CENTURY* 183, 211 (Jean E. Kalicki & Anna Joubin-Bret eds., 2015).

⁹⁴ IISD Model Agreement, *supra* note 91, preamble [emphasis supplied in text].

⁹⁵ JESWALD W. SALACUSE, *THE LAW OF INVESTMENT TREATIES* 289 (Oxford Univ. Press 2d ed. 2015) (referring to the transfer provisions in art. 1109(3) of the NAFTA and art. 14(4) of the Canada Model FIPA).

it may know beforehand any and all rules and regulations that will govern its investments, as well as the goals of the relevant policies and administrative practices or directives, to be able to plan its investment and comply with such regulations.⁹⁶

To achieve this, foreign investors generally rely on legal instruments like IIAs when entering a host State to receive protection in the form of specific treatment standards. Absolute protections like the fair and equitable treatment, full protection and security, compensation for expropriation, and the right to transfer capital, profits, and income from the host State provide a peace of mind for foreign investors. Additional treatment standards on national treatment, most favored nation (MFN) treatment, and the right to transfer capital, profits, and income from the host State may provide an open and transparent regulatory framework on investment that is favorable to foreign investors.

Investors in the international investment law system are usually multinational enterprises (MNEs) and the nationality of a corporation is determined by its place of incorporation or main seat of business.⁹⁷ An investor's nationality establishes which BIT applies,⁹⁸ but this can create space for opportunistic acts since tribunals typically do not scrutinize the

⁹⁶ *Tecmed v. United Mexican States*, ICSID Case No. ARB (AF)/00/2, Award, para. 154 (May 29, 2003).

⁹⁷ Christoph Schreuer, *Investments, International Protection*, in MAX PLANCK ENCYCLOPEDIA OF PUBLIC INTERNATIONAL LAW, para. 32 (Rüdiger Wolfrum ed., 2013), available at http://www.univie.ac.at/intlaw/wordpress/pdf/investments_Int_Protection.pdf.

⁹⁸ *E.g.*, DOLZER & SCHREUER, *supra* note 41, at 44.

nationality of a company's owner to determine whether an ulterior motive is at play.⁹⁹ This enables investors to engage in "forum planning" or "treaty shopping" (e.g. Philip Morris tobacco packaging case¹⁰⁰), which is not illegal *per se* in international investment law.¹⁰¹ Furthermore, the complex ownership structures of corporations conceal the "true" owner of the MNE which blurs investor nationality through direct shareholdings of affiliates, cross-shareholdings where affiliates own each other's shares, and shared ownerships like joint ventures. Although MNEs do not create complex internal ownership structures for the purpose of receiving IIA protections or to engage in corporate malfeasance, the effect is that affiliates that are far removed from the corporate headquarters may be able to seek the protections afforded under an investment treaty. This problem provides the theme of the 2016 edition of the World Investment Report.¹⁰²

Multinational enterprises are not the only type of foreign investors provided for in international investment agreements. Investors like sovereign wealth funds (SWFs) and state-owned enterprises (SOEs), private equity funds, and third-party funders are also recognized as foreign

⁹⁹ See Schreuer, *supra* note 97, paras. 33-34.

¹⁰⁰ Philip Morris Asia Ltd. v. Australia, *supra* note 32.

¹⁰¹ E.g., DOLZER & SCHREUER, *supra* note 41, at 52. See CME Czech Republic v. Czech Republic, UNCITRAL, Partial Award, para. 419 (Sep. 13, 2001) (rejecting the argument that Claimant should be barred from treaty shopping because "a party may seek its legal protection under any scheme provided by the laws of the host country"). *But see* Mobil Corp. v. Venezuela, ICSID Case No. ARB/07/27, Award, para. 204 (June 10, 2010) (rebuking the abusive and manipulative practice of restructuring investments for the purpose of gaining access to ICSID arbitration).

¹⁰² WIR 2016, *supra* note 13, at 124.

investors and recognizing their differences is important as investment objectives are bound to vary by investor type.¹⁰³ SWFs are usually managed under the high involvement of the home government and may be used as a vehicle that redistributes wealth.¹⁰⁴ The governments of countries such as the UAE, Singapore, Russia, Kuwait, Hong Kong, and China, and Norway invest through their SWFs.¹⁰⁵ As foreign investors, SWFs raise a special red flag for host States because they pursue investment goals in circumstances that lack transparency and conditions that are not closely monitored by the financial market authorities of the country with the SWF.¹⁰⁶ Unlike private equity funds that invest internationally for profit-making, the investment decisions of SWFs may be politically motivated and therefore reach into sectors and assets of the host State that are considered strategic or sensitive.¹⁰⁷ Despite some of these negative perceptions, SWFs are a valid source of foreign capital that host States can gain from as with the traditional forms of FDI like greenfield investments by strategic investors.¹⁰⁸ However, the distinction between investor types has become less relevant due to

¹⁰³ WIR 2013, *supra* note 58, at 10.

¹⁰⁴ Edwin M. Truman, *Sovereign Wealth Funds: Threat or Salvation?*, PETERSON INST. FOR INT'L ECON. (Sep. 2010), <http://www.piie.com/publications/briefs/truman4983.pdf>.

¹⁰⁵ *Id.*

¹⁰⁶ OECD, INTERNATIONAL INVESTMENT OF SOVEREIGN WEALTH FUNDS: ARE NEW RULES NEEDED?, OECD INVESTMENT NEWSLETTER (Oct. 2007), *available at* <http://www.oecd.org/daf/inv/investment-policy/39979894.pdf>.

¹⁰⁷ *Id.*

¹⁰⁸ *Id.*

globalization and can crossover when, for example, SWFs invest in private equity funds.¹⁰⁹ Aside from SWFs, the intentionally open-nature of the term “investments” under the ICSID Convention enables foreign minority shareholders to receive investment treaty protection because most IIAs contain a broad definition of “investments” acts to include shareholding and participation in a company.

Although not a direct contracting party to the IIAs, foreign investors are nonetheless obligated to the terms of the investment treaty and must abide to the foreign investment laws of the host State, which retains the right to ban foreign investment or allow admission in the industries and regions specified by the host State. Foreign investors should refer to the positive or negative list which identifies the sectors that are open or closed off to foreign investors. Countries such as the United States, Canada, and Japan grant a right of access to foreign investments typically using language that includes “with respect to the establishment, acquisition, expansion, management, conduct, operation, and sale or other disposition of investments.”¹¹⁰ Foreign investors may also be bound to the performance requirements of a host State.¹¹¹

The current generation of IIAs may also require that foreign investors abide to a certain standard of behavior to contribute to the sustainable development objectives provided by the international standards of the UN

¹⁰⁹ WIR 2013, *supra* note 58, at 10.

¹¹⁰ *E.g.*, North American Free Trade Agreement, arts. 1102 & 1103, Dec. 17, 1992 [hereinafter NAFTA].

¹¹¹ Korea-U.S. FTA, art. 11.8, June 30, 2007.

Guiding Principles on Business and Human Rights, the updated OECD Guidelines on Multinational Enterprises, and/or the FAO/World Bank/UNCTAD/IFID Principles on Responsible Agricultural Investment.¹¹² Moreover, calls to reform the ISDS system so that foreign investors are not given greater dispute settlement rights than domestic investors are also under contemplation.¹¹³ Although foreign investors have generally relied on BITs and other IIAs to receive absolute protections such as through the fair and equitable treatment standard, most favored nation clause, and the expropriation provision, these substantive provisions are being subjected to the current IIA overhaul because they affect the States' right to regulate for public interest.¹¹⁴ Additionally, suggestions to restrain the situations that foreign investors may initiate investor-State arbitration claims are being reviewed. Under the broad definition of "investment" that permits indirect or minority shareholders to receive investment treaty protection,¹¹⁵ the ISDS system has inadvertently provided foreign investors with a means of creeping into the regulatory space of host States. It is ironic that, without the investor-State dispute settlement mechanism, foreign investors may become vulnerable to the discriminatory and arbitrary measures of a host State. However, concerns exist that the ISDS mechanism has enabled foreign investors to be abusive so that it has become necessary for host States to find

¹¹² WIR 2015, *supra* note 25, at 127.

¹¹³ *Id.* at 128.

¹¹⁴ *Id.* at 135.

¹¹⁵ WIR 2016, *supra* note 13, at 123 (describing the complexity in MNE ownership structure and its impact on investment policymaking).

a way that helps them to preserve regulatory space without breaching international treaty obligations. For this reason, recommendations have been made to remove non-IIA based claims to prevent foreign investors from seeking recourse for investment contract breaches and to require from all of the contracting States the consent to investor-State arbitration.¹¹⁶

4. Investor-State Tribunals and Arbitrators

Before investor-State arbitrations, an injured foreign investor had to resort to diplomatic protection by seeking recourse through their home government, which then made the sole determination of whether to pursue a claim on behalf of its private individual.¹¹⁷ However, the establishment of the BIT regime and ICSID enabled a departure from this traditional stance that diplomatic protection is a discretionary right of the State by allowing foreign investors to bypass its home State and instead directly initiate an arbitration against the host State. Three tribunal members are usually selected by the disputing parties so that the foreign investor and the respondent State each chooses one arbitrator while the third arbitrator is decided by the parties' agreement or their appointed arbitrators.¹¹⁸ The professional background of the individual arbitrators sitting on an arbitral

¹¹⁶ WIR 2015, *supra* note 25, at 148.

¹¹⁷ CHRISTOPHER F. DUGAN ET AL., *INVESTOR-STATE ARBITRATION* 347 (Oxford Univ. Press 2008); Salacuse & Sullivan, *supra* note 9, at 68-69. For more on diplomatic protection, see generally IAN BROWNLIE, *PRINCIPLES OF PUBLIC INTERNATIONAL LAW* (Oxford Univ. Press, 6th ed. 2003); Yoram Dinstein, *Diplomatic Protection of Companies Under International Law*, in *INTERNATIONAL LAW: THEORY AND PRACTICE – ESSAYS IN HONOUR OF ERIC SUY* 505 (Karel Wellens ed., 1998).

¹¹⁸ ICSID, *RULES OF PROCEDURE FOR ARBITRATION PROCEEDINGS* ch. I(3) (2003).

tribunal might be considered by the disputing parties when making their selection. According to a 2012 survey conducted by the OECD, more than 50% of the arbitrators have been appointed by foreign investors in other ISDS arbitration cases and that the vast majority of the arbitrators are from Europe or North America.¹¹⁹ Moreover, the outcome of an ISDS case may be affected by whether the arbitrator enjoys expertise in commercial arbitration or public international law.¹²⁰ Generally speaking, commercial arbitrators may be inclined to focus on the private nature of the dispute while public international lawyers may view the arbitration as part of a public world order so that the conduct of the State is subject to the rules of public international law.¹²¹

The nature of investor-State tribunals is perplexing because the standards of treatment and guarantees made in investment treaties may be enforced in a decentralized dispute settlement mechanism characterized by a public international law/private commercial law divide. Public interest issues affecting the State are addressed in a dispute settlement mechanism where interpretations that favor private interest over public interest may decrease the legitimacy of international investment law. The authoritative

¹¹⁹ OECD, INVESTOR-STATE DISPUTE SETTLEMENT PUBLIC CONSULTATION (May 16-July 9, 2012) 43-44, *available at* <http://www.oecd.org/investment/internationalinvestmentagreements/50291642.pdf>.

¹²⁰ See J. J. Gass, *Introductory Note: Arbitration, Insurance, Investment, Corruption, and Poverty*, in *POVERTY AND THE INTERNATIONAL ECONOMIC LEGAL SYSTEM: DUTIES TO THE WORLD'S POOR* 139 (Krista N. Schefer ed., 2013).

¹²¹ See Stephen W. Schill, *The Sixth Path: Reforming Investment Law from Within*, in *RESHAPING THE INVESTOR-STATE DISPUTE SETTLEMENT SYSTEM: JOURNEYS FOR THE 21ST CENTURY* 621, 634 (Jean E. Kalicki & Anna Joubin-Bret eds., 2015).

decision-making process is made in an open field where *ad hoc* tribunals (as opposed to standing courts) must weigh between polarized paradigms and investment tribunals have to grapple between the respondent State's regulatory act and the private investor's investment contract to determine the proper standard of review. International investment law is unique for this reason, but from an adjudicative standpoint, the overlapping area results in a "clash of paradigms"¹²² that makes it particularly difficult for the investment tribunals to produce a harmonized set of legal standards appeasable to the various stakeholders shaping international investment law.

In international investment law, the public/private tension occurs during the treaty-making phase and when an investor-State arbitration has been initiated to challenge the regulatory act of a State. Under public international law, investment tribunals would examine the "interstate treaty relationship" of an IIA, whereas under private commercial law, the focus is on the "investor-state disputing relationship."¹²³ When principles of private law like party autonomy and confidentiality are at play during an investor-State arbitration, the domestic regulatory space of the host State is diminished and creates problems of regulatory chills especially when unanticipated payouts are awarded in an arbitration loss even though the authority of international investment tribunals depends on how well these

¹²² Roberts, *supra* note 82, at 52. Roberts coins the term "clash of paradigms" to describe the phenomenon that occurs "in competing conceptualizations of the investment treaty system as a subfield within public international law, as a species of international arbitration or as a form of internationalized judicial review." *Id.* at 47.

¹²³ *Id.* at 58.

ambiguities are shaped by the investment treaty adjudicative bodies.¹²⁴ The decision-making process, and consequently the outcome of the case, will therefore be greatly affected depending on whether an investment tribunal views the dispute from a public or private standpoint. For example, how should an investment tribunal treat a joint interpretive statement unanimously presented by the contracting States of an investment agreement? Such a situation actually occurred – and was met with mixed reaction – when the NAFTA parties issued a joint interpretative statement (“FTC Note”) on the minimum standard of treatment to prohibit an expansive reading of the provision by the NAFTA tribunals. For example, although the tribunal in *Pope and Talbot* cautiously accepted the FTC Note as an interpretation as opposed to an amendment (primarily because such a determination was not required), it was not shy to comment that if such a choice were necessary, the tribunal would have concluded the joint statement to be an amendment.¹²⁵ In another example, however, the *ADF* tribunal accepted the FTC Note as a subsequent agreement amongst the three NAFTA parties regarding its interpretation¹²⁶ in which “[n]o more authentic and authoritative source of instruction on what the Parties

¹²⁴ Gus van Harten, *The Public-Private Distinction in the International Arbitration of Individual Claims Against the State*, 56 INT’L COMP. CORP. L.Q. 371, 381-87 (2007).

¹²⁵ *Pope & Talbot v. Canada*, UNCITRAL, Award, para. 47 (May 31, 2002). See also *Merrill & Ring Forestry v. Canada*, UNCITRAL, Award, para. 192 (Mar. 31, 2010) (observing that the FTC Note was “closer to an amendment of the treaty, than a strict interpretation”).

¹²⁶ See generally Georg Nolte, *Jurisprudence Under Special Regimes Relating to Subsequent Agreements and Subsequent Practice*, in TREATIES AND SUBSEQUENT PRACTICE 210, 241 (Georg Nolte ed., 2013).

intended to convey in a particular provision of NAFTA, is possible.”¹²⁷ Although the situation described here is merely one instance of a clash of paradigms, States “implicitly delegate[]”¹²⁸ adjudicatory and regulatory authority to independent, international third parties that have to navigate through a legal system with less than clear standards of treatment in international investment. Creating jurisprudence on international investment law and maintaining host State policy is therefore a delicate task that harbors an allocation of power problem and needs to be addressed in a manner that does not cut down on the base values and dignity of the stakeholders in the field of international investment law.¹²⁹

Investment tribunals have to deal with other heavyweight concerns. The ISDS clause has been controversial for both developed and developing

¹²⁷ *ADF Group Inc. v. United States*, ICSID Case No. ARB(AF)/00/1, Award, para. 177 (Jan. 9, 2003). See *Mondev v. United States*, ICSID Case No. ARB(AF)/99/2, Award, para. 121 (Oct. 11, 2002) (stating that the *Mondev* tribunal has “no difficulty in accepting [the FTC Note] as an interpretation of the phrase ‘in accordance with international law’”); *Chemtura Corp. v. Canada*, UNCITRAL, Award, para. 120 (Aug. 2, 2010) (stating that the *Chemtura* tribunal “must interpret the scope of Article 1105 in accordance with the FTC Note”).

¹²⁸ ALVAREZ, PUBLIC INTERNATIONAL LAW, *supra* note 68, at 25. See UNCTAD, DISPUTE SETTLEMENT, *supra* note 73, at 8 (stating that both developing and developed countries view ISDS with skepticism).

¹²⁹ To generally understand the basic features of a policy-oriented approach to law, see Myres S. McDougal, *Jurisprudence for a Free Society*, 1 GA. L. REV. 1 (1966); Myres S. McDougal, *Impact of International Law on National Law: A Policy-Oriented Perspective*, 4 S. D. L. REV. 25 (1959); Myres S. McDougal, *Law as a Process of Decision: A Policy-Oriented Approach to Legal Study*, 1 NAT. L. F. 54 (1956); Harold D. Lasswell & Myres S. McDougal, *Jurisdiction in Policy-Oriented Perspective*, 19 U. FLA. L. REV. 486 (1967); W. Michael Reisman, *Myres S. McDougal: Architect of a Jurisprudence for a Free Society*, 66 MISS. L.J. 15 (1997); Harold D. Lasswell & Myres S. McDougal, *Criteria for a Theory About Law*, 44 S. CAL. L. REV. 362 (1971); Harold D. Lasswell & Myres S. McDougal, *Trends in Theories About Law: Comprehensiveness in Conceptions of Constitutive Process*, 41 GEO. WASH. L. REV. 1 (1973).

States because investment tribunals determine whether the laws of the host State have breached the IIA and then impose compensation awards. Investment tribunals have been chastised by the international community for making awards that undermine the financial stability of a host State and arouse the emotions of populists who want to reduce the market liberalization efforts advanced in their State. Moreover, the role of the investment tribunal deserves attention because the authority to decide on a standard of review affects how broadly or narrowly it will interpret the term “investment.” An investment tribunal that permits a narrow scope of interpretation will limit disputes to the actual investment even though a breach can occur in broader areas like investment authorization or other investment contracts.¹³⁰ In this case, the investment tribunal does not create new rights for the investor but affirmatively protects its existing rights pursuant to the IIA. Alternatively, tribunals that favor broad interpretations may consider investment-related events to include disputes that occurred during the negotiations process.¹³¹ In such a situation, tribunals may be more willing to protect expectations as they existed at the time the decision to invest was made without deeply inquiring into whether that expectation

¹³⁰ See, e.g., Yas Banifatemi, *The Law Applicable in Investment Treaty Arbitration*, in *ARBITRATION UNDER INTERNATIONAL INVESTMENT AGREEMENTS: A GUIDE TO THE KEY ISSUES* 191 (Katia Yannaca-Small ed., 2010); Tony Cole, *The Boundaries of Most Favored Nation Treatment in International Investment Law*, 33 *MICH. J. INT’L L.* 537 (2012).

¹³¹ See Penelope Ridings, *Investment Negotiations: Walking the Tightrope between Offensive and Defensive Interests*, Thomson Reuters (Oct. 5, 2016), <http://insider.thomsonreuters.co.nz/2016/10/investment-negotiations-walking-the-tightrope-between-offensive-and-defensive-interests/>.

was reasonable from the start.¹³² Some tribunals have accepted even broader standards of review to uphold an investor's expectation of a reasonable rate of return which was based exclusively on the investor's business plans at the time investment was made and had no legal basis under the laws or representations of the host State.¹³³ Regardless of how investment tribunals approach their interpretive task, their role is not merely about enforcing private contracts and must appreciate their larger function as providing a public international law framework for States and foreign investors because they are "actors not only engaged in dispute settlement, but also in global governance."¹³⁴

Investment tribunals also have to meet the procedural expectations of the contracting States. States agree to the ISDS clause with the expectation that investment tribunals will resolve their disputes in a manner more efficiently and swiftly than the local courts of host States; for instance, some European courts are notorious for their sluggishness.¹³⁵ Additionally,

¹³² Jonathan Bonnitcha, *The Problem of Moral Hazard and its Implications for the Protection of "Legitimate Expectations" under the Fair and Equitable Treatment Standard*, INVESTMENT TREATY NEWS (Apr. 7, 2011), <http://www.iisd.org/itn/2011/04/07/the-problem-of-moral-hazard/> (stating that expectations are legitimate if reasonable given the political and economic circumstances of the State).

¹³³ *Walter Bau AG v. Thailand*, UNCITRAL, Award, para. 12.3 (July 1, 2009). - See also *MTD v. Chile*, ICSID Case No. ARB/01/7, Award, para. 163 (May 21, 2004).

¹³⁴ Stephan W. Schill, *Enhancing International Investment Law's Legitimacy: Conceptual and Methodological Foundations of a New Public Law Approach*, 52 VA. J. INT'L L. 57, 59-61 (2011).

¹³⁵ E.g., Craig Garbe, *Investment Arbitration and the Canada-EU Comprehensive Economic and Trade Agreement: Time for a Change?*, INVESTMENT TREATY NEWS (July 11, 2011), <http://www.iisd.org/itn/2011/07/11/investment-arbitration-and-the-canada-eu-comprehensive-economic-and-trade-agreement-time-for-a-change/> ("Italian courts [] are so notoriously slow that litigants may purposely 'torpedo'

investment tribunals are expected to adjudicate with a reliable degree of fairness, objectiveness, and predictability that may not be available in the local court of a host State. Moreover, investment tribunals have also been subjected to the persistent efforts of civil society organizations to make the adjudicative process more transparent because disputing parties may opt to hold confidential proceedings, typically at the requests of States. Furthermore, investment tribunals have the additional task of considering the role and influence of *amicus* submissions in their decision-making process and, more generally, the development of international investment law.¹³⁶

5. International Organizations

International organizations may not be contracting parties in IIAs, but their external role in the international community for creating and reinforcing a desirable investment environment should not be underestimated. Since the mid-1970s, OECD countries created the *OECD Code of Liberalization of Capital Movements*¹³⁷ and the *OECD Declaration and Decisions on International Investment and Multinational Enterprises*¹³⁸ to

actions they know they will lose, but want to delay, by commencing them in Italy.”).

¹³⁶ See Katia F. Gómez, *Rethinking the Role of Amicus Curiae in International Investment Arbitration: How to Draw the Line Favorably for the Public Interest*, 35 *FORDHAM INT’L L.J.* 510, 563 (2012) (“In the wake of multiple courts’ and some tribunals’ decision to admit amicus curiae submissions, several rules on investment arbitration have increasingly recognized the possibility that the general interest is protected through amicus submissions.”).

¹³⁷ OECD, *OECD CODE OF LIBERALIZATION OF CAPITAL MOVEMENTS* (2016), available at https://www.oecd.org/daf/inv/investment-policy/CapitalMovements_WebEnglish.pdf.

¹³⁸ OECD, *DECLARATION ON INTERNATIONAL INVESTMENT AND MULTINATIONAL*

promote an open and transparent investment environment and to encourage the positive economic and societal contributions of foreign investors. In the 1990s, the OECD countries attempted to form a multilateral organization that would keep pace with FDI developments and coordinate market liberalization movements through the Multilateral Agreement on Investment (MAI).¹³⁹ Although the MAI was intended to provide a more consistent and reliable investment climate through a broad multilateral framework, disagreements between the developed and developing countries could not be overcome. Efforts of the OECD have not discontinued despite such setbacks. Since 2006, the OECD and non-OECD countries have embarked on the Freedom of Investment and National Security project to provide participating governments the opportunity to discuss how an open investment environment and the duty to protect their essential security interests could best be balanced.¹⁴⁰ In March 2016, it also hosted a conference on investment treaties titled “The Quest for Balance between Investor Protection and Governments’ Right to Regulate.”

Although the effort of the OECD should not be denied, developing countries may find more comfort level in international organizations like the UNCTAD which is based on membership more universal than the OECD. The UNCTAD Work Programme on International Investment Agreements

ENTERPRISES (May 25, 2011).

¹³⁹ OECD, Negotiating Group on the Multilateral Agreement on Investment, *Multilateral Agreement on Investment Draft Consolidated Text*, DAFNE/MAI(98)7/REV1 (Apr. 22, 1998) [hereinafter Draft MAI].

¹⁴⁰ OECD Investment Comm., *Progress Report, in 7th Roundtable on Freedom of Investment, National Security and ‘Strategic’ Industries* (Mar. 26, 2008), <http://www.oecd.org/investment/investment-policy/40473798.pdf>.

regularly identifies emerging issues and trends regarding IIAs from a sustainable development perspective. These findings are published for the benefit of policymakers, scholars, and other IIA stakeholders in the annual publication of the *World Investment Report*. As previously mentioned, the sustainable development work of the UNCTAD as presented in the IPFSD was developed to provide a guide for national and international investment policymaking.¹⁴¹ For example, the IPFSD recommends that future IIAs include a provision on compensation to better determine the amount to what is “equitable in light of the circumstances of the case” and that IIAs state detailed rules on compensation for when an IIA obligation has been breached.¹⁴² The purpose of this recommendation is to address the fact that BITs and other IIAs typically do not mention forms of remedies and compensation instead permitting international arbitration tribunals to make that determination based on their own discretions. Under international law, the standard full compensation may include moral damages, loss of future profits, and consequential damages. But host States could better manage their payout risk to avoid large, unexpected compensations by placing a safeguard on international arbitration tribunals to prevent creeping into the policymaking space of a host State.¹⁴³

The UNCITRAL also recently announced a progressive update on its transparency rules. The Mauritius Convention on Transparency, which

¹⁴¹ UNCTAD, INVESTMENT POLICY FRAMEWORK FOR SUSTAINABLE DEVELOPMENT (2015).

¹⁴² *Id.* at 108.

¹⁴³ *Id.*

opened for signature in March 2015, crystallizes the movement towards transparency and recognizes “the need for provisions on transparency in the settlement of treaty-based investor-State disputes to take account of the public interest involved in such arbitrations.”¹⁴⁴ Unlike the existing UNCITRAL Rules on Transparency which apply only to UNCITRAL investor-State arbitrations based on treaties concluded on or after April 1, 2014, the Mauritius Convention is a groundbreaking step forward because it covers “any investor-State arbitration, whether or not initiated under the UNCITRAL Arbitration Rules”¹⁴⁵ and to treaties concluded before April 1, 2014. The Mauritius Convention expands third party participation to increase transparency during investor-State arbitrations and will also have an effect on the recently concluded TPP. Not only is the TPP the most transparent of any IIAs concluded to date, but it also reflects certain components of the Mauritius Convention such as the allowing of *amicus curiae* submissions¹⁴⁶ and the publishing of documents.¹⁴⁷

As seen in recent years, international organizations may reflect regional affiliations. Treaty-making at the regional level can involve negotiations between organizations of a particular regional cluster such as when ASEAN formally commenced negotiations with Australia, China,

¹⁴⁴ Convention on Transparency in Treaty-based Investor-State Arbitration, preamble, Mar. 17, 2015.

¹⁴⁵ *Id.* art. 2.

¹⁴⁶ TPP, *supra* note 11, art. 9.23 [“Conduct of the Arbitration”].

¹⁴⁷ *Id.* art. 9.24 [“Transparency of Arbitral Proceedings”].

Japan, India, New Zealand, and Korea for the RCEP in November 2012.¹⁴⁸ The RCEP is considered to be an alternative to the TPP which includes the United States but not China and aims to establish an investment environment based on principles of promotion, protection, facilitation, and liberalization as provided for in its *Guiding Principles and Objectives for Negotiating the Regional Comprehensive Economic Partnership*.¹⁴⁹ The TPP connects the United States, Australia, Brunei, Canada, Chile, Japan, Malaysia, Mexico, New Zealand, Peru, Singapore and Vietnam.¹⁵⁰ Moreover, a megaregional cluster can be potentially created with the conclusion of just a few treaties as demonstrated by the EU.

6. Civil Societies

Especially after the NAFTA claims, the Argentinean ICSID cases, and the proliferation of international investment agreements, civil societies and other stakeholders have become actively involved in the development of investment policies.¹⁵¹ At the 2009 World Economic Forum, UN Secretary-General Ban Ki-moon stated, “Our times demand a new definition of leadership – global leadership. They demand a new constellation of international organization – governments, civil society and the private sector, working together for a collective global good.”¹⁵² External intervention in

¹⁴⁸ WIR 2013, *supra* note 58, at 103.

¹⁴⁹ *Id.*

¹⁵⁰ See Trans-Pacific Partnership, Trade Ministers’ Report to Leaders (Oct 8. 2013), available at <https://ustr.gov/sites/default/files/tpp%20trade%20ministers%20report%20to%20leaders%2010082013.pdf>.

¹⁵¹ WIR 2013, *supra* note 58, at 92.

¹⁵² The Secretary-General, *Plenary Speech at World Economic Forum on ‘The Global*

the form of civil society organizations did not exist during the early years of international investment, but formed after the emergence of some early NAFTA claims¹⁵³ which triggered the thought that one of the ways of achieving sustainable economic development would be by encouraging healthy levels of civil involvement to consequently persuade NAFTA countries like the United States and Canada to move towards greater openness in certain areas of the international law regime. They achieved this by bringing to surface issues related to economic security including jobs and wages, democratic decision-making, the environment, health and food safety, and other areas of consumer well-being.

Civil society can include formal and informal organizations that are not affiliated to any particular country or occur indigenously like protests in the streets. Civil society may also refer to the social movements and voluntary acts that stem from communities and citizen groups and may include domestic or international associations and non-governmental organizations, networks and campaigns, trade unions, and grassroots political forces.¹⁵⁴ The United Nations Development Programme (UNDP),

Compact: Creating Sustainable Markets', Davos, Switz. (Jan. 29, 2009), available at http://www.unep.org/pdf/speeches/davos09.globalcompact_dcsFINAL.English.pdf.

¹⁵³ See Jack J. Coe Jr., *Transparency in the Resolution of Investor-State Disputes – Adoption, Adaptation, and NAFTA Leadership*, 54 U. KAN. L. REV. 1339, 1364-69 (2006) (providing an overview of the tribunals' right to admit amicus participation in the context of early NAFTA Chapter 11 cases arising out of investment disputes).

¹⁵⁴ Mario Pianta, *UN World Summits and Civil Society: The State of the Art 6* (Civil Society and Social Movements Programme Paper No. 18, 2005), available at http://works.bepress.com/cgi/viewcontent.cgi?article=1057&context=mario_pianta.

which provides a good example of civil society activities that takes place in the field of international human rights, collaborates with civil society organizations at the country, regional, and global levels to encourage civil participation in addressing problems related to poverty and gender equality.

Foreign investment can become a sensitive issue and set off negative public attitudes even in countries like the United States and Europe despite their stance as strong proponents of market liberalization.¹⁵⁵ Negotiations for the Transatlantic Trade and Investment Partnership (TTIP)¹⁵⁶ commenced in July 2013 through the advocated efforts of the U.S. and European banks, agribusinesses, and other influential industry groups, but was met with opposition by civil societies because of concerns that the TTIP would permit EU corporations to weaken U.S. safeguard regulations on the environment, health, and finance to eventually harm the interests of consumers, the workforce, and the environment.¹⁵⁷ The sentiment was mutual in Europe where many worried that EU safety regulations would be undermined by U.S. corporate influence.¹⁵⁸ Civil society organizations raised similar concerns when the Korea-U.S. FTA was on the discussion table. The TPP is another investment agreement that was widely criticized by civil

¹⁵⁵ ALVAREZ, PUBLIC INTERNATIONAL LAW, *supra* note 68, at 20.

¹⁵⁶ Formerly known as Trans-Atlantic Free Trade Agreement (TAFTA).

¹⁵⁷ E.g., Public Citizen, *The Transatlantic Trade and Investment Partnership (TTIP): U.S. and European Corporations' Latest Venue to Attack Consumer and Environmental Safeguards?*, <http://www.citizen.org/tafta>.

¹⁵⁸ E.g., Paul Gallagher, *TTIP: Big Business and US to Have Major Say in EU Trade Deals, Leak Reveals*, INDEPENDENT (Mar. 18, 2016), <http://www.independent.co.uk/news/business/news/ttip-big-business-and-us-to-have-major-say-in-eu-trade-deals-leak-reveals-a6937141.html>.

society organizations because negotiations with major corporations occurred behind closed doors. Aside from the leaked version available on the internet, the draft text of the TPP, at any phase, was not officially made available to the public.

Civil societies have a self-designated role as promoters of transparency and have given effect to this task by demanding that investor-State arbitrations allow non-party submissions. Non-party submissions may increase transparency of the investor-State arbitration by allowing third parties to access documents in proceedings often unavailable for public disclosure. Moreover, increased openness and a view into how the proceedings function may encourage the legitimacy of investor-State arbitrations.¹⁵⁹ The first *amicus curiae* brief permitted in an ICSID arbitration occurred in May 2005¹⁶⁰ when the tribunal in *Suez/Vivendi v. Argentina* decided that it had the power to accept such non-party submissions from civil society organizations and received a submission from a coalition of five NGOs in February 2007¹⁶¹ despite objections by the claimant. The investment dispute arose out of circumstances similar to the Argentine ICSID cases elaborated in this Dissertation. The claimants invested in a

¹⁵⁹ *Suez/Vivendi Universal v. Argentina*, ICSID Case No. ARB/03/19, Order in Response to a Petition for Transparency and Participation as *Amicus Curiae*, para. 22 (May 19, 2005) [hereinafter *Suez/Vivendi Amicus Curiae*]. See WIR 2015, *supra* note 25, at 148.

¹⁶⁰ *Suez/Vivendi Amicus Curiae*, *supra* note 159.

¹⁶¹ *Suez/Vivendi Universal v. Argentina*, ICSID Case No. ARB/03/19, Order in Response to a Petition by Five Non-Governmental Organizations for Permission to Make an *Amicus Curiae* Submission (Feb. 12, 2007) [hereinafter *Suez/Vivendi Five NGOs Petition*].

concession for water distribution and waste water treatment services in 1993 during Argentina's privatization efforts, but with the enactment of the Emergency Act and the government's subsequent regulatory act of refusing to increase water and sewage treatment tariffs, the claimants were unable to meet their financial obligations and eventually defaulted on their debts.¹⁶² Argentina argued that it adopted those measures to safeguard the inhabitants' right to water.¹⁶³ In January 2005, five NGOs requested the *Suez/Vivendi* tribunal to accept *amicus curiae* submissions since the case involved an important public interest regarding water accessibility and to open hearings to the public and disclose documents produced during the arbitration proceedings.¹⁶⁴ To grant the request for *amicus curiae* submissions of the NGOs, the *Suez/Vivendi* tribunal found that the three conditions for accepting non-party submissions were satisfied. First, the tribunal found the subject matter of the case to be appropriate since "this case does involve matters of public interest of such a nature that have traditionally led courts and other tribunals to receive *amicus* submissions from suitable nonparties."¹⁶⁵ Second, the tribunal determined that the five NGO petitioners were suitable to act as *amici curiae* based on their expertise, experience, and independence based on the coalition's description of their knowledge on human rights and sustainable development, including the

¹⁶² *Suez/Vivendi Universal v. Argentina*, ICSID Case No. ARB/03/19, Award, paras. 2-3 (Apr. 9, 2015).

¹⁶³ *Suez/Vivendi Universal v. Argentina*, ICSID Case No. ARB/03/19, Decision on Liability, para. 252 (July 30, 2010) [hereinafter *Suez/Vivendi*, Decision on Liability].

¹⁶⁴ *Suez/Vivendi Amicus Curiae*, *supra* note 159, para 1.

¹⁶⁵ *Id.* para. 20.

right to water.¹⁶⁶ Finally, the tribunal considered the procedure to govern the *amicus curiae* submission “to safeguard due process and equal treatment as well as the efficiency of the proceedings.”¹⁶⁷ Despite the efforts of the NGOs to present to the tribunal with relevant and knowledgeable arguments and perspectives and the tribunal’s own recognition that the *Suez/Vivendi* case involves a fundamental public interest, the final decision was made in favor of the claimants. Although the NGOs were successful in persuading the *Suez/Vivendi* tribunal to accept *amicus* submissions, their effort fell short of setting an ICSID case example for transparency when the tribunal denied them access to the arbitration documents because the tribunal considered the coalition to have sufficient information even without having to disclose the arbitration record.¹⁶⁸

Civil society can make contributions towards greater transparency because *amicus curiae* submissions are meant to provide specific, expert knowledge on matters of public interest and therefore need to be based on the relevant facts and information of the investor-State arbitration case for them to be meaningful.¹⁶⁹ For civil society organizations, the obstacles to achieving greater transparency is not limited to politics, but can also be brought upon administratively. For example, some South African civil society organizations were administratively restrained when they could not obtain the underlying treaties to be reviewed in the *Piero Foresti and Others*

¹⁶⁶ *Id.* para. 24; *Suez/Vivendi Five NGOs Petition*, *supra* note 161, para. 16.

¹⁶⁷ *Suez/Vivendi Amicus Curiae*, *supra* note 159, para 29.

¹⁶⁸ *Suez/Vivendi Five NGOs Petition*, *supra* note 161, para. 24.

¹⁶⁹ See WIR 2015, *supra* note 25, at 124.

ICSID case. They were compelled to go through a time-consuming procedure pursuant to South Africa's Promotion of Access to Information Act to access the IIAs.¹⁷⁰ When contracting States either completely fail or do not upload the IIA in a timely fashion for public viewing on the UNCTAD website, this can create inefficiencies that sacrifice transparency since civil society organizations and the general public cannot access them.¹⁷¹ In matters related to trade secrets, confidential business information, state secrets, civil society organizations understandably have limited or is completely denied access to these important documents. Protection of certain information is a legally granted privilege available in the jurisprudence of many countries, and likewise, also protected under the general principles of international and the investor-State arbitral rules. For instance, the 2013 UNCITRAL arbitration rules provides that "the arbitral tribunal may conduct the arbitration in such manner as it considers appropriate."¹⁷² For civil society organizations, the trouble occurs when a signed investment treaty is not accessible domestically or internationally, consequently preventing foreign investors from knowing what protections

¹⁷⁰ Julie A. Maupin, *Transparency in International Investment Law: The Good, the Bad and the Murky*, in *TRANSPARENCY IN INTERNATIONAL LAW* 142, 156 (Andrea Bianchi & Anne Peters eds., 2013).

¹⁷¹ Howard Mann, UNCTAD, *The Right of States to Regulate and International Investment Law*, in *THE DEVELOPMENT DIMENSION OF FDI: POLICY AND RULE-MAKING PERSPECTIVES* 222, UNCTAD/ITE/IIA/2003/4 (2003), available at http://unctad.org/en/Docs/iteiia20034_en.pdf (arguing that civil society distaste for the furtive manner in which the investor-state arbitration process is conducted "discredits the entire process in the eyes of civil society groups") [hereinafter Mann, *Right to Regulate*].

¹⁷² UNCITRAL, *Model Law on International Commercial Arbitration*, art. 17 (2013).

have been secured for them when they conduct business in the host State and also obstructing the general public from their right to know how their country's sovereignty and right to regulate will be affected.¹⁷³

When law is understood to contain a communicative process of authoritative decision-making so that "any communication between elites and politically relevant groups which shapes wide expectations about appropriate future behavior must be considered as functional lawmaking,"¹⁷⁴ the question of how civil societies can influence international investment decision-making becomes an important one. In this communicative spirit, civil societies have already been raising concerns that the commitments in IIAs force the surrender of national sovereignty in an imbalanced manner, especially when treaty obligations challenge the legitimacy or altogether prevent governments from making domestic legislations for the public good.¹⁷⁵ What is troubling about IIAs, as seen through the lens of civil societies, is that many States view foreign investment as a means to achieving national economic development even though "IIAs have become a charter of rights for foreign investors, with no concomitant responsibilities or liabilities, no direct legal links to promoting

¹⁷³ Maupin, *supra* note 170, at 160.

¹⁷⁴ Michael W. Reisman, *International Law-making: A Process of Communication*, 75 AM. SOC'Y INT'L L. PROC. 101, 107 (1981). See also Manuel Castells, *The New Public Sphere: Global Civil Society, Communication Networks, and Global Governance*, 616 ANNALS AM. ACAD. POL. & SOC. SCI. 78, 79 (2008) ("It is the interaction between citizens, civil society, and the state, communicating through the public sphere, that ensures that the balance between stability and social change is maintained in the conduct of public affairs.").

¹⁷⁵ Mann, *Right to Regulate*, *supra* note 171, at 211.

develop objectives, and no protection for the public welfare in the face of environmentally or socially destabilizing foreign investment.”¹⁷⁶ Given that the international investment law system is “a prime example of the ways that international law is increasingly turning to non-[S]tate actors not only as objects of the law but as law-making or law-influencing subjects,”¹⁷⁷ civil societies can provide broad access and participation to the international investment decision-making process as well as provide the expertise, information, and perspectives from the initial phases of when states enter into IIA negotiations.

II. Problem Identification

The purpose of this Dissertation is to give much deserved attention to the public order carve-out as provided in IIAs by determining whether a public order concept specially adapted to the international investment law system is emerging and if the public order carve-out provides the flexibility needed to enable host States to preserve their regulatory space. The public order carve-out considered in this Dissertation is a narrow concept as represented by Article XI of the U.S.-Argentina BIT which provides that:

This Treaty shall not preclude the application by either Party of measures necessary for the maintenance of public order, the fulfillment of its obligations with respect to the maintenance or restoration of international peace or security, or the protection of its own essential security interests.¹⁷⁸

¹⁷⁶ *Id.* at 212.

¹⁷⁷ ALVAREZ, PUBLIC INTERNATIONAL LAW, *supra* note 68, at 410.

¹⁷⁸ U.S.-Argentina BIT, Nov. 14, 1991.

The five Argentine ICSID cases discussed in this Dissertation are the *CMS*, *Continental Casualty*, *Enron*, *LG&E*, and *Sempra* cases (collectively referred here as the “Argentine ICSID cases”).¹⁷⁹ Aside from the *Continental Casualty* and the *LG&E* tribunals, the other three tribunals rejected Argentina’s treaty-based public order and essential security interest defenses arising out of the NPM provision and declared that the emergency measures enacted during its financial crisis in the early 2000s did not meet the burden of proof under the customary international law defense of necessity.¹⁸⁰ The tribunals for these five cases are collectively referred here as the “Argentine ICSID tribunals.”

Since the Argentine ICSID cases, the international investment law system has been plagued by questions of whether investor-State tribunals unreasonably restrain the regulatory acts of States or other reasonable exercises of regulatory public interest as investor-State tribunals creep into the policy space of many developing countries.¹⁸¹ When successfully

¹⁷⁹ *CMS v. Argentina*, ICSID Case No. ARB/01/8, Award (May 12, 2005); *Continental Casualty v. Argentina*, ICSID Case No. ARB/03/9, Award (Sep. 5, 2008); *Enron Corp. Ponderosa Asset, L.P. v. Argentina*, ICSID Case No. ARB/01/3, Award (May 22, 2007); *LG&E v. Argentina*, ICSID Case No. ARB/02/1, Decision on Liability (Oct. 3, 2006); *Sempra Energy Int’l v. Argentina*, ICSID Case No. ARB/02/16, Award (Sep. 28, 2007).

¹⁸⁰ See generally Andrea K. Bjorklund, *Improving the International Investment Law and Policy System: Report of the Rapporteur Second Columbia International Investment Conference: What’s Next in International Investment Law and Policy?*, in *THE EVOLVING INTERNATIONAL INVESTMENT REGIME: EXPECTATIONS, REALITIES, OPTIONS* 213, 217-18 (José E. Alvarez et al. eds., 2011) (stating that the perceived crisis in investor-State arbitration is a matter of open debate amongst scholars. For example, Professor Thomas Wälde believes that the investment arbitration system is not experiencing a *crise de croissance* while Howard Mann firmly disagrees. A moderate view is offered by Professor Brigitte Stern who believes that the instability seen in the investor-state arbitration regime will be resolved as the system further matures.).

¹⁸¹ *Id.* See also SURYA P. SUBEDI, *INTERNATIONAL INVESTMENT LAW: RECONCILING*

invoked, the public order carve-out permits the cost that should have been absorbed by the host State to possibly shift to the private investor allowing the State to avoid liability even when a breach arises.¹⁸² Deeper understanding of the transformation process of this generic version of the public order carve-out can provide the groundwork for equipping host States with a flexible balancing tool that can meet the dynamic forms of today's investment treaties while effectively enabling host States to preserve their regulatory space without breaching international treaty commitments. Regrettably, the closest that the ICSID tribunals ever came to analyzing the public order carve-out was during the 2007-2008 period after foreign investors brought investor-State arbitration claims against Argentina after its economy collapsed in December 2001. Aside from the 2007 analytical work of William Burke-White and Andreas von Staden that extensively examined the interpretation and application of the NPM provision in BITs,¹⁸³ further

POLICY AND PRINCIPLE 2 (Hart Pub. 2d ed. 2012) (stating that host States are compelled to "outsource" public policy matters to international arbitral tribunals).

¹⁸² William W. Burke-White & Andreas von Staden, *Investment Protection in Extraordinary Times: The Interpretation and Application of Non-Precluded Measures Provisions in Bilateral Investment Treaties*, 48 VA. J. INT'L L 307, 314 (2008) [hereinafter Burke-White & von Staden, *Investment Protection*].

¹⁸³ William W. Burke-White, *The Argentine Financial Crisis: State Liability Under BITs and the Legitimacy of the ICSID System* (U. Pa. Faculty Scholarship Paper No. 193), available at http://scholarship.law.upenn.edu/cgi/viewcontent.cgi?article=1192&context=faculty_scholarship [hereinafter Burke-White, *State Liability*]. See Burke-White & von Staden, *Investment Protection*, *supra* note 182 (providing a scholarly examination of the NPM provision in international investment law). See also Jürgen Kurtz, *Adjudging the Exceptional at International Law: Security, Public Order and Financial Crisis* 35 (Jean Monnet Working Paper 06/08, 2008), available at <http://jeanmonnetprogram.org/wp-content/uploads/2014/12/080601.pdf> [hereinafter Kurtz, *Adjudging Security*].

study of the public order carve-out as a balancing tool for host States did not continue. Yet, almost a decade after the Argentine ICSID cases, we are experiencing an increase in new drafting, yet unevaluated methods that strive to better preserve the regulatory space of host States.¹⁸⁴ For example, many investment chapters in free trade agreements now contain WTO/GATS-style general exceptions provisions that, once again, are minimally guided in lieu of the BIT-style NPM public order carve-out as a way of enabling host States to preserve their regulatory power. My goal is not to decide between the two types of treaty exceptions, but to point out that without any one stakeholder adequately addressing the evolutionary steps in-between the huge leap from the NPM provisions in BITs to the WTO/GATS-style general exceptions in IIAs, current efforts made to “reclaim” the regulatory space of host States to pursue public interest objectives after an investment treaty enters into effect may not properly take place because of a systemic lack of understanding regarding the operation of the public order carve-out in the context of international investment law.

The need for a comprehensive perspective of the public order carve-out that takes into account the position of the stakeholders in investment treaty practice is more important than ever in the current investment climate. The meaning of the term “public order” is not defined in IIAs, thus leaving the interpretation of the ambiguous “necessary for the maintenance of public order” phrase solely up to an international arbitration tribunal that cannot always be expected to fully appreciate the complexities leading up to the host State’s catastrophe. The application of the public order carve-out will be

¹⁸⁴ See ch. 3 of this Dissertation.

affected by how each of the contracting States understands the term because the concept of public order is “deeply rooted and infused” in the legal and political culture of one’s society.¹⁸⁵ Despite the broad expanse of the international investment law system, the interpretive tools available to international investment tribunals are surprisingly limited. Concerned actors including policymakers and academics have made numerous attempts to address the ambiguity inherent in the public order clause. In 2008, the Freedom of Investment Roundtable hosted another international forum that would enable countries to collectively consider whether country policies on national security could operate transitively so as to apply to the NPM concepts on public order and essential security interests.¹⁸⁶ The conclusion was that an element of commonness was absent because the parties had not developed a shared understanding of the meaning and use of those NPM terms.¹⁸⁷

Although most IIAs currently in force do not contain treaty exceptions because the bulk of these agreements were concluded when providing for treaty exceptions was not a common drafting practice during the period before the Argentine ICSID cases, countries have changed their

¹⁸⁵ William W. Burke-White & Andreas von Staden, *Non-Precluded Measures Provisions, the State of Necessity, and State Liability for Investor Harms in Exceptional Circumstances*, in *LATIN AMERICAN INVESTMENT TREATY ARBITRATION: THE CONTROVERSIES AND CONFLICTS* 104, 133 & 135 (Thomas E. Carbonneau & Mary H. Mourra eds., 2008) [hereinafter Burke-White & von Staden, *NPM Provisions*].

¹⁸⁶ OECD, *SECURITY-RELATED TERMS IN INTERNATIONAL INVESTMENT LAW AND NATIONAL SECURITY STRATEGIES* 3 (May 2009) [hereinafter OECD, *SECURITY-RELATED TERMS*], available at <http://www.oecd.org/daf/inv/investment-policy/42701587.pdf>.

¹⁸⁷ *Id.*

stance and are rebalancing their rights and obligations through the tool of treaty exceptions.¹⁸⁸ Moreover, scholarship in international investment law especially since 2007 focuses on the various areas that could be the subject of an investment treaty exception.¹⁸⁹ However, one must take caution not to over tilt the scale so that the purpose of investment protection erodes.¹⁹⁰

The fear that foreign investors will not make investments in developing countries should their substantive rights be reduced is undoubtedly a major concern, but not one that trumps all other concerns including those held by the host States. Although IIAs may have been instrumental in liberalizing the foreign investment laws of countries and protecting foreign investments, the stakeholders in the current investment environment are aware that IIAs have “gone too far in limiting sovereign

¹⁸⁸ Kenneth J. Vandeveld, *Rebalancing Through Exceptions*, 17 LEWIS & CLARK L. REV. 449, 451 (2013) [hereinafter Vandeveld, *Rebalancing*].

¹⁸⁹ See generally UNCTAD, *BITs*, *supra* note 8, at 87 (noting that the various areas in public order and essential security, taxation, human health, natural resources, culture, prudential measures for financial services, and other miscellaneous topics have been the subject of general treaty exceptions in BITs during the 10-year span covered in this study); SALACUSE, *supra* note 42, 398-400 (providing a brief overview on treaty exceptions). See generally, e.g., Julien Chaisse, *Exploring the Confines of International Investment and Domestic Health Protections – Is a General Exceptions Clause a Forced Perspective?*, 39 AM. J. L. & MED. 332 (2013) (exploring the NPM provision from as it relates to the intersection between international investment and domestic health protections).

¹⁹⁰ Ian Laird, *The Emergency Exception and the State of Necessity*, in INVESTMENT TREATY LAW: CURRENT ISSUES II: NATIONALITY AND INVESTMENT TREATY CLAIMS AND FAIR AND EQUITABLE TREATMENT IN INVESTMENT TREATY LAW 237, 238 (Federico Ortino et al. eds., 2007). See also UNCTAD, *BITs*, *supra* note 8, at 80 (“In this sense, a general exception is a mechanism enabling the contracting parties to strike a balance between investment protection, on the one hand, and the safeguarding of other values considered to be fundamental by the countries concerned, on the other hand.”).

rights of host countries.”¹⁹¹ The investment law system is no longer dominated by only one value, but must make space for another competing value – the preservation of the regulatory space of host States in IIAs. This acknowledgement should be made for the goal of formulating a public order carve-out framework that can better address the demands of the States. Although Argentina raised defenses under both the essential security and the public order carve-outs, commentaries relating to the Argentine ICSID cases one-sidedly focus on the essential security clause, even though it is just one of the prongs in the NPM provision in the U.S.-Argentina BIT. What is troubling is that even for the ICSID tribunals that allowed Argentina’s NPM defense, the public order carve-out was not fully analyzed leaving its potential unanswered at a time when States are wanting to protect their right to regulate.

This Dissertation is organized in the following manner. Chapter 2 attempts to identify the concept of public order under international law by first sorting through the multiple meanings of the term “public order” according to various legal traditions. This step is taken in recognition of the fact that investor-State tribunals produce unpredictable and uncertain interpretations on the concept of public order because its usage and meaning differ for each IIA. Then, it draws from the experiences of the EU, WTO, and international human rights conventions to gain understanding of the concept of public order from the perspective of international organizations. Chapter 3 analyzes the States’ treatment of the public order concept in IIAs by observing the textual evolution that has occurred from FCNs to TIPs (trade

¹⁹¹ SUBEDI, *supra note* 181, at 2.

and investment partnerships). Furthermore, viewing the public order carve-out in the context of investment treaties may be useful for identifying the specific areas of concern held by States so that the public order concept can be better established to suit the needs of the stakeholders in international investment law. Chapter 4 examines the treatment of the public order carve-out by the Argentine ICSID tribunals to highlight the conflict between the public order carve-out as a treaty exception and the customary international law on necessity as codified in ILC Article 25. Such a clarification may help legitimize the international investment law system by identifying the review standard that may be applied by investment tribunals, thus producing more predictable and consistent awards. Chapter 5 evaluates the potential of the public order carve-out as a balancing tool that can better recognize the regulatory interests of host States. The main thesis of this Chapter is to argue that the public order carve-out in IIAs should be recognized as an exception provision that can limit the substantive obligation of an investment treaty. Chapter 6 concludes that the public order carve-out is capable of balancing the interests of States by providing an effective balancing tool for host States so they may better regulate domestic policy space without breaching IIA obligations.

Chapter 2: Preserving Regulatory Space through the Public Order Carve-out Provision in IIAs

I. The Multiple Meanings of “Public Order”

The origin of public order can be difficult to pin down for international investment law because the concept may be derived from various sources including natural law, principles of morality and universal justice, community of States, *jus cogens*, customary international law, treaties, and cases.¹⁹² The concept is in flux and its content can change according to the evolving values of one’s society. To illustrate, the terms “public order” and “public policy” are sometimes used interchangeably but each of the notions actually originates from different legal backgrounds. As will be explained in the section below, public order (*ordre public*) bars the application of certain foreign laws that go against the good moral principles of the forum State. This concept of public order which has a fundamental and even a constitutional element is familiar to the legal traditions of France, Italy, and Switzerland.¹⁹³ However, the term “public policy” is used in the Anglo-American legal traditions to avoid confusion with the English concept of law and order. U.S. courts also recognize that public policy is a fluid concept that can be molded according to the prevailing thought of the time and may require the new application of old principles.¹⁹⁴

¹⁹² See Martin Hunter & Gui Conde E Silva, *Transnational Public Policy and its Application in Investment Arbitration*, 4 J. WORLD INVESTMENT 367, 369 (2003); JULIAN D.M. LEW, LOUKAS A. MISTELIS & STEFAN M. KRÖLL, *COMPARATIVE INTERNATIONAL COMMERCIAL ARBITRATION* para. 24-114 (Kluwer Law Int’l 2003).

¹⁹³ OECD, *SECURITY-RELATED TERMS*, *supra* note 186, at 8.

¹⁹⁴ See, e.g., *Bron v. Weintraub*, 42 N.J. 87 (1964); *Henningsen v. Bloomfield Motors*,

The meaning of public order might also be considered with the “right to regulate” phrase that frequently appears in the current discussion on investment treaty-making, but is usually used without a concrete definition of what falls under the right to regulate concept. However, one possible understanding of the right to regulate concept may be available in Article 25 of the IISD Model International Agreement on Investment on the “inherent right” of host States which provides that:

(A) Host states have, in accordance with the general principles of international law, the right to pursue their own development objectives and priorities.

(B) In accordance with customary international law and other general principles of international law, host states have the right to take regulatory or other measures to ensure that development in their territory is consistent with the goals and principles of sustainable development, and with other social and economic policy objectives.

[...].¹⁹⁵

The right to regulate concept is embedded in paragraph (B) and the above two paragraphs may be understood as providing a broad set of rights for States to meet their development goals that may also raise social, economic, and other policy objectives.¹⁹⁶ The commentary provided by the IISD

Inc., 32 N.J. 358, 403 (1960).

¹⁹⁵ IISD Model Agreement, *supra* note 91, art. 25.

¹⁹⁶ IISD, Model International Agreement on Investment for Sustainable Development: Negotiators' Handbook 38 (April 2006), *available at* https://www.iisd.org/pdf/2005/investment_model_int_handbook.pdf.

acknowledges that it “reverses the trend among many arbitrators of interpreting international investment agreements based on the single objective of protecting investor and investment rights.”¹⁹⁷ The *World Investment Report* by the UNCTAD states that the “right to regulate in the public interest so as to ensure that IIAs’ limits on the sovereignty of States do not unduly constrain public policymaking” should be safeguarded.¹⁹⁸ The areas of public policymaking envisioned by the UNCTAD are the provisions on MFN, FET, or indirect expropriation as well as other provisions that create exceptions for national security or public policies such as on health, safety, labor rights, the environment, or sustainable development.¹⁹⁹ The European concept on the right to regulate is reflected in the TTIP which proposes that the States’ right to regulate shall not be affected for “measures necessary to achieve legitimate policy objectives, such as the protection of public health, safety, environment or public morals, social or consumer protection or promotion and protection of cultural diversity.”²⁰⁰ The effect of using the “right to regulate” phrase is not clear but may be a means of distinguishing the older BITs from the modern IIAs that consciously strive to rebalance investor rights by preserving a host State’s right to regulate.²⁰¹ More generally, it may operate as a buzz word

¹⁹⁷ *Id.*

¹⁹⁸ WIR 2015, *supra* note 25, at xi.

¹⁹⁹ *Id.*

²⁰⁰ TTIP, *supra* note 12, art. 2.

²⁰¹ Stephan W. Schill & Marc Jacob, *Trends in International Investment Agreements, 2010-2011: The Increasing Complexity of International Investment Law*, in YEARBOOK ON INT’L INVESTMENT LAW & POLICY 2011-2012 141, 143 (Karl P. Sauvant ed.,

that represents the widely-held beliefs of the IIA stakeholders about the future direction that international investment law should be taken.²⁰² This Dissertation mostly uses the term “public order” as seen in Article XI of the U.S.-Argentina BIT rather than the term “right to regulate.” The right to regulate concept is somewhat alien to the existing BITs and whether it creates a right, exception, reservation or some other justification or carve-out is not clear.²⁰³ In this regards, the right to regulate concept may contain a broader scope than the public order carve-out in the non-precluded measures (NPM) provisions of BITs.

Keeping in mind the different terminologies meant to preserve the regulatory space of host States, the focus of this Chapter is to examine the concept of public order in international investment law by getting a better understanding of the concept of public order at the national and international levels. An important goal is to identify which concept of public order is being used in the public order carve-out in NPM provisions like Article XI of the U.S.-Argentina BIT.

A. The National Law Concept of Public Order

The *ordre public* concept has long existed in several French bodies of law including the Napoleon Civil Code and the French Constitution of 1789 and its subsequent version as “a notion that everyone understands without

2013).

²⁰² *Id.*

²⁰³ See J. ANTHONY VANDUZER ET AL., INTEGRATING SUSTAINABLE DEVELOPMENT INTO INTERNATIONAL INVESTMENT AGREEMENTS: A GUIDE FOR DEVELOPING COUNTRY NEGOTIATORS 239 (Commonwealth Secretariat 2013) (suggesting that the right to regulate concept is too open-ended to succeed in IIA negotiations).

having to give it a precise definition.”²⁰⁴ The French legal dictionary defines *ordre public* as “the rules that are imposed for reasons of morality or security and that are needed for the conduct of social relations.”²⁰⁵ Moreover, *ordre public* is divided into the principle of *ordre public interne*, which is well-established in French law as parts of national mandatory laws, and the lesser understood notion of *ordre public externe/international*.²⁰⁶ *Ordre public interne* is established by legislative acts to statutorily restrict private conducts offensive to public order. The more difficult concept to define under French jurisprudence has been the *ordre public externe/international*, which is invoked only when one of the two elusive conditions is satisfied: the morals of civilized society conflict with the foreign rule or the character of French civilization may be harmed by the foreign law.²⁰⁷ Despite attempts to identify the categories under *ordre public externe/international*, compiling a concrete list that could help define the concept of *ordre public externe/international* turned out to be an unsuccessful effort since none of the proposed definitions purporting to sanctify notions of political, economic,

²⁰⁴ See OECD, SECURITY-RELATED TERMS, *supra* note 186, at 8-9.

²⁰⁵ *Id.*

²⁰⁶ Kent Murphy, *The Traditional View of Public Policy and Ordre Public in Private International Law*, 11 GA. J. INT’L & COMP. L. 591, 596 (1981); Max Habicht, *The Application of Soviet Laws and the Exception of Public Order*, 21 AM. J. INT’L L. 238, 243 (1927). See also Catherine Kessedjian, *Public Order in European Law*, 1 ERASMUS L.R. 25, 26 (2007); Paul Lagarde, *Reference to Public Order (“Ordre Public”) in French International Law*, in CULTURAL DIVERSITY AND THE LAW: STATE RESPONSES FROM AROUND THE WORLD 521, 524 (Marie-Claire Foblets et al. eds., 2010); George A. Bermann & Etienne Picard, *Administrative Law*, in Introduction to French Law 57, 79 (Kluwer Law Int’l 2008).

²⁰⁷ Murphy, *supra* note 206, at 596.

and moral order or safeguard the ethical, religious, economic, and political beliefs – all of which are at the core of the French sociolegal framework – could actually assist judges with their interpretive task.²⁰⁸ Thus, the approach settled for was to have a generalized definition of international public order.²⁰⁹ It is interesting that this brief discussion of the growing pains that the French experienced in the course of developing the international public order concept is highly relevant to our discussion of the public order carve-out in IIAs because of their shared concerns and similar base of problems.

Likewise, other countries have also grappled with the internal concept of public order, which was initially more frequently applied than the international public order concept in private international law cases.²¹⁰ Unlike the French, the German concept of public order (*öffentliche Ordnung*) avoids narrow categorizations of public order by simply declaring that foreign laws that violate German morals or the purpose of a German law

²⁰⁸ Habicht, *supra* note 206, at 243-44.

²⁰⁹ *Id.* at 245.

²¹⁰ Cf. PIETER SANDERS, TRENDS IN THE FIELD OF INTERNATIONAL COMMERCIAL ARBITRATION 224 (Hague Academy Int'l L. 1975) observing that:

More and more we see a distinction between domestic public policy (*ordre public interne*) and international public policy (*ordre public international*) gaining ground. The notion of the latter is more restricted than the former. International public policy, according to a generally accepted doctrine, is confined to violation of really fundamental conceptions of legal order in the country concerned. For the sake of international commercial arbitration the distinction between domestic and international public policy is of great importance.

cannot be enforced.²¹¹ German courts determine whether “disparity between the respective political or social views that have given rise to the relevant foreign law and the conflicting German law are so great that to apply the foreign law would undermine the foundations of German political or economic life.”²¹² In Germany, public order is an important part of its legal system but operates in adjunct to its laws “as a residual legal category”²¹³ whereas the French approach holistically develops the concept within the French legal framework.²¹⁴ Moreover, the German public order is usually associated with public security or safety such that the two concepts are used interchangeably, but distinguishable because public order is not legally defined while public security is statutorily established, thus revealing the dwindling influence of the concept of public order in German law.²¹⁵ However, public order in the United States does not conform to the French or German approach and is usually equated to the common law concept of police power.²¹⁶ In the United States, public order is a concept that is

²¹¹ Habicht, *supra* note 206, at 245-46.

²¹² Murphy, *supra* note 206, at 598.

²¹³ Burke-White & von Staden, *NPM Provisions*, *supra* note 185, at 135.

²¹⁴ Murphy, *supra* note 206, at 599. *See also* OECD, SECURITY-RELATED TERMS, *supra* note 186, at 9.

²¹⁵ OECD, SECURITY-RELATED TERMS, *supra* note 186, at 9 (“Another driver that continually narrows the scope of public order is the fact that all authoritative limitations of civil liberties require authorization by a general law; by virtue of this fact, such limitations are taken out of the domain of public order and into that of public security.”).

²¹⁶ *See, e.g.*, Gudgeon, *supra* note 1, 121 (referring to the U.S. constitutional concept of police power as the equivalent to the phrase “maintenance of public order”).

prevalent in the criminal law context for acts that deviate from social norms and customs and include offenses like, for example, obscenity, loitering, and lewdness; it may be the basis for police power; or, it may refer to public authority. Professor Newcombe refutes roughly equating police power with public order, which “causes significant confusion” because all kinds of domestic regulations could potentially fall under the purview of police power (implying that no compensation is due), thus begging the question of how regulatory taking, in which just compensation would be due, and taking for public good, in which no compensation is due, ought to be distinguished when both situations ultimately require the property owner to shoulder the burden that may result from such a taking.²¹⁷ A better equivalent of *ordre public* in common law tradition may be the concept of public policy, which in American jurisprudence refers to “the mandatory rules of law which could be relied upon to justify setting aside other binding obligations.”²¹⁸ Courts in the United States have set aside judgments or voided contracts in the name of public policy which, according to Black’s Law Dictionary, is defined as a “community common sense and common conscience, extended and applied throughout the state to matters of public morals, health; safety, welfare and the like; it is that general and well-settled opinion as to man’s plain, palpable duty to his fellow men, having due regard to all circumstances of each particular relation and situation.”²¹⁹

²¹⁷ Andrew Newcombe, *The Boundaries of Regulatory Expropriation in International Law*, 20 ICSID REV. 1 (2005), available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=703244.

²¹⁸ OECD, SECURITY-RELATED TERMS, *supra* note 186, at 10.

²¹⁹ *Id.*

Having different concepts of public order among the States has, for better or worse, deterred the formation of a universally applicable concept of public order for the international community of States, thus “enhancing the domestic particularities of legal interpretation and preserving the territorial orientation and fragmentation of the application of law” since the domestic concept of public order could prevail over foreign substantive law.²²⁰ However, what should be distinguished is that in the case a forum court is requested to enforce a foreign arbitration award, it may refuse application on public policy grounds for substantive reasons such as if the award resulted from, *inter alia*, corruption or unfair dealings, but also for procedural reasons like those based on violation of due process.²²¹ The latter situation is memorialized in the Convention on the Recognition and Enforcement of Foreign Arbitral Awards (New York Convention), which provides that recognition and enforcement of an arbitral award may be refused under Article V.2 if it “would be contrary to the public policy of that country.”²²² Other procedure-based “public policy” defenses may be raised under Article V.1 of the New York Convention such as if one party “was not given proper notice of the appointment of the arbitration or of the arbitration

²²⁰ JOANNA JEMIELNIAK, *LEGAL INTERPRETATION IN INTERNATIONAL COMMERCIAL ARBITRATION* 196 (Routledge 2016).

²²¹ Stephen M. Schwebel & Susan G. Lahne, *Public Policy and Arbitral Procedure*, in *JUSTICE IN INTERNATIONAL LAW: FURTHER SELECTED WRITINGS* 220, 223 (Cambridge Univ. Press 2011) (quoting Julian D. M. Lew’s summary of the relevance of national public policy to international commercial arbitration).

²²² Convention on the Recognition and Enforcement of Foreign Arbitral Awards, art. V.2(b), June 10, 1958, 330 U.N.T.S 38 [hereinafter New York Convention].

proceedings or was otherwise unable to present his case”²²³ or the “composition of the arbitral authority or the arbitral procedure was not in accordance with the agreement of the parties, or... was not in accordance with the law of the country where the arbitration took place.”²²⁴ This type of framework forms the basis of international public order and operates in a “negative” manner as a reservation or exception which enables the adjudicator to reject the application of a foreign law that was decided on the merits in its court.²²⁵ Similar to the New York Convention concept of procedural public order, a comparable notion exists in international investment law through Article 52 of the ICSID Convention, which allows any one of the disputing party to request annulment of the award even though it does not explicitly mention the term “public order” and is not based on a particular law of a State. Article 52 of the ICSID states, in pertinent part, the following:

- (1) Either party may request annulment of the award by an application in writing addressed to the Secretary-General on one or more of the following grounds:
 - (a) that the Tribunal was not properly constituted;
 - (b) that the Tribunal has manifestly exceeded its powers;
 - (c) that there was corruption on the part of a member

²²³ New York Convention art. V.1(b).

²²⁴ New York Convention art. V.1(d).

²²⁵ Pierre Lalive, *Transnational (or Truly International) Public Policy and International Arbitration*, in *COMPARATIVE ARBITRATION PRACTICE AND PUBLIC POLICY IN ARBITRATION* 258, 260 (Pieter Sanders ed., 1987).

of the Tribunal;

(d) that there has been a serious departure from a fundamental rule of procedure; or

(e) that the award has failed to state the reasons on which it is based.²²⁶

Although procedural public policy is built into the ICSID Convention, its contribution in terms of permitting a host State to take measures for the maintenance of public order is limited.

B. The International Law Concept of Public Order

The above section discussed one understanding of the concept of public order that prevents the application of a foreign law in the court of the forum State or the recognition of a foreign judgment or arbitral award by those courts as enshrined in Article V of the New York Convention and Article 36 of the 1985 UNCITRAL Model Law. International public order (*ordre public international*) is a narrow concept of public policy that stems from the domestic public policies of a State so that the court of the forum State will refer to its own international public order.²²⁷ However, international public policy may also suggest another meaning to represent the international consensus of universally accepted norms. Such an understanding of international public policy treats it as a kind of supra-national principle.²²⁸

This concept of an international public order for public international

²²⁶ ICSID Convention, *supra* note 52, art. 52.

²²⁷ World Duty Free Company v. Kenya, ICSID Case No. Arb/00/7, Award, para. 138 (Oct. 4, 2006).

²²⁸ *Id.* paras. 138-39.

law was introduced by Pierre Lalive at the International Council for Commercial Arbitration (ICCA) Congress in 1986 to refer to those norms which are universally acknowledged in other legal systems so that transactions derived from bribery, bad morals, and illicit influences would be illegal.²²⁹ Lalive identified this set of legal principles, not belonging to any one State, as transnational public policy. According to the resolution adopted by the Institut de droit international in 1989, the transnational public policy may provide guidelines in international arbitrations by setting forth the principle that “in no case shall an arbitrator violate principles of international public policy as to which a broad consensus has emerged in the international community.”²³⁰ What comprises the transnational public policy will be determined by the legal systems of the States, thus containing some domestic aspects, but should transcend this by formulating a “truly international purpose”²³¹ based upon the general principles of morality accepted by civilized nations.

In international arbitration cases, transnational public policy may allow an arbitrator to prevent the enforcement of a parties’ agreement if the alleged contract or investment was based on corruption, racial or religious discrimination, drug or human (including organs) trafficking, terrorism, or trade of illegal goods (such as stolen art or the supplying of arms to illegal

²²⁹ Lalive, *supra* note 225, at 260.

²³⁰ INST. OF INT’L L., Resolution on Arbitration between States, State Enterprises or State Entities, and Foreign Enterprises, *reprinted in* 16 YEARBOOK COM. ARB. 236, 238 (Albert Jan van den Berg ed., 1991).

²³¹ Lalive, *supra* note 225, at 277.

organizations).²³² Some attempts have been made to define international public policy. The ICSID tribunal in *Inceysa v. El Salvador* described the concept as “a series of fundamental principles that constitute the very essence of the State, and its essential function is to preserve the values of the international legal system against actions contrary to it.”²³³ The *Inceysa* tribunal considered that the rights arising out of an investment which violated several general principles of law could not be recognized as a matter of international public policy.²³⁴ In particular, it identified “respect for the law” is an uncontroversial matter of public policy in any civilized country.²³⁵ Couple months after the *Inceysa* award, this concept was mentioned again in another ICSID case. Upon determining that the investment contract was obtained by bribing the Kenyan president, the ICSID tribunal in *World Duty Free v. Kenya* noted some arbitral tribunals have considered “universal values... such as ‘good morals,’ bonas mores,’ ethics of international trade’ or ‘transnational public policy.’”²³⁶ But it also affirmed that tribunals bearing such a task must identify the legal order that provides the source of the transnational public policy principle such as through instruments including

²³² See Pierre Mayer, *Effect of International Public Policy in International Arbitration?*, in PERVASIVE PROBLEMS IN INTERNATIONAL ARBITRATION 61, 63 (Loukas A. Mistelis & Julian D.M. Lew eds., 2006). See also JULIAN D.M. LEW, LOUKAS A. MISTELIS & STEFAN M. KRÖLL, COMPARATIVE INTERNATIONAL COMMERCIAL ARBITRATION 423 (Kluwer Law Int’l 2003).

²³³ *Inceysa Vallisoletana v. El Salvador*, ICSID Case No. ARB/03/26, Award, para. 245 (Aug. 2, 2006).

²³⁴ *Id.* para. 249.

²³⁵ *Id.* para. 248.

²³⁶ *World Duty Free*, *supra* note 227, para. 141.

conventions and arbitral awards.²³⁷ In *Plama v. Bulgaria*, the ICSID tribunal stated that investments obtained through fraudulent misrepresentation and false statements are against international public policy, particularly against the principle of good faith “which is part not only of Bulgarian law... but also of international law.”²³⁸

The concept of transnational public policy is not without controversy. On one hand, it is advocated because international arbitrators, who are not pinned to any particular State unlike national courts, need their own principles of public policy that can be universally applied.²³⁹ From this perspective, transnational public policy is even viewed as “a necessary device in international arbitration”²⁴⁰ to prevent parties from harming certain important social values. For example, the fine line between corruption and facilitation payments is not always clear, but a tribunal may be justified in invoking transnational public policy to protect the value of not recognizing investments arising out of corruption although the subjective standard of the arbitrators will inevitably be incorporated. On the other hand, the transnational public policy is far from being universally accepted.

²³⁷ *Id.* See FARSHAD GHODOOSI, *INTERNATIONAL DISPUTE RESOLUTION AND THE PUBLIC POLICY EXCEPTION* 109 (Routledge 2017).

²³⁸ *Plama Consortium Ltd. v. Bulgaria*, ICSID Case No. ARB/03/24, Decision on Jurisdiction, para. 144 (Feb. 8, 2005).

²³⁹ See Kenneth-Michael Curtin, *Redefining Public Policy in International Arbitration of Mandatory National Laws*, 64 DEF. COUNS. J. 271, 283 (1997) (stating that principles like fundamental fairness would be maintained in transnational public policy since the concept houses “a collection of internationally accepted and fundamental principles of public policy”).

²⁴⁰ Mayer, *supra* note 232, at 62.

One main reason is because of the view that existing domestic and international law sources already have national mandatory rules against acts like corruption, fraud, and slavery. The argument that the principles of transnational public policy is already covered by international public order seems justified. Another reason that the transnational public policy is not highly favored is due to the controversial notion that *jus cogens* norms may be made as the equivalent to transnational public policy.²⁴¹ Some scholars argue that the two principles should not be conflated because *jus cogens* norms are from customary international law while transnational public policy is legislation-based.²⁴² Opponents also claim that even if *jus cogens* establishes international public order, transnational public policy may not be necessary for the purpose of invalidating certain treaties since *jus cogens* norms already fulfill that role.²⁴³

Regardless of the controversy, the purpose of the transnational public

²⁴¹ See Catherine Kessedjian, *Public Order in European Law*, 1 ERASMUS L.R. 25, 26 (2007). See also ILA Comm. Int'l Com. Arb., *Final Report on Public Policy as a Bar to Enforcement of International Arbitral Awards*, in *New Delhi Conference* (2002). For more on the controversy, see Rafael Nieto-Navia, *International Peremptory Norms (Jus Cogens) and International Humanitarian Law*, in *MAN'S INHUMANITY TO MAN: ESSAYS ON INTERNATIONAL LAW IN HONOUR OF ANTONIO CASSESE* 595 (Lal Chand Vohrah et al. eds., 2003). See generally Stefan Kadelbach, *Jus Cogens, Obligations Erga Omnes and other Rules – The Identification of Fundamental Norms*, in *THE FUNDAMENTAL RULES OF THE INTERNATIONAL LEGAL ORDER: JUS COGENS AND OBLIGATIONS ERGA OMNES* 21, 31 (Christian Tomuschat & Jean-Marc Thouvenin eds., 2006) (explaining that the ICJ “has not yet expressly, directly and unequivocally relied on *jus cogens*” with such statements being present in separate or dissenting opinions).

²⁴² *Jurisdictional Immunities of the State (Germany v. Italy with Greece Intervening)*, 2012 I.C.J. 99, 124, para. 58 (Feb. 3).

²⁴³ See, e.g., ANTONIO CASSESE, *INTERNATIONAL LAW* 143 (Oxford Univ. Press 2001).

policy is to equip international arbitral tribunals with their own public policy principles. Under this scheme, investment tribunals owe no duty to accept the arguments of a host State that relies on its domestic laws to deny a principle of transnational public policy.²⁴⁴ An international public order concept such as the transnational public policy can empower arbitrators. Gaillard and Savage assert that arbitrators owe an obligation to invalidate national laws that violate transnational public policy principles.²⁴⁵ Mourre argues that the transnational public policy enables the “higher interests of the world community” to be preserved.²⁴⁶ Schreuer notes that ICSID tribunals owe a similar duty to disregard investment agreements that violate basic principles and consistent with the ICSID Convention.²⁴⁷ The concept of transnational public policy may provide one means of balancing interests by directly handing international arbitral tribunals with the authority to invalidate parts of an IIA that violates such principles but needs to be distinguished from whether the States’ concept of public order can be recognized at the international level, which is examined in the following

²⁴⁴ Hunter & Silva, *supra* note 192, at 372.

²⁴⁵ EMMANUEL GAILLARD & JOHN SAVAGE, FOUCHARD, GAILLARD, GOLDMAN ON INTERNATIONAL COMMERCIAL ARBITRATION 861 (Emmanuel Gaillard & John Savage eds., 1999).

²⁴⁶ Alexis Mourre, *Arbitration and Criminal Law: Reflections on the Duties of the Arbitration*, 22 ARB. INT’L 95, 115 (2006).

²⁴⁷ CHRISTOPH H. SCHREUER ET AL., THE ICSID CONVENTION: A COMMENTARY 567 (Cambridge Univ. Press, 2d ed. 2009) (stating that the only suitable reaction of ICSID tribunals in such a case would be to refuse “to apply and enforce arrangement which serve the violation of one of these principles”). *See also* Stephen Jagusch, *Issues of Substantive Transnational Public Policy*, in INTERNATIONAL ARBITRATION AND PUBLIC POLICY 23, 41 (Devin Bray & Heather L. Bray eds., 2015).

section.

II. The State Concept of Public Order in the Context of International Organizations

A. Public Order in the European Union

The European Union prefers the term “public policy” in the Treaty on the Functioning of the European Union (TFEU), which was formerly known as the Treaty Establishing the European Economic Community (EC Treaty), as well as the decisions of the European Court of Justice (ECJ). The TFEU recognizes that public policy is subjective because it is “linked to the way societies structure themselves”²⁴⁸ and is silent on how the concept of public order may be defined or applied even though the phrase “public policy” is used in Articles 30, 39, 46, 58, and 186 of the EC Treaty.²⁴⁹ For example, the term “public policy” is used instead of “public order” in Article 30 as shown below:

The provisions of Articles 28 and 29 shall not preclude prohibitions or restrictions on imports, exports or goods in transit justified on grounds of public morality, public policy or public security; the protection of health and life of humans, animals or plants; the protection of national treasures possessing artistic, historic or archaeological value; or the protection of industrial and commercial property. Such prohibitions or restrictions shall not, however, constitute a

²⁴⁸ Kessedjian, *supra* note 241, at 28.

²⁴⁹ Consolidated Version of the Treaty Establishing the European Community, Dec. 24, 2002, 2002 O.J. (C 325) 33 [hereinafter EC Treaty].

means of arbitrary discrimination or a disguised restriction on trade between Member States.²⁵⁰

The impact of the EU concept of public policy is better illustrated in the ECJ decisions. The ECJ permits States some regulatory space when deciding the meaning of public policy and also recognizes that the meaning of public policy may change over time. In addressing cases concerning the movement of citizens from one member State to another member State for situations justified on reasons of public policy, public security, or public health, the ECJ established in *Yvonne van Duyn v. Home Office* that the concept of public policy could operate as a legal justification but must be strictly interpreted by taking into consideration “the particular circumstances justifying recourse to the concept of public policy may vary from one country to another and from one period to another.”²⁵¹ A few years later, the ECJ provided in *Régina v. Pierre Bouchereau* that a public policy justification requires that the measure poses a “genuine and sufficiently serious threat” to society and that it affects “the fundamental interests of society.”²⁵² It also affirmed the decision in *Yvonne van Duyn* that a strict standard of review will

²⁵⁰ *Id.* art. 30.

²⁵¹ Case 41/74, *Van Duyn v. Home Office*, 1974 E.C.R. 1337, para. 18 (considering whether the public policy exception allows derogation from the freedom of movement of workers, a core principle of European Community law).

²⁵² Case 30-77, *Régina v. Pierre Bouchereau*, 1977 E.C.R. 1999, para. 35, which states the following:

The concept of public policy presupposes, in any event, the existence, in addition to the perturbation of the social order which any infringement of the law involves, of a genuine and sufficiently serious threat to the requirements of public policy affecting one of the fundamental interests of society.

apply.²⁵³ Moreover, the ECJ established that member States do not have the right to change a directive that fully addresses an issue in question;²⁵⁴ here, Directives 64/221, 68/360 and 73/148 are the relevant measures that comprehensively address the right of entry and residence of foreign nationals and the public policy and security grounds for refusal. Finally, the application of the public policy exception is curbed by Article 10 of the EC Treaty which requires that member States “abstain from any measure which could jeopardize the attainment of the objectives of this Treaty.”²⁵⁵

Despite such guidelines favoring a narrow interpretation of public policy, the ECJ decided a rare application of the EU public policy exception for an economic matter in *Regina v. Thompson*²⁵⁶ even though it generally does not permit member States to use public policy for economic considerations. In this dispute, the United Kingdom sought to use the public policy defense to prohibit the importation of certain gold coins and the exportation of certain silver coins not circulated as legal tender within the country claiming that such coins would destroy confidence in the United Kingdom currency even if melted down or destroyed against the law of the United Kingdom. The ECJ held that the ban issued by the United Kingdom was justified on grounds of public policy because the right to mint coinage is “traditionally regarded as involving the fundamental interests of the

²⁵³ *Id.* para. 33.

²⁵⁴ Case C-363/89, *Danielle Roux v. Belgian State*, 1991 E.C.R. I-273, paras. 29-31. For a more recent example, see Case C-277/02, *EU-Wood-Trading v. Sonderabfal-Management-Gesellschaft Rheinland-Pfalz*, 2004 E.C.R. I-11957.

²⁵⁵ EC Treaty, *supra* note 249, art. 10.

²⁵⁶ Case 30/77, *Regina v. Thompson*, 1978 E.C.R. 2247.

State.”²⁵⁷ However, when France invoked the public policy exception in *Cullet v. Centre Leclerc*²⁵⁸ to justify its implementation of minimum retail prices for fuel to avoid civil disorder, the ECJ held that the measure was a quantitative restriction made in breach of EU law. In the more recent case of *Eglise de Scientologie v. France*, the ECJ reaffirmed its long-held position that the public policy exception may not be invoked for economic reasons:

It should be observed, first, that while Member States are still, in principle, free to determine the requirements of public policy [...] in light of their national needs, those grounds must, in the Community context and, in particular, as derogations from the fundamental principle of free movement of capital, be interpreted strictly, so that their scope cannot be determined unilaterally by each Member States without any control by the Community institutions. Thus, public policy and public security may be relied on only if there is a genuine and sufficiently serious threat to a fundamental interest of society. Moreover, those derogations must not be misapplied so as, in fact, to serve purely economic ends.²⁵⁹

Moreover, a public policy defense will be hard to overcome because any national legislation that impedes the objective of the EU, which is to establish a common market by promoting the free movement of goods, services, capital and workers, and freedom of establishment, will be trumped

²⁵⁷ *Id.* para. 32.

²⁵⁸ Case 231/83, *Cullet v. Centre Leclerc*, 1985 E.C.R. 305.

²⁵⁹ Case C-54/99, *Eglise de Scientologie v. France*, 2000 ECR I-1335, para. 17.

by EU law.²⁶⁰ Even if the ECJ determines the meaning of public policy within EU law, the public policy provisions in the TFEU should be understood as providing a certain degree of regulatory space to member States.²⁶¹ However, the degree conferred to the member States will depend on whether the EU legal order embraces public policy as an “utmost symbol of culture... constitut[ing] a richness, not an impairment”²⁶² or views the member States’ varying standards of public policy as an impediment to achieving the goals of the EU by adding unnecessary transaction costs and legal uncertainty.²⁶³

In the context of international investment law, the European Commission released a fact sheet in November 2013 outlining the urgent need to strike a better balance between investor protection and the States’ right to regulate. According to the Commission, the right to regulate “reaffirm[s] the right of the Parties to regulate to pursue legitimate public policy objectives” so that the substantive rules of IIAs do not challenge legitimate government public policy decisions and proposes to achieve this objective by “clarifying and improving” the guarantees on investment protection.²⁶⁴ Consistent with the EU FTAs, the Commission also promised

²⁶⁰ Case 26/62, *Van Gend en Loos v. Nederlandse Administratie der Belastingen*, 1963 E.C.R. 1, 12 (ruling that the provisions of the Treaty Establishing the European Economic Community, which preceded the TFEU, is capable of conferring legal rights to individuals and that the courts of the member EU States must recognize and enforce those rights).

²⁶¹ Jan Kleinheisterkamp, *European Policy Space in International Investment Law*, 27 ICSID REV. 416, 418 (2012).

²⁶² Kessedjian, *supra* note 241, at 36.

²⁶³ Kleinheisterkamp, *supra* note 261, at 418.

²⁶⁴ EUROPEAN COMM’N, FACT SHEET: INVESTMENT PROTECTION AND INVESTOR-TO-STATE DISPUTE SETTLEMENT IN EU AGREEMENTS (Nov. 2013),

to establish as a standing principle in IIAs that a State retains the right to regulate when in pursuit of legitimate public policy objectives affecting the environment, public health and safety, protection and promotion of cultural diversity, society, and security. The Commission's effort to clarify and improve the investment protection provisions so as to permit regulatory space is visible in the expropriation context. The standard for determining indirect expropriation is whether the State's act for public interest was without discrimination. This is exemplified in the lengthy annex on expropriation in the EU-Singapore FTA provided as follows:

The Parties confirm their shared understanding that:

1. Article 9.6 (Expropriation) addresses two situations. The first is direct expropriation where a covered investment is nationalised or otherwise directly expropriated through formal transfer of title or outright seizure. The second is indirect expropriation where a measure or series of measures by a Party has an effect equivalent to direct expropriation in that it substantially deprives the covered investor of the fundamental attributes of property in its covered investment, including the right to use, enjoy and dispose of its covered investment, without formal transfer of title or outright seizure.
2. The determination of whether a measure or series of measures by a Party, in a specific situation, constitutes an indirect expropriation requires a case-by-case, fact-based inquiry that considers, among other factors:

http://trade.ec.europa.eu/doclib/docs/2013/november/tradoc_151916.pdf.

- (a) the economic impact of the measure or series of measures and its duration, although the fact that a measure or a series of measures 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;
- (b) the extent to which the measure or series of measures interferes with the possibility to use, enjoy or dispose of the property; and
- (c) the character of the measure or series of measures, notably its object, context and intent.

For greater certainty, except in the rare circumstance where the impact of a measure or series of measures is so severe in light of its purpose that it appears manifestly excessive, non-discriminatory measure or series of measures by a Party that are designed and applied to protect legitimate public policy objectives such as public health, safety and the environment, do not constitute indirect expropriation.²⁶⁵

In addition to clarifying the limits of certain substantive guarantees that may adversely affect the right to regulate, the EU has proposed an independent investment court which can help States to preserve their right to regulate. In the Canada-EU CETA, a permanent tribunal and an appeals tribunal are created to promote transparency and impartiality.²⁶⁶ The scope

²⁶⁵ EU-Singapore FTA, annex 9-A [“Expropriation”] [awaiting signature].

²⁶⁶ Canada-EU CETA, *supra* note 18, arts. 8.27, 8.28 & 8.29.

of investment disputes an investor-State tribunal can hear has been restricted to breaches of a certain few investment protection provisions such as on non-discrimination, expropriation, and fair and equitable treatment. Moreover, claims made to challenge the regulatory measure of a State may be lessened because the Canada-EU CETA does not consider an investor's loss of expected profits to be a breach of the obligation.²⁶⁷ A similar framework on public policy is provided in the currently under negotiations TTIP, which also attempts to quell fears that the right to regulate in public interest will be jeopardized by including a specific article providing for the States' right to regulate. Under the heading "Investment and Regulatory Measures/Objectives," Article 2 of the TTIP states that:

1. The provisions of this section shall not affect the right of the Parties to regulate within their territories through measures necessary to achieve legitimate policy objectives, such as the protection of public health, safety, environment or public morals, social or consumer protection or promotion and protection of cultural diversity.
2. For greater certainty, the provisions of this section shall not be interpreted as a commitment from a Party that it will not change the legal and regulatory framework, including in a manner that may negatively affect the operation of covered instruments or the investor's expectations of profits.

[...].²⁶⁸

²⁶⁷ *Id.* art. 8.9 ["Investment and Regulatory Measures"].

²⁶⁸ TTIP (draft), *supra* note 12, art. 2.

The recent string of investment treaties concluded by the EU appears to show a growing sensitivity towards the States' desire to retain their regulatory authority and attempts to meet their demands by creating a positive framework that enumerates the possible legitimate public policy objectives.

B. Public Order in the WTO/GATS

Decisions made by a WTO panel do not directly affect ISDS decisions, but may be analogous because the legal issues for construing the term "public order" share similarities whether in the context of an international investment agreement or trade agreement. Whereas international investment law has yet to fully consider the public order carve-out, an interpretation of the term "public order" was made in the case between the United States and Antigua in *United States – Measures Affecting the Cross-Border Supply of Gambling and Betting Services* (the *U.S. – Gambling* case).²⁶⁹

The WTO provision applicable to public order is Article XIV of GATS, which is modeled after Article XX of GATT.²⁷⁰ Paragraph (a) of Article XIV of GATS states that:

Subject to the requirement that such measures are not applied in a manner which would constitute a means of arbitrary or unjustifiable discrimination between countries where like conditions prevail, or a disguised restriction on trade in

²⁶⁹ Panel Report, *United States – Measures Affecting the Cross-Border Supply of Gambling and Betting Services*, WT/DS285/R (Nov. 10, 2004) [hereinafter *U.S. – Gambling*]. Shrimp Appellate Body

²⁷⁰ General Agreement on Tariffs and Trade, art. XX, Apr. 15, 1994, 1867 U.N.T.S. 187 [hereinafter GATT]. The chapeaux of both provisions are identical, but key differences exist between Article XIV of GATS and Article XX of GATT. For example, the public order exception does not exist in the latter, thus allowing States to exercise greater regulatory autonomy in comparison to the GATT.

services, nothing in this Agreement shall be construed to prevent the adoption or enforcement by any Member of measures:

- (a) necessary to protect public morals or to maintain public order [...].²⁷¹

The Panel in the *U.S. – Gambling* case was the first to construe the term “public order” from Article XIV(a) of GATS when Antigua claimed that some federal and state laws in the United States had effectively imposed a “total prohibition” which prevented it from providing cross-border gambling and betting services. Although the term “public order” is not defined in the GATS *per se*, the Panel referred to the dictionary meaning of the words “public” and “order” to establish their ordinary meanings and read in conjunction, footnote 5 appended to Article XIV(a), which limits the public order exception to be invoked only where a genuine and sufficiently serious threat is posed to one of the fundamental interests of society,²⁷² to mean that the phrase “public order” is “the preservation of the fundamental interests of a society, as reflected in public policy and law [where] fundamental interests can relate, *inter alia*, to standards of law, security and morality.”²⁷³ Moreover, the Panel asserted that defining public order engages a fluid process that “can vary in time and space, depending upon a

²⁷¹ General Agreement on Trade in Services, art. XIV, Apr. 15, 1994, 1869 U.N.T.S. 183 [hereinafter GATS].

²⁷² *Id.* n. 5.

²⁷³ *U.S. – Gambling*, *supra* note 269, para. 6.467. The United States’ argued that the meaning of the “public order” stems from the French concept of *ordre public* and that the American equivalent would be public policy. *Id.* para. 6.458.

range of factors, including prevailing social, cultural, ethical and religious values” and that members should therefore decide the appropriate level of these “societal concepts” based on their own values.²⁷⁴ In finding that the United States’ measures against gambling and betting services were for the maintenance of public order as set forth in Article XIV(a), the Panel analyzed footnote 5 with the dictionary definition of the terms “public” and “order” to conclude that public order “refers to the preservation of the fundamental interest of a society, as reflected in public policy and law.”²⁷⁵ Moreover, the Panel explained that the concept of public order encompasses fundamental interests relating to law, security, and morality.²⁷⁶

Article XIV(a) of GATS requires that the measures of a WTO member enacted to protect public order be necessary. The Panel in the *U.S. – Gambling* case relied on the parameters established in *Korea – Various Measures on Beef (Korea – Beef)*, the first case to interpret the term “necessary” in Article XX of GATT covering general exceptions. In *Korea – Beef*, the Appellate Body cautioned away from a restrictive meaning of the term “necessary,” which usually implies “indispensable” or “of absolute necessity” or “inevitable,”²⁷⁷ in support of a meaning that recognizes the term as “an adjective expressing degrees, and may express mere convenience or that

²⁷⁴ *Id.* para. 6.461.

²⁷⁵ *Id.* paras. 6.467 & 6.474.

²⁷⁶ *Id.*

²⁷⁷ Appellate Body Report, *Korea – Measures Affecting Imports of Fresh, Chilled and Frozen Beef*, para. 161, WT/DS161/AB/R, WT/DS169/AB/R (Dec. 11, 2000).

which is indispensable or an absolute physical necessity.”²⁷⁸ Affirming the “weighing and balancing” test articulated by the Appellate Body in *Korea – Beef*,²⁷⁹ the Panel in the *U.S. – Gambling* case articulated a weighing and balancing test that would determine whether the measure in question was “necessary” to maintain public order and is stated as follows:

(a) the importance of interests or values that the challenged measure is intended to protect. (With respect to this requirement, the Appellate Body [in *Korea – Beef*] has suggested that, if the value or interest pursued is considered important, it is more likely that the measure is “necessary”.)

(b) the extent to which the challenged measure contributes to the realization of the end pursued by that measure. (In relation to this requirement, the Appellate Body [in *Korea – Beef*] has suggested that the greater the extent to which the measure contributes to the end pursued, the more likely that the measure is “necessary”.)

(c) the trade impact of the challenged measure. (With regard to this requirement, the Appellate Body has said that, if the measure has a relatively slight trade impact, the more likely that the measure is “necessary.” The Appellate Body [in *Korea – Beef*] has also indicated that whether a reasonably available WTO-consistent alternative measure exists must be taken into

²⁷⁸ *Id.* para. 160 (quoting from BLACK’S LAW DICTIONARY).

²⁷⁹ *Id.* paras. 162, 163 & 166.

consideration in applying this requirement.)²⁸⁰

The Appellate Body in *U.S. – Gambling* affirmed the Panel’s finding that the U.S. measures were made to protect public morals and maintain public order within the meaning of GATS Article XIV(a), but disagreed regarding the issue of whether the measures were necessary. Unlike the Panel, the Appellate Body found that the measures, in fact, were necessary because the United States had provided the evidence and arguments to establish a *prima facie* case based on the weighing and balancing test described above.²⁸¹ The Appellate Body explained that the purpose of the weighing and balancing test is to determine whether the challenged measure is necessary or whether an alternative measure is “reasonably available.” It then stated that if the claimant raises an alternative measure, but that the respondent State proves that such an alternative measure was not reasonably available, then “it follows that the challenged measure must be ‘necessary’” under Article XIV(a) of the GATS.²⁸² In handling the evidence, the Appellate Body also stated that the role of the Panel is to “independently and objectively assess the ‘necessity’” of the challenged measure.²⁸³

In the context of international investment law, the recent generation of IIAs contains general exceptions provisions that resemble the Article XX

²⁸⁰ *U.S.-Gambling*, *supra* note 269, para. 6.477.

²⁸¹ Appellate Body Report, *United States – Measures Affecting the Cross-Border Supply of Gambling and Betting Services*, WT/DS285/AB/R (Apr. 7, 2005) [hereinafter *U.S. – Gambling Appellate Body Report*].

²⁸² *Id.* para. 311.

²⁸³ *Id.* para. 304.

of the GATT or Article XIV of the GATS.²⁸⁴ The inclusion of WTO/GATS-inspired general exceptions provisions in IIAs first showed up in the 1988 draft Multilateral Agreement on Investment (MAI).²⁸⁵ Despite some observations that the presence of the WTO/GATS-inspired general exceptions provisions in IIAs is not prevalent when taking into account the entire BIT/IIA universe,²⁸⁶ the popularity of these provisions may be observed in the IIAs concluded over the last several years. According to the 2016 World Investment Report, while only 12% of the earlier IIAs concluded from 1962 to 2011 contain such the WTO/GATS-inspired general exceptions

²⁸⁴ Joshua P. Meltzer, *Investment*, in BILATERAL AND REGIONAL TRADE AGREEMENTS: COMMENTARY AND ANALYSIS 245, 296 (Simon Lester et al. eds., 2015). See Roger P. Alford, *The Convergence of International Trade and Investment Arbitration*, 12 SANTA CLARA J. INT'L L. 35, 39 (2013) (explaining that States seek FTAs with investment chapters because the trade part of such agreements enable multinational corporations to access supply chain inputs that are comparatively cheaper while the investment chapter provides investments with specific guarantees like those on non-discriminatory treatment and expropriation).

²⁸⁵ OECD, Negotiating Group on the Multilateral Agreement on Investment, *Multilateral Agreement on Investment Commentary to the Consolidated Text*, DAF/MAI(98)8/REV1 pt. VI, para. 1.3 (Apr. 22, 1998), available at <http://www1.oecd.org/daf/mai/pdf/ng/ng988r1e.pdf> ("The majority view was that the MAI should provide an absolute guarantee that an investor will be compensated for an expropriated investment.").

²⁸⁶ See Andrew Newcombe, *The Use of General Exceptions in IIAs: Increasing Legitimacy or Uncertainty?*, in IMPROVING INTERNATIONAL INVESTMENT AGREEMENTS 267, 279 (Armand de Mestral & Celine Levesque eds., 2013) [hereinafter Newcombe, *Use of General Exceptions in IIAs*] (commenting that most IIAs do not incorporate WTO-like general exceptions provisions and is not representative of a consistent drafting practice of the States); Levent Sabanogullari, *The Merits and Limitations of General Exception Clauses in Contemporary Investment Treaty Practice*, INVESTMENT TREATY NEWS (May 21, 2015), <https://www.iisd.org/itn/2015/05/21/the-merits-and-limitations-of-general-exception-clauses-in-contemporary-investment-treaty-practice/> (commenting that in the current universe of more than 3,200 IIAs, those with general exceptions "still constitute a minority in the ocean").

provision, it appears in 58% of the IIAs concluded from 2012 to 2014.²⁸⁷ Even if the practice is infrequent in BITs, other IIAs particularly in the Asian region such as the Japan-Singapore New Age Economic Partnership Agreement (2003), India-Singapore CECA (2005), Japan-Malaysia Economic Partnership (2005), and Korea-Singapore FTA (2005), tend to require general exceptions clauses in their investment chapters.²⁸⁸

C. Public Order in Human Rights Conventions

Although the intersection between international investment law and human rights is still being explored, it may be insightful to look at two aspects of this intersection between the two institutions. The first area to consider is the public order concept in international human rights jurisprudence. The second area concerns the use of international human rights obligations by respondent States in investor-State arbitrations to justify the challenged measure.²⁸⁹

1. Public Order Concept in International Human Rights

The development of the public order concept in international human rights and under international investment law contains similar issues

²⁸⁷ More than 1,400 IIAs were surveyed. From 2012 to 2014, 40 IIAs were surveyed and from 1962 to 2011, 1,372 IIAs were surveyed. For more detail, see WIR 2016, *supra* note 13, at 114.

²⁸⁸ Japan-Singapore New Age Economic Partnership Agreement, art. 83, Jan. 13, 2002; India-Singapore Comprehensive Economic Cooperation Agreement, art. 6.11, June 29, 2005; Korea-Singapore FTA, art. 21.2, Aug. 4, 2005. See Andrew Newcombe, *General Exceptions in International Investment Agreements*, in SUSTAINABLE DEVELOPMENT IN WORLD INVESTMENT LAW 355, 359 (Marie-Claire C. Segger et al. eds., 2011) [hereinafter Newcombe, *General Exceptions*].

²⁸⁹ See UNCTAD, *Selected Recent Developments in IIA Arbitration and Human Rights*, in IIA MONITOR NO. 2, UNCTAD/WEB/DIAE/IA/2009/7 (United Nations 2009), http://unctad.org/en/Docs/webdiaeia20097_en.pdf.

because, in both fields, “the notion of *public order* or *ordre public* is likewise vague and largely undefined,” but also differ because public order “is often invoked both to limit the enjoyment of human rights in peacetime and to justify their suspension in crisis situations”²⁹⁰ in international human rights while the concept of public order takes on a grander role to give effect to a regulatory measure during periods of crises under international investment law. Despite this fundamental difference, the debates on forming the meaning of public order in international human rights may be relevant in international investment law. For example, public order is not defined in the *travaux préparatoires* to the American Convention on Human Rights (ACHR) although the term is explicitly scattered throughout this treaty.²⁹¹ Under the title “Freedom of Thought and Expression,” Article 13 of the ACHR guarantees that all individuals are entitled to the freedom of thought and expression, but the second paragraph provides a carve-out of the general rule by stating that:

2. The exercise of the right provided for in the foregoing paragraph shall not be subject to prior censorship but shall be subject to subsequent imposition of liability, which shall be expressly established by law to the extent necessary to ensure:
 - a. respect for the rights or reputations of others; or
 - b. the protection of national security, public order,

²⁹⁰ ANNA-LENA SVENSSON-MCCARTHY, *THE INTERNATIONAL LAW OF HUMAN RIGHTS AND STATES OF EXCEPTION: WITH SPECIAL REFERENCE TO THE TRAVAUX PRÉPARATOIRES AND CASE-LAW OF THE INTERNATIONAL MONITORING ORGANS* 148 (Kluwer Law Int’l 1998).

²⁹¹ American Convention on Human Rights, arts. 13(2), 15, 16(2) & 22(3), Nov. 22, 1969, 1144 U.N.T.S. 143 [hereinafter ACHR].

or public health or morals.²⁹²

The scope of Article 13(2) was interpreted narrowly when Costa Rica requested the Inter-American Court of Human Rights to consider whether its domestic measure requiring compulsory membership in a professional association in order to practice journalism in Costa was in violation of Article 13 of the ACHR.²⁹³ The Court interpreted the term “necessary” to require a compelling governmental interest as used in the U.S. Constitutional sense so that “the restrictions must be justified by reference to governmental objectives which, because of their importance, clearly outweigh the social need for the full enjoyment of the right Article 13 guarantees.”²⁹⁴ Practically, this means that a State should pursue the means that least restricts Article 13 of the ACHR.²⁹⁵ When a domestic measure that purports to act in public order has the potential to violate human rights, it “must be subjected to an interpretation that is strictly limited to the ‘just demands’ of ‘a democratic society,’ which takes account of the need to balance the competing interests involved and the need to preserve the object and purpose of the [ACHR].”²⁹⁶

Moreover, the interpretation of “public order” correlates to how the concept legally and culturally exists in a country. Drafting history of various multilateral treaties on human rights reveal the tension among the States that,

²⁹² ACHR art. 13(2).

²⁹³ Compulsory Membership in an Association Prescribed by Law for the Practice of Journalism (Arts. 13 and 28 American Convention on Human Rights), 1985 Inter-Am. Ct. H.R. (ser. A) No. 5, para. 11 (Nov. 13, 1985).

²⁹⁴ *Id.* para. 46.

²⁹⁵ *Id.*

²⁹⁶ *Id.* para. 67.

on one hand, have a clear understanding of the concept of public order, and the States that, on the other hand, argue that public order is vague and elusive. This conflict was especially highlighted between France and the United Kingdom. Under French law, *ordre public* is a general principle of law underlying a democratic society that includes public order in the criminal law sense but also “aspects of a nation’s democratic legal order including a state’s international legal commitments”²⁹⁷ while public order can be basically met by any State reason and is more broadly perceived in the United Kingdom. For example, when Article 29(2) of the Universal Declaration of Human Rights (UDHR) was being drafted, countries expressed diverse views over the use of specific terms like “public order,” “general welfare,” and “democratic society” as shown below:

(2) In the exercise of his rights and freedoms, everyone shall be subject only to such limitations as are determined by law solely for the purpose of securing due recognition and respect for the rights and freedoms of others and of meeting the just requirements of morality, public order and the general welfare in a democratic society.²⁹⁸

The drafting history of Article 29(2) of the UDHR shows that Uruguay had opposed the use of the term “public order” due to a lack of clarity that could lead States to act arbitrarily and Australia wanted to omit the term “public”

²⁹⁷ SVENSSON-MCCARTHY, *supra* note 290, at 165.

²⁹⁸ Universal Declaration of Human Rights, G.A. Res. 217A, at 71, U.N. GAOR, 3d Sess., 1st plen. mtg., U.N. Doc A/810 (Dec. 10, 1948). The general rule set forth in paragraph 1 of Article 29 of the UDHR provides that “[e]veryone has duties to the community in which alone the free and full development of his personality is possible.”

to use the word “order” for the same fear that countries will be tempted to enact arbitrary measures.²⁹⁹ However, France persuaded the drafters to include the term “public order” in Article 29(2). France argued that including the term “public order” was imperative because the term “order” (without the word “public” preceding it) and the term “general welfare” were familiar to English law, but foreign to French law which would render it untranslatable.³⁰⁰ France did not dismiss the concerns raised by the other countries. By pairing the term “public order” with the phrase “in a democratic society,” France addressed the concern related to arbitrariness so that other suggestions like the expression “security for all” would be dropped to make way for the term “public order.”³⁰¹ In a subsequent discussion over the use of the term “public order” in Article 29(2), the issue was raised again when the Third Committee of the General Assembly protested over the words “morality” and “public order.”³⁰² However, France explained that the concept of “general welfare” was too vague and broad as understood in English law whereas the French understanding of *bien-être général* was used much more narrowly usually in the economic and social context.³⁰³ France believed that the concept of public order included

²⁹⁹ Comm’n on Human Rights, 3d. Sess., 74th mtg. at 12, U.N. Doc. E/CN.4/SR.74 (June 15, 1948).

³⁰⁰ *Id.* at 12-13.

³⁰¹ *Id.* at 12, 15.

³⁰² U.N. GAOR, 3d Sess., 3d Comm., 153d mtg. at 645-46, U.N. Doc. A/C.3/SR.153 (Nov. 23, 1948).

³⁰³ U.N. GAOR, 3d Sess., 3d Comm., 154th mtg. at 652-53, U.N. Doc. A/C.3/SR.154 (Nov. 24, 1948) [hereinafter U.N. GAOR, 154th mtg.].

“anything essential to the life of a country including primarily, its security,”³⁰⁴ and when used in conjunction with the words “morality, “public order,” and “general welfare,” fulfilled the democratic demands of a State.³⁰⁵ In essence, the complementary expression for “general welfare” in France’s mind was contained in the terms “public order.”

Although the United Kingdom was not vocal during discussion of the term “general welfare” when Article 29(2) of the UDHR was being drafted, it adopted a more outward stance during the drafting of Article 18(3) of the International Covenant on Civil and Political Right (ICCPR) when it proposed to use the expression “for the prevention of disorder” to avoid the use of the term “order,” which has roots in French law and is foreign to Anglo-Saxon jurisprudence.³⁰⁶ Unlike Article 18(3) of the ICCPR which uses the single term “order,” Article 19 in paragraph 3(b) refers to both the translated and French terms of “public order” and *ordre public* to provide an exception to the general rule on the freedom of expression and information.³⁰⁷ Unlike the United Kingdom which refused the term “public order” for fear of inviting inappropriately broad interpretations that may

³⁰⁴ SVENSSON-MCCARTHY, *supra* note 290, at 151.

³⁰⁵ U.N. GAOR, 154th mtg., *supra* note 303, at 653 (“all the demands of the democratic State were taken into account”).

³⁰⁶ International Covenant on Civil and Political Rights, G.A. Res. 2200A (XXI), art. 18.3, 21 U.N. GAOR Supp. (No. 16) at 52, U.N. Doc A/6316 (Dec. 16, 1966) [hereinafter ICCPR] (“Freedom to manifest one’s religion or beliefs may be subject only to such limitations as are prescribed by law and are necessary to protect safety, order, health, or morals or the fundamental rights and freedoms of others.”).

³⁰⁷ ICCPR art. 19.3(b) (“For the protection of national security or of public order (ordre public), or of public health or morals.”).

reverse the exception into the norm, the United States' version, "of national security, public order, safety, health or morals," was unanimously adopted including by France.³⁰⁸ In another interesting example, the drafters of the International Covenant on Economic, Social and Cultural Rights (ICESCR) debated on whether the public order concept should be dually applied in the limitation clause of Article 4³⁰⁹ when it appears elsewhere for use in the context of a specific article in Article 8.³¹⁰ The conclusion was that the term "public order" ought not to appear as a general exception and was therefore barred from reaching into Article 4. Not all countries agreed with this outcome, however, with France particularly arguing that there was "an absolute necessity for harmonizing the rights of the individual on the one hand and the requirements of the community on the other."³¹¹ But others like China and Egypt questioned the relevance of permitting the concept of

³⁰⁸ See Comm'n on Human Rights, 6th Sess., 167th mtg. at 6, para. 22, U.N. Doc. E/CN.4/SR.167 (Apr. 24, 1950).

³⁰⁹ International Covenant on Economic, Social and Cultural Rights, G.A. Res. 2200A (XXI), 21 U.N. GAOR Supp. (No. 16) at 49, U.N. Doc. A/6316 (Dec. 16, 1966) [hereinafter ICESCR]. Article 4 of the ICESCR states the following:

The States Parties to the present Covenant recognize that, in the enjoyment of those rights provided by the State in conformity with the present Covenant, the State may subject such rights only to such limitations as are determined by law only in so far as this may be compatible with the nature of these rights and solely for the purpose of promoting the general welfare in a democratic society.

³¹⁰ ICESCR art. 8 (allowing a limitation to be placed on the rights of individuals to form and join trade unions if necessary "in the interests of national security or public order or for the protection of the rights and freedoms of other").

³¹¹ See U.N. GAOR, 10th Sess., annexes (Agenda Item 28, Pt. II) at 25, para. 51, U.N. Doc. A/2929 (July 1, 1955).

public order to spill over into Article 4 because such an open application would lead to broad interpretations that “might easily nullify the whole concept of self-determination.”³¹²

Even if the public order clause is included in the human rights treaties, some balance must be found nonetheless to allow States to implement domestic measures that protect public order without defeating the purpose of the agreement. The Siracusa Principles were established to provide interpretative guidelines on certain limitation clauses in the above-mentioned ICCPR including “public order (*ordre public*)” in Article I.B.iii:

22. The expression “public order (*ordre public*)” as used in the Covenant may be defined as the sum of rules which ensure the functioning of society or the set of fundamental principles on which society is founded. Respect for human rights is part of public order (*ordre public*).

23. Public order (*ordre public*) shall be interpreted in the context of the purpose of the particular human right which is limited on this ground.

24. State organs or agents responsible for the maintenance of public order (*ordre public*) shall be subject to controls in the exercise of their power through the parliament, courts, or other competent independent bodies.³¹³

³¹² *Id.* at 25, para 52. For China and Egypt’s stance, see JAMES C. HATHAWAY, *THE RIGHTS OF REFUGEES UNDER INTERNATIONAL LAW* 579 (Cambridge Univ. Press 2005).

³¹³ U.N. Econ. & Soc. Council, *Siracusa Principles on the Limitation and Derogation Provisions in the International Covenant on Civil and Political Rights*, annex at 4, U.N. Doc. E/CN.4/1985/4 (Sep. 28, 1984).

The above illustrations reveal that the core of the debate on public order turns on whether to give it a narrow, restrictive meaning or grant a broad interpretation. A narrow meaning of public order would make the concept closer to public security and the “prevention of disorder,”³¹⁴ restricting the use of this limitation clause to permissible situations such as in Articles 30 and 39 of the EC Treaty without further consideration that extends beyond this finite scope. However, a broad interpretation would make the concept of public order akin to general welfare and consistent with the French legal understanding of *ordre public*. Professor Roel de Lange observes that even within a single treaty, the concept of public order is not firmly set in stone and that the degree of interpretation varies according to the article in question. For example, public order in Articles 30 and 39 of the EC Treaty are given a restrictive interpretation whereas Articles 81 and 82 of the same treaty have a special public order status, which is essentially a broad application of the concept of public order.³¹⁵ Article 81 forbids agreements and practices aimed at restricting competition and Article 82 prohibits abuses by a dominant position within the common market, but

³¹⁴ European Convention on Human Rights, art. 8, Nov. 4, 1950, 213 U.N.T.S. 221 [hereinafter ECHR]. Article 8 of the ECHR omits the expression “public order” as seen below:

2. There shall be no interference by a public authority with the exercise of this right except such as is in accordance with the law and is necessary in a democratic society in the interests of national security, public safety or the economic wellbeing of the country, for the prevention of disorder or crime, for the protection of health or morals, or for the protection of the rights and freedoms of others.

³¹⁵ Roel de Lange, *The European Public Order, Constitutional Principles and Fundamental Rights*, 1 ERASMUS L.R. 1, 9 (2007).

even these safeguarding provisions can be overridden for public order reasons creating a host of foreseeable and unforeseeable problems.³¹⁶

2. Raising the Human Rights Defense in IIAs

Human rights implications may arise in investor-State arbitrations. For instance, Argentina claimed in the *CMS* case that no investment treaty could prevail given the “economic and social crisis that affected the country compromised basic human rights.”³¹⁷ However, the *CMS* tribunal rejected Argentina’s human rights defense.³¹⁸ In *Sempra Energy International v. Argentina*, Argentina attempted to defend its emergency measure using its human rights obligations in the Inter-American Convention. When Argentina’s counsel questioned Professor Reisman, expert witness for the claimant, “[W]ould Argentina have been compelled because of the Inter-American Convention to maintain its constitutional order towards the end of 2001, 2002, and afterwards?” he stated, “Yes.”³¹⁹ Although the *Sempra* tribunal declared that Argentina’s constitutional order and basic human rights and liberties were not endangered due to the economic crisis,³²⁰ the significance of this exchange highlights that a respondent State is bound to its obligations arising out of IIAs and human rights conventions, and more broadly, to the obligations set forth under other competing areas of public

³¹⁶ *Id.*

³¹⁷ *CMS v. Argentina*, *supra* note 179, para. 114.

³¹⁸ *Id.* para. 121.

³¹⁹ *Sempra v. Argentina*, *supra* note 179, para. 331.

³²⁰ *Id.* para. 332.

international law.³²¹ An expert witness in another ICSID case against Argentina stated that “[n]o arbitration on the protection of investments may overlook the fact that one of the parties to the dispute is the State which cannot set aside the issues relating to public law affected by such negotiation, and this includes human rights issues.”³²² In *Suez/Vivendi v. Argentina*, Argentina tried to justify its investment treaty breach by arguing that it has a human rights obligation to let its people exercise their right to water. The *Suez/Vivendi* tribunal was not persuaded since Argentina is equally bound under international law to both human rights and treaty obligations and, to this extent, it declared that “Argentina’s human rights obligations and its investment treaty obligations are not inconsistent, contradictory, or mutually exclusive.”³²³ However, it should also be pointed out that Argentina’s reliance on human rights may have been due to the fact that the public order carve-out (or another variation of a NPM provision) did not exist in any of the three underlying BITs (*i.e.*, the Argentina-France BIT, the Argentina-Spain BIT, and the Argentina-United Kingdom BIT).

Moreover, States may explicitly provide for the recognition of human rights in IIAs but its scope varies. Whereas the draft 2015 India Model BIT originally stipulated that “Investors and their Investments shall be subject to and comply with the Law of the Host State [which] includes, but is not

³²¹ Susan L. Karamanian, *Human Rights Dimension of Investment Law*, in *HIERARCHY IN INTERNATIONAL LAW: THE PLACE OF HUMAN RIGHTS* 236, 259 (Erika de Wet & Jure Vidmar eds., 2012).

³²² *Id.* (quoting expert witness Professor Monica Pinto in *Impregilo v. Argentina*, ICSID Case No. ARB/07/17, Supplemental Expert Report, para. 7 (Jan. 5, 2010)).

³²³ *Suez/Vivendi*, Decision on Liability, *supra* note 163, para. 262.

limited to... [the] law relating to human rights,”³²⁴ the final text of the 2016 India BIT eliminates the provision by stating that:

Investors and their enterprises operating within its territory of each Party shall endeavour to voluntarily incorporate internationally recognized standards of corporate social responsibility in their practices and internal policies, such as statements of principle that have been endorsed or are supported by the Parties. These principles may address issues such as labour, the environment, human rights, community relations and anti-corruption.³²⁵

Despite the loss of mandatory language in the 2016 India Model BIT regarding the application of human rights, the truth is that IIAs usually do not provide explicit provisions on human rights. The 2015 Norway Model BIT explicitly recognizes the duty of the contracting States to observe human rights principles by stating the following in the preamble:

Reaffirming their commitment to democracy, the rule of law, human rights and fundamental freedoms in accordance with their obligations under international law, including the principles set out in the United Nations Charter and the Universal Declaration of Human Rights [...].³²⁶

³²⁴ India Model BIT (2015), art. 12.1(v) [“Compliance with Law of Host State”], *available at* https://www.mygov.in/sites/default/files/master_image/Model%20Text%20for%20the%20Indian%20Bilateral%20Investment%20Treaty.pdf.

³²⁵ India Model BIT (2016), art. 12 [“Corporate Social Responsibility”], *available at* http://finmin.nic.in/reports/ModelTextIndia_BIT.pdf.

³²⁶ Norway Model BIT, preamble (2015).

It additionally empowers the joint committee to discuss human rights issues whenever necessary.³²⁷ The 2004 Canada Model FIPA and the 2012 U.S. Model BIT, however, do not address human rights. The investment chapters of the TPP, EU-Vietnam FTA, and Canada-EU CETA as well as the proposed TTIP, to name just a few, also do not contain human rights provisions.

Even in the area of international human rights, the concept of public order is not absolute or universal and is “a function of time, place, and circumstances.”³²⁸ Some investor-State tribunals refer to human rights jurisprudence for guidance on IIA terms like “expropriation” or “nationalization” because investment treaties usually do not define such property-depriving terms and may indirectly affect the public order carve-out. However, it must also be underscored that IIAs fundamentally differ from international human rights treaties. Although human rights obligations in IIAs may provide a ground for lawful State measures,³²⁹ human rights conventions are not based on reciprocity or contractual terms and, therefore, the concept of public order in IIAs may contain a different objective than in international human rights.³³⁰

³²⁷ *Id.* art. 23.3.viii.

³²⁸ SVENSSON-MCCARTHY, *supra* note 290, at 166.

³²⁹ Patrick Dumberry & Gabrielle Duman Aubin, *How to Incorporate Human Rights Obligations in Bilateral Investment Treaties?*, INVESTMENT TREATY NEWS (Mar. 22, 2013), <https://www.iisd.org/itn/2013/03/22/how-to-incorporate-human-rights-obligations-in-bilateral-investment-treaties/>. See also LUKE E. PETERSON & KEVIN R. GRAY, IISD, INTERNATIONAL HUMAN RIGHTS IN BILATERAL INVESTMENT TREATIES AND IN INVESTMENT TREATY ARBITRATION (2005), https://www.iisd.org/pdf/2003/investment_int_human_rights_bits.pdf.

³³⁰ DIANE A. DESIERTO, NECESSITY AND NATIONAL EMERGENCY CLAUSES: SOVEREIGNTY IN MODERN TREATY INTERPRETATION, 272-73 (Martinus Nijhoff

III. The Customary International Law Source of the Public Order Concept

Another area of the public order concept that should be explored is whether it can be pinned to customary international law. This is actually a complicated, multi-layered question because the ILC Articles on State Responsibility (as a codification of customary international law) do not explicitly include the public order concept.³³¹ The early Argentine ICSID tribunals of *CMS*, *Enron*, and *Sempra* were given the interpretative task of the public order carve-out in Article XI of the U.S.-Argentina BIT, but seemed to have inferred from the “necessary to maintain public order” language to conclude that the public order carve-out should be interpreted under the necessity doctrine of customary international law.³³² A strong reason for this connection between the BIT public order carve-out and the customary international law necessity defense may have come from the ICSID tribunals’ acceptance of the respondent State’s defense that the regulatory act should be excluded under customary international law and/or the BIT. In fact, this

2012).

³³¹ See, e.g., Jorge E. Viñuales, *State of Necessity and Peremptory Norms in International Investment Law*, 14 *LAW & BUS. REV. AMS.* 79-80 (2008). Cf. Robert D. Sloane, *On the Use and Abuse of Necessity in the Law of State Responsibility*, 106 *AM. J. INT’L L.* 447, 452-53, 498 (2012) (arguing that ILC art. 25 should not be seen as the equivalent to the necessity doctrine under customary international law).

³³² Further discussed in ch. 4 of this Dissertation.

is how Argentina formed its defense argument in *CMS*,³³³ *Enron*,³³⁴ *Sempre*,³³⁵ *LG&E*,³³⁶ and *Continental Casualty*.³³⁷ However, was it legally convincing to treat the customary defense on necessity as providing the elements to the treaty-based public order carve-out? This is addressed in greater detail in Chapter 4, but a discussion of the necessity defense under customary international law and its historical flow may provide some insight on whether the rigidity of the necessity defense ought to be maintained as an increasing number of IIAs contain exceptions like the public order carve-out.

The early doctrine of necessity was connected to a State's right to self-preservation meaning that a State threatened with self-preservation had the right to take any steps necessary to maintain its existence even if such an act would result in a breach of international law. Hugo Grotius, considered to be the "Father of International Law," recognized that wartime demands may compel any one power to take control of neutral territory, an act that would be justified under the right of necessity.³³⁸ However, Grotius also emphasized that invoking the right of necessity had to be based on a real belief that the other power would do the same.³³⁹ The occupying power was

³³³ *CMS v. Argentina*, *supra* note 179, para. 99.

³³⁴ *Enron v. Argentina*, *supra* note 179, para. 93.

³³⁵ *Sempre v. Argentina*, *supra* note 179, para. 98.

³³⁶ *LG&E v. Argentina*, *supra* note 179, para. 202.

³³⁷ *Continental Casualty v. Argentina*, *supra* note 179, para. 88.

³³⁸ HUGO GROTIUS, *ON THE LAW OF WAR AND PEACE* 80 (A.C. Campbell 2001) (1901).

³³⁹ *Id.*

to take the least amount of land as possible to avoid burdening the real owner from enjoying and using the soil.³⁴⁰ Perhaps most importantly, Grotius wrote that the occupying power act with the intention that the neutral soil will be restored to its lawful owners once the state of necessity stops.³⁴¹ This last point is reiterated when Grotius emphasizes that “under the plea of necessity... nothing short of extreme exigency can give one power a right over what belongs to another no way involved in the war” and that “no emergency can justify any one in taking and applying to his own use what the owner stands in equal need of himself.”³⁴² Furthermore, “even where the emergency can be plainly proved, nothing can justify... taking or applying the property of [the neutral sovereign], beyond the *immediate demands of that* emergency” because the “*use and consumption* of [the neutral territory has been] absolutely unlawful.³⁴³ Consequently, when the period of necessity ends, the occupied territory must be returned to its sovereign³⁴⁴ with payment of full value for the difference in condition.³⁴⁵

With Grotius’s work serving as one of several doctrinal foundations to the law of necessity, Burleigh Cushing Rodick who authored a widely cited treatise on necessity in international law extracted the following stipulations common to the concept of necessity:

³⁴⁰ *Id.*

³⁴¹ *Id.*

³⁴² *Id.* at 336.

³⁴³ *Id.*

³⁴⁴ *Id.* at 80.

³⁴⁵ *Id.* at 336.

1. There must be an absence of *mens rea* on the part of one who exercises the alleged right.
2. There must be a real and vital danger, either to life, or to property.
3. The danger must be imminent in point of time.
4. In seizing the property of neutrals the amount seized should be no greater than is necessary for the particular object in view.
5. Consideration must be given to the equities involved...
6. The person who has exercised the right is bound whenever possible to make restitution or given an equivalent to the owner.³⁴⁶

With Rodick and early international law scholars of the nineteenth century unequivocally assuming that a State's fundamental rights included the right of self-preservation and existence, acts based on necessity also became a right that States could resort to when defending themselves.³⁴⁷ This, of course, begs the question of whose right of self-preservation to uphold when a dispute between States occur.³⁴⁸ Modern international law addresses this conflict, to some extent, by employing the broader concept of "essential interests" to refashion the traditional idea that self-preservation is not a right,

³⁴⁶ BURLEIGH CUSHING RODICK, *THE DOCTRINE OF NECESSITY IN INTERNATIONAL LAW* 6 (Columbia Univ. Press 1928).

³⁴⁷ See Roman Boed, *State of Necessity as a Justification for Internationally Wrongful Conduct*, 3 *YALE HUM. RTS. & DEV. L.J.* 1, 6 (2000) (citing Amos S. Hershey and Charles G. Fenwick who emphasize the right of self-preservation as the fundamental right of States); Sloane, *supra* note 331, at 455.

³⁴⁸ *Id.*

but one of several essential interests that a State may protect even in the face of a breach of an international commitment.³⁴⁹

In the 1970s, ILC Special Rapporteur Roberto Ago examined the international law concept of necessity by surveying the practice of international adjudicative bodies and his seminal work, which laid the groundwork for draft Article 33 to later become Article 25 of the ILC on State Responsibility, not only rejected the theory of fundamental rights of States but also believed that the idea of a right of self-preservation distorted contemporary international legal reality.³⁵⁰ Moreover, in declaring that “the idea of a subjective right of necessity... is absolute nonsense today,” Ago rejected necessity as a State’s right and instead argued that the concept of necessity ought to be understood as an excuse.³⁵¹ In other words, when necessity is exercised as a right, the State declaring such a right would be granted a legal claim against the other State.³⁵² But when necessity is invoked as an excuse, the acting State implicitly acknowledges the

³⁴⁹ *Id.* at 6-7.

³⁵⁰ ILC, ADDENDUM – EIGHTH REPORT ON STATE RESPONSIBILITY BY MR. ROBERTO AGO, SPECIAL RAPPORTEUR – THE INTERNATIONALLY WRONGFUL ACT OF THE STATE, SOURCE OF INTERNATIONAL RESPONSIBILITY (PT. 1), para. 7, at 16, U.N. Doc. A/CN.4/318/Add.5-7 (1980) [hereinafter AGO REPORT], available at http://legal.un.org/ilc/documentation/english/a_cn4_318_add5_7.pdf.

³⁵¹ *Id.* para. 9, at 18. Cf. Not all scholars agree with the excuse concept. JAN KITTRICH, THE RIGHT OF INDIVIDUAL SELF-DEFENSE IN PUBLIC INTERNATIONAL LAW 46 (2008) (“After the adoption of the Draft Articles in 1980, some members of the international community disapproved of the [ILC’s] notion of the criterion *essential interest* [sic]. According to some nations its meaning was too vague as to invite potential abuse and to cause more problems.”).

³⁵² AGO REPORT, *supra* note 350, para. 9, at 18.

legitimacy of whatever is being denied to the other side.³⁵³

Support for the position that necessity is not a fundamental State right is available in early international law cases. In *The Neptune*, the owners of an American vessel company complained before an arbitral commission established under the Jay Treaty that Britain, then at war with France, had seized its vessel stocked with foodstuffs *en route* to France and that a British court compelled the cargo goods to be sold to the British government at a lesser value than the vessel company would have received had the vessel arrived at its proper destination.³⁵⁴ However, Britain claimed that it paid what was due, that is, the invoice price and a 10 percent profit, and did not owe any additional difference based on what the American vessel company would have received had it reached the French port. Although Britain argued that it seized a third-party vessel due to a food shortage in Britain, a few of the arbitral commissioners concluded that Britain was not entitled to rely on necessity to justify its act. American commissioner Mr. Pinkney was of the following opinion:

I shall not deny that *extreme necessity* may justify such a measure [the seizure of food supplies owned by a neutral party]. It is only important to ascertain whether that *extreme necessity* existed on this occasion and upon what terms the right it communicated might be carried into exercise.

³⁵³ *Id.* See also Boed, *supra* note 347, at 7, n. 24.

³⁵⁴ *The Neptune*, reprinted in J.B. MOORE, 4 INTERNATIONAL ADJUDICATIONS: MODERN SERIES 372 (John Bassett Moore ed., 1931) (judgment made in 1797) [hereinafter, MOORE, INTERNATIONAL ADJUDICATIONS]. For more accounts of this case, see AGO REPORT, *supra* note 350, para. 48, at 34.

We are told by Grotius that the necessity must not be imaginary, that it must be real and pressing, and that even then it does not give a right of appropriating the goods of others until all other means of relief consistent with the necessity have been tried and found inadequate.³⁵⁵

Mr. Gore, another American commissioner, similarly held that the facts did not warrant a legitimate reliance on necessity from Grotius's perspective:

[T]he necessity must be really extreme to give any right to another's goods; second, that it should be requisite that there should not be the like necessity in the owner; third, when absolute necessity urges us to take, we should then take no more than it requires.³⁵⁶

Likewise, American Commissioner Mr. Trumbull questioned whether Britain was under a "pressing" need at the time of the capture such that its act would be justified by necessity, but found that:

The necessity which can be admitted to supersede all laws and to dissolve the distinctions of property and right must be absolute and irresistible, and we cannot, until all other means of self-preservation shall have been exhausted, justify by the plea of necessity the seizure and application to our own use of that which belongs to others.³⁵⁷

³⁵⁵ AGO REPORT, *supra* note 350, para. 48, at 34 (quoting MOORE, INTERNATIONAL ADJUDICATIONS, *supra* note 357, at 398-99).

³⁵⁶ Quote reprinted in J.B. MOORE, 4 HISTORY AND DIGEST OF THE INTERNATIONAL ARBITRATIONS TO WHICH THE UNITED STATES HAS BEEN A PARTY 3843-3885 (U.S. Gov't Printing Office, 1898).

³⁵⁷ Quote reprinted in BIN CHENG, GENERAL PRINCIPLES OF LAW AS APPLIED BY

At the time *The Neptune* was decided, necessity was an unquestioned right linked to the preservation of a State's existence, but Professor Bin Cheng identified in his widely regarded 1953 publication several elements from *The Neptune* case coherently considered in modern international arbitration practice:

1. When the existence of a State is in peril, the necessity of self-preservation may be a good defence for certain acts which would otherwise be unlawful.
2. This necessity 'supersedes all laws,' 'dissolves the distinctions of property and rights' and justifies the 'seizure and application to our own use of that which belongs to others.'
3. This necessity must be 'absolute' in that the very existence of the State is in peril.
4. This necessity must be 'irresistible' in that all legitimate means of self-preservation have been exhausted and proved to be of no avail.
5. This necessity must be actual and not merely apprehended.
6. Whether or not the above conditions are fulfilled in a given case, is a property subject of judicial inquiry. If they are not, the act will be regarded as unlawful and damages

INTERNATIONAL COURTS AND TRIBUNALS 70 (Cambridge Univ. Press 2006) (1953).

will be assessed in accordance with principles governing reparation for unlawful acts.³⁵⁸

The modern trend has been to widen the scope of necessity to include essential interests other than preservation of a State's existence as observed by Ago in the *Torrey Canyon* incident.³⁵⁹ The *Torrey Canyon*, operating under the Liberian flag, was an American-owned supertanker carrying 117,000 tons of crude oil. When the tanker was aground off the coast of Cornwall but outside British territorial waters, the oil began to leak (going down in history as one of the massive oil spill accidents) and, in a short period of time, began to threaten the wildlife and population off the southwestern coast of England.³⁶⁰ To be fair, no one possessed the expertise to deal with this first-of-a-kind crisis.³⁶¹ With 30,000 tons of oil already contaminating the sea, followed up with impending fear that the remaining cargo would also makes

³⁵⁸ *Id.* at 71.

³⁵⁹ AGO REPORT, *supra* note 350, para. 35, at 28 (“A case which occurred in our own times and which may be regarded as typical from the standpoint of fulfilment of the conditions we consider essential in order for the existence of a ‘state of necessity’ to be recognized is the ‘*Torrey Canyon*’ incident.”). *But cf.* Sloane, *supra* note 331, at 455 (disagreeing with Special Rapporteur Roberto Ago’s emphatic view that “the concepts of self-preservation and state of necessity are in no way identical, nor are they indissolubly linked in the sense that one is merely the basis and justification of the other”).

³⁶⁰ See Albert E. Utton, *Protective Measures and the “Torrey Canyon”*, 9 B.C.L. REV. 613 (1968) (providing an overview of the *Torrey Canyon* incident); AGO REPORT, *supra* note 350, para. 35, at 28 (describing the *Torrey Canyon* case to analyze the concept of “state of necessity”); Patrick Barkham, *Oil Spills: Legacy of the Torrey Canyon*, GUARDIAN (June 24, 2010), <http://www.theguardian.com/environment/2010/jun/24/torrey-canyon-oil-spill-deepwater-bp> (stating the aftermaths of the *Torrey Canyon* incident on the present environment).

³⁶¹ See AGO REPORT, *supra* note 350, para. 35, at 28.

its way into the sea, the British Government employed a salvage firm to refloat the tanker.³⁶² However, the salvage attempt was a disastrous failure that led to the breaking of the tanker and spilling the oil into the waters.³⁶³ Not left with much choice, the British Government burned the oil by bombing the *Torrey Canyon* and no one, including the shipowner or the Governments of the parties concerned, protested to Britain's handling of the crisis.³⁶⁴ Although the shipowner had implicitly abandoned the *Torrey Canyon*, the British Government planned to proceed with the bombing at all costs – regardless of the wishes of the shipowner – without providing any legal justification for its act.³⁶⁵ Ago remarked that “even if the shipowner had not abandoned the wreck, and even if he had tried to oppose its destruction, the action taken by the British Government outside the areas subject to its jurisdiction would have had to be recognized as internationally lawful, since the conditions for a ‘state of necessity’ were clearly fulfilled” as exemplified by the fact that Britain's decision to bomb came only after the exhaustion of all other methods.³⁶⁶ This observation was again affirmed by the ILC drafters of Draft Article 33 (Commentary) and also recognized a departure from the traditional concept that necessity was inextricably linked to the self-preservation and existence of a State.³⁶⁷

³⁶² *Id.*

³⁶³ *Id.*

³⁶⁴ *Id.*

³⁶⁵ *Id.*

³⁶⁶ *Id.*

³⁶⁷ ILC, Draft Articles on Responsibility of States for Internationally Wrongful Acts with Commentaries, art. 33, at 94 (2008) [hereinafter State Responsibility Draft with

The shift of the modern understanding of necessity towards the essential interest concept of necessity rather than the notion of self-preservation was affirmed in an international dispute between Hungary and Czechoslovakia (later Slovakia) in 1997 by the International Court of Justice.³⁶⁸ Czechoslovakia brought a claim against Hungary in the *Gabcikovo-Nagymaros Case* twelve years after both countries had signed a treaty agreeing to construct dams that would produce electricity, improve watercourse, and protect against flooding along the Danube River which bordered both nations.³⁶⁹ Hungary sought to temporarily abandon parts of the project due to financial hardship and environmental concerns which were intensified by negative public attention.³⁷⁰ When the two countries failed to reach a new agreement addressing these growing concerns, Czechoslovakia retaliated by engaging in a river diversion that extracted most of the water from the riverbed and dropped the overall water level. This tumultuous event would have escalated into a violent international

Commentaries], available at http://untreaty.un.org/ilc/texts/instruments/english/commentaries/9_6_2001.pdf. See also Boed, *supra* note 347, at 11.

³⁶⁸ *Gabčíkovo-Nagymaros Project (Hungary v. Slovakia)*, 1997 I.C.J. 7, 36-46, paras. 49-58 (Sep. 25) [hereinafter *Gabčíkovo-Nagymaros Project*]. See Aaron Schwabach, *Diverting the Danube: The Gabčíkovo-Nagymaros Dispute and International Freshwater Law*, 14 BERKELEY J. INT'L L. 290 (1996) (providing background information to the *Gabčíkovo-Nagymaros* dispute). See generally Heiko Fürst, *The Hungarian-Slovakian Conflict over the Gabčíkovo-Nagymaros Dams: An Analysis*, INST. FOR PEACE RES. & SECURITY POL'Y, <http://www.columbia.edu/cu/ece/research/intermarium/vol6no2/furst3.pdf> (explaining the conflict between Hungary and Czechoslovakia).

³⁶⁹ *Gabčíkovo-Nagymaros Project*, *supra* note 368, paras. 15-20.

³⁷⁰ *Id.* paras. 22-40 (describing the Hungarian claim of state of ecological necessity in justification of abandoning the project); Fürst, *supra* note 368, at 2.

conflict had the European Community not intervened.³⁷¹ Hungary's main argument was that its breach of treaty was justifiable due to ecological necessity.³⁷²

This case is significant because even though the ICJ found that Hungary had not satisfied the conditions to establish necessity, the Court accepted the underlying premise that a breaching State may take acts to respond to a threat of environmental catastrophe and that it may be excused if necessity can be validly established.³⁷³ Additionally, by accepting the existence of a state of necessity defense in customary international law,³⁷⁴ the ICJ contributed to establishing a linkage between the concept of necessity and the Draft Article 33 (the equivalent to Article 25) of the ILC to permit a state of necessity as a ground for precluding wrongdoing by a State in breach of its international obligations:

The [ICJ] considers, first of all, that the state of necessity is a ground recognized by customary international law for precluding the wrongfulness of an act not in conformity with an international obligation. It observes moreover that such ground for precluding wrongfulness can only be accepted on an exceptional basis. The International Law Commission was of the same opinion when it explained that it had opted for a

³⁷¹ Fürst, *supra* note 368, at 2-3.

³⁷² Gabčíkovo-Nagymaros Project, *supra* note 368, para. 40.

³⁷³ *Id.* para. 57; Boed, *supra* note 347, at 12.

³⁷⁴ See Michael Waibel, *Two Worlds of Necessity in ICSID Arbitration: CMS and LG&E*, 20 LEIDEN J. INT'L L. 637 (2007) ("Necessity as a circumstance precluding state responsibility has long-standing roots in customary international law.").

negative form of words in Article 33 of its Draft...³⁷⁵

Thus, the modern day concept of necessity is no longer narrowly limited to the preservation and existence of a State, but opens up the possibility that a State may be excused from international breach when an essential state interests is in grave and imminent peril. The application of the customary international law defense of necessity as reflected in ILC Article 25 in the Argentine ICSID cases is further discussed in Chapter 4 of this Dissertation.

IV. Concluding Remarks

Chapter 2 aimed to highlight the polysemic nature of the term “public order” and laid out the multiple meanings of public order. Understanding the treatment of the public order concept at the national and international level is an important step that helps us to gain insight on how the public order concept emerged in international investment law. First and foremost, the legal traditions of a country and its formation of the concept of public order will dictate how the term “public order” is used. Anglo-Saxon countries with common law backgrounds better recognize the term “public policy” rather than “public order,” while civil law countries such France, Italy, and Spain prefer the French expression “*ordre public*” (public order).³⁷⁶

³⁷⁵ Gabčíkovo-Nagymaros Project, *supra* note 368, para. 51. See Massimiliano Montini, *The Necessity Principle as an Instrument to Balance Trade and the Protection of the Environment*, in ENVIRONMENT, HUMAN RIGHTS & INTERNATIONAL TRADE 135, 139 (Francesco Francioni ed., 2001) (“The most important instrument in which the concept of necessity as a general principle of international law has crystallized in contemporary international law is the instrument of the *state of necessity*, as defined by the International Law Commission [.]”).

³⁷⁶ See generally Murphy, *supra* note 172 (discussing the origins of public policy and *ordre public*); Habicht, *supra* note 172 (reflecting the concern of early legal scholars that “[o]ne of the most controversial rules of private international law is the

The use of one term over another may affect the scope and standard of review when the public order carve-out is invoked. Under public international law, which regulates relations between States and non-State actors including international organizations, multinational corporations, and individuals,³⁷⁷ a coherent and consolidated meaning of public order also does not exist amongst multilateral agreements and they typically do not provide an explicit definition or an enumerated list of what kinds of acts would be for the maintenance of public order. The scope of public order may be broad so as to include public health, but an overly broad interpretation of public order that categorically includes measures relating to the economy or protection of culture may be problematic.³⁷⁸ In both older and recent investment treaty practice, the term “public order” has appeared in

exception of public order” and also briefly noting the different expressions used to describe the term “public policy” such as “public order” and “*ordre public*”); Kessedjian, *supra* note 241, at 26 (admitting that “[t]o this date it is unclear to me whether there is a difference in content or method between the concepts in French law and in English law or common law”).

³⁷⁷ MARTIN DIXON, TEXTBOOK ON INTERNATIONAL LAW 4 (Oxford Univ. Press 2013).

³⁷⁸ OECD, INTERNATIONAL INVESTMENT PERSPECTIVES: FREEDOM OF INVESTMENT IN A CHANGING WORLD 110 (2007) [hereinafter OECD, ESSENTIAL SECURITY INTERESTS], *available at* <https://www.oecd.org/investment/internationalinvestmentagreements/40243411.pdf>.

conjunction with the terms “public health,”³⁷⁹ “public morals or morality,”³⁸⁰ or “decency”³⁸¹ and the phrases “reason of public order, national security or sound development of national economy”³⁸² or the “maintenance of defence, national security and public order, protection of the environment, morality and public health.”³⁸³ As a next step, Chapter 3 specifically considers the States’ treatment of the public order carve-out in IIA practice by examining its textual transformations to reveal a drafting practice that seems to prefer

³⁷⁹ E.g., Israel-Germany BIT, Protocol, para. 2, June 24, 1976 (“Measures that have to be taken for reasons of public security and order, *public health* [emphasis supplied] or morality shall not be deemed ‘treatment less favorable’ within the meaning of Article 3.”); New Zealand-China BIT, art. 11, Nov. 22, 1988 (“The provisions of this Agreement shall not in any way limit the right of either Contracting Party to apply prohibitions or restrictions... directed to the protection of its essential security interests, or to the protection of *public health* [emphasis supplied] or the prevention of disease and pests in animals or plants.”).

³⁸⁰ E.g., OECD Code of Liberalization of Capital Movements, art. 3 (recommending that a Member is not prevented “from taking action which it considers necessary for: i) the maintenance of public order or the protection of public health, *morals* [emphasis supplied] and safety...”); GATS, *supra* note 271, annex 1B (“... necessary to protect *public morals* or to maintain public order” with footnote 5 of art. XIV(a) stating that “[t]he public order exception may be invoked only where a genuine and sufficiently serious threat is posed to one of the fundamental interests of society”); ICCPR art. 12(3) (“The above-mentioned rights shall not be subject to any restrictions except those which are provided by law, are necessary to protect national security, public order (*ordre public*), public health or *morals* [emphasis supplied] or the rights and freedoms of others, and are consistent with the other rights recognized in the present Covenant.”).

³⁸¹ Constitution and Convention of the International Telecommunication Union, art. 34(2), Dec. 22, 1992, 1825 U.N.T.S. 330 (“... which may appear dangerous to the security of the State or contrary to its laws, to public order or to *decency* [emphasis supplied]”).

³⁸² China-Japan BIT, protocol, para. 3, Aug. 27, 1988. In accordance with Chinese BIT practice, the China-Japan BIT imposes a strict nexus requirement (“in case it is *really necessary* [emphasis supplied] for the reason of public order...”). *Id.* See also TITI, *supra* note 79, at 192.

³⁸³ Hungary-Russia BIT, art. 2, Mar. 6, 1995.

greater specificity than the version of the public order carve-out seen in the U.S.-Argentina BIT. Although language that adds precision to an important carve-out that affects the ability of host States to regulate generally appears to be the right direction, it must be approached with a degree of caution.

Chapter 3: States' Treatment of the Public Order

Carve-out in IIAs

I. Textual Transformation of the Public Order Carve-out in IIAs

A. Prior to the 1980s: Public Order Provisions in FCNs

Long before the BIT program took place in the United States, public order provisions were prevalent even in the Friendship, Commerce and Navigation (FCN) treaties. In a much earlier example not commonly seen in modern IIAs, the term “public order” was used in conjunction with religion as seen in the U.S.-Austria FCN Treaty (1928) which states that:

The nationals of each of the High Contracting Parties in the exercise of the right of freedom of worship, within the territories of the other, as herein above provided, may, without annoyance or molestation of any kind by reason of their religious belief or otherwise, conduct services either within their own houses or within any appropriate buildings which they may be at liberty to erect and maintain in convenient situations, provided their teachings and practices are **not inconsistent with public order** or public morals and provided further they conform to all laws and regulations duly established in these territories; and they may also be permitted to bury their dead according to their religious customs in suitable and convenient places established and maintained for the purpose, subject to the established mortuary and sanitary laws and regulations of the place of

burial.³⁸⁴

The practice of coupling public order with religion is seen again in the U.S.-Ethiopia FCN Treaty (1951), which provides that:

3. Nationals of either High Contracting Party within the territories of the other High Contracting Party shall enjoy freedom of conscience and worship provided their religious practices are **not contrary to public order**, safety or morals: shall have the right to communicate with other persons inside and outside such territories; and shall be accorded most-favored-nation treatment with respect to engaging in religious, philanthropic, educational and scientific activities. They shall also be permitted to engage in the practice of professions for which they have qualified.³⁸⁵

The U.S.-Italy FCN Treaty (1948) uses the public order carve-out in two different ways. It is first used to restrain the movement of aliens by providing in Article I that:

1. The nationals of either High Contracting Party shall be permitted to enter the territories of the other High Contracting Party, and shall be permitted freely to reside and travel therein.

[...]

4. The provisions of paragraph 1 of this Article shall not be

³⁸⁴ U.S.-Austria Friendship, Commerce and Consular Rights Treaty, art. 5, June 19, 1928 [emphasis supplied in text].

³⁸⁵ U.S.-Ethiopia Amity and Economic Relations Agreement, art. VI(3), Sep. 7, 1951 [hereinafter U.S.-Ethiopia FCN Treaty] [emphasis supplied in text].

construed to preclude the exercise by either High Contracting Party of reasonable surveillance over the movement and sojourn of aliens within its territories or the enforcement of measures for the exclusion or expulsion of aliens **for reasons of public order**, morals, health or safety.³⁸⁶

The second use of the public order carve-out in the U.S.-Italy FCN Treaty is in regards to religion and also affects the right of individuals to assemble.

Article XI provides, in pertinent part, that:

1. The nationals of either High Contracting Party shall, within the territories of the other High Contracting Party, be permitted to exercise liberty of conscience and freedom of worship, and they may, whether individually, collectively or in religious corporations or associations, and without annoyance or molestation of any kind by reason of their religious belief, conduct services, either within their own houses or within any other appropriate buildings, provided that their teachings or practices are **not contrary to public morals or public order**.³⁸⁷

After the Second World War, the term “public order” continued to be included in the U.S. FCN treaties but began to be phrased as a carve-out that could be invoked only out of necessity to protect an essential interest of the State. For example, the U.S.-Germany FCN Treaty (1954) provides a public order carve-out in the context of the movement of aliens that is also limited

³⁸⁶ U.S.-Italy FCN Treaty, art. I, Feb. 2, 1948 [emphasis supplied in text].

³⁸⁷ *Id.* art. XI [emphasis supplied in text].

by the term “necessary” to state that:

1. Nationals of either Party shall, subject to the laws relating to the entry and sojourn of aliens, be permitted to enter the territories of the other Party, to travel therein freely, and to reside at places of their choice. Nationals of either Party shall in particular be permitted to enter the territories of the other Party and to remain therein: (a) for the purpose of carrying on trade between the territories of the two Parties and engaging in related commercial activities; (b) for the purpose of developing and directing the operations of an enterprise in which they have invested, or in which they are actively in the process of investing, a substantial amount of capital.

[...]

5. The provisions of the present Article shall be subject to the right of either Party to apply measures that are **necessary** to maintain public order and protect the public health, morals and safety.³⁸⁸

This similar wording is also used in the U.S.-Denmark FCN Treaty (1951),³⁸⁹ U.S.-Japan FCN Treaty (1953),³⁹⁰ U.S.-Netherlands FCN Treaty (1956),³⁹¹

³⁸⁸ U.S.-Germany FCN Treaty, art. II, Oct. 29, 1954 [emphasis supplied in text].

³⁸⁹ U.S.-Denmark FCN Treaty, art. II(3), Oct. 1, 1951.

³⁹⁰ U.S.-Japan FCN Treaty, art. I(3), Apr. 9, 1953.

³⁹¹ U.S.-Netherlands FCN Treaty, art. II(4), Mar. 27, 1956.

U.S.-Korea FCN Treaty (1956),³⁹² U.S.-Belgium FCN Treaty (1961),³⁹³ and the U.S.-Luxembourg FCN Treaty (1962).³⁹⁴ However, in the final FCN concluded by the United States with Thailand, the concept of public order is not present perhaps overshadowed or even replaced by the security interests exceptions to better protect U.S. interests.³⁹⁵ The U.S.-Thailand FCN Treaty (1966) provides that a State is not precluded from taking measures “necessary to fulfill the obligations of either Party for the maintenance or restoration of international peace and security, or necessary to protect its essential security interests.”³⁹⁶

B. Prior to the 2000s: Public Order Provisions in BITs

In 1962, the OECD presented the Draft Convention on the Protection of Foreign Property, which received OECD approval in 1967.³⁹⁷ The OECD Draft Convention does not use the term “public order,” but attempts to specify what kinds of “derogations” are permitted in Article 6, which provides that:

A Party may take measures in derogation of this Convention only if:

- (i) involved in war, hostilities or other grave public

³⁹² U.S.-Korea FCN Treaty, art. II(3), Nov. 28, 1956.

³⁹³ U.S.-Belgium FCN Treaty, art. II(5), Feb. 21, 1961.

³⁹⁴ U.S.-Luxembourg FCN Treaty, art. II(5), Feb. 23, 1962.

³⁹⁵ See Vandeveld, *Rebalancing*, *supra* note 188, at 452.

³⁹⁶ U.S.-Thailand FCN Treaty, art. XII(e), May 29, 1966.

³⁹⁷ OECD, Draft Convention on the Protection of Foreign Property (Oct. 12, 1967) [hereinafter OECD Draft Convention], <https://www.oecd.org/investment/internationalinvestmentagreements/39286571.pdf>.

emergency of a nation-wide character due to force majeure or provoked by unforeseen circumstances or threatening its essential security interests; or

(ii) [...]

Any such measures shall be provisional in character and shall be limited in extent and duration to those strictly required by the exigencies of the situation.³⁹⁸

The Commentary stresses that derogations may be permitted when the public emergency satisfies the following conditions. The public emergency must be grave to the point of it causing nation-wide repercussions and must be due to *force majeure* or be provoked by unforeseen circumstances or threaten the essential security interest of the State. The Commentary explicitly states that civil wars, riots, any other kinds of civil disturbances may be a result of *force majeure* (including, but not limited to, storm damage, earthquakes, and volcanic eruptions) or unforeseen circumstances within the meaning of the first paragraph in Article 6.³⁹⁹ The OECD Draft Convention was not formally adopted, but has influenced subsequent BITs.⁴⁰⁰

Despite the evolving public order language towards a narrower scope, during the time that the 1983 U.S. Model BIT was being drafted, the inclusion of the public order carve-out presented a “philosophical dilemma” for the United States because while it sought to secure high investor

³⁹⁸ *Id.* art. 6.

³⁹⁹ OECD, notes and comments to art. 6, para. 2(b).

⁴⁰⁰ RUDOLF DOLZER & MARGRETE STEVENS, *BILATERAL INVESTMENT TREATIES 2* (Martinus Nijhoff 1995).

protections for its nationals, the NPM provision was not necessarily included to preserve regulatory public interest. The United States ironically sought to justify economic sanctions (such as freezing foreigners' assets in the United States) against the contracting States through the NPM provision so that its obligations under a particular BIT would not be breached.⁴⁰¹ Yet, the United States was simultaneously concerned that developing States would use the NPM provision against the United States. Since no solution could be provided to resolve this dilemma, the United States avoided expanding or narrowing the scope of the NPM provision during BIT negotiations.⁴⁰² In a sense, the public order carve-out was not developed because developed countries had no demand for it since strengthening the public order carve-out meant that investor protection would be decreased while weakening the public order carve-out would reduce the flexibility of the developed, contracting State.

In the first U.S. BIT concluded between the United States and Panama in 1982, the public order carve-out is provided in isolation, not connected to any other substantive provision of the BIT, in the following manner:

1. This treaty shall not preclude the application by either Party of any and all measures **necessary for the maintenance of public order**, the fulfillment of its obligations with respect to the maintenance or restoration of international peace and security, or the production of its own essential security

⁴⁰¹ VANDEVELDE, *supra* note 3, at 200 (stating that the United States was increasingly using sanctions like the freezing of assets in the U.S. to implement its foreign policy objectives).

⁴⁰² *Id.*

interests.⁴⁰³

Panama insisted on a clarification of the public order carve-out to which the United States rather unsatisfactorily replied that acts taken for the maintenance of public order are limited to domestic measures and that it does not authorize “either Party to take such measures in the territory of the other.”⁴⁰⁴ The U.S. practice of not elaborating on the meaning of the term “public order” has since remained although later documents occasionally reveal the term to mean that the “maintenance of public order would include measures taken pursuant to a Party’s police powers to ensure public health and safety.”⁴⁰⁵ A handful of U.S. BITs including those with Morocco (1985),⁴⁰⁶ Congo (1990),⁴⁰⁷ Argentina (1991),⁴⁰⁸ Ecuador (1993),⁴⁰⁹ Haiti

⁴⁰³ U.S.-Panama BIT, art. X, para. 1, Oct. 27, 1982 [emphasis supplied in text].

⁴⁰⁴ Letter from George P. Shultz, U.S. Secretary of State, to Ronald Reagan, U.S. President (Feb. 20, 1986), *available at* <http://www.state.gov/documents/organization/43582.pdf> [hereinafter Letter from Shultz regarding U.S.-Panama BIT] (noting that “[b]ecause of political sensitivities in Panama, the Panamanians insisted on a separate exchange of notes (information copy attached) clarifying the standard provision in the BIT which exempts measures taken for public order”); Letter from Everett E. Briggs, U.S. Ambassador to Panama, to Jorge Aradia Arias, Panama Foreign Relations Minister (July 12, 1985), *available at* <http://www.state.gov/documents/organization/43582.pdf>.

⁴⁰⁵ Letter from Warren Christopher, U.S. Secretary of State, to William J. Clinton, U.S. President (Sep. 7, 1994), *available at* <http://2001-2009.state.gov/documents/organization/43560.pdf> (regarding the NPM provision in the U.S.-Estonia BIT, art. IX, Apr. 19, 1994).

⁴⁰⁶ U.S.-Morocco BIT, art. IX.1, July 22, 1985.

⁴⁰⁷ U.S.-Congo BIT, art. X, Feb. 12, 1990.

⁴⁰⁸ U.S.-Argentina BIT, art. XI, Nov. 14, 1991.

⁴⁰⁹ U.S.-Ecuador BIT, art. IX, Aug. 27, 1993.

(1983),⁴¹⁰ Kyrgyzstan (1993),⁴¹¹ Estonia (1994),⁴¹² and Latvia (1995)⁴¹³ each contain a public order carve-out like the language seen in the U.S.-Panama BIT. The U.S.-Poland BIT (1990)⁴¹⁴ also includes a public order carve-out but under the heading “Reservation of Rights” with an accompanying letter from the U.S. President that states: “Also expressly reserved is a Party’s right to take any measures that are necessary to protect public order or essential security interests.”⁴¹⁵ In the Bangladesh-U.S. BIT (1986), Bangladesh demanded that the Protocol to the treaty explicitly reiterate that the right of nationals and companies to employ personnel of their choice shall be subject to the NPM provision in Article X, which also includes the public order carve-out, due to “strong Bangladesh insistence that one of the principal benefits of foreign investment is the development of local employee skills.”⁴¹⁶ The overall effect of such clarifications is unclear, but can be

⁴¹⁰ U.S.-Haiti BIT, art. X, Dec. 13, 1983.

⁴¹¹ U.S.-Kyrgyzstan BIT, art. X, Jan. 19, 1993.

⁴¹² U.S.-Estonia BIT, art. IX, Apr. 19, 1994.

⁴¹³ U.S.-Latvia BIT, art. IX, Jan. 13, 1995.

⁴¹⁴ U.S.-Poland BIT, art. XII, Mar. 21, 1990.

⁴¹⁵ Letter from Lawrence Eagleburger, U.S. Secretary of State, to George H. W. Bush, U.S. President (June 8, 1990), *available at* <http://www.state.gov/documents/organization/210528.pdf>.

⁴¹⁶ Bangladesh-U.S. BIT, protocol, para. 3, Mar. 12, 1986 provides the following:

3. The provisions of Article II... concerning the right of nationals and companies to employ personnel of their choice, shall be subject to the provision of Article X [“Measures not Precluded by this Treaty”]. Furthermore, as for any laws concerning the employment of foreign nationals which require the employment of a Party’s own nationals in certain positions or the employment of a certain percentage of its own nationals in positions in connection with

perceived as one way that a party strives to hedge itself to be able to take measures and in case of an investor-State arbitration.

However, the public order clause was dropped from the 1994 U.S. Model BIT. It would be inappropriate to interpret this omission as forbidding States from acting on behalf of their public interests. Rather, the omission may have been part of a greater effort to provide reliable investor protection by ensuring that States recognized their obligations so as to not defeat the purpose of BITs.⁴¹⁷ The omission is continued in Article 18 on “Essential Security” of the 2004 U.S. Model BIT, which exists verbatim in the updated 2012 U.S. Model BIT, provides that:

Nothing in this Treaty shall be construed:

1. to require a Party to furnish or allow access to any information the disclosure of which it determines to be contrary to its essential security interests; or
2. to preclude a Party from applying measures that it considers necessary for the fulfillment of its obligations with respect to the maintenance or restoration of international peace or security, or the protection of its own essential security interests.

investment made in its territory by nationals or companies of the other Part, each Party agrees to administer such laws flexibly, taking into account *inter alia*, the nature of the investment, the requirements of the positions in question, and the availability of qualified nationals.

⁴¹⁷ ALVAREZ, PUBLIC INTERNATIONAL LAW, *supra* note 68, at 323.

C. Current Trends: FTA Investment Chapters with Regulatory Space Carve-outs

1. Preamble

The preamble of some recent IIAs appeals to a broader range of public interest concerns that goes beyond investment protection and promotion even if the exact treaty formulation seen in the above examples is not used. As statements describing the common goals of the contracting parties, preambles do not create substantive obligations but is nevertheless important because they contribute to the interpretation of the overall treaty.⁴¹⁸ Moreover, by intentionally placing non-economic objectives on the same platform as investment objectives, language in the preamble that aims to preserve regulatory space can prevent investment protection guarantees from being interpreted too broadly so as to play a hand at the public policy objectives of a host State.⁴¹⁹ For example, the preamble of the TPP tries to elaborate on the concept of public order in a positive manner by affirming that the party States' commit to the following:

Recognize their inherent right to regulate and resolve to preserve the flexibility of the Parties to set legislative and regulatory priorities, safeguard public welfare, and protect legitimate public welfare objectives, such as public health,

⁴¹⁸ See J. Anthony VanDuzer, *Sustainable Development Provisions in International Trade Treaties: What Lessons for International Investment Agreements?*, in *SHIFTING PARADIGMS IN INTERNATIONAL INVESTMENT LAW* 142, 149 (Steffen Hindelang & Markus Krajewski eds., 2016).

⁴¹⁹ See Vid Prislund & Ruben Zandvliet, *Labor Provisions in International Investment Agreements: Prospects for Sustainable Development*, in *YEARBOOK ON INT'L INVESTMENT LAW & POLICY 2012-2013* 357, 385 (Andrea K. Bjorklund ed., 2014).

safety, the environment, the conservation of living or non-living exhaustible natural resources, the integrity and stability of the financial system and public morals.⁴²⁰

While the TPP does not use the term “public order,” it relies on the phrase “legitimate public welfare objectives” to allow States to regulate on issues of public health, safety, the environment, and the conservation of natural resources. Although the question of whether the term “public order” and phrase “legitimate public welfare objectives” can be used interchangeably has not been explicitly addressed by any of the stakeholders, this Dissertation assumes that the two styles of expression overlap in their common goal of preserving the regulatory space of host States.⁴²¹ The preamble in the Canada-EU CETA also preserves regulatory space by stating that the contracting States retain the right “to regulate within their territories and the Parties’ flexibility to achieve legitimate policy objectives, such as public health, safety, environment, public morals and the promotion and protection of cultural diversity.”⁴²² Another variation exists in the China-Australia FTA where the preamble “[u]phold[s] the rights of their governments to regulate in order to meet national policy objectives, and to preserve their flexibility to safeguard public welfare.”⁴²³ Not all recently concluded IIAs include such language in the preamble as in the EU-Vietnam

⁴²⁰ TPP, *supra* note 11, preamble.

⁴²¹ The phrase “legitimate public welfare objectives” usually shows up in the expropriation annex of IIAs. But some recent IIAs use this phrase in the main part of the investment chapter even outside of the expropriation context to preserve the States’ regulatory public interests.

⁴²² Canada-EU CETA, *supra* note 18, preamble.

⁴²³ China-Australia FTA, *supra* note 34, preamble.

FTA.

2. Scope of Application

The heading “Scope of Application” is not seen frequently in IIAs, but warrants discussion here because of the 2007 Colombia Model BIT which provides that the agreement “shall not be construed so as to prevent a Party from adopting or maintaining measures intended to preserve public order.”⁴²⁴ The Colombia Model BIT is interesting because, according to the “Explanation of Some Issues of the BIT Model” that is appended to the model BIT, it contains the explanation that “[a]ccording to the Colombian Constitution[,] the State shall have the possibility of guarantying public order” as established under the jurisprudence of the Constitutional Court regarding the Colombian concept of public order.⁴²⁵ This treaty language linking the IIA to domestic legislation is somewhat reflected in the U.S.-Colombia FTA (2006). The Schedule of Colombia in Annex II provides that national treatment may not apply because “Colombia reserves the right to adopt any measure for reasons of public order pursuant to Article 100 of the *Constitución Política de Colombia*.”⁴²⁶ Article 100 of the Colombia Constitution, which permits the government to derogate from its international treaty obligation on public reason ground,⁴²⁷ states in pertinent part that:

⁴²⁴ Colombia Model BIT, art. II (2007).

⁴²⁵ *Id.* Explanation of Some Issues of the BIT Model on Article II, *available at* http://www.italaw.com/documents/inv_model_bit_colombia.pdf.

⁴²⁶ U.S.-Colombia FTA, annex II, Schedule of Colombia, Nov. 22, 2006 [hereinafter U.S.-Colombia FTA Annex II].

⁴²⁷ CHESTER BROWN, COMMENTARIES ON SELECTED MODEL INVESTMENT TREATIES 209 (OUP 2013).

Aliens in Colombia will enjoy the same civil rights as Colombian citizens. Nevertheless, for reasons of public order, the law may impose special conditions or nullify the exercise of specific civil rights by aliens.⁴²⁸

Although the term “public order” is not statutorily defined in Colombian law, the Constitutional Court of Colombia described the concept as follows:

Public order refers to conditions necessary for the harmonious and peaceful development of social relations and therefore for the effectiveness of correlated rights and duties. Public order is a requirement for peaceful coexistence, it is the normal scene of relations between power and freedom. That is why public order is linked to the required security, peace and health conditions for the development of life within a community and for its members to assert themselves as free and responsible beings.⁴²⁹

Thus, even without an explicit public order carve-out in the investment chapter, Colombia has reserved its regulatory power and may do so for public order reasons if it follows the rules of procedures required in the Colombian Constitution.⁴³⁰ However, as indicated in the U.S.-Colombia

⁴²⁸ CONST. COL. art. 100; Colombia Model BIT, *supra* note 424, Explanation of Some Issues of the BIT Model on Article II.

⁴²⁹ BROWN, *supra* note 427, at 209 (translating Corte Constitucional de la Republica de Colombia, Oct. 2, 2002 (C-802/02-119) (Col.)).

⁴³⁰ U.S.-Colombia FTA Annex II, *supra* note 426. *See also* Colombia Model BIT, *supra* note 424, art. II, para. 3 stating the following:

Nothing contained in this Agreement shall bind either Contracting Party to protect investments made with capital or assets derived

FTA, Colombia has to fulfill certain conditions before the public order exception may be triggered. In addition to providing a written notice in a prompt manner, the public order measure must first be consistent with the following constitutional requirements.⁴³¹ Article 213 of the Colombian Constitution permits the Colombian President to declare a state of internal disturbance when public order is imminently threatened and cannot be stabilized using ordinary police power.⁴³² Moreover, laws that contribute to the state of disturbance may be suspended although they must be given effect as soon as public order is restored.⁴³³ Article 214 of the Colombian Constitution provides that international standards shall apply to the preservation of human rights and fundamental freedoms and that they may not be waived under the pretense of restoring public order.⁴³⁴ Article 215 presupposes the events not fathomed in Articles 212 and 213 to include situations in which a grave public calamity calling for a state of emergency may have to be declared due to a disruption of the economic, social, or ecological order of the State.⁴³⁵ Also, in order to adopt any measure for

from illegal activities, and it shall not be construed so as to prevent a Contracting Party from adopting or maintaining measures intended to preserve public order, the fulfillment of its duties for the keeping or restoration of international peace and security; or the protection of its own essential security interests.

⁴³¹ BROWN, *supra* note 427, at 209.

⁴³² CONST. COL. art. 213.

⁴³³ *Id.*

⁴³⁴ *Id.* art. 214.

⁴³⁵ *Id.* art. 215.

reasons of public order, Colombia must prove that the measure must be adopted or maintained only where a genuine and sufficiently serious threat is posed to one of the fundamental interests of society, is not applied in an arbitrary or unjustifiable manner, does not constitute a disguised restriction on investment, and is necessary and proportional to the objective it seeks to achieve.⁴³⁶

3. National Treatment and Most Favored Nation Treatment

Although European Model BITs are usually known for their simplicity with a focus on providing substantive investment protections, some European Model BITs use the public order carve-out in the context of their national and MFN treatment provisions.⁴³⁷ The 2008 German Model BIT states that: “Measures that have to be taken for reasons of public security and order shall not be deemed treatment less favorable within the meaning of this Article.”⁴³⁸ The 2008 United Kingdom Model BIT similarly provides an exception to the national and MFN treatment provisions by providing that a contracting State may adopt or enforce measures necessary to protect “public security or public order.”⁴³⁹

The EU-Singapore FTA also includes the public order carve-out in its national treatment provision, but is different from the preceding examples

⁴³⁶ U.S.-Colombia FTA Annex II, *supra* note 426.

⁴³⁷ See TITI, *supra* note 79, at 43 (stating that European Model BITs are “laconic instruments, free of elucidations”).

⁴³⁸ Germany Model BIT, art. 3 (2008).

⁴³⁹ United Kingdom Model BIT, art. 7 (2008).

because it includes the phrase in “like situations.”⁴⁴⁰ How this phrase will be interpreted under investment law depends on the investor-State tribunal, but for reference purposes, the NAFTA tribunals concluded that investments are in “like circumstances” when a legitimate policy objective is available; moreover, the UNCITRAL tribunal in *S.D. Myers v. Canada* affirmed the use of GATT Article XX to interpret the phrase “like circumstances.”⁴⁴¹ Under the heading “National Treatment,” Article 9.3 of the EU-Singapore FTA provides that:

3. Notwithstanding paragraphs 1 and 2, a Party may adopt or enforce measures that accord to covered investors and investments of the other Party less favourable treatment than that accorded to its own investors and their investments, in like situations, subject to the requirement that such measures are not applied in a manner which would constitute a means of arbitrary or unjustifiable discrimination against the covered investors or investments of the other Party in the territory of a Party, or is a disguised restriction on covered investments, where the measures are:

- (a) **necessary** to protect public security, public morals or **to maintain public order** [footnote

⁴⁴⁰ EU-Singapore FTA, *supra* note 265, art. 9.3.3 [awaiting signature].

⁴⁴¹ See *S.D. Myers v. Canada*, UNCITRAL, Separate Concurring Opinion, para. 129, (Nov. 13, 2000) (although the tribunal held that the measure banning PCB exports could not be justified under Article XX of the GATT, but stated that “the phrase ‘like circumstances’ in Article 1102 in many cases does require the same kind of analysis as is required in Article XX cases under the GATT.”). See also ANDREW D. MITCHELL ET AL., *NON-DISCRIMINATION AND THE RULE OF REGULATORY PURPOSE IN INTERNATIONAL TRADE AND INVESTMENT LAW* 81 (Edward Elgar Pub. 2016).

omitted] [...].⁴⁴²

In the TPP, a public order carve-out is not explicitly expressed in the national and MFN treatment provisions, but the “like circumstances” language in Article 9.4 on national treatment contains a footnote to elucidate that: “For greater certainty, whether treatment is accorded in ‘like circumstances’ [as set forth in Articles 9.4 and 9.5, respectively, the national treatment and MFN provisions] depends on the totality of the circumstances, including whether the relevant treatment distinguishes between investors or investments on the basis of legitimate public welfare objectives.”⁴⁴³

4. WTO/GATS-inspired General Exceptions

In addition to providing the content of the public order carve-out, recent IIAs are increasingly using various aspects of the WTO/GATS general exceptions provisions. The chapeau language of Article XX of the GATT or Article XIV of the GATS may be imported into IIAs to test how the challenged domestic was given effect. For reference purposes, the chapeau of Article XX of the GATT states that:

Subject to the requirement that such measures are not applied in a manner which would constitute a means of arbitrary or unjustifiable discrimination between countries where the same conditions prevail, or a disguised restriction on international trade, nothing in this Agreement shall be construed to prevent the adoption or enforcement by any

⁴⁴² EU-Singapore FTA, *supra* note 265, art. 9.3.

⁴⁴³ TPP, *supra* note 11, art. 9.4, n. 14.

contracting party of measures [...].⁴⁴⁴

Adding the chapeau language may limit the scope of the public order carve-out in IIA, but ultimately the question of how it will be interpreted and how much of the WTO jurisprudence will be acknowledged by an investment tribunal remains to be determined. The WTO is, however, well-settled in stating that the purpose of the chapeau is to prevent abuse of the exceptions provided under Article XX of the GATT.⁴⁴⁵ As seen below, the Appellate Body in *U.S. – Shrimp* described the delicate task involved in interpreting and applying the chapeau:

The task of interpreting and applying the chapeau is, hence, essentially the delicate one of locating and marking out a line of equilibrium between the right of a Member to invoke an exception under Article XX and the rights of the other Members under varying substantive provisions (e.g., Article XI) of the GATT 1994, so that neither of the competing rights will cancel out the other and thereby distort and nullify or impair the balance of rights and obligations constructed by the Members themselves in that Agreement. The location of the line of equilibrium, as expressed in the chapeau, is not fixed and unchanging; the line moves as the kind and the shape of the measures at stake vary and as the facts making

⁴⁴⁴ GATT, *supra* note 270, art. XX.

⁴⁴⁵ Appellate Body Report, *United States – Standards for Reformulated and Conventional Gasoline*, WT/DS2/AB/R (Apr. 29, 1996); Appellate Body Report, *United States – Import Prohibition of Certain Shrimp and Shrimp Products*, WT/DS58/AB/R (Oct. 12, 1998) [hereinafter *U.S. – Shrimp Appellate Body Report*].

up specific cases differ.⁴⁴⁶

The general exceptions provisions in Article XIV of the GATS also contains the chapeau but is phrased slightly differently than Article XX of the GATT. Instead of using the term “same conditions,” Article XIV of the GATS uses the term “like conditions” and whereas Article XX of the GATT applies to measures of “any contracting party,” Article XIV of the GATS covers measures by “any Member.” For closer inspection, the text of Article XIV of the GATS is provided below:

Subject to the requirement that such measures are not applied in a manner which would constitute a means of arbitrary or unjustifiable discrimination between countries where like conditions prevail, or a disguised restriction on trade in services, nothing in this Agreement shall be construed to prevent the adoption or enforcement by any Member of measures [...].⁴⁴⁷

The minor differences in the terms used in both versions of the chapeau have generally been treated the same. In *U.S. – Gambling*, the Appellate Body affirmed the Panel’s finding that the requirements set forth in the chapeaus of Article XX of the GATT and Article XIV of the GATS are similar so that the analysis used in the former would be considered to be relevant for analyzing the chapeau in Article XIV of the GATS.⁴⁴⁸ In investment treaty practice, the chapeau language may be modified to better fit the IIA context.

⁴⁴⁶ U.S. – Shrimp Appellate Body Report, *supra* note 445, para. 159.

⁴⁴⁷ GATS, *supra* note 271, art. XIV.

⁴⁴⁸ U.S. – Gambling Appellate Body Report, *supra* note 281, para. 291.

The Colombia-Japan BIT (2011) changes some language but closely follows the model of Article XIV of the GATS which, unlike Article XX of the GATT, contains a public order carve-out. Article 15 of the Colombia-Japan BIT provides that:

1. Subject to the requirement that such measures are not applied by a Contracting Party in a manner which would constitute a means of arbitrary or unjustifiable discrimination against the other Contracting Party, or a disguised restriction on investments of investors of that other Contracting Party in the Area of the former Contracting Party, nothing in this Agreement... shall be construed to prevent that former Contracting Party from adopting or enforcing measures, including those to protect the environment:

[...]

(b) **necessary** to protect public morals or **to maintain public order** [...].⁴⁴⁹

A truncated version of GATS Article XIV is provided in the Macedonia-Morocco BIT (2010) providing only a portion of the language used in the chapeau:

6. Nothing in this Agreement shall be construed to prevent a Contracting Party from taking any action that is **considered as necessary for the protection of** public security, **order** or public health or protection of environment, provided that such measures are not applied in a manner which would

⁴⁴⁹ Colombia-Japan BIT, art. 15, Sep. 12, 2011.

constitute a means of arbitrary or unjustified discrimination.⁴⁵⁰

In this example, the term “public” does not immediately precede the term “order” and the commas are placed so that order is in the same category as public health and environment protection. Whether this is indicative of the contracting States’ desire to control the scope of the public order carve-out remains to be determined.

On a similar note, the 2016 Azerbaijan Model BIT states in Article 5 titled “General Exceptions” that:

2. Nothing in this Agreement shall be construed to prevent a Contracting Party from taking any action that is **considered as necessary for the protection of** national security, **public order** or public health, morality, or protection of environment, provided that such measures are not applied in a manner which would constitute a means of arbitrary or unjustified discrimination.⁴⁵¹

The placement of the commas is interesting because it appears to group the concept of public order with public health. Future investment tribunals may have the opportunity to decide on whether the commas narrow the scope of the public order carve-out.

The term “public order” is used in some IIAs, but it is an open concept with little jurisprudence in international investment law to aid its

⁴⁵⁰ Macedonia-Morocco BIT, art. 2.6, May 11, 2010.

⁴⁵¹ Azerbaijan Model BIT, art.5 (2016).

clarification.⁴⁵² Moreover, the openness of the term “public order” raises the question of whether it also covers threats to national security or whether its confines should be limited to domestic civil disorder.⁴⁵³ Although most investment treaties do not clarify the meaning of public order, some IIAs are influenced by the language in Article XIV of the GATS which provides a clarification note for the term “public order.” Immediately after the chapeau, Article XIV of the GATS enumerates public order as a measure that may be adopted or enforced by any Member when necessary as seen below:

[See above for GATS Article XIV chapeau]:

(a) **necessary** to protect public morals or **to maintain public order** [footnote 5]

(footnote original) 5 The public order exception may be invoked only where a genuine and sufficiently serious threat is posed to one of the fundamental interests of society.

A less common variation is available in the ASEAN-China Investment Agreement (2009) which retains the Article XIV phrase “like conditions” as provided below:

1. Subject to the requirement that such measures are not applied in a manner which would constitute a means of arbitrary or unjustifiable discrimination between the Parties, their investors or their investments where like conditions

⁴⁵² UNCTAD, *The Protection of National Security in IIAs*, in UNCTAD SERIES ON INTERNATIONAL INVESTMENT POLICIES FOR DEVELOPMENT 74 (2009) [hereinafter UNCTAD, *Protection*].

⁴⁵³ *Id.*

prevail, or a disguised restriction on investors of any Party or their investments made by investors of any Party, nothing in this Agreement shall be construed to prevent the adoption or enforcement by any Party of measures:

- (a) **necessary** to protect public morals or **to maintain public order** [footnote 10] [...].⁴⁵⁴

Footnote 10 of the ASEAN-China Investment Agreement achieves the same meaning as footnote 5 of Article XIV of the GATS by stating that: “For the purpose of this Sub-paragraph, footnote 5 of Article XIV of the GATS is incorporated into and forms part of this Agreement *mutatis mutandis*.”⁴⁵⁵

The Singapore-India Comprehensive Economic Cooperation Agreement (Singapore-India CECA) implements an entirely different framework. Most visible is a provision titled “Measures in the Public Interest” in Article 6.10 as set forth below:

Nothing in this Chapter shall be construed to prevent:

- (a) a Party or its regulatory bodies from adopting, maintaining or enforcing any measure, on a nondiscriminatory basis; or
- (b) the judicial bodies of a Party from taking any measures;

consistent with this Chapter that is in the public interest, including measures to meet health, safety or environmental

⁴⁵⁴ ASEAN-China Investment Agreement, art. 16.1(a), Aug. 15, 2009.

⁴⁵⁵ *Id.* art. 16.1(a), n. 10.

concerns.⁴⁵⁶

A provision on general exceptions modeled after Article XIV of the GATS is successively placed in Article 6.11 of the Singapore-India CECA and provides for the public order carve-out without a clarification note in the following form:

1. Subject to the requirement that such measures are not applied in a manner which would constitute a means of arbitrary or unjustifiable discrimination against the other Party or its investors where like conditions prevail, or a disguised restriction on investments of investors of a Party in the territory of the other Party, nothing in this Chapter shall be construed to prevent the adoption or enforcement by a Party of measures:

(a) **necessary** to protect public morals or **to maintain public order** [...].⁴⁵⁷

In another variation found in the New Zealand-Singapore Closer Economic Partnership Agreement (NZ-Singapore CEPA), the provision titled “General Exceptions” contains some of the influences of the general exceptions provisions in the WTO/GATS but modifies the language to fit its investment treaty purpose. Article 71 of the New Zealand-Singapore CEPA provides that:

Provided that such measures are not used as a means of arbitrary or unjustified discrimination against persons of the

⁴⁵⁶ Singapore-India CECA, art. 6.10, June 29, 2005.

⁴⁵⁷ *Id.*

other Party or as a disguised restriction on trade in goods and services or investment, nothing in this Agreement shall preclude the adoption by any Party of measures in the exercise of its legislative, rule-making and regulatory powers:

- a) **necessary to protect public order** or morality, public safety, peace and good order and to prevent crime [...].⁴⁵⁸

In a more interesting example, the “General Exceptions” article of the 2015 Norway Model BIT provides a provision that resembles Article XIV of the GATS but contains a footnote identifying the applicable standard of review for interpretation purposes and another footnote defining the meaning of the public order exception. Article 24 of the 2015 Norway BIT provides, in relevant part, the following:

Subject to the requirement that such measures are not applied in a manner which would constitute a means of 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** [footnote 3]:

- i. to protect public morals or **to maintain public order** [footnote 4] [...].⁴⁵⁹

This version is noteworthy because footnote 3 provides that: “For greater

⁴⁵⁸ New Zealand-Singapore CEPA, art. 71, Nov. 14, 2000.

⁴⁵⁹ Norway Model BIT, *supra* note 326, art. 24.

certainty, the concept of ‘necessity’ in this Article shall include measures taken by a Party as provided for by the precautionary principle, including the principle of precautionary action.”⁴⁶⁰ It also appends to the term “public order” a footnote 4 which states that: “The public order exception may be invoked only where a genuine and sufficiently serious threat is posed to one of the fundamental interests of society.”⁴⁶¹ These two clarification notes seem to underscore Norway’s priority on the preservation of regulatory space and is consistent with the stance taken in the 2007 Norway Model BIT. According to a commentary issued by Norwegian government in respect to the 2007 Norway Model BIT, it expressed that:

The main condition on concluding investment agreements is that the agreements shall be able to fulfill their economic and political functions without intervening unnecessarily in Norwegian exercise of authority... A prerequisite for Norway on concluding investment agreements must be that the agreements do not intervene in the state’s legitimate exercise of authority where major public interests are affected.⁴⁶²

The Norway Model BIT is an unusual example that attempts to control a certain aspect of the interpretation process normally delegated to the investor-State tribunals. Also, IIAs such as the Korea-Japan BIT (2002),⁴⁶³ the

⁴⁶⁰ *Id.* art. 24 n. 3.

⁴⁶¹ *Id.* art. 24 n. 4.

⁴⁶² Comments on the Model for Future Investment Agreements (Norway) 14 (Dec. 19, 2007), *available at* <http://www.italaw.com/sites/default/files/archive/ita1029.pdf>.

⁴⁶³ *Id.*

Colombia-Japan BIT (2011),⁴⁶⁴ and the EU-Singapore FTA⁴⁶⁵ usually only provide the clarification note seen in footnote 5 of the GATS Article XIV.

5. Other Variations of the Public Order Carve-out

As States continue to figure out the best possible way to preserve regulatory public interest even after concluding investment treaties, variations in the scope of the public order carve-out and the nexus that establishes the relationship between the means taken and the objective sought are being tested in IIA practice. In particular, whether the public order carve-out should operate as a self-judging clause is not uniformly established. According to the informal EU proposal of the TTIP between the European Union and the United States, the right to regulate provision is placed near the opening of the investment chapter. Presumably not intended to be self-judging, Article 2 is titled “Investment and Regulatory Measures/Objectives” and aims to preserve the right of a State to regulate “through measures necessary to achieve legitimate policy objectives, such as the protection of public health, safety, environment or public morals, social or consumer protection or promotion and protection of cultural diversity.”⁴⁶⁶

In contrast, Article 9.16 of the TPP titled “Investment and Environmental, Health and other Regulatory Objectives” incorporates the self-judging clause as shown below:

Nothing in this Chapter shall be construed to prevent a Party from adopting, maintaining or enforcing any measure

⁴⁶⁴ Colombia-Japan BIT, *supra* note 449, art. 15.1(b).

⁴⁶⁵ EU-Singapore FTA, *supra* note 265, art. 9.3.3.

⁴⁶⁶ TTIP (draft), *supra* note 12, art. 2.1.

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, health or other regulatory objectives.⁴⁶⁷

The variation in the TPP also omits the term “necessary,” which is frequently used to establish the standard for the public order carve-out, by making environmental, health, and other regulatory objectives a matter of the contracting States’ self-judgment.

An even broader version of this provision is found in the 2016 India Model BIT under the heading “General Exceptions” which provides that:

1. Nothing in this Treaty precludes the host State from taking action or measures of general applicability which **it considers necessary** with respect to the following, including:

(i) protecting public morals or **maintaining public order**.⁴⁶⁸

Not only is this provision self-judging as indicated by the “which it considers necessary” phrase, but it conveys the desire to cover a wide range of regulatory acts through the phrase “general applicability.” Moreover, the same provision provides in the third paragraph that: “Nothing in this Treaty shall apply to any Measure taken by a local body or authority at the district, block or village level in the case of India.”⁴⁶⁹ Unlike the 2003 India Model BIT which did not provide a public order carve-out, the 2016 India Model

⁴⁶⁷ TPP, *supra* note 11, art. 9.15 [emphasis supplied in text].

⁴⁶⁸ 2016 India Model BIT, *supra* note 38, art. 16.1.

⁴⁶⁹ *Id.* art. 16.3.

BIT shows a strong desire to preserve regulatory space but how India's contracting parties will react remains to be seen.

Other IIAs contain provisions that are similar to the general exceptions provisions, but do not actually absolve the host State from liability because the provision uses the phrase "consistent with this Chapter" which is understood to mean that the enacted measure must not derogate from the relevant IIA. An example of this kind of language is in the EFTA-Ukraine FTA (2010):

Nothing in this Chapter shall be construed to prevent a Party from adopting, maintaining or enforcing any measure **consistent with this Chapter** that is in the public interest, such as measures to meet health, safety or environmental concerns or reasonable measures for prudential purposes.⁴⁷⁰

Such language may have been influenced by provision titled "Environmental Measures" in the NAFTA which states that:

Nothing in this Chapter 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 concerns.⁴⁷¹

Some BITs such as the one between Belgium-Luxembourg and Guatemala demand public order as a condition for invoking national

⁴⁷⁰ EFTA-Ukraine FTA, art. 4.8.1, June 24, 2010 [emphasis supplied in text].

⁴⁷¹ NAFTA, *supra* note 110, art. 1114.

security even though their relationship has not been defined in international investment law. Article 3 under the heading “Protection of Investments” of the Belgium-Luxembourg and Guatemala BIT (2005) provides that:

1. All investments, whether direct or indirect, made by investors of one Contracting Party shall enjoy a fair and equitable treatment in the territory of the other Contracting Party. Except for measures **required to maintain public order**, such investments shall enjoy continuous protection and security, i.e. excluding any unjustified or discriminatory measure which could hinder, either in law or in practice, the management, maintenance, use, possession or liquidation thereof.⁴⁷²

Finally, some IIAs provide a high level of protection in favor of investors by altogether excluding the general exceptions provision as in the case of the Korea-South Africa BIT (1995), Bangladesh-Thailand BIT (2002), and the UAE-Russia BIT (2010). Contracting Parties that do not conclude IIAs for the purpose of market liberalization may believe that existing substantive provisions such as the fair and equitable treatment and the expropriation provisions provide an adequate level of protection to the host State while preserving the purpose of investor protection.⁴⁷³ However, excluding the general exceptions provision may more readily invite

⁴⁷² BLEU-Guatemala BIT, art. 3, Apr. 14, 2005.

⁴⁷³ APEC-UNCTAD, INTERNATIONAL INVESTMENT AGREEMENTS NEGOTIATORS HANDBOOK: APEC/UNCTAD MODULES 123 (2012) [hereinafter APEC IIA HANDBOOK], *available at* http://investmentpolicyhub.unctad.org/Upload/Documents/UNCTAD_APEC%20Handbook.pdf.

investors to challenge the host State in an international arbitration than if the IIA had contained such a provision.

6. Consultations

The public order carve-out may be provided in the ISDS provision of an IIA. For example, the Colombia-Panama FTA (2013) states that measures taken to preserve or maintain public order are non-justiciable by an investment tribunal.⁴⁷⁴ Yet, the China-Australia FTA (2015) provides another variation. Modeled after Article XX of the GATT, it therefore does not include a public order carve-out therein; however, the public order carve-out is available under the consultations provision of the China-Australia FTA. Paragraph 4 of Article 9.11 provides that:

4. Measures of a Party that are non-discriminatory and for the legitimate public welfare objectives of public health, safety, the environment, public morals or **public order shall not be the subject of a claim** under this Section [Investor-State Dispute Settlement].⁴⁷⁵

Furthermore, in the case a claimant alleges that a challenged measure breaches a substantive provision of the investment chapter, the respondent State may attempt to remove the justiciability of the issue by contending that the measure in question falls within the scope of paragraph 4 (provided above). This is stipulated in paragraph 5 of Article 9.11 which states that:

5. The respondent may, within 30 days of the date on which it receives a request for consultations (as provided for in

⁴⁷⁴ Colombia-Panama FTA, annex 14-D, para. 3, Sep. 20, 2013.

⁴⁷⁵ China-Australia FTA, *supra* note 34, art. 9.11.4 [emphasis supplied in text].

paragraph 1), state that it considers that a measure alleged to be in breach of an obligation under Section A is of the kind described in paragraph 4, by delivering to the claimant and to the non-disputing Party a notice specifying the basis for its position (a ‘public welfare notice’).⁴⁷⁶

Moreover, under the heading “Future Work Program,” Article 9.9 imposes a duty upon the parties, unless otherwise agreed, to review the investment chapter and the China-Australia BIT⁴⁷⁷ within three years after the FTA takes effect.⁴⁷⁸ This article also provides that the Parties “shall commence negotiations on a comprehensive Investment Chapter” based on the non-exhaustible list of issues available in paragraph 3(b) of Article 9.9.⁴⁷⁹

Taking these provisions together, it appears that Australia, in the aftermath of the Philip Morris arbitration, and China have sought to preserve greater regulatory power. The inclusion of the public order carve-out in the section addressing ISDS sends a message that challenges made to measures taken under “legitimate public welfare objectives” is not a proper subject of claim. But what remains unclear is to what extent this provision is self-judging, if at all.

⁴⁷⁶ *Id.* art. 9.11.5.

⁴⁷⁷ China-Australia BIT, July 11, 1988. The China-Australia BIT does not contain a NPM provision or general exceptions provision. The lack of such features has apparently been made up for in the China-Australia FTA.

⁴⁷⁸ China-Australia FTA, *supra* note 34, art. 9.9.1.

⁴⁷⁹ They include minimum standard of treatment, expropriation, transfers, performance requirements, senior management and board of directors, investment-specific state to state dispute settlement, and the application of investment protections and ISDS to services supplied through commercial presence.

The 2015 Brazil Model BIT also prohibits public order measures from the scope of the ISDS clause by providing in its security exceptions provision the following:

1. Nothing in this Agreement shall be construed to prevent a Party from adopting or maintaining measures **aimed at** preserving its national security or **public order**, or to apply the provisions of their criminal laws or comply with its obligations regarding the maintenance of international peace and security in accordance with the provisions of the United Nations Charter.
2. Measures adopted by a Party under paragraph 1 of this Article or the decision based on national security laws or **public order** that at any time prohibit or restrict the realization of an investment in its territory by an investor of another Party **shall not be subject to the dispute settlement mechanism** under this Agreement.⁴⁸⁰

These variations do not represent the mainstream drafting practice of investment treaties, but are important to note because such provisions reflect the priorities of the contracting States and how they strive to find a balance between fulfilling IIA obligations and preserving regulatory space.

II. Other Methods of Preserving Regulatory Space in IIAs

A. Legitimate Public Welfare Objectives

Although the topic of expropriation is outside the scope of this Dissertation, some recognition of the phrase “legitimate public welfare,”

⁴⁸⁰ Brazil Model BIT, art. 13 (2015).

which originates out of the nationalization and expropriation context, is relevant because when the scope of public order clause becomes overly broad, the periphery between regulatory takings and public interest considerations may get obscured since they both rely on the regulatory nature of a host State's act to justify that measure.⁴⁸¹ Although not the main theme of this Dissertation, an additional factor to consider is related to whether the existence of a legitimate public welfare and/or the public order carve-out absolves a State from the duty to compensate. The standard of compensation for expropriation is relatively well-established in international law according to the compensation standard set forth under the Hull Rule that prompt, adequate, and effective compensation be paid.⁴⁸² But, whether this rule also applies for breaches committed under the public order carve-

⁴⁸¹ For example, contrary to the pro-investor stance taken by the United States, it has included the concept of indirect expropriation since the 2004 U.S. Model BIT perhaps to control for its position as a "frequent NAFTA defendant." José E. Alvarez & Tegan Brink, *Revisiting the Necessity Defense: Continental Casualty v. Argentina*, in *YEARBOOK ON INT'L INVESTMENT LAW & POLICY* 2010-2011 319, 343 (Karl P. Sauvant ed., 2012).

⁴⁸² *But see* M. Sornarajah, *Compensation for Nationalization: The Provision in the Energy Charter*, in *The Energy Charter Treaty: An East-West Gateway for Investment and Trade* 386, 392 (Thomas Wälde ed., 1996) (stating that the embracement of Hull formula is overstated and that "[t]he inclusion of the Hull standard in the treaty must not lead to the general conclusion that there has been a shift towards the acceptance of the standard").

out is not as clearly settled.⁴⁸³ The “more subtle question”⁴⁸⁴ that lingers is whether a measure made for the maintenance of public order can avoid the duty to compensate.⁴⁸⁵ Despite the classic position developed during the 1960s and 1970s that governments must compensate injured investors when expropriation occurs regardless of its policy objective or non-discriminatory nature,⁴⁸⁶ some degree of uncertainty has appeared in modern practice. For example, the *LG&E* tribunal denied compensation to the claimant for the period of the state of necessity and, similarly, the *Continental Casualty* tribunal upheld Argentina’s reasoning that “if Art[icle] XI is applicable to the

⁴⁸³ *LG&E v. Argentina*, *supra* note 179, para. 30 (tribunal stating that questions as to the applicable standard, measure of compensation, and the method to quantify it “are particularly thorny... for treaty breaches other than expropriation” and that “[t]here are no express provisions in the Treaty addressing these issues and pre-existing guidance in arbitral jurisprudence is very limited”). See Margaret B. Devaney, *Remedies in Investor-State Arbitration: A Public Interest Perspective*, INVESTMENT TREATY NEWS (Mar. 22, 2013), https://www.iisd.org/itn/2013/03/22/remedies-in-investor-state-arbitration-a-public-interest-perspective/#_ftn4 (stating that only a minor portion of “an extensive body of literature map[ping] the tensions between regulatory sovereignty and investor protection... makes reference to public interest considerations at the remedies stage of the investor-[S]tate arbitration process”).

⁴⁸⁴ JÜRGEN KURTZ, *THE WTO AND INTERNATIONAL INVESTMENT LAW: CONVERGING SYSTEMS* 186 (Cambridge Univ. Press 2016) [hereinafter KURTZ, *CONVERGING SYSTEMS*].

⁴⁸⁵ Yas Banifatemi, *The Emerging Jurisprudence on the Most-Favored-Nation Treatment in Investment Arbitration*, in INVESTMENT TREATY LAW: CURRENT ISSUES III REMEDIES IN INTERNATIONAL INVESTMENT LAW EMERGING JURISPRUDENCE OF INTERNATIONAL INVESTMENT LAW 241 (Andrea K. Bjorklund et al., 2009) (stating that other areas of international investment law like national treatment, most favored nation treatment, and umbrella clauses “as a cause of exoneration of a State’s international responsibility are topics that remain today hotly debated and have yet to yield a consistent body of case law”).

⁴⁸⁶ Alvarez & Brink, *supra* note 481, at 342.

dispute at issue no compensation is due since 'there is no treaty violation.'"⁴⁸⁷

The concern in this Dissertation is that cases of indirect expropriation that also affect the right to regulate in international investment law have been supplanting investment disputes based on direct expropriation where the issue is finding the appropriate balance between the act of a host government made for a legitimate public purpose and a decline in an investment caused by the regulation.⁴⁸⁸ The first batch of indirect expropriation cases arising out of domestic measures arose under NAFTA as investors attacked regulatory measures enacted for the protection of the environment, health, and other matters affecting public interests.⁴⁸⁹ The NAFTA language below provides an early example of an expropriations provision covering for the possibility of creeping expropriations:

1. No Party may directly or indirectly nationalise or expropriate an investment of an investor of another Party in its territory or **take a measure tantamount** to nationalisation or expropriation of such an investment, except:

- (a) for a public purpose;
- (b) on a non-discriminatory basis;
- (c) in accordance with due process of law and Article 1105 (1)15; and
- (d) on payment of compensation in accordance with

⁴⁸⁷ *Continental Casualty*, *supra* note 179, para. 86.

⁴⁸⁸ OECD, "Indirect Expropriation" and the "Right to Regulate" in INTERNATIONAL INVESTMENT LAW 2 (OECD Working Papers on Int'l Investment No. 2004/04), available at https://www.oecd.org/daf/inv/investment-policy/WP-2004_4.pdf.

⁴⁸⁹ *See id.*

paragraphs 2 through 6 [describing the valuation criteria of expropriation and the payment form and procedure to be observed].⁴⁹⁰

The need to more directly address the creeping expropriations problem by clarifying the boundary between indirect expropriation and the right to regulate was evident in the Report by the Chairman to the Multilateral Agreement on Investment (MAI) Negotiating Group (Chairman's Report). Annex 3 of the Chairman's Report, titled "Treatment of Investors and Investments," provides a provision under the title "Right to Regulate" in Article 3 stating that:

A Contracting Party may adopt, maintain or enforce any measure that it considers appropriate to ensure that investment activity is undertaken in a manner sensitive to health, safety or environmental concerns, provided such measures are consistent with this agreement.⁴⁹¹

In the same annex of the Chairman's Report, Article 5 on expropriation and compensation appends an interpretative note stating that:

This Article is intended to incorporate into the MAI existing international legal norms. The reference to expropriation or nationalisation and 'measures tantamount to expropriation or nationalisation' reflects the fact that international law requires compensation for an expropriatory taking without

⁴⁹⁰ NAFTA, *supra* note 110, art. 1110 [emphasis supplied in text].

⁴⁹¹ OECD, Report by the Chairman to the Negotiating Group on the Multilateral Agreement on Investment, DAF/MAI(98)17, annex 3, art. 3 ["Right to Regulate"], available at <http://www1.oecd.org/daf/mai/pdf/ng/ng9817e.pdf>.

regard to the label applied to it, even if title to the property is not taken. It does not establish a new requirement that Parties pay compensation for losses which an investor or investment may incur through regulation, revenue raising and other normal activity in the public interest undertaken by governments. It is understood that default by a sovereign state subject to rescheduling arrangements undertaken in accordance with international law and practices is not expropriation within the meaning of this Article.⁴⁹²

Under the heading “General Exceptions” in Annex 7 of the Chairman’s Report, a public order carve-out is made in paragraph 3 but, as if to draw the distinction between expropriation and measures taken for the maintenance of public order, expropriation is not covered in this provision.⁴⁹³ The public order carve-out is provided for in the following manner:

3. Subject to the requirement that such measures are not applied in a manner which would constitute a means of arbitrary or unjustifiable discrimination between Contracting Parties, or a disguised investment restriction, nothing in this Agreement shall be construed to prevent any Contracting Party from taking any measure **necessary for the maintenance of public order** [footnote 25].⁴⁹⁴

⁴⁹² *Id.* annex 3, art. 5, n. 5.

⁴⁹³ *Id.* annex 7, para. 1 (“This Article shall not apply to [expropriation and compensation and protection from strife].”)

⁴⁹⁴ *Id.* annex 7, para. 3.

Footnote 25 seeks to clarify the term “public order” by stating that: “The public order exception may be invoked only where a genuine and sufficiently serious threat is posed to one of the fundamental interests of society.”⁴⁹⁵

The scope of the phrase “legitimate public welfare” is experiencing a change in scope as it is being tested in the traditional contexts outside of expropriation. For instance, the national treatment provision in the TPP contains an interpretative note stating that:

For greater certainty, whether treatment is accorded in ‘like circumstances’ under Article 9.4 (National Treatment) or Article 9.5 (Most-Favoured-Nation Treatment) depends on the totality of the circumstances, including whether the relevant treatment distinguishes between investors or investments on the basis of legitimate public welfare objectives.⁴⁹⁶

In another use of the phrase in the performance requirements provision of the TPP, Article 9.10 provides that the contracting States are excused from certain obligations if “adopting or maintaining measures to protect legitimate public welfare, provided that such measures are not applied in an arbitrary or unjustifiable manner, or in a manner that constitutes a disguised restriction on international trade or investment.”⁴⁹⁷ Finally, the “legitimate public welfare objectives” language is included in the annex of the TPP to

⁴⁹⁵ *Id.* annex 7, n. 25.

⁴⁹⁶ TPP, *supra* note 11, art. 9.4.

⁴⁹⁷ *Id.* art. 9.10.3(h).

explicitly provide for situations of indirect expropriations by stating that:

[Paragraph 3 omitted]

(b) Non-discriminatory regulatory actions by a Party that are designed and applied to protect legitimate public welfare objectives, such as public health [footnote omitted], safety and the environment, do not constitute indirect expropriations, except in rare circumstances.⁴⁹⁸

The phrase “legitimate public welfare objectives” may sometimes be replaced by another expression, “legitimate policy objectives,” but the difference is not immediately clear on its face. The preamble of the Canada-EU CETA states from the onset that the two Parties “[recognize] that the provisions of this Agreement preserve the right to regulate within their territories and resolving to preserve their flexibility to achieve legitimate policy objectives, such as public health, safety, environment, public morals and the promotion and protection of cultural diversity.”⁴⁹⁹ The Canada-EU CETA is noteworthy because it marks the first EU investment treaty that clarifies the relationship between legitimate public policy objectives and indirect expropriation. Annex X.11 on expropriation states that a question of indirect expropriation allegedly caused by a regulatory measure will be submitted to a factual inquiry that will ask, amongst others, the economic effect of the measure on a foreign investment, the length of the measure, and the extent to which the measure impedes with “distinct, reasonable

⁴⁹⁸ *Id.* annex 9-B [Expropriation], para. 3(b).

⁴⁹⁹ Canada-EU CETA, *supra* note 18, preamble.

investment-backed expectations,” and the object, context, and intent of the measure enacted by the State.⁵⁰⁰ Cognizant of the host State’s regulatory purpose and balancing the scope of NPM-like clauses, this Annex further clarifies that the parties understand that measures of legitimate public policy acts made for the protection of “health, safety and the environment” are permissible “except in the rare circumstance where the impact of the measure... is so severe in light of its purpose that it appears manifestly excessive.”⁵⁰¹ Chapter 28 of the Canada-EU CETA, which covers exceptions for the entire treaty, provides in Section B of the investment chapter a public order carve-out during the establishment phase of an investment; moreover, it also provides a public order carve-out in Section C of the investment chapter, which contains provisions on national treatment, MFN, and senior management and boards of directors.⁵⁰²

The TTIP, which is currently under negotiations, the protection granted in Article 2, titled “Investment and Regulatory Measures/Objectives,” clarifies in the expropriation annex that:

For greater certainty, except in the rare circumstance when the impact of a measure or series of measures is so severe in light of its purpose that it appears manifestly excessive, non-discriminatory measures of a Party that are designed and applied to protect legitimate public welfare objectives, such as the protection of public health, safety, environment or

⁵⁰⁰ *Id.* annex 8-A, para. 2.

⁵⁰¹ *Id.* annex 8-A.

⁵⁰² *Id.* art. 28.3.

public morals, social or consumer protection or promotion and protection of cultural diversity do not constitute indirect expropriation.⁵⁰³

As the TTIP negotiations continue, it remains to be seen whether Article 2 will be the only provision that carves out regulatory space for the contracting States or if a general exceptions provision, which is not currently included, will eventually also be considered. A similar model is available in the 2009 ASEAN Comprehensive Investment Agreement which also incorporates an expropriation provision whose effects may be curbed by a WTO-inspired general exceptions provision that enables an ASEAN member State to seek legal excuse after directly expropriating a foreign property.⁵⁰⁴

But, in general, pairing indirect expropriation with a phrase such as “legitimate public welfare” creates quite a bit of confusion since the expropriation annex simultaneously contains the phrase “to protect legitimate public welfare objectives, such as health, safety and the environment.”⁵⁰⁵ Lévesque condemns the inclusion of “what arguably is a police power exception *in addition to* a general exceptions provision” by contending that “it is not logical to have both provisions *if* the general exceptions provision was already meant to act as a ‘police power’ exception.”⁵⁰⁶ Questioning the soundness of such treaty practice, Alvarez

⁵⁰³ TTIP (draft), *supra* note 12, annex I, para. 3.

⁵⁰⁴ ASEAN Comprehensive Investment Agreement, art. 14(1) & annex 2, Feb. 26, 2009.

⁵⁰⁵ E.g., Canada Model FIPA, annex B-13(1) (2004); ASEAN-Australia-New Zealand FTA, Annex on Expropriation and Compensation & ch. 15, art. 1 [“General Exceptions”], Feb. 27, 2009.

⁵⁰⁶ Céline Lévesque, *The Inclusion of GATT Article XX exceptions in IIAs: A Potentially*

and Brink comment that “[a]n exception from compensation for a direct taking of property because the expropriating government was pursuing one of the public purposes enumerated in the GATT’s Article XX would not only be inconsistent with the BIT’s expropriation guarantee itself but also with the pre-existing customary Hull Rule.”⁵⁰⁷ Moreover, the fact that an expropriation is indirect⁵⁰⁸ ought not to exculpate the State from the duty to compensate so that “the classic requirement in investment treaties continues to apply” and compensation is due “even when acting without discrimination and for a compelling public interest.”⁵⁰⁹

B. Reservations

Contracting States may achieve a similar effect to the public order carve-out in IIAs by including a Schedule of Commitments and Reservations even if the actual agreement does not make such an inclusion. A schedule of reservations allows the State to enter into investment treaties while preserving some of their domestic interests by “exclud[ing] the domestic effects of some international laws which they regard as incompatible with

Risky Policy, in PROSPECTS IN INTERNATIONAL INVESTMENT LAW AND POLICY 363, 369 (Roberto Echandi & Pierre Sauvé eds., 2013).

⁵⁰⁷ Alvarez & Brink, *supra* note 481, at 342.

⁵⁰⁸ An example of a typical provision on indirect expropriation is selected from the 2012 U.S. Model BIT, annex B [Expropriation], para. 4(b) and is as follows:

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.

⁵⁰⁹ KURTZ, CONVERGING SYSTEMS, *supra* note 484, at 185.

the will of the domestic legislature.”⁵¹⁰ Schedules must be mutually agreed to by both contracting States, which usually use scheduling as a way of safeguarding certain interests during the pre-establishment stage. Contracting States may prefer to draft their Schedules using the negative list approach, which is when the substantive obligations of a treaty will apply across all economic sectors and to all governmental measures unless a reservation has been carved out in advance by the Contracting Party.⁵¹¹ This approach helps a host State to maintain its power to regulate by keeping certain sensitive sectors and policies out of the treaty scope. Under the negative list approach, existing non-conforming measures are carved out as exclusions from the treaty and the identification of certain sectors will enable the host State to bring in non-conforming measures in the future. U.S. BIT practice also favors the negative list approach and a mere handful of sectors relating to nuclear energy, customs brokerage services, and domestic air services are completely prohibited to foreign investors.⁵¹²

However, using reservations to preserve regulatory space may present unforeseen circumstances because the restrictions demanded by one

⁵¹⁰ BAŞAK ÇALI, *THE AUTHORITY OF INTERNATIONAL LAW: OBEDIENCE, RESPECT, AND REBUTTAL* 109 (Oxford Univ. Press 2015).

⁵¹¹ APEC IIA HANDBOOK, *supra* note 473, at 110.

⁵¹² See, e.g., U.S.-CHINA BUSINESS COUNCIL, *SUMMARY OF U.S. NEGATIVE LISTS IN BILATERAL INVESTMENT TREATIES* (2014), available at <https://www.uschina.org/sites/default/files/Negative%20list%20summary.pdf>. In addition to the U.S.-China BIT, negotiations for the negative list negotiation has brought on tension between the two countries with China demanding that the United States’ national security policy in China be narrowed while the United States has been requesting that the sectors banned to U.S. investors be truncated. *China, U.S. to Start Negative List BIT Negotiations*, XINHUANET (July 9, 2014), http://news.xinhuanet.com/english/china/2014-07/10/c_133472362.htm.

Contracting Party may change according to the treatment received from the other Contracting Party. In such a case, a host State will provide access to a sector otherwise closed off to foreign investors if its investors receive the same benefit in the other Contracting Party's country. Another major drawback of the negative list approach is that drafters must cautiously and painstakingly review all of the existing non-conforming measures and include them in the Schedule and/or Reservations because non-conforming measures that are not scheduled may become the subject of a dispute. The negative list approach, however, allows drafters to consider future non-conforming measures and alter existing measures without violating the treaty. For sectors that have been already excluded, States reserve their regulatory space. As seen in the Annexes of several FTAs, Contracting Parties provide two lists. The first list contains existing non-conforming measures not subject to further restrictions and the second list identifies certain sectors that may be subject to restrictive measures. But again, from a practical perspective, it would be extremely difficult for drafters to foresee all of the potential non-conforming measures.

An example of the public order carve-out set forth as a reservation is available in the Korea-U.S. FTA (2007). For example, the Foreign Investment Protection Act (FIPA) of Korea stipulates that foreign investment may be restricted, *inter alia*, if it "threatens the maintenance of national safety and public order."⁵¹³ Whereas Annex II of the Colombia Schedule provides an exception for public order based on the Colombian Constitution, the public order carve-out to national treatment with respect to the establishment,

⁵¹³ Foreign Investment Promotion Act (Korea), art. 4(2), Act No. 6643 (Jan. 26, 2002).

acquisition, and expansion of investments is carved out in Annex II of the Korean Schedule in the Korea-U.S. (KORUS) FTA in the following form:⁵¹⁴

1. Korea reserves the right to adopt, with respect to the establishment or acquisition of an investment, any measure that is necessary for the maintenance of public order pursuant to Article 4 of the *Foreign Investment Promotion Act* (2007) and Article 5 of the *Enforcement Decree of the Foreign Investment Promotion Act* (2007), provided that Korea promptly provides written notice to the United States that it has adopted such a measure and that the measure:

(a) is applied in accordance with the procedural requirements set out in the *Foreign Investment Promotion Act* (2007), *Enforcement Decree of the Foreign Investment Promotion Act* (2007), and other applicable law;

(b) is adopted or maintained only where the investment poses a genuine and sufficiently serious threat to the fundamental interests of society;

(c) is not applied in an arbitrary or unjustifiable manner;

(d) does not constitute a disguised restriction on investment; and

⁵¹⁴ For a detailed explanation of the exceptions of art. 4 of the FIPA, see Hi-Taek Shin & Julie A. Kim, *Balancing the Domestic Regulatory Need to Control the Inflow of Foreign Direct Investment Against International Treaty Commitments: A Policy-Oriented Study of the Korean Foreign Investment Promotion Act and the Korea-U.S. FTA*, 19 ASIA PAC. L. REV. 177, 188-92 (2011).

(e) is proportional to the objective it seeks to achieve.⁵¹⁵

The application of this carve-out has not yet been tested by an international arbitration tribunal, but Annex II of the Korean Schedule⁵¹⁶ may be interpreted as Korea's intention to make a horizontal reservation of future regulatory space across all sectors.⁵¹⁷ This may be possible because reservations in Annex II in order "to ensure that a party maintains flexibility to adopt or maintain measures that would be inconsistent with FTA disciplines."⁵¹⁸ Annex I of the Korean Schedule identifies five sectors affected by Article 4 of FIPA - agriculture and livestock, adult education, distribution services pertaining to agriculture and livestock, electric power industry, and the gas industry - to exempt existing laws that may violate the national treatment obligation required in KORUS FTA.⁵¹⁹ Moreover, if a dispute arises over whether a measure has been taken for the maintenance of public order, Annex II of the Korean Schedule permits the claimant to bring a claim using the ISDS system based on the ICSID Convention, UNCITRAL rules, or any other form of arbitration agreed between the

⁵¹⁵ Korea-U.S. FTA, *supra* note 111, annex II, Schedule of Korea.

⁵¹⁶ *Id.*

⁵¹⁷ Shin & Kim, *supra* note 514, at 186 ("Though not reciprocated in the United States Schedule of Annex II, the Korean Schedule of Annex II reserves the right of Korea to adopt more restrictive measures for all sectors concerning national treatment for the maintenance of public order.").

⁵¹⁸ U.S. INT'L TRADE COMM'N, U.S.-KOREA FREE TRADE AGREEMENT: POTENTIAL ECONOMY-WIDE AND SELECTED SECTORAL EFFECTS 6-8 (2007).

⁵¹⁹ Korea-U.S. FTA, *supra* note 111, annex I, Schedule of Korea.

Contracting Parties provided that Korea has adopted the measure that it gave prompt, written notice to the United States and that the claimant suffered a loss or damage as a result of the measure. However, in the case that Korea is able to satisfy its burden of proof according to the criteria enumerated above in subparagraphs (a) through (e) of paragraph 1, then no award will be granted to the claimant.⁵²⁰

This template was used again in Annex II of the Korean Schedule in Korea-Australia FTA (KAFTA)⁵²¹ with the minor exception that KAFTA refers to the 2012 version of the Foreign Investment Promotion Act and the Enforcement Decree of the Foreign Investment Promotion Act. The KAFTA feasibility joint study conducted in April 2008 reiterates Korea's position that restrictions to FDI are not permissible except when a sector has been positively identified or affects "national security, public order, public health, environmental preservation or social morals."⁵²² Negotiated after Australia's public backlash against the ISDS system, the investment chapter of KAFTA claims to contain several safeguards that would enable Parties a greater exercise of their discretion when regulating "public welfare" objectives. The meaning of "public welfare" is not exact, and its relationship to public order not readily discernible, but may be inferred to include environmental, cultural, and public health policies.⁵²³

⁵²⁰ Korea-U.S. FTA, *supra* note 111, annex II, Schedule of Korea.

⁵²¹ Korea-Australia FTA, *supra* note 34.

⁵²² ITS GLOBAL & KOREAN INST. FOR INT'L ECON. POL'Y, AUSTRALIA - REPUBLIC OF KOREA FREE TRADE AGREEMENT FEASIBILITY STUDY 88 (Apr. 17, 2008), <http://dfat.gov.au/trade/agreements/kafta/Documents/rok-au-study-report.pdf>.

⁵²³ Letter of Submission from Dr. Jeffrey D. Wilson, Professor at Murdoch Univ., to

The scheduling of reservations permits host State to achieve a sense of balance by having the opportunity to preserve their regulatory power without having to feel completely helpless when dealing with foreign investors. When host States carve-out reservations and specify sectors that will remain closed off to foreign investment, it offers a chance for them to consider their foreign investment policies while protecting the State from investor claims and unexpected financial liabilities. Scheduling reservations is just one of a few avenues that States can use to absolve themselves from facing major liabilities and may operate with other provisions within the IIA such as on General Exceptions or Exclusions from the Scope of Investor-State Dispute Settlement. Some BITs like that between Korea and Kuwait (2004)⁵²⁴ and India and Nepal (2011)⁵²⁵ do not contain a Schedule of Reservations or general exceptions provision. IIAs may be drafted in this way if, for example, the Contracting Parties do not anticipate that non-conforming measures will be enacted after the conclusion of the treaty.

C. National Security

National security exceptions cover an area that is different from what the public order carve-out aims to regulate, but should be discussed because the two provisions often appear together especially in the earlier BITs. National security exceptions enable States to set aside security concerns from

Senate Foreign Affairs, Defence and Trade References (Aug. 22, 2014), *available at* <http://www.aph.gov.au/DocumentStore.ashx?id=24d1215e-6bc9-4bf1-a3a4-fffbac2c42d0&subId=299349>.

⁵²⁴ Korea-Kuwait BIT, July 15, 2004.

⁵²⁵ India-Nepal BIT, Oct. 21, 2011 (containing, however, a denial of benefits clause in art. 14).

the purview of the international investment agreement, thus giving room to States that desire to balance their sovereign interests while maintaining their promises on investor protection. The scope of the national security exception as used in IIAs is broad including areas such as essential security interest, public order, international peace and security, and certain information.⁵²⁶ Unlike today's IIAs, previous generations of BITs frequently do not contain the national security provision. Some modern national security clauses are framed on Article XXI of the GATT and Article XIV *bis* of the GATS. Other IIAs merge the national security provision into the general exceptions article or completely omit the provision on national security so that it simply exists under the heading "Essential Security Interests." Some IIAs insert an open construction of the national security clause by using a term like "public security," which is not defined in the underlying treaty.⁵²⁷ In FTAs with investment chapters, the national security provision may be a standalone chapter or article that applies not only to the investment chapter, but to the broader treaty as well. Whichever form the national security clause takes, there must be a nexus between the measure and the situation. Below are some examples of the aforementioned variations on the national security clause. The Hungary-Russian Federation BIT (1995) uses the term "national security" as follows:

This Agreement shall not preclude the application of either Contracting Party of measures, necessary for the maintenance of defence, national security and public order, protection of

⁵²⁶ WIR 2014, *supra* note 15, at 125.

⁵²⁷ *Id.* at 126.

the environment, morality and public health.⁵²⁸

However, the U.S. Model BITs have since the start of the U.S. BIT program used the term “essential security interests” instead of the term “national security.” Under the heading “Measures Not Precluded by Treaty,” Article 10 of the first U.S. Model BIT drafted in 1982 provides the following:

1. This Treaty shall not preclude the application by either Party or any political subdivision thereof of (a) any and all measures necessary for the maintenance of public order and morals, the fulfillment of its obligations with respect to the maintenance or restoration of international peace or security, or the protection of its own essential security interests; or (b) any and all measures regarding the ownership of real property within its territory.

Article 18 of 2012 U.S. Model BIT has the heading “Essential Security” and also limits access to sensitive information by providing that:

Nothing in this Treaty shall be construed:

1. to require a Party to furnish or allow access to any information the disclosure of which it determines to be contrary to its essential security interests; or
2. to preclude a Party from applying measures that it considers necessary for the fulfillment of its obligations with respect to the maintenance or restoration of international peace or security, or the protection of its own essential security interests.

⁵²⁸ Hungary-Russia BIT, *supra* note 383, art. 2.

Another variation using the phrase “essential security interests” is placed in the Mauritius BIT with the Belgium and Luxembourg European Union (BLEU) (2005):

The provisions of this Agreement shall not in any way limit the right of either Contracting Party to apply prohibitions or restrictions of any kind or take any other action, which is directed to the protection of its essential security interests, or to the protection of public health or the prevention of diseases and pests in animals or plants.⁵²⁹

The Macedonia-Morocco BIT (2010) uses a broader term than national security by using the term “public security” as follows:

Nothing in this Agreement shall be construed to prevent a Contracting Party from taking any action that is considered as necessary for the protection of public security, order or public health or protection of environment, provided that such measures are not applied in a manner which would constitute a means of arbitrary or unjustified discrimination.⁵³⁰

Recognizing that the term “national security” raises a vagueness issue since IIAs typically do not define them, some national security provisions contain an exhaustive list of specific situations like the protection of strategic industries or in time of a war or an armed conflict to narrow down the cases in which States may invoke the exception. Under this

⁵²⁹ Mauritius-BLEU BIT, art. 14, Nov. 30, 2005.

⁵³⁰ Macedonia-Morocco BIT, *supra* note 450, art. 2.

comprehensive list approach, which is better associated with FTAs than in BITs,⁵³¹ at least one of the listed conditions must be present. Since the national security clause will become more difficult to invoke, Contracting Parties will deal with greater certainty and predictability and provide a disincentive to protecting strategic industries.⁵³² For example, the India-Malaysia Comprehensive Economic Cooperation Agreement (CECA) (2011) enumerates four specific circumstances relating to the State's essential security interests that require a severe crisis like war or other emergency case which must exist in order to trigger the national security exception. Moreover, this provision is not contained in the investment chapter but in the chapter providing for general exceptions. Article 12.2 on "Security Exceptions" of the India-Malaysia CECA states the following:

Nothing in this Agreement shall be construed:

[...]

(b) to prevent a Party from taking any actions which it considers necessary for the protection of its essential security interests:

(i) relating to the traffic in arms, ammunition and implements of war and to such traffic in other goods and materials or relating to the supply of services as carried on, directly or indirectly, for the purpose of supplying

⁵³¹ UNCTAD, *Protection*, *supra* note 452, at 85.

⁵³² *Id.* at 88.

or provisioning a military establishment;

- (ii) taken in time of war or other emergency in international relations;
- (iii) relating to fissionable and fusionable materials or the materials from which they are derived; or
- (iv) relating to protection of critical public infrastructure, including communications, power and water infrastructure from deliberate attempts intended to disable or degrade such infrastructure [...].⁵³³

Article 18 of the China-Japan-Korea Trilateral Investment Treaty (2012) also contains an exhaustive list of the circumstances that enable States to invoke the national security exception:

1. Notwithstanding any other provisions in this Agreement other than the provisions of Article 12 [covering compensation for losses or damages due to armed conflict or civil strife], each Contracting Party may take any measure:

(a) which it considers necessary for the protection of its essential security interests:

- (i) taken in time of war, or armed conflict, or other emergency in that Contracting Party or in international

⁵³³ India-Malaysia CECA, art. 12.2, Feb. 18, 2011.

relations; or

(ii) relating to the implementation of national policies or international agreements respecting the non-proliferation of weapons;

(b) in pursuance of its obligations under the United Nations Charter for the maintenance of international peace and security.⁵³⁴

In addition to being present in the general exceptions provision, the national security provision may be present along with the public order clause. Measures necessary for the maintenance of public order may take effect due to a number of factors such as economic crises or civil disturbances. An example is in Article X of the Bangladesh-U.S. BIT (1986) which states the following:

This Treaty shall not preclude the application by either Party of any and all measures necessary for the maintenance of public order, the fulfilment of its obligations with respect to the maintenance or restoration of international peace or security, or the protection of its own essential security interests.⁵³⁵

In Article 15 of the Columbia-Japan BIT (2011), the vagueness of the term “public order” within the national security provision is addressed in a note following the public order clause as follows:

⁵³⁴ China-Japan-Korea Trilateral Investment Treaty, art. 18, May 13, 2012.

⁵³⁵ Bangladesh-U.S. BIT, *supra* note 416, art. X.

1. [...] nothing in this Agreement other than Article 12 [Treatment in Case of Strife] shall be construed to prevent that former Contracting Party from adopting or enforcing measures [...]:

(b) necessary to protect public morals or to maintain public order;

Note: The public order exception may be invoked only where a genuine and sufficiently serious threat is posed to one of the fundamental interests of society.⁵³⁶

A specific circumstance sometimes mentioned in the national security provision is for the protection of international peace and/or security. This broadens the scope of the national security exception because it permits States to invoke the exception even if the conflict does not directly affect it. Perhaps foreseeing the chance for abuse, some BITs limit international obligations to those that occur from the United Nations Charter. Article X of Bangladesh-U.S. BIT (1986) uses a generic formulation for national security in international situations:

1. This Treaty shall not preclude the application by either Party of any and all measures necessary for the maintenance of public order, the fulfilment of its obligations with respect to the maintenance or restoration of international peace or security, or the protection of its own essential security interests.⁵³⁷

⁵³⁶ Colombia-Japan BIT, *supra* note 449, art. 15.1.

⁵³⁷ Bangladesh-U.S. BIT, *supra* note 416, art. X.1.

However, the Canada-Jordan BIT (2009) requires its Contracting Parties to limit international obligations to those that arise from the United Nations Charter:

4. Nothing in this Agreement shall be construed:

[...]

(c) to prevent any Party from taking action in pursuance of its obligations under the *Charter of the United Nations* [sic] for the maintenance of international peace and security.⁵³⁸

National security exception may concern prohibiting the dissemination of certain information when counter to essential security interests. Such a carve-out may be needed when an IIA contains a transparency obligation or to prevent the disclosure of sensitive information in investor-State arbitration proceedings. Article 10 of the Canada-Jordan BIT (2009) shows a typical example:

4. Nothing in this Agreement shall be construed:

(a) to require any Party to furnish or allow access to any information the disclosure of which it determines to be contrary to its essential security interests; [...].⁵³⁹

Under the heading “Transparency of Arbitral Proceedings,” Article 26 of the ASEAN-Australia-New Zealand FTA (2009) specifically forbids the release of certain information in a tribunal setting:

⁵³⁸ Canada-Jordan BIT, art. 10, para. 4, June 28, 2009.

⁵³⁹ *Id.*

The tribunal shall not require a Party to furnish or allow access to information the disclosure of which would impede law enforcement or would be contrary to the Party's law protecting Cabinet confidences, personal privacy or the financial affairs and accounts of individual customers of financial institutions, or which it determines to be contrary to its essential security.⁵⁴⁰

Although more commonly seen in the general exceptions provisions, some national security exceptions contain safeguards against arbitrary or unjustifiable discrimination between investments or between investors, or a disguised restriction on international trade or investment. This language is more frequent in general exceptions than national security exceptions because the latter usually gives States full discretion. Other formulations have included the requirement that the measure must be in accordance with domestic laws or that a Contracting Party will not use the measure in order to avoid its obligations. These requirements against abuse of the national security exception has not been addressed in investor-State proceedings. For example, Article 2 of the Macedonia-Morocco BIT (2010) provides that a measure not be applied arbitrarily or for discrimination:

Nothing in this Agreement shall be construed to prevent a Contracting Party from taking any action that is considered as necessary for the protection of public security, order or public health or protection of environment, provided that such measures are not applied in a manner which would

⁵⁴⁰ ASEAN-Australia-New Zealand FTA, *supra* note 505, art. 26.

constitute a means of arbitrary or unjustified discrimination.⁵⁴¹

Article 13 of the India-Lithuania BIT (2011) contains another variation of the national security exception:

Nothing in this Agreement precludes the host Contracting Party from taking action for the protection of its essential security interests or in circumstances of extreme emergency in accordance with its laws normally and reasonably applied on a non-discriminatory basis.⁵⁴²

Article 18 of the China-Japan-Korea Trilateral Investment Treaty (2012) prohibits using national security measures as a means of avoiding its treaty obligations:

2. In cases where a Contracting Party takes any measure, pursuant to paragraph 1 [covering security exceptions], that does not conform with the obligations of the provisions of this Agreement other than the provisions of Article 12 [covering compensation for losses or damages due to armed conflict or civil strife], that Contracting Party shall not use such measure as a means of avoiding its obligations.⁵⁴³

Contracting Parties reserve the highest degree of autonomy when measures taken under the national security provision are excluded from judicial review. Although this type of drafting is rare because of the potential

⁵⁴¹ Macedonia-Morocco BIT, *supra* note 450, art. 2.

⁵⁴² India-Lithuania BIT, art. 13, Mar. 31, 2011.

⁵⁴³ China-Japan-Korea Trilateral Investment Treaty, *supra* note 536, art. 18, para. 2.

for abuse of the national security exception, a few IIAs such as the India-Malaysia CECA (2011) provides the following in its annex titled “Non-Justiciability of Security Exceptions”:

With respect to the interpretation and/or implementation of this Chapter, the Parties confirm their understanding that disputes submitted to arbitration pursuant paragraphs 7 and 8 of Article 10.14 (The Settlement of Investment Disputes between a Party and an Investor of the Other Party), where the disputing Party asserts as a defence that the measure alleged to be a breach is within the scope of a security exception as set out in Article 12.2 (Security Exceptions), any decision of the disputing Party taken on such security considerations shall be nonjusticiable in that it shall not be open to any arbitral tribunal to review the merits of any such decision, even where the arbitral proceedings concern an assessment of any claim for damages and/or compensation, or an adjudication of any other issues referred to the tribunal.⁵⁴⁴

A more succinct variation is offered in Article 12 of the Mexico-Netherlands BIT (1998):

The dispute settlement provisions of this Schedule shall not apply to the resolutions adopted by a Contracting Party for national security reasons.⁵⁴⁵

⁵⁴⁴ India-Malaysia CECA, *supra* note 533, annex 12-2.

⁵⁴⁵ Mexico-Netherlands BIT, art. 12, May 13, 1998.

The national security exception may also prevent the justiciability of investment disputes arising from such a context. Article 23 of the Iceland-Mexico BIT (2005) excludes investor-State proceedings if the measures are in connection to the acquisition of a domestic investment:

The dispute settlement provision... shall not apply to the resolutions adopted by a Contracting Party which, for national security reasons, prohibit or restrict the acquisition of an investment in its territory, owned or controlled by its nationals, by investors of the other Contracting Party, according to the legislation of each Contracting Party.⁵⁴⁶

Some questions may arise as to the relationship between the national security exception and another provision that enables compensation for losses incurred due to armed conflict or civil strife because they often apply and arise out of the same event. Some IIAs clarify the relationship to allow both provisions to operate simultaneously as in Article 15 of the Japan-Vietnam BIT (2003):

1. Notwithstanding any other provisions in this Agreement other than the provisions of Article 10 [covering compensation for losses due to armed conflicts and civil strife], each Contracting Party may:

(a) take any measure which it considers necessary for the protection of its essential security interests; [...].⁵⁴⁷

⁵⁴⁶ Iceland-Mexico BIT, art. 23, June 24, 2005.

⁵⁴⁷ Japan-Vietnam BIT, art. 15, Nov. 14, 2003.

Another example is in Article 15 of the Colombia-Japan BIT (2011) and this variation requires information disclosure for cases arising out of the civil strife clause:

2. Nothing in this Agreement other than Article 12

[Treatment in case of Strife] shall be construed:

- (a) to require a Contracting Party to furnish or to allow access to any information whose disclosure would be contrary to its essential security interests;
- (b) to prevent a Contracting Party from taking any action which it considers necessary for the protection of its essential security interests: [...].⁵⁴⁸

Moreover, some IIAs do not contain any exception for national security perhaps to grant the highest level of investor protection, but at the risk of subordinating a State's essential security interests. Explicitly including a national security provision is preferable because it creates a better level of certainty and predictability in case of an investor-State dispute. Contracting Parties that opt to exclude the national security provision may do so relying on other safeguarding provisions in the agreement such as those on general exceptions and other reservations and/or carve-outs that exempt certain measures and/or industries from treaty obligations. The Australia-Mexico BIT (2005), Barbados-Canada BIT (1996), and the China-Guyana BIT (2003) all do not contain a national security provision. While the 2004 Canadian Model BIT is silent on national security, the Canada-China BIT provides in an annex a carve-out for national security that

⁵⁴⁸ Colombia-Japan BIT, *supra* note 449, art. 15, para. 2.

excludes the application of disputes between the Contracting Parties (Article 15) and the entire Part C covering investor-State arbitration claims.⁵⁴⁹ Specifically, Canada merely states in Annex D.34 that foreign investments potentially affecting national security will be screened in accordance to the Investment Canada Act while China provides extra clarification of the phrase “national security review” in a separate footnote.⁵⁵⁰

D. Essential Security Interest

Whether the term “essential security interest” might merit a narrower interpretation than “national security” was evaluated in a 2009 study by UNCTAD, but it concluded that “it is far from obvious that Contracting Parties, by choosing one of these alternatives, actually intended to introduce such a distinction” and further observed that the task of clarifying these terms should be left to the arbitral tribunals.⁵⁵¹ While the origins of “national security” in IIAs may have evolved from fear of military threats or other similar acts, the UNCTAD study acknowledged that the contemporary meaning of “national security” could reasonably include issues relating to

⁵⁴⁹ Canada-China BIT, annex D.34, Sep. 9, 2012 (unlike its China counterpart, Canada has not appended a footnote explaining the term “national security review”).

⁵⁵⁰ *Id.* annex D.34, n. 13 stating that:

For China, ‘national security review’ may include a review of various forms of investments for national security purposes. At the time of the entry into force of this Agreement, the specific legal document on China’s national security review is the *Circular of the General Office of the State Council on the Establishment of the Security Review System For The Merger and Acquisition of Domestic Enterprises by Foreign Investors*, focusing on the review of mergers and acquisitions of domestic enterprises by foreign investors.

⁵⁵¹ UNCTAD, *Protection*, *supra* note 452, at 73.

public health and the environment in addition to other events that undermine the political, economic, financial, cultural, or social stability of a State⁵⁵² as detailed in Article 2 of the Hungary-Russia BIT (1995):

This Agreement shall not preclude the application of either Contracting Party of measures, necessary for the maintenance of defence, national security and public order, protection of the environment, morality and public health.⁵⁵³

In contrast, the NPM provision in Article XI of the U.S.-Argentina BIT (1991) opts for the term “essential security interests” and makes no mention of the term “national security” in the entire BIT:

This Treaty shall not preclude the application by either Party of measures necessary for the maintenance of public order, the fulfillment of its obligations with respect to the maintenance or restoration of international peace or security, or the protection of its own essential security interests.⁵⁵⁴

Article 18 under the heading “Essential Security” of the 2004 and 2012 U.S. Model BIT provides that:

Nothing in this Treaty shall be construed:

1. to require a Party to furnish or allow access to any information the disclosure of which it determines to be contrary to its essential security interests; or

⁵⁵² See *id.* at 7.

⁵⁵³ Hungary-Russia BIT, *supra* note 383, art. 2.

⁵⁵⁴ U.S.-Argentina BIT, *supra* note 178, art. XI.

2. to preclude a Party from applying measures that it considers necessary for the fulfillment of its obligations with respect to the maintenance or restoration of international peace or security, or the protection of its own essential security interests.

Although the draft MAI was never realized, the article titled “General Exceptions” also used the term “essential security interests” to the exclusion of “national security” to cover the protection of essential security interests related to times of war, armed conflict, or other emergency in international relations; or, to the implementation of national policies or international agreements respecting the non-proliferation of weapons of mass destruction; or, to arms production.⁵⁵⁵

While countries like Brazil, Denmark, Greece, Italy, and South Africa have never included an essential security interest provision, the United States has always included it in its BITs and FTAs with investment chapters.⁵⁵⁶ Moreover, the scope of the essential security interest provisions differs by IIA. The essential security provision in Article XI of the U.S.-Argentina BIT is not defined by a specific set of situations. States will change the scope of this open formulation depending on the priorities and concerns of the country. For example, the 2007 Colombian Model BIT intentionally restricts the scope of the essential security interests provision so that the Contracting Parties can regulate against investments that are derived from illegal activities:

⁵⁵⁵ Draft MAI, *supra* note 139, ch. VI [“Exceptions and Safeguards”].

⁵⁵⁶ OECD, ESSENTIAL SECURITY INTERESTS, *supra* note 378, at 98.

3. Nothing contained in this Agreement shall bind either Contracting Party to protect investments made with capital or assets derived from illegal activities, and it shall not be construed so as to prevent a Party from adopting or maintaining measures intended to preserve public order, the fulfilment of its duties for the keeping or restoration of international peace and security; or the protection of its own essential security interests.⁵⁵⁷

The essential security interest provision in the 2004 Canadian Model BIT is also limited to specific circumstances and while not tested in an investor-State proceeding may exclude economic crises when interpreted as an exhaustive list:⁵⁵⁸

4. Nothing in this Agreement shall be construed:
- (b) to prevent any Party from taking any actions that it considers necessary for the protection of its essential security interests
 - (i) relating to the traffic in arms, ammunition and implements of war and to such traffic and transactions in other goods, materials, services and technology undertaken directly or indirectly for the purpose of supplying a military or other security establishment,

⁵⁵⁷ Colombia Model BIT, *supra* note 424, art. II.3.

⁵⁵⁸ UNCTAD, *Protection*, *supra* note 452, at 85.

(ii) taken in time of war or other emergency in international relations, or
(iii) relating to the implementation of national policies or international agreements respecting the non-proliferation of nuclear weapons or other nuclear explosive devices [...].⁵⁵⁹

To avoid the question of whether a grave crisis is within the scope of the essential security interests provision, some provisions will clarify that the list of circumstances is not exhaustive. An example is in the provision titled “Security” in the New Zealand-Singapore CEPA (2000) providing that:

Nothing in this Agreement shall be construed:

(a) as preventing either Party from taking any action which it considers necessary for the protection of its essential security interests, including **but not limited to** action relating to traffic in arms, ammunition and implements of war and to such traffic in other goods and materials as is carried on directly or indirectly for the purpose of supplying a military establishment, and any action taken in time of war or other emergency in domestic or international relations [...].⁵⁶⁰

In another variation of the essential security interests provision, the

⁵⁵⁹ Canada Model FIPA, *supra* note 505, art. 10.

⁵⁶⁰ New Zealand-Singapore CEPA, *supra* note 458, art. 76(a).

phrase “serious internal disturbances” is used to describe situations that affect the maintenance of law and order theoretically expanding the scope of this provision to include grave economic crises. For instance, Article 83 of the Association Agreement between EU and Egypt (2001) provides the following:

Nothing in this Agreement shall prevent a Party from taking any measures:

[...]

(c) which it considers essential to its own security in the event of **serious internal disturbances** affecting the maintenance of law and order, in time of war or serious international tension constituting threat of war or in order to carry out obligations it has accepted for the purpose of maintaining peace and international security.⁵⁶¹

Although the inclusion of the essential security interest provision constitutes a small part of international investment agreements, its growth has been remarkable with more than half of the IIAs concluded in 2015 containing a self-judging essential security interest provision.⁵⁶² Narrow essential security interest provisions limit the scope of self-judging to specific subjects. However, broad essential provisions carry the risk of giving a wide amount of discretion to host States in the absence of any defined conditions

⁵⁶¹ EU-Egypt Association Agreements, art. 83(c), June 25, 2001.

⁵⁶² Karl P. Sauvant et al., *The Rise of Self-Judging Essential Security Interest Clauses in International Investment Agreements*, COLUMBIA CTR. ON SUSTAINABLE INVESTMENT (Dec. 5, 2016), <http://ccsi.columbia.edu/files/2016/10/No-188-Sauvant-Ong-Lama-and-Petersen-FOR-WEBSITE-FINAL.pdf>.

or restrictions.

III. Concluding Remarks

The broad nature of the public order concept and the multiple meanings associated with the term have been presented in this Chapter to reveal that the States' understanding of the concept of public order is ultimately difficult to know and perhaps even more difficult for the investor-State tribunals to apply in case of an investment dispute. Some public order carve-out provisions require that the measure not be applied arbitrarily or discriminatorily sometimes also appending a clarification note stating that public order may be invoked only for a genuine and sufficiently serious threat against the fundamental interests of society. The motivation behind such efforts is because of the reality that interpretation of the public order carve-out would be subject to the reality of indeterminacy, which is what makes international investment law both so acceptable and unacceptable.⁵⁶³

The inclusion of a public order carve-out is not prevailing investment treaty practice, but has existed in the early treaties like FCNs, then BITs, and in the current IIAs. The States' intention for including the public order carve-out since the beginning of investment treaties may have been for it to perform, at the minimum, a mitigating role to the substantive treaty obligations that are traditionally pro-investor when an exceptional situation as set forth in the agreement arises. Under current IIA practice, the public order carve-out may have been treated as a source of aggravation that creates indeterminacies within international investment law because the public order carve-out functions as an exception to a rule in a treaty-based system

⁵⁶³ See SAVERIO DI BENEDETTO, *INTERNATIONAL INVESTMENT LAW AND THE ENVIRONMENT* 218-19 (Edward Elgar Pub. 2013).

where BITs typically contain obligations and no exceptions provisions. Another emerging practice has been to avoid the use of the term “public order,” possibly due to the fact that a consensus has been hard to attain for the States.⁵⁶⁴ Regardless, some contracting States attempt to achieve a similar effect that can preserve their regulatory space by weaving provisions that allow for the pursuit of legitimate public welfare objectives and other public interest concerns into the substantive provisions of the investment treaty. Such an approach may better assist the investment tribunals to identify where the contracting States intended to have the public order carve-out apply and views it in combination with the substantive provision that the public order carve-out is embedded in. This rationale is appealing because the scope of the public order carve-out should follow a balanced approach since a methodical framework that factors in public purposes is underdeveloped especially in international investment law.⁵⁶⁵ When interpreting the public order carve-out, the struggle for investor-State tribunals arises because an exaggerated sense of equilibrium that includes cases which should have been excluded and *vice versa* ultimately weakens rules and “compels the move to ‘discretion’ which it was the very purpose to avoid.”⁵⁶⁶ But an approach that embeds the public order carve-out as limiter of a substantive IIA obligation may help investment tribunals to better balance the purpose of IIAs and the need for host State to retain their regulatory authority in specific circumstances.

⁵⁶⁴ See ch. 3 of this Dissertation.

⁵⁶⁵ Sabanogullari, *supra* note 286.

⁵⁶⁶ MARTTI KOSKENNIEMI, FROM APOLOGY TO UTOPIA: THE STRUCTURE OF INTERNATIONAL LEGAL ARGUMENT 591-92 (Cambridge Univ. Press 2005).

Chapter 4: Treatment of the Public Order Carve-out by the ICSID Tribunals in Cases Arising out of the U.S.-Argentina BIT

I. Fact Pattern of the Argentine ICSID Cases

The ICSID cases addressing the NPM provision in Article XI of the U.S.-Argentina BIT discussed in this Dissertation (listed here in the order of the award date) have been between Argentina and *CMS*, *Enron*, *LG&E*, *Sempra*, and *Continental Casualty*. These cases are given special focus in this Dissertation because they have been instrumental in bringing spotlight attention to the need for host States to be able to take certain regulatory interests without breaching investment treaty obligations. Although these cases were brought before the ICSID tribunal in the early 2000s, since the final annulment decision in 2010, the IIA stakeholders have yet to determine how to balance interests by enabling States to preserve their regulatory space leaving this as a still very much unsettled issue in international investment law. In addition, according to the 2016 World Investment Report, the U.S.-Argentina BIT is the most frequently sought BIT from which ISDS claims occur where the majority of the claims arise from the emergency measures that Argentina adopted during its economic crisis.⁵⁶⁷ Argentina has countered this claim by arguing that it was entitled to enact the emergency act under Article XI of the U.S.-Argentina BIT as provided below:

⁵⁶⁷ WIR 2016, *supra* note 13, at 105 (stating that 20 investor-State arbitration cases arose out of the U.S.-Argentina BIT in 2015). See also Julia Calvert, *State Strategies for the Defence of Domestic Interests in Investor-State Arbitration*, 7 INVESTMENT TREATY NEWS (Feb. 2016), <http://www.iisd.org/itn/wp-content/uploads/2016/02/iisd-itn-february-2016-english.pdf>.

This Treaty shall not preclude the application by either Party of measures necessary for the maintenance of public order, the fulfillment of its obligations with respect to the maintenance or restoration of international peace or security, or the protection of its own essential security interests.⁵⁶⁸

The most controversial aspect of this provision is related to the interpretation of the term “necessary.” As will be seen in the Argentine ICSID tribunals’ reasoning of this NPM provision, the *Enron*, *Sempra*, and *CMS* tribunals conflated the customary law on necessity with the terms of the NPM provision while the *LG&E* and *Continental Casualty* tribunals relied on the primary/secondary approach.⁵⁶⁹ Especially controversial is the “only way” element contained in Article 25 of the ILC, which was accepted by all of the Argentine ICSID tribunals as the codification of the customary law on necessity, because a literal interpretation excludes the application of the defense if an alternative measure existed for the host State regardless of factors such as time, cost, and effectiveness of implementing such an alternative.

In deciding that Argentina did not meet the burden of proof under the customary law on necessity, the ICSID tribunals in *CMS*, *Enron*, and *Sempra* determined that there would be no need to analyze the NPM provision of the U.S.-Argentina BIT.⁵⁷⁰ Despite the same fact pattern and

⁵⁶⁸ U.S.-Argentina BIT, art. XI.

⁵⁶⁹ See Kurtz, *Adjudging Security*, *supra* note 183.

⁵⁷⁰ *CMS v. Argentina*, *supra* note 179, para. 373; *Enron v. Argentina*, *supra* note 179, para. 339; *Sempra v. Argentina*, *supra* note 179, para. 391.

respondent State, the *Continental Casualty* and *LG&E* tribunals decided differently from the other three cases mentioned here to find that the emergency measures were necessary to maintain the public order and essential security interest of Argentina.⁵⁷¹ Nonetheless, in all five of these cases, the ICSID tribunals concluded that Argentina could not properly resort to the defense provided under ILC Article 25 because its emergency measure did not satisfy the “only way” and/or the “no State contribution” requirement.⁵⁷² Article 25 of the ILC states the following criteria:

1. Necessity may not be invoked by a State as a ground for precluding the wrongfulness of an act not in conformity with an international obligation of that State unless the act:

- (a) is the only way for the State to safeguard an essential interest against a grave and imminent peril;
- and

⁵⁷¹ *LG&E v. Argentina*, *supra* note 179, para. 266; *Continental Casualty v. Argentina*, *supra* note 179, para. 192.

⁵⁷² In addition to the five Argentine ICSID cases discussed in this Dissertation, the investment tribunals sitting in other cases involving Argentina as the respondent State also decided that Argentina did not meet the conditions of ILC Article 25. The following cases did not arise out of the U.S.-Argentina BIT, but was initiated by other BITs concluded by Argentina and do not contain a NPM provision. Here, the tribunals considered Argentina’s necessity defense under customary international law and decided that Argentina’s burden of proof under the strict requirements of the customary necessity defense was not met. *See National Grid v. Argentina*, UNCITAL, Award, paras. 259-260 (Nov. 3, 2008); *Suez/Vivendi, Decision on Liability*, *supra* note 163, paras. 260 [“only way”] & 263 [“contribution”]; *Impregilo v. Argentina*, ICSID Case No. ARB/07/17, Award, paras. 356-59 [“contribution”] (June 21, 2011).

(b) does not seriously impair an essential interest of the State or States towards which the obligation exists, or of the international community as a whole.

2. In any case, necessity may not be invoked by a State as a ground for precluding wrongfulness if:

- (a) the international obligation in question excludes the possibility of invoking necessity; or
- (b) the State has contributed to the situation of necessity.⁵⁷³

From 2001 to 2002, Argentina went through a serious economic breakdown that forced the government to default on its debt, implement bank freezing measures to prohibit withdrawals beyond a certain amount and overseas transfers through a series of measures known as *corralito*, and impose foreign exchange controls.⁵⁷⁴ In the wake of the plummeting Argentina peso,⁵⁷⁵ which had been previously fixed to the U.S. dollar, the government enacted on January 6, 2002 the Public Emergency and Exchange

⁵⁷³ State Responsibility Draft with Commentaries, *supra* note 367, art. 25, at 80.

⁵⁷⁴ Marie Thjoernelund, *State of Necessity as an Exemption from State Responsibility for Investments*, in 13 MAX PLANCK YEARBOOK OF UNITED NATIONS LAW 423, 440-41 (Armin von Bogdandy et al. eds., 2009). See JIM SAXTON, U.S. CONGRESS JOINT ECON. COMMITTEE, ARGENTINA'S ECONOMIC CURES: CAUSES AND CURES 12 (2003), available at <http://www.hacer.org/pdf/Schuler> (stating that the bank freeze from December 2001 was due to the large withdrawals that occurred in the previous month).

⁵⁷⁵ ANNAMARIA VITERBO, INTERNATIONAL ECONOMIC LAW AND MONETARY MEASURES: LIMITATIONS TO STATES' SOVEREIGNTY AND DISPUTE SETTLEMENT 262 (Edward Elgar Pub. 2012) (remarking that almost 40% of the peso had lost its value at one point in the end of 2001).

Regime Reform Act (the Emergency Act).⁵⁷⁶ The Emergency Act, which officially declared social, economic, administrative, financial, and foreign exchange public emergency, unpegged the peso from the dollar to allow the Argentinean currency to freely float and depreciate.⁵⁷⁷ The value of foreign investments tanked and investors were outraged by the “pesification” that resulted because bank loans, credits, contracts, and all other assets originally secured in the U.S. dollar were forcibly converted into the devaluing pesos.⁵⁷⁸ As the economic, social, and political structure of Argentina deteriorated, the public displayed their anger in violent street demonstrations leading key politicians to resign including the seeing of five different presidents in the course of ten days.⁵⁷⁹ Ultimately, dissatisfied

⁵⁷⁶ See generally Jeanne C. Olivier, *Political Risk Insurance: A Valuable Product?*, 4 LATINLAWYER (Mar. 1, 2005), http://www.shearman.com/~media/Files/NewsInsights/Publications/2005/02/Political-Risk-Insurance-A-Valuable-Product/Files/Download-PDF-Political-Risk-Insurance-A-Valuable_/FileAttachment/pdf_latinlawyer.pdf.

⁵⁷⁷ On January 6, 2002, the Argentine government approved the Public Emergency and Foreign Exchange Regime Reform Act No. 25,561 enacted by Executive Order No. 50/2002. See also VITERBO, *supra* note 575, at 262.

⁵⁷⁸ VITERBO, *supra* note 575, at 262.

⁵⁷⁹ E.g., *Demonstrators Bang Pots, Pans to Protest Argentina's Policies*, CNN, Nov. 9, 2012, <http://edition.cnn.com/2012/11/08/world/americas/argentina-protests>; Marc Rogers, *2001-2011: A Decade from Crisis*, ARGENTINA INDEPENDENT, Dec. 19, 2011, <http://www.argentinaindependent.com/currentaffairs/analysis/2001-2011-a-decade-from-crisis>; Marc Rogers, *2001-2011: The Day that Changed Argentine History*, ARGENTINA INDEPENDENT, Dec. 20, 2011, <http://www.argentinaindependent.com/currentaffairs/analysis/2001-2011-chronicle-of-a-day-that-changed-argentine-history>; Clifford Krauss, *Reeling from Riots, Argentina Declares a State of Siege*, N.Y. TIMES (Dec. 20, 2001), available at <http://www.nytimes.com/2001/12/20/world/reeling-from-riots-argentina-declares-a-state-of-siege.html>; Max Seitz, *The Day Argentina Hit Rock Bottom*, BBC, Dec. 19, 2005, <http://news.bbc.co.uk/2/hi/business/4534786.stm> (affirming that Argentina had inaugurated five presidents in only ten days); *The Events that Triggered Argentina's Crisis*, BBC, Dec. 21, 2001,

foreign investors sought to challenge the Argentine emergency measures in an international arbitral tribunal but the results that unfolded revealed a serious shortcoming in the international investment system. Consequently, the emerging fact pattern that arose as a consequence of the Argentinean economic crisis may be generalized as involving an aggrieved foreign investor who claims that it suffered serious investment losses due to the enactment of the Emergency Act.

The first ICSID tribunal to interpret Article XI of the U.S.-Argentina BIT arose when CMS submitted a request for arbitration in ICSID in July 2001 against the Argentine government alleging that Argentina's unilateral adjustment of the tariff formula applicable to gas transportation companies in which CMS, a gas transporting company incorporated in the United States, had a 30 percent stake was a breach of treaty.⁵⁸⁰ One of the powers delegated to the Argentine executive branch during the economic crisis in the Emergency Act was to terminate the indexation of tariffs to U.S. dollar indices. However, CMS protested that at the time of the investment, Argentina had permitted the company to calculate tariffs in U.S. dollars as a part of its energy privatization incentives, but pay in pesos at the applicable exchange rate while adjusting for inflation on a semi-annual basis for the duration of the license agreement ending in 2027 in accordance with its laws.⁵⁸¹ When the Emergency Act came into effect, however, the peso

<http://news.bbc.co.uk/2/hi/business/1721103.stm> (providing a timeline of the events that led to the Argentinean economic crisis).

⁵⁸⁰ CMS v. Argentina, *supra* note 179, para. 4. See Thjoernelund, *supra* note 574, at 443.

⁵⁸¹ Thjoernelund, *supra* note 574, at 443.

devalued significantly reducing the real earnings and value of CMS's investment.

Under a similar fact pattern as described above, the claimants in *Enron v. Argentina* owned an indirect equity interest in an Argentinean gas transportation company that was created during the privatization efforts in Argentina when the legislative framework included benefits to attract foreign investment like calculating tariffs in U.S. dollars but permitting payment in pesos, the promise that a price freeze would not be imposed on the tariff system, and other specific guarantees.⁵⁸² However, the Emergency Act revoked the right of Enron to calculate tariffs in U.S. dollars instead forcibly converting U.S. dollars into pesos at the fixed exchange rate of one dollar to one peso. Claimants sought arbitration alleging that the emergency measures significantly decreased their investment value in the Argentinean company. Again, this fact pattern repeats similarly in *Sempra Energy v. Argentina* with the claimant arguing that it suffered losses when the emergency measures, which were supposed to be provisional, permanently modified the legislative framework that was enacted to attract foreign investment.⁵⁸³

In *Continental Casualty Company v. Argentina*, an American insurance company alleged that its investment in the privatization of Argentina's worker's compensation insurance scheme resulted in serious losses because of the emergency measures forced the restriction on asset transfers out of the

⁵⁸² *Enron v. Argentina*, *supra* note 179, paras. 41-46.

⁵⁸³ *Sempra v. Argentina*, *supra* note 179, para. 260.

country, pesification of U.S. dollar deposits, and devaluation of the peso.⁵⁸⁴ In *LG&E v. Argentina*, the ICSID tribunal considered the public order carve-out as argued by Argentina, based on its description of the events that included massive street demonstrations, school and business shutdowns, transportation halts, and five consecutive presidential resignations that took place as a result of the economic crisis, to justify that the price freeze in the gas distribution sector was a legitimate emergency measure within the scope of the public order carve-out that was necessary to sustain Argentina's basic infrastructure, which relied on natural gas energy, during a time of severe economic hardship.⁵⁸⁵ The claimant, LG&E, disagreed that the public order carve-out in Article XI was to be interpreted so broadly instead arguing that measures enacted for public order reasons ought to be limited to "actions taken pursuant to a state's police powers, particularly in respect of public health and safety."⁵⁸⁶

Although each of the five ICSID tribunals decided under very similar fact patterns on the applicability of the NPM provision which includes the public order carve-out, the result was split due to the gap in interpretative guidance on how investment tribunals should treat the NPM provision under the U.S.-Argentina BIT.⁵⁸⁷ Several issues contemplated or avoided by

⁵⁸⁴ *Continental Casualty v. Argentina*, *supra* note 179, para. 19.

⁵⁸⁵ *LG&E v. Argentina*, *supra* note 179, para. 216. See Thjoernelund, *supra* note 574, at 459.

⁵⁸⁶ *LG&E v. Argentina*, *supra* note 179, para. 221. See Thjoernelund, *supra* note 574, at 459-60.

⁵⁸⁷ See, e.g., *Enron v. Argentina*, *supra* note 179, para. 333 ("no specific guidance... [t]his is what makes necessary to rely on the requirements of state of necessity under customary international law")

the ICSID tribunals that are worth considering are discussed below in Section II.

II. The Argentine ICSID Tribunals' Standard of Review for the Public Order Carve-out

A. ILC Article 25 as Applied to the Public Order Carve-out

In 1947, the United Nations General Assembly, acting within its powers under Article 13 of the UN Charter to “initiate studies and make recommendations for the purpose of... encouraging the progressive development of international law and its codification,” appointed the newly established International Law Commission (ILC) to execute this ambitious, but noble mandate.⁵⁸⁸ With State responsibility named as one of the first 14 topics to be worked on by the ILC, the Commission prepared Draft Articles on the International Responsibility of the States, which were provisionally adopted on its first reading in 1980, and included the following codification on the state of necessity in Draft Article 33:

1. A state of necessity may not be invoked by a State as a ground for precluding the wrongfulness of an act of that State not in conformity with an international obligation of the State unless:

(a) the act was the only means of safeguarding an essential interest of the State against a grave and imminent peril; and

⁵⁸⁸ U.N. Charter, art. 13, June 26, 1945.

(b) the act did not seriously impair an essential interest of the State towards which the obligation existed.

2. In any case, a state of necessity may not be invoked by a State as a ground for precluding wrongfulness:

(a) if the international obligation with which the act of the State is not in conformity arises out of a peremptory norm of general international law; or

(b) if the international obligation with which the act of the State is not in conformity is laid down by a treaty which, explicitly or implicitly, excludes the possibility of invoking the state of necessity with respect to that obligation; or

(c) if the State in question has contributed to the occurrence of the state of necessity.⁵⁸⁹

In 1997, the ILC appointed Special Rapporteur James Crawford to make a second reading of the Draft Articles and, in December 2001, the General Assembly adopted in its fifty-third session a final version containing 59 articles with Draft Article 33 being revised into Article 25 as provided below:⁵⁹⁰

1. Necessity may not be invoked by a States as a ground for

⁵⁸⁹ The text of the 1980 Draft Articles on International Responsibility of States is reprinted in James Crawford, *Revising the Draft Articles on State Responsibility*, 10 EJIL 435, 458 (1999).

⁵⁹⁰ See James Crawford, *Articles on Responsibility of States for Internationally Wrongful Acts*, U.N. AUDIOVISUAL LIBRARY OF INT'L LAW, <http://legal.un.org/avl/ha/rsiwa/rsiwa.html> (providing a procedural history of the Articles on Responsibility of States for Internationally Wrongful Acts).

precluding the wrongfulness of an act not in conformity with an international obligation of that State unless the act:

(a) is the only way for the State to safeguard an essential interest against a grave and imminent peril; and

(b) does not seriously impair an essential interest of the State or States towards which the obligation exists, or of the international community as a whole.

2. In any case, necessity may not be invoked by a State as a ground for precluding wrongfulness if:

(a) the international obligation in question excludes the possibility of invoking necessity; or

(b) the State has contributed to the situation of necessity.⁵⁹¹

The work of the ILC has generally commanded respect in international law and used in practice, including by the ICJ.⁵⁹² It also affirms Professor Ago's thesis that necessity is not founded in a State's right to self-preservation, but instead ought to be "ascribed to that situation the force of a circumstance precluding the wrongfulness of the act" satisfied in the strictest of conditions as required in the second paragraph of Draft Article 33 and Article 25 of the

⁵⁹¹ State Responsibility Draft with Commentaries, *supra* note 367, art. 25, at 80.

⁵⁹² Crawford, *supra* note 590. *See generally* Boed, *supra* note 347, at 13 (The ILC has also been responsible for producing other "landmark treaties" including the Vienna Convention on the Law of Treaties, the Vienna Conventions on Diplomatic and Consular Relations, and the Geneva Conventions on the Law of the Sea).

ILC.⁵⁹³ The 2001 Commentary on the ILC Articles explicitly favors this position citing the fact that international tribunals have considered Article 25 in such a context with the “plea of necessity [being] accepted in principle, or at least not rejected.”⁵⁹⁴ Referring to the final and current version of the codification on the state of necessity in Article 25, I will now consider how the ICSID tribunals in the Argentinean awards analyzed the key elements of Article 25.

1. “Essential Interest”

In developing the concept of essential interest, Professor Ago commented that “it would be pointless to attempt to go into greater detail and establish categories of interests to be considered essential” because how essential an interest is “naturally depends on the totality of the conditions in which a State finds itself in a variety of specific situations” and further advised that the concept of essential interest ought to be “appraised in relation to the particular case in which such an interest is involved, and not predetermined in the abstract.”⁵⁹⁵ Strongly influenced by Ago, the ILC drafted its article on necessity without providing an enumeration of what “essential interest” is, and the term has been meant to justify an act done to preclude wrongful conduct in order to protect an essential interest of the State even if the threat has no bearing to its sovereign existence:

The interest protected by the subjective right vested in the foreign State, which is to be sacrificed for the sake of an

⁵⁹³ AGO REPORT, *supra* note 350, para. 77, at 50.

⁵⁹⁴ State Responsibility Draft with Commentaries, *supra* note 367, art. 25, cmt. 3, at 81.

⁵⁹⁵ AGO REPORT, *supra* note 350, para. 12, at 19.

“essential interest” of the obligated State, must obviously be inferior to that other interest. It is particularly important to make this point because... the idea that the only interest for the protection of which the excuse of necessity might be invoked is the very existence of the State has now been completely discarded. Consequently, the interest in question cannot be one which is comparable [*citation omitted*] and equally essential to the foreign State concerned.⁵⁹⁶

Despite his refusal to identify specific instances of essential interest, Ago nonetheless provided some examples of what may be “essential” under Article 25 such as when a State’s “political or economic survival, the continued functioning of its essential services, the maintenance of internal peace, the survival of a sectors of its population, the preservation of the environment of its territory or a part thereof.”⁵⁹⁷

The ICSID cases arising out of the Argentine economic crisis (described earlier in this Chapter) discuss essential interest in the context of investment arbitration with Argentina contending that economic emergency qualifies as an essential interest within the meaning of Article 25 of the ILC.⁵⁹⁸ In *CMS*, Argentina argued that the Emergency Act which allowed the pesification was necessary to protect essential economic interests⁵⁹⁹ and the tribunal also determined that its first step of analysis would be to address

⁵⁹⁶ *Id.* at 20, para. 15.

⁵⁹⁷ *Id.* at 14, para. 2.

⁵⁹⁸ *CMS v. Argentina*, *supra* note 179, para. 305.

⁵⁹⁹ *Id.* para. 312.

whether an essential interest of the State was being adversely affected.⁶⁰⁰ Accepting that Article 25 of the ILC is an embodiment of the customary international rule on necessity,⁶⁰¹ the tribunal was not satisfied that Argentina had met the requirements,⁶⁰² and even though it acknowledged that “leading economists are of the view that the crisis was of catastrophic proportions,” it quickly pointed out that this was debatable.⁶⁰³ Without further deliberation on the impact of the Argentine economic crisis on the meaning of essential interest, the tribunal hastily concluded that wrongfulness could not be precluded under the circumstances presented by Respondent and wrapped up its analysis on the element of essential interest by stating that “situations of this kind are not given in black and white but in many shades of grey.”⁶⁰⁴ Similar to the view held by the *CMS* tribunal, the tribunal in *Enron v. Argentina* sympathized that the crisis in Argentina was severe and “unlikely that business could have continued as usual,” but also stressed the division in expert opinions concerning the degree of the Argentine economic crisis to make a finding that the situation did not affect an essential interest of the State.⁶⁰⁵ The tribunal in *Sempra Energy v. Argentina*

⁶⁰⁰ *Id.* para. 319.

⁶⁰¹ *Id.* at para 315.

⁶⁰² *Id.* paras. 319-22.

⁶⁰³ *Id.* para. 320. See also ANDREAS KULICK, *GLOBAL PUBLIC INTEREST IN INTERNATIONAL INVESTMENT LAW 137* (Cambridge Univ. Press 2012) (stating that the *CMS* tribunal rejected the argument that the economic crisis affected Argentina’s essential interest).

⁶⁰⁴ *CMS*, *supra* note 179, para. 320.

⁶⁰⁵ *Enron v. Argentina*, *supra* note 179, paras. 305-6.

found that the Argentine crisis did not fall within the meaning of essential security, oddly, because: “The tribunal believes that the constitutional order was not on the verge of collapse, as evidenced by, among many examples, orderly constitutional transition that carried the country through five different Presidencies in a few days’ time, followed by elections and the reestablishment of public order.”⁶⁰⁶ Moreover, the *Sempra* tribunal literally reiterated the statements made four months earlier in the *Enron* tribunal that an essential interest cannot be established since expert opinions strongly disagree on the severity of the Argentine economic crisis.⁶⁰⁷

Unlike the conclusions derived from the pithy analyses of the above-mentioned tribunals, particularly the *CMS* and *Enron* tribunals, the *LG&E v. Argentina* tribunal referred to the contributive works of ILC Special Rapporteurs Robert Ago and James Crawford to concur that an essential interest is not limited to a State’s existence and may relate to “economic, financial or those interests related to the protection of the State against any danger seriously compromising its internal or external situation.”⁶⁰⁸ Importantly, after reviewing in great detail the events triggering and following the Argentine economic crisis,⁶⁰⁹ the *LG&E* tribunal found that the

⁶⁰⁶ *Sempra v. Argentina*, *supra* note 179, para. 332.

⁶⁰⁷ *Id.* paras. 347-48. *Cf.* *Enron v. Argentina*, *supra* note 179, paras. 305-6. KULICK, *supra* note 603, at 137 (noting the absurdity of the argument espoused by the *Sempra* tribunal and commenting that “as is the case in almost every academic discipline, economic scholars will always differ in their evaluation of the severity of crises”).

⁶⁰⁸ *LG&E v. Argentina*, *supra* note 179, paras. 251-52.

⁶⁰⁹ *Id.* paras. 231-37.

essential interests of Argentina were threatened during the period from December 2001 until April 2003 because it “faced an extremely serious threat to its existence, its political and economic survival.”⁶¹⁰

The tribunal in *Continental Casualty v. Argentina* also absolved Argentina, but strayed from the manner in which previous decisions were made when it analyzed the necessity defense in the context of only Article XI of the U.S.-Argentina BIT, “and not on the arguably higher requirements of the customary international law defense of state of necessity.”⁶¹¹ While aware of the stricter conditions in Article 25 of the ILC,⁶¹² the *Continental Casualty* tribunal claimed that a State’s act to protect an essential interest “does not require that ‘total collapse’ of the country or that a ‘catastrophic situation’ has already occurred before responsible national authorities may have recourse to its protection” since any such effort made to protect would be useless “if there is nothing left to protect.”⁶¹³ In both the LG&E and *Continental Casualty* tribunals, the exact phrase considered was the treaty language of “essential security interests” in Article XI of the underlying BIT

⁶¹⁰ *Id.* para. 257.

⁶¹¹ See August Reinisch, *Introductory Note*, in 2 GLOBAL COMMUNITY: YEARBOOK OF INT’L LAW AND JURISPRUDENCE 768 (Giuliana Z. Capaldo ed., 2009) (commenting that the tribunal did not decide “on the arguably higher requirements of the customary international law defense of state of necessity”). See also *Continental Casualty v. Argentina*, *supra* note 179, paras. 85, 184, 192-193 (Additionally, the *Continental Casualty* tribunal was influenced by the approach used in Article XX of the GATT). For criticism of this approach, see Alvarez & Brink, *supra* note 481, at 343.

⁶¹² *Continental Casualty v. Argentina*, *supra* note 179, n. 264, at 79 (stating that this tribunal realizes that ILC Article 25 “is more restrictive than Art. XI”).

⁶¹³ *Id.* para. 180.

rather than the term “essential interest” as used in Article 25 of the ILC.

2. “Grave and Imminent Peril”

Article 25 of the ILC requires that the threat to a State’s essential interest be from a grave and imminent peril.⁶¹⁴ Regarding the first prong, specific criteria is not provided on how to measure the graveness of a peril. The ILC Commentary on Article 25 does not offer additional insight on the meaning of grave, and similarly, Ago simply states that the threat to an essential interest must be “extremely grave.”⁶¹⁵ The peril must also be imminent. Ago implies that imminent means “representing a present danger”⁶¹⁶ and the ILC Commentary on Article 25 requires that the peril “be imminent in the sense of proximate,”⁶¹⁷ but recognizes that this second prong does not exclude certain situations where imminence and peril do not go hand-in-hand.⁶¹⁸ Above all, the peril must be objectively identifiable and therefore not sufficient that the peril is apprehended or contingent.⁶¹⁹

⁶¹⁴ State Responsibility Draft with Commentaries, *supra* note 367, art. 25, cmt. 15, at 83.

⁶¹⁵ AGO REPORT, *supra* note 350, para. 13, at 19.

⁶¹⁶ *Id.*

⁶¹⁷ State Responsibility Draft with Commentaries, *supra* note 367, art. 25, cmt. 15, at 83.

⁶¹⁸ *Id.* quoting Gabčíkovo-Nagymaros Project, *supra* note 368, para. 54:

That does not exclude ... that a “peril” appearing in the long term might be held to be “imminent” as soon as it is established, at the relevant point in time, that the realization of that peril, however far off it might be, is not thereby any less certain and inevitable.

⁶¹⁹ State Responsibility Draft with Commentaries, *supra* note 367, art. 25, cmts. 15-16, at 83.

The tribunals in *CMS*, *Enron*, and *Sempra* disagreed that the economic crisis in Argentina put an essential interest of the State in grave and imminent peril. The first issue identified by the *CMS* tribunal was whether the U.S.-Argentina BIT, which was “clearly designed to protect investments at a time of economic difficulties or other circumstances leading to the adoption of adverse measures by the Government,” could be avoided by a plea of necessity or emergency which, in turn, depends on the gravity of the economic situation.⁶²⁰ The tribunal clearly stated the following:

A severe crisis cannot necessarily be equated with a situation of total collapse. And in the absence of such profoundly serious conditions it is plainly clear that the Treaty will prevail over any plea of necessity. However, if such difficulties, without being catastrophic in and of themselves, nevertheless invite catastrophic conditions in terms of disruption and disintegration of society, or are likely to lead to a total breakdown of the economy, emergency and necessity might acquire a different meaning.⁶²¹

After dedicating a few succinct lines⁶²² to comment that while it was persuaded that the situation in Argentina was difficult, the tribunal

⁶²⁰ *CMS v. Argentina*, *supra* note 179, paras. 353-54.

⁶²¹ *Id.* para. 354.

⁶²² *NEWCOMBE & PARADELL*, *supra* note 43, at 519 (lamenting the brevity of tribunal reasoning on “grave and imminent peril” and advocating for “more detailed references to [] documentary evidence and/or witness or expert testimony... given the importance of these cases in the development of IIA jurisprudence”).

concluded that the “relative effect of the crisis”⁶²³ does not satisfy Article 25 of the ILC because, however severe, it “did not result in total economic and social collapse.”⁶²⁴ The tribunal in *Enron* acknowledged that a State has the duty to prevent “the worsening of a situation,” but insisted on “convincing evidence that the events were out of control or had become unmanageable.”⁶²⁵ The *Sempra* tribunal later affirmed this identical analysis.⁶²⁶

However, in the context of Article XI of the BIT, the *LG&E* tribunal found that the peril in Argentina was “an extremely serious threat,”⁶²⁷ the situation necessitated “immediate, decisive action to restore civil order and stop the economic decline,” and concluded that denying economic catastrophe as a legitimate essential interest protectable under the treaty would be to “diminish the havoc that the economy can wreak on the lives of an entire population and the ability of the Government to lead.” Plainly stated, the tribunal held that “[w]hen a State’s economic foundation is under siege, the severity of the problem can equal that of any military invasion.”⁶²⁸

⁶²³ *CMS v. Argentina*, *supra* note 179, para. 322.

⁶²⁴ *Id.* para. 355.

⁶²⁵ *Enron v. Argentina*, *supra* note 179, para. 307. See Iboronke T. Odumosu-Ayanu, *International Investment Law and Disasters: Necessity, Peoples, and the Burden of (Economic) Emergencies*, in *THE INTERNATIONAL LAW OF DISASTER RELIEF* 314, 323 (David D. Caron et al. eds., 2014) (“Under this formula the necessity defense would be unavailable except the state was facing imminent collapse.”).

⁶²⁶ *Sempra v. Argentina*, *supra* note 179, para. 349.

⁶²⁷ *LG&E v. Argentina*, *supra* note 179, para. 257.

⁶²⁸ *Id.* para. 238.

Also analyzing the grave and imminent peril requirement as applicable to Article XI, the *Continental Casualty* tribunal recognized the severity of the economic crisis in Argentina and differed from the opinion in *CMS* that a total collapse of the State was required or that a catastrophic situation was taking place.⁶²⁹

3. “Only Way for the State to Safeguard”

In Ago’s report, the “only means” requirement is satisfied when it is absolutely “impossible for the peril to be averted by any other means, even one which is much more onerous but which can be adopted without a breach of international obligations.”⁶³⁰ This view was affirmed in the ILC Commentary on Article 25 stating that the conditions for a state of necessity will not be met “if there are other (otherwise lawful) means available, even if they may be more costly or less convenient.”⁶³¹ Referring heavily to the ICJ decision in the *Gabčíkovo-Nagymaros Project* case, the ILC Commentary observed that the term “way” may include a State’s unilateral and/or cooperative acts such as with other interested governments or international organizations.⁶³² Moreover, the State’s act may not be excessive and must be

⁶²⁹ *Continental Casualty v. Argentina*, *supra* note 179, para. 180. See Odumosu-Ayanu, *supra* note 625, at 324 (commenting that the lack of “clear rules before emergencies occur” has contributed to the diverging opinions of the Argentine ICSID tribunals).

⁶³⁰ AGO REPORT, *supra* note 350, para. 14, at 20.

⁶³¹ State Responsibility Draft with Commentaries, *supra* note 367, art. 25, cmt. 15, at 83.

⁶³² *Id.*

“strictly necessary for the purpose.”⁶³³ In that case, the ICJ refused Hungary relief under the state of necessity defense upon finding that other means of safeguarding its environmental interest in the nearby region and water supply were available.⁶³⁴

The interpretation of the “only way” requirement by the *CMS*, *Enron*, and *Sempra* tribunals was harshly criticized for establishing an unachievable ceiling.⁶³⁵ Due to the difference in opinion because “distinguished economics” and the parties, the *CMS* tribunal stated that whether the Emergency Act was the only way of safeguarding Argentina’s essential interest was “debatable” and declared that providing policy alternatives was beyond the role of the tribunal whose duty is “to establish whether there was only one way or various ways and thus whether the requirements for the preclusion of wrongfulness have or have not been met.”⁶³⁶ In similar language, the tribunals in *Enron* and *Sempra* stated that countries dealing with economic crises are given a number of choices and to argue that only one such means was available to Argentina during its time of crisis is an unreasonable assumption.⁶³⁷ Although the *LG&E* tribunal attempts to form

⁶³³ *Id.*

⁶³⁴ Gabčíkovo-Nagymaros Project, *supra* note 368, paras. 55-57 (“The Court moreover considers that Hungary could... have resorted to other means in order to respond to the dangers that it apprehended.”).

⁶³⁵ See, e.g., KULICK, *supra* note 603, at 138 (“an absurd threshold impossible to pass”).

⁶³⁶ *CMS v. Argentina*, *supra* note 179, para. 323.

⁶³⁷ Compare *Enron v. Argentina*, *supra* note 179, para. 308 (“A rather sad world comparative experience in the handling of economic crises, shows that there are always many approaches to address and correct such critical events, and it is difficult to justify that none of them were available in the Argentine case.”) *with*

an understanding of “only means” as required in Article 25 of the ILC in its decision,⁶³⁸ it ends the analysis based on a mere finding that “an economic recovery package was the only means to respond to the crisis” with one additional remark that “[a]lthough there may have been a number of ways to draft the economic recovery plan... an across-the-board response was necessary.”⁶³⁹ The tribunal in *Continental Casualty* seems to have discussed the “only way” requirement synonymously with the “reasonably available” alternative measure standard used in WTO jurisprudence to “preserve for the responding Member its right to achieve its desired level of protection.”⁶⁴⁰

At least two problems stand out in the Argentine ICSID tribunals’ interpretation of the “only way” requirement. First, none provided a *legal* inquiry of the term “only way”⁶⁴¹ and the tribunals rather artlessly stated

Sempra v. Argentina, *supra* note 179, para. 350 (“A rather sad global comparison of experiences in the handling of economic crises shows that there are always many approaches to addressing and resolving such critical events. It is therefore difficult to justify the position that only one of them was available in the Argentine case.”).

⁶³⁸ LG&E v. Argentina, *supra* note 179, para. 250.

⁶³⁹ *Id.* para. 257.

⁶⁴⁰ *Continental Casualty v. Argentina*, *supra* note 179, para. 195 (citing U.S. – Gambling Appellate Body Report, *supra* note 281, para. 308) (referring to GATS Art. XIV). *See also* Panel Report, Brazil – Measure Affecting Imports of Retreaded Tyres, para. 7.211, WT/DS332/R (June 12, 2007) (“We do not exclude however that there may be circumstances in which a highly restrictive measure is necessary, if no other less trade restrictive alternative is reasonably available to the member concerned to achieve its objectives.”).

⁶⁴¹ *Enron Corp. Ponderosa Asset, L.P. v. Argentina*, ICSID Case No. ARB/01/3, Decision on the Application for Annulment, para. 369 (July 30, 2010) [hereinafter *Enron Annulment*] (“The first question concerns the legal definition of the expression ‘only way’ in Article 25(1)(a) of the ILC Articles.”). *See also* Paul B. Maslo, *Are the ICSID Rules Losing Their Appeal? Annulment Committee Decisions Make ICSID Rules a Less Attractive Choice for Resolving Treaty-Based Investor-State Disputes*, 54 VA. J. INT’L L. DIG. 1, 5 (2014) (noting that the expression “only way” was not addressed in a legal context); Luke Eric Peterson, *Another Argentine Crisis Award is*

that Argentina had not met this requirement based on the economists' disagreement over whether the measures adopted were the only means possible. In its review of the tribunal in *Enron v. Argentina*, this point was criticized by the *Enron* annulment committee which stated that the term "only way" possesses more than one possible meaning that may be literal⁶⁴² or be the best of a worst few choices but likely to cause the least amount of breach to international law.⁶⁴³ The *Enron* Committee further observed that the inquiry should also delve into the relative effectiveness of the other measure⁶⁴⁴ and that a standard as to who will decide on the existence of an alternative measure must also be considered.⁶⁴⁵ Moreover, as shown above, the diverging opinions of the tribunals expose the lack of uniformity behind the meaning of "only way."⁶⁴⁶ In *CMS v. Argentina*, the tribunal opted for a

Annulled; ICSID Committee Strikes Down \$100+ Million Verdict in Favor of Enron Corporation, INVESTMENT ARBITRATION REPORTER (Aug. 2, 2010), <http://www.iareporter.com/articles/another-argentine-crisis-award-is-annulled-icsid-committee-strikes-down-100-million-verdict-in-favour-of-enron-corporation> ("[T]he [Enron Annulment] committee found that the arbitrators skirted across this requirement in a "cursory" manner - relying on the opinion of an economic expert who said Argentina had multiple policy options in confronting the earlier crisis - rather than engaging in a detailed analysis of the legal meaning of the phrase the "only way" .).

⁶⁴² Enron Annulment, *supra* note 641, para. 369.

⁶⁴³ *Id.* para. 370.

⁶⁴⁴ *Id.* para. 371.

⁶⁴⁵ *Id.* para. 372.

⁶⁴⁶ Jorge E. Viñuales, *Sovereignty in Foreign Investment Law*, in THE FOUNDATIONS OF INTERNATIONAL INVESTMENT LAW: BRINGING THEORY INTO PRACTICE 317, 349 (Zachary Douglas et al. eds., 2014) ("Does 'the only way' mean the only realistically available way or the only way out of a set including theoretical measures or measures that the state has never applied or has no experience in handling.").

very strict and perhaps too literal of an interpretation of the term “only way” so that any other existing means, no matter how unreasonable, would deny satisfaction of the requirement. Based on this narrow perspective, the tribunal in *CMS* gave weight to the suggestion that the dollarization of the Argentine economy⁶⁴⁷ in the middle of a raging crisis would have been another option,⁶⁴⁸ but at the same time, discharged itself from the responsibility of knowing which of those alternatives Argentina ought to have selected.⁶⁴⁹

4. “Act did not Seriously Impair an Essential Interest”

Article 25.1(b) of the ILC introduces a second condition requiring the face-off between the acting State’s essential interest and the essential interest of the other State or States concerned, or of the international community as a whole so that the essential interest seeking to be protected is above all other interests, “not merely from the point of view of the acting State but on a reasonable assessment of the competing interests, whether [] individual or collective.”⁶⁵⁰ Ago also emphasized that the essential interest of the acting State must not be “comparable and equally essential” to a third State.⁶⁵¹

In *CMS v. Argentina*, the tribunal noted that Argentina’s protection of

⁶⁴⁷ *CMS v. Argentina*, *supra* note 179, para. 323.

⁶⁴⁸ See Viñuales, *supra* note 646, at 349 (stating that the distinguished experts’ dollarization proposition in *CMS* was unreasonable given its risk and complexity, which, in a bad case scenario, could force Argentina to lose control over its monetary sovereignty).

⁶⁴⁹ *CMS v. Argentina*, *supra* note 179, para. 323.

⁶⁵⁰ State Responsibility Draft with Commentaries, *supra* note 367, cmt. 17, at 84.

⁶⁵¹ AGO REPORT, *supra* note 350, para. 15, at 20.

its essential interest was not at the detriment of the essential interest of the international community.⁶⁵² The tribunal in *LG&E v. Argentina* also took the stance that Argentina's Emergency Act did not impair the essential interests of other States.⁶⁵³ While the tribunals in *Sempra* and *Enron* were also satisfied that the essential interest of the international community as whole was not affected,⁶⁵⁴ it claimed that in the context of an investment treaty where the ultimate beneficiaries are identifiable, the essential interests of the Claimants would be adversely affected if a state of necessity were to be established.⁶⁵⁵ However, the annulment committee in *Enron* criticized the tribunal's reasoning because "[it] considered that the principle of necessity would not, or might not, apply in the context of a BIT if *the application of the principle of necessity* would seriously impair an essential interest of a national of the other contracting State to the BIT,"⁶⁵⁶ and is to be distinguished from the condition of Article 25.1(b) which places in question the acting State's conduct. Moreover, the Committee found that it could not ascertain whether the tribunal had made a proper legal inquiry for Article 25.1(b).⁶⁵⁷ The tribunal in *Continental Casualty* did not address this requirement and was

⁶⁵² CMS v. Argentina, *supra* note 179, para. 325.

⁶⁵³ LG&E v. Argentina, *supra* note 179, para. 257.

⁶⁵⁴ Enron v. Argentina, *supra* note 179, para. 310; *Sempra v. Argentina*, *supra* note 179, para. 352.

⁶⁵⁵ Enron v. Argentina, *supra* note 179, para. 342; *Sempra v. Argentina*, *supra* note 179, paras. 390-91.

⁶⁵⁶ Enron Annulment, *supra* note 641, para. 383.

⁶⁵⁷ *Id.* para. 384.

also not picked up as an issue by the annulment committee.

B. The Argentine ICSID Tribunals' Treatment of the NPM Treaty Provision

1. Is Article XI of the U.S.-Argentina BIT Self-Judging?

During the ICSID proceedings, Argentina argued that the NPM provision should be self-judging since it would be subject to less stringent review standards than what would be required by the customary law on necessity.⁶⁵⁸ This was an important point of contention for Argentina because if determined to be self-judging, its NPM provision would be subject to the less stringent good faith review as opposed to a substantive review. In the *Nicaragua v. U.S.* case decided in 1986 before the ICJ, the United States contended that a certain provision under Article XXI arising out of the underlying 1956 FCN Treaty between the two disputing States is self-judging. The relevance of the *Nicaragua* case is that it was first mentioned by the expert witnesses in the *CMS* proceeding due to textual similarity between Article XXI and Article XI of the U.S.-Argentina BIT.⁶⁵⁹ The pertinent part of Article XXI of the FCN treaty is provided as below:

[T]he present Treaty shall not preclude the application of measures:

[...]

(d) necessary to fulfill the obligations of a Party for the

⁶⁵⁸ *CMS v. Argentina*, ICSID Case No. ARB/01/8, Decision of the Ad Hoc Committee on the Application for Annulment of the Argentine Republic, para. 112 (Sep. 25, 2007) [hereinafter *CMS Annulment*]; *Enron Annulment*, *supra* note 641, para. 324; *Sempra v. Argentina*, *supra* note 179, para. 366; *Continental Casualty v. Argentina*, *supra* note 179, para. 87; *LG&E v. Argentina*, *supra* note 179, para. 208.

⁶⁵⁹ *CMS v. Argentina*, *supra* note 179, para 339 (providing the expert opinion for the claimant, Professor Alvarez referred to the *Nicaragua* case to support the view that the NPM provision in the U.S.-Argentina BIT is not self-judging)

maintenance or restoration of international peace and security, or necessary to protect its essential security interests.⁶⁶⁰

According to the expert opinion provided on behalf of CMS, Professor Alvarez referred to the *Nicaragua* case to support the view that the NPM provision in the U.S.-Argentina BIT is not self-judging.⁶⁶¹ In contrast, in her expert testimony for Argentina, Dean Slaughter argued that post-*Nicaragua*, the United States “desired to safeguard certain sovereign interests by means of ‘non-precluded measures’ such as those of Article XI”⁶⁶² after receiving the ICJ ruling in *Nicaragua* that Article XXI is not self-judging.⁶⁶³

The *Continental Casualty* tribunal believed that the question of whether Article XI is self-judging arose due to the “lack of documentation” at the moment in time when the United States had negotiated and signed the U.S.-Argentina BIT and that the *Nicaragua* case does not serve as conclusive proof that the United States intended to permanently make provisions similar to Article XXI of the U.S.-Nicaragua FCN Treaty self-judging.⁶⁶⁴ Moreover, the presence of the self-judging clause in the unratified U.S.-

⁶⁶⁰ Military and Paramilitary Activities (*Nicaragua v. U.S.*), 1986 I.C.J. 14, Merits, para. 221 (June 27, 1986) [hereinafter *Nicaragua* case].

⁶⁶¹ CMS v. Argentina, *supra* note 179, para. 339.

⁶⁶² *Id.* para. 350.

⁶⁶³ *But see* Kenneth J. Vandevelde, *Of Politics and Markets: The Shifting Policy of the BITs*, 11 INT’L TAX & BUS. LAWYER 159, 172-73 (1993) (explaining that the United States seemed to have abandoned the position held in *Nicaragua*). Professor Vandevelde appeared as the expert for the claimant in the *Continental Casualty* case.

⁶⁶⁴ *E.g.*, *Continental Casualty v. Argentina*, *supra* note 179, para. 186.

Russia BIT is not adequate evidence given that the United States did not pursue the position held in the *Nicaragua* case and only agreed to a self-judging clause in the BIT with Russia based on Russia's demand.⁶⁶⁵ Unlike the language available under the NPM provision of the U.S.-Argentina BIT, a self-judging clause has to be expressly stated and, to this extent, the CMS tribunal cited to the examples of the GATT and BITs including the U.S.-Russia BIT to declare that the "which it considers necessary" language must be present.⁶⁶⁶ This position is consistent with the other two cases later decided by the ICJ in connection with the necessity defense arising out of the essential security interest clause. The *Oil Platforms* case affirmed the stance taken in the *Nicaragua* case by stating that:

As the Court emphasized, in relation to the comparable provision of the 1956 United States/Nicaragua Treaty in the [*Nicaragua* case], 'the measures taken must not merely be such as tend to protect the essential security interests of the party taking them, but must be 'necessary' for that purpose'; and whether a given measure is "necessary" is 'not purely a question for the subjective judgment of the party.'⁶⁶⁷

As to the self-judging nature of such provisions, the ICJ in the *Gabčíkovo-Nagymaros* case likewise concluded that "the State concerned is not the sole

⁶⁶⁵ CMS v. Argentina, *supra* note 179, para. 368 (tribunal pointing out that the U.S.-Russia BIT [signed on June 17, 1992] was never ratified). See also *Continental Casualty v. Argentina*, *supra* note 179, para. 186.

⁶⁶⁶ CMS v. Argentina, *supra* note 179, para. 370.

⁶⁶⁷ *Oil Platforms (Iran v. U.S.)*, 2003 I.C.J. 161, Judgment, para. 43 (Nov. 6) (quoting *Nicaragua* case, *supra* note 660, para. 282) [hereinafter *Oil Platforms* case].

judge of whether those conditions have been met.”⁶⁶⁸

The issue of whether Article XI is self-judging is relevant to determining the scope of the public order carve-out. For example, if NPM provisions are self-judging, then measures that have been adopted to address economic emergencies such as prohibiting the free transfer of funds in breach of a treaty term may legitimately fall within the scope of the public order carve-out as provided within the NPM provision. On a more general level, if determined that the NPM provision is self-judging, the scope of the public order carve-out may be expanded to encompass situations not explicitly provided for in the underlying treaty including economic emergencies and other special situations perhaps relating to public health, the environment, or cultural preservation. On the other hand, if the NPM provision is not self-judging, then the scope of the public order would be closer to the concept of police powers.⁶⁶⁹ In practice, aside from the tribunal in *Continental Casualty*, the other ICSID tribunals mentioned here could have understood the public order carve-out as referring to a State’s police power that would permit acts that preserve domestic public order and provide protection to citizens.⁶⁷⁰ Arguments have been made that the public order carve-out does not, however, envision “all measures that advance the public interest since otherwise Article XI would have been phrased differently, e.g.,

⁶⁶⁸ Gabčíkovo-Nagymaros Project, *supra* note 368, para. 51.

⁶⁶⁹ See Howard Mann, IISD, *Investment Agreements and the Regulatory State: Can Exceptions Clauses Create a Safe Haven for Governments?*, in Background Papers for the Developing Country Investment Negotiators’ Forum (Oct. 1-2, 2007), http://www.iisd.org/pdf/2007/inv_agreements_reg_state.pdf (explaining that a State’s *bona fide* exercise of police powers excludes the obligation to compensate).

⁶⁷⁰ Alvarez & Brink, *supra* note 481, n.19, at 322.

‘necessary to protect the public welfare.’”⁶⁷¹ On the other hand, if the NPM provision is not self-judging, then the scope of public order would be closer to the concept of police powers⁶⁷² and curtail the host State’s regulatory power so that only situations like violent protests or ongoing street demonstrations that destabilize the presidential authority of a country may have the chance of raising a defense out of the public order clause. This was indeed the situation that Argentina faced in the economic crisis from 2001 to 2002.⁶⁷³ The precise nature of the NPM provision is therefore important for tribunals to determine because questions pertaining to whether a State has the right to identify the existence of an economic crisis and follow-up with responsive measures, whether the emergency measures should be subject to tribunal scrutiny, and whether the public order clause releases a host State from the obligation to compensate are all affected.⁶⁷⁴

2. The Conflation Method

Under the conflation method, the treaty provision and customary international law are interpreted together so that the criteria provided under customary law becomes a part of the requirement of the treaty provision.⁶⁷⁵

⁶⁷¹ *Id.* n. 19, at 323.

⁶⁷² Mann, *supra* note 669, at 6.

⁶⁷³ For a brief overview of Argentina’s economic history and a claim that poor economic policies drove an ordinary recession into a grave situation, see SAXTON, *supra* note 574.

⁶⁷⁴ VITERBO, *supra* note 575, at 272.

⁶⁷⁵ See Kurtz, *Adjudging Security*, *supra* note 183 (identifying the relationship between the NPM provision and the customary necessity defense used by the Argentine ICSID tribunals as confluence, *lex specialis*, and primary-secondary to advocate the last methodology). Many other scholars also choose to describe the Argentine ICSID awards in a similar manner. *E.g.*, Andreas von Staden, *Towards*

For example, after the CMS tribunal found that the NPM provision was not self-judging and therefore could not be tested under a mere good faith review,⁶⁷⁶ the CMS tribunal adopted the conflation approach by integrating the requirements of ILC Article 25 (assumed to represent the customary law on necessity⁶⁷⁷) into the NPM provision of the U.S.-Argentina BIT. The CMS tribunal conducted an analysis of the necessity defense heavily based on the elements stated in ILC Article 25 prior to engaging in a review of the treaty provision so that when the time came for the NPM provision to be interpreted, the CMS tribunal determined the treaty provision “in the context of [ILC] Article 25.”⁶⁷⁸ The appeal of this approach may be that since the NPM provision of the actual BIT did not provide the conditions for invoking a state of necessity, a tribunal may rightfully rely upon customary international law.⁶⁷⁹ The *Sempra* tribunal clearly offered the position that the absence of an express reference to customary law in a treaty provision would

Greater Doctrinal Clarity in Investor-State Arbitration: The CMS, Enron, and Sempra Annulment Decisions, in 2 CZECH YEARBOOK OF INT’L LAW 207, 225 (Alexander J. Bělohávek & Naděžda Rozehnalová eds., 2011) [hereinafter von Staden, *Towards Greater Clarity*].

⁶⁷⁶ CMS v. Argentina, *supra* note 179, para. 374 (concluding that whether Argentina’s “state of necessity or emergency meets the conditions laid down by customary international law and the treaty provisions” would have to be determined based on a substantive review).

⁶⁷⁷ *Id.* 315 (“The Tribunal, like the parties themselves, considers that Article 25 of the Articles on State Responsibility adequately reflect the state of customary international law on the question of necessity.”).

⁶⁷⁸ *Id.* 357

⁶⁷⁹ *Sempra v. Argentina*, *supra* note 179, para. 376 (stating that “the Treaty provision is inseparable from the customary law standard insofar as the definition of necessity and the conditions for its operation are concerned, given that it is under customary law that such elements have been defined”).

not prevent the application of the customary law on the obligation arising out of an international agreement.⁶⁸⁰

However, of the five Argentine awards discussed here, the *CMS*, *Enron*, and *Sempra* cases were subjected to annulment hearings by the ICSID annulment committees. The *CMS* annulment committee did not annul the award, but delivered a strong criticism of the conflation method used by the tribunal to fault it for analyzing necessity only under customary international law to the exclusion of Article XI of the BIT.⁶⁸¹ In particular, the committee chided that the tribunal did not analyze the relationship between Article XI and the necessity defense under customary law to ultimately determine whether both sources of law were applicable, “simply assuming that Article XI and Article 25 [of the ILC] are on the same footing.”⁶⁸² Despite even stating that the NPM provision of the treaty should have been treated as a *lex specialis*, the committee referred to the limitations of its authority as an annulment committee to refrain from annulling the award⁶⁸³ even though it went as far to identifying the correct interpretative

⁶⁸⁰ *Id.* para. 348

⁶⁸¹ *CMS Annulment*, *supra* note 658, paras. 123, 128 -136.

⁶⁸² *Id.* para. 131.

⁶⁸³ *Id.* para. 136 stating that:

The Committee recalls, once more, that it has only a limited jurisdiction under Article 52 of the ICSID Convention [on the grounds for the annulment of an award]. In the circumstances, the Committee cannot simply substitute its own view of the law and its own appreciation of the facts for those of the Tribunal. Notwithstanding the identified errors and lacunas in the Award, it is the case in the end that the Tribunal applied Article XI of the Treaty. Although applying it cryptically and defectively, it

position as treating Article XI of the BIT as a *lex specialis*.⁶⁸⁴

The *Sempra* annulment committee criticized the conflation approach by stating that “equating Article XI of the BIT with ILC Article 25”⁶⁸⁵ led to manifest errors of law so that the award must be annulled “in respect of failure to apply Article XI of the BIT.”⁶⁸⁶ The *Sempra* annulment committee determined that Article XI is distinguishable from the customary law on necessity in respect “to the sphere of operation of these rules, to their nature and operation, their content, scope, and as well as to their effects.”⁶⁸⁷ The NPM provision of the treaty is intended to operate as a reservation to an act that would have violated the BIT, but for such a provision.⁶⁸⁸ ILC Article 25, as the codification of the customary law on necessity, operates as an excuse by presuming that a breach has already taken place due to the wrongful act of a State so that the task of a tribunal is to determine whether the wrongful act was taken out of necessity as set forth under the conditions of ILC Article 25.⁶⁸⁹ Despite some textual resemblance, ILC Article 25 must not be used as

applied it. There is accordingly no manifest excess of powers.

⁶⁸⁴ *Id.* para 133.

⁶⁸⁵ *Sempra Energy Int’l v. Argentina*, ICSID Case No. ARB/02/16, Decision on the Argentine Republic’s Application for Annulment of the Award, para. 160 (June 29, 2010) [hereinafter *Sempra Annulment*].

⁶⁸⁶ *Id.* para. 159.

⁶⁸⁷ *Id.* para. 112.

⁶⁸⁸ *Id.* para. 187.

⁶⁸⁹ *Id.* para. 200; *CMS Annulment*, *supra* note 658, para. 129.

“a guide to *interpretation* of the terms used in Article XI.”⁶⁹⁰

A month after the *Sempra* annulment, the *Enron* annulment committee made its decision but on different grounds than the previous two annulments. Here, the *Enron* annulment committee annulled the award on the basis of finding that the tribunal did not satisfy some elements, particularly, the “only way” requirement in ILC Article 25.⁶⁹¹ With respect to the conflation of Article XI and the customary law on necessity, the *Enron* annulment committee proclaimed that no annullable error occurred since “it is not for the Committee to determine whether or not that interpretation was correct.”⁶⁹² Unlike what was expected, the *Enron* annulment committee’s decision was inconsistent with the decisions made by the *CMS* and *Sempra* annulment committees, once again leaving the interpretation of the necessity standard in a state of limbo. Arguably, though, the *Enron* annulment committee’s disagreement with the tribunal’s finding that the NPM provision was not relevant upon finding that the conditions stipulated in the ILC Article 25 were not met may, at the minimum, be an implicit acknowledgement that consideration of the NPM provision was due.⁶⁹³

The problem with the conflation method is that the NPM provision may get displaced when the condition of the customary law on necessity are superimposed onto Article XI. Such a reading is redundant because the customary defense is available to all States whether or not it is expressly

⁶⁹⁰ *Sempra* Annulment, *supra* note 685, para. 199.

⁶⁹¹ *Enron* Annulment, *supra* note 641, para. 405.

⁶⁹² *Id.* para 403.

⁶⁹³ *Id.* paras. 404-5. See von Staden, *Towards Greater Clarity*, *supra* note 675, at 221.

included in a treaty. In order to give meaning to Article XI, it should be analyzed as if the customary defense on necessity did not exist because to assign it any other form of interpretation would be to essentially deny the existence of what was negotiated for between the contracting States.⁶⁹⁴ Additionally, the conflation method yields the ironic outcome that one of the provisions under the BIT is denied, while also providing the legal instrument to bring an investment dispute.

3. The Primary/Secondary Method

This approach proposes treating the NPM provision as a primary rule when assumed to be the *lex specialis* on the customary law on necessity while treating the customary defense as a secondary rule.⁶⁹⁵ However, treating the NPM provision as a *lex specialis* leads to two interpretative options that can result in the *lex specialis* either displacing the customary law on necessity or letting the customary rule apply in a residual manner.

The reasoning provided by the *LG&E* tribunal contains some considerations that suggest the displacement of the customary law on

⁶⁹⁴ Burke-White, *State Liability*, *supra* note 183, at 14 (“As a matter of policy, the incorporation of the necessity defense into the NPM clause fails to recognize the actual understanding of the U.S. and Argentina, whereby, in exchange for granting investors greater protections than would have been available in customary law, the states also sought to preserve for themselves greater freedom of action through the NPM clause than would have been available in customary international law.”).

⁶⁹⁵ See Javier El-Hage, *How to Apply the Customary Necessity Rule to the Argentine Cases? An Analysis of ICSID Decisions with Respect to the Interaction between Article XI of the U.S.-Argentina BIT and the Customary Rule of Necessity*, in *YEARBOOK ON INT’L INVESTMENT LAW & POLICY* 2011-2012 447, 471-72 (Karl P. Sauvant ed., 2013) (referring to the primary/secondary method as a “harmonized fallback” decision). See generally Eric David, *Primary and Secondary Rules*, in *THE LAW OF INTERNATIONAL RESPONSIBILITY* 27 (James Crawford et al. eds., 2010) (describing an overview of the primary/secondary rules in the context of international State responsibility).

necessity.⁶⁹⁶ In the course of treating Article XI as a *lex specialis*, the *LG&E* tribunal excluded the application of the customary law on necessity to conclude that Argentina met the requirements of Article XI. Furthermore, it engaged in a knowingly incomplete analysis of ILC Article 25 to claim support of the tribunal's conclusion that Argentina's emergency measure meets the necessity requirement of Article XI.⁶⁹⁷ Whereas the "only way" element of ILC Article 25 was what strongly persuaded the tribunals in *CMS*, *Enron*, and *Sempra* to prevent Argentina from successfully arguing the necessity defense, the *LG&E* tribunal refused to hear a similar argument instead declaring that Article XI demands that a State act based on the several options open to it in order to maintain public order.⁶⁹⁸ In making its determination based on the NPM provision of the BIT rather than customary rule on necessity, the *LG&E* tribunal appears to also have relaxed the absolute standard of necessity to something that can apply if a measure provides "a legitimate way"⁶⁹⁹ even though better jurisprudence would have resulted had the *LG&E* tribunal made a definite choice between displacing or applying residually the customary law on necessity.⁷⁰⁰ This approach is

⁶⁹⁶ The reasoning undertaken with respect to Article XI and the customary law on necessity in the *LG&E* case has been controversial, but the purpose here is to provide as simplistically as possible an example of the primary/secondary method where the *lex specialis* operates to displace customary international law. For more on the controversy surrounding the *LG&E* case, see El-Hage, *supra* note 695, at 471. See also Kurtz, *Adjudging Security*, *supra* note 183, at 39.

⁶⁹⁷ *LG&E v. Argentina*, *supra* note 179, para. 258.

⁶⁹⁸ *Id.* para. 239.

⁶⁹⁹ *Id.* para. 239.

⁷⁰⁰ Kurtz, *Adjudging Security*, *supra* note 183, at 39.

not without concerns though. For example, an investor-State tribunal might manifestly exceed its powers⁷⁰¹ if it allows the treaty rule to displace a customary rule especially when the treaty itself does not clearly and unambiguously state that some or all of its provisions shall prevail in the case of a conflict with customary law. Although the investor in *UPS v. Canada* had contended that Canada's conduct should be reviewed under the relevant articles of the ILC, the NAFTA tribunal declared that the ILC Articles do not apply because Canada's conduct should be reviewed under the specific provisions in the NAFTA under the principle of *lex specialis*.⁷⁰²

The alternative option is to designate the *lex specialis* as the primary rule so that the customary norm will operate residually as the secondary rule. The *Continental Casualty* tribunal and the annulment committees of *CMS* and *Sempra* relied on the primary/secondary rule approach to analyzing the relationship between the NPM provision of the BIT and the customary defense on necessity. In *Continental Casualty*, the tribunal reasoned that although the conditions under which Article XI and ILC Article 25 operate are different, a connection exists between the two sources of law so that it would be appropriate for the tribunal to analyze Article XI unless ILC Article 25 aids the interpretation of the treaty provision.⁷⁰³ The *CMS* annulment commitment strongly emphasized the differences between Article XI and ILC Article 25 to find that the tribunal had made a manifest error of law.

⁷⁰¹ ICSID Convention, *supra* note 52, art. 52.

⁷⁰² United Postal Service of America Inc. v. Canada, UNCITRAL, Award on the Merits, paras. 59-62 (May 24, 2007) [hereinafter *UPS v. Canada*].

⁷⁰³ *Continental Casualty v. Argentina*, *supra* note 179, paras. 166-68.

Unlike the tribunal which was rebuked for not taking a clear position, the CMS annulment committee stated that “the excused based on customary international law could only be subsidiary to the exclusion based on Article XI.”⁷⁰⁴

In supporting the primary/secondary approach, the *Sempra* annulment committee found that the tribunal also made a manifest error of law when it incorrectly determined that ILC Article 25 is the primary rule that prevails over the NPM provision when it should have been Article XI.⁷⁰⁵ Under international law, this method has grounding in the jurisprudence of the ICJ as reflected in the *Oil Platforms* case. In the *Oil Platforms* case, the ICJ did not agree that the treaty exception allowing a State to take measures necessary to protect essential security interests was intended to override the international law rules on the use of force; accordingly, the Court applied the customary rules on self-defense to gain premise for the interpretation of the treaty standard that the measure taken was, indeed, necessary for the protection of essential security interests.⁷⁰⁶

4. Other Related Interpretation Concerns

Further understanding of the public order clause as used in Article XI of the U.S.-Argentina BIT may be realized when examining it from a liability and compensation standpoint. When tribunals and scholars

⁷⁰⁴ CMS Annulment, *supra* note 658, para. 132.

⁷⁰⁵ *Sempra* Annulment, *supra* note 685, para. 208.

⁷⁰⁶ *Oil Platforms* case, *supra* note 667, para. 41 (“The [ICJ] cannot accept that [the underlying treaty] was intended to operate wholly independently of the relevant rules of international law on the use of force...”).

describe the public order clause as, for instance, a “carve out,”⁷⁰⁷ “exception,”⁷⁰⁸ “emergency exception,”⁷⁰⁹ “exemption,”⁷¹⁰ “circumstance precluding wrongfulness,”⁷¹¹ “ground for exclusion,”⁷¹² or “derogation clause,”⁷¹³ it becomes unclear as to whether these words are being used as a legal term of art, in a vernacular sense, or something in-between. Professor Salacuse explains that provisions like Article XI “except contracting parties from core treaty obligations under exceptional circumstances in which a country’s important national interests are at stake,”⁷¹⁴ but in practice, the

⁷⁰⁷ E.g., SALACUSE, *supra* note 42, at 398 (“Thus, most investment treaties have provisions that carve out exceptions to the general standards of treatment that they seek to apply to investments between the two countries.”).

⁷⁰⁸ E.g., OECD, *INTERNATIONAL INVESTMENT PERSPECTIVES* 168 (OECD 2006).

⁷⁰⁹ E.g., Ian A. Laird et al., *International Investment Law and Arbitration: 2008/2009 in Review*, in *YEARBOOK ON INT’L INVESTMENT LAW & POLICY 2009-2010* 87, 139 (Karl P. Sauvant ed., 2010).

⁷¹⁰ E.g., Anne van Aaken & Jürgen Kurtz, *Emergency Measures and International Investment Law: How Far Can States Go?*, in *YEARBOOK ON INT’L INVESTMENT LAW & POLICY 2009-2010* 505, 534 (Karl P. Sauvant ed., 2010) (“In general, both these categories of *exemption* are relatively rare and reflect new trends in investment treaty rule-making. In contrast, older investment treaties will only typically *exempt* measures “necessary” to maintain “public order” or to protect “essential security interests.”). See, e.g., *CMS v. Argentina*, *supra* note 179, para. 99 (Argentina argued that its economic emergency should be “grounds for exemption of liability under international law and the Treaty”).

⁷¹¹ *State Responsibility Draft with Commentaries*, *supra* note 367, art. 27, at 85.

⁷¹² *LG&E v. Argentina*, *supra* note 179, para. 261.

⁷¹³ E.g., *Sempra Energy Int’l v. Argentina*, ICSID Case Nos. ARB/02/16 & ARB/03/02, Opinion of José E. Alvarez, para. 51 (Sep. 28, 2007) (when discussing the public order/essential security derogation clause in the U.S. BIT, which is identical to Article XI of the U.S.-Argentina BIT) [hereinafter *Sempra*, Alvarez Opinion].

⁷¹⁴ SALACUSE, *supra* note 42, 398.

Argentine ICSID awards have shown that the issue is actually much less straightforward because the outcome on liability and compensation will significantly change depending on how NPM provisions like Article XI are viewed by tribunals.

Additionally, the period of calculation for damages appears to be affected by how the NPM provision is categorized. Professor Burke-White contends that if the role of NPM provisions is “not intended to prevent liability, they would not in fact serve the purpose of guaranteeing greater freedom of action to states in cases of emergency as such states would remain liable notwithstanding the NPM clause.”⁷¹⁵ Burke-White’s concern was displayed when the CMS tribunal stated that even if the Respondent State had met the necessity requirements established in the NPM provision and/or Article 25 of the ILC,⁷¹⁶ it would not free Argentina from liability or the duty to compensate in the absence of a restitution agreement between the parties; without such an agreement, the tribunal stated that it would determine the amount of compensation.⁷¹⁷ This position on compensation was rejected, although not annulled, by the CMS annulment committee when it declared that the NPM provision of “Article XI, if and for so long as it applied, excluded the operation of the substantive provisions of the BIT” so that no compensation would be owed during the period of economic crisis.⁷¹⁸ This interpretive approach is consistent with the previous finding

⁷¹⁵ Burke-White, *supra* note 183, at 16.

⁷¹⁶ *Id.* n. 50. See also CMS v. Argentina, *supra* note 179, para. 317.

⁷¹⁷ CMS v. Argentina, *supra* note 179, para. 408.

⁷¹⁸ CMS Annulment, *supra* note 658, para. 146.

made by the *LG&E* tribunal which declared that “Article XI establishes the state of necessity as a ground for exclusion from wrongfulness of an act of the State, and therefore, the State is exempted from liability.”⁷¹⁹ Accordingly, the same tribunal held that Argentina is “exempt of responsibility” for the consequences of the measures enacted during the state of necessity, which began on December 1, 2001 and ended on April 26, 2002.⁷²⁰ *Continental Casualty* also followed the same approach when it did not include breaches arising during the state of necessity in its calculation for compensation.⁷²¹ The *Sempra* tribunal had awarded the Claimant, but the *Sempra* annulment committee annulled the entire award even for breaches occurring outside the period of the state of necessity because “Article 25 does not offer a guide to interpretation of the terms used in Article XI. The most that can be said is that certain words or expressions are the same or similar.”⁷²² With the Argentine ICSID tribunals taking substantially different stances on the issue of whether a state of necessity precludes liability and compensation,⁷²³

⁷¹⁹ *LG&E v. Argentina*, *supra* note 179, para. 261.

⁷²⁰ *Id.* para. 266 (“Based on the analysis of the state of necessity, the Tribunal concludes that, first, said state started on December 1, 2001 and ended on April 26, 2003; second, during that period Argentina is exempt of responsibility, and accordingly, the Claimants should bear the consequences of the measures taken by the host State.”).

⁷²¹ *Continental Casualty v. Argentina*, *supra* note 179, para. 304.

⁷²² *Sempra Annulment*, *supra* note 685, para. 199.

⁷²³ Rocío Digón, *The Decision on Liability in LG&E v. Argentina*, in *THE REASONS REQUIREMENT IN INTERNATIONAL INVESTMENT ARBITRATION: CRITICAL CASE STUDIES* 117, 144 (Guillermo Aguilar Alvarez & W. Michael Reisman eds., 2008) (stating that this issue is unsettled in international law); SERGEY RIPINSKY & KEVIN WILLIAMS, *DAMAGES IN INTERNATIONAL INVESTMENT LAW* 341 (BICIL 2008) (“At this point in time, this question does not have a clear-cut answer; the law is

Professor Reisman nonetheless reminds us that the purpose of international investment law should not be compromised:

[O]f course governments in these circumstances must take measures to restore public order, but from the investment *law* standpoint – and this is for the future of all investments – international investment law says you may do it, but you must pay compensation. If exceptions are made for like these or other circumstances, the entire purpose of modern investment law, which is to accelerate the movement of private funds into developing countries for development purposes, will be frustrated.⁷²⁴

But does it continue to make sense when these private funds, which were collected for the development of a developing country, have to be paid-out for allegedly breaching an investment treaty under which the BIT provides no possibility of excuse? In all fairness, and despite the accusation of the tribunal in *LG&E* that international law does not mention whether a state of necessity precludes compensation,⁷²⁵ it is not completely silent. The ILC Articles on State Responsibility avoids a straightforward answer thus leaving that determination up to the arbitral tribunals who are ideally in the best position to understand the facts of each case. Nonetheless, the ILC Articles on State Responsibility identifies six circumstances that preclude wrongfulness: consent (Article 20), self-defense (Article 21),

unsettled.”).

⁷²⁴ *Sempra v. Argentina*, *supra* note 179, para. 396 (quoting Professor Reisman) [emphasis in original].

⁷²⁵ *LG&E v. Argentina*, *supra* note 179, para. 260.

countermeasures (Article 22), *force majeure* (Article 23), distress (Article 24), and necessity (Article 25). When testifying for the Claimant in *Sempra*, Professor Alvarez asserted that the provision on supervening impossibility of performance in Article 61 of the Vienna Convention on the Law of Treaties and the ILC articles on *force majeure*, distress, and necessity are the “relevant rules of international law applicable in the relations between the parties’ which... need to be used when interpreting the U.S.-Argentina BIT.”⁷²⁶ A defense based on *force majeure* is not frequently discussed within the realm of international investment law, but has managed to receive minor spotlight in *CMS*, *Enron*, and *Sempra*.⁷²⁷ In commenting specifically about the public order clause, Alvarez explains that Article XI “needs to be understood in light of the customary international law exception for ‘distress’ as [] codified... in [ILC] Article 24” and that distress, which in practice must invoke elementary humanitarian considerations during a state of extreme urgency,⁷²⁸ does not involve the unilateral actions of a State to alleviate its economic circumstance.⁷²⁹ However, whether *force majeure* or distress will play an increased role in international investment law is dubious.⁷³⁰

Nevertheless, in the case that a circumstance precluding

⁷²⁶ *Sempra*, Alvarez Opinion, *supra* note 713, para. 51.

⁷²⁷ *CMS v. Argentina*, *supra* note 179, paras. 227, 256; *Enron v. Argentina*, *supra* note 179, paras. 214-18; *Sempra v. Argentina*, *supra* note 179, paras. 243-46.

⁷²⁸ *Sempra*, Alvarez Opinion, *supra* note 713, para. 58.

⁷²⁹ *Id.*

⁷³⁰ TITI, *supra* note 79, at 258 (arguing that, in this case, *force majeure* rather than distress is “a more likely player in investment disputes, although it is likely that its own role as a state defense will also remain marginal.”)

wrongfulness is found, Article 27 of the ILC states that a finding of a circumstance precluding wrongfulness is “without prejudice to: (a) compliance with the obligation in question, if and to the extent that the circumstance precluding wrongfulness no longer exists; (b) the question of compensation for any material loss caused by the act in question.”⁷³¹ The ILC Commentary on Article explains that the expression “without prejudice to” was inserted to recognize that even though “it is not possible to specify in general terms when compensation is payable,”⁷³² compensation would be due under certain circumstances. In practice, the application of ILC Article 27 has produced some controversy. The *LG&E* tribunal was criticized for equating this deliberate omission (to not enumerate the circumstances that mandate compensation in ILC Article 27) with not having to analyze the issue of when compensation would be payable under a state of necessity.⁷³³ But, this finding was made in the midst of an unsettled debate where Claimant argued that “Article 27 [of the ILC] makes clear that Argentina’s obligations to Claimants are not extinguished and Argentina must compensate Claimants for the losses incurred as a result of the Government’s

⁷³¹ State Responsibility Draft with Commentaries, *supra* note 367, art. 27. *See also* *Enron v. Argentina*, *supra* note 179, para. 303 (“This is not to say that the Articles are a treaty or even a part of customary law themselves; it is simply the learned and systematic expression of the development of the law on state of necessity by decisions of courts and tribunals and other sources along a long period of time.”).

⁷³² State Responsibility Draft with Commentaries, *supra* note 367, cmt. 1, at 86. *See id.* at 71 (the ILC Commentary on Article 27 states that a circumstance precluding wrongfulness does not terminate a treaty, but instead requires that performance resumes once the period of necessity ends).

⁷³³ Digón, *supra* note 723, at 143. *See also* *LG&E v. Argentina*, *supra* note 179, para. 260.

actions”⁷³⁴ and Respondent interpreted the same ILC Article 27 as “requir[ing] compensation only for the damage arising after the emergency is over, and not for that taking place during the emergency period”⁷³⁵ and not “requir[ing] the payment of compensation for measures subject to the defense of necessity.”⁷³⁶ Despite efforts to find clues in international law on the matter of whether a state of necessity precludes compensation, progress remains to be seen. Whereas the CMS tribunal was “satisfied that Article 27 establishes the appropriate rule of international law on this issue,”⁷³⁷ the CMS annulment committee said that the tribunal was incorrect in applying Article 27 of the ILC when it did not even accept Argentina’s necessity defense because, first, “Article 27 covers cases in which the state of necessity precludes wrongfulness *under customary international law*,”⁷³⁸ and second, it should have separately assessed the compensation matter under the treaty to determine if the State’s actions were within the scope of Article XI of the BIT, but where Article XI applies, compensation would be excluded.⁷³⁹

⁷³⁴ E.g., *LG&E v. Argentina*, *supra* note 179, para. 225 (discussing the claimant’s view).

⁷³⁵ E.g., *Sempra v. Argentina*, *supra* note 179, para. 394 (discussing the respondent’s view).

⁷³⁶ E.g., *CMS Annulment*, *supra* note 658, para. 139.

⁷³⁷ *CMS v. Argentina*, *supra* note 179, para. 390.

⁷³⁸ *CMS Annulment*, *supra* note 658, para. 145 (“In the present case, the Tribunal rejected Argentina’s defense based on state of necessity. Thus Article 27 was not applicable and the paragraphs relating to that Article were obiter dicta which could not have any bearing on the operative part of the Award.”) [emphasis supplied in text].

⁷³⁹ *Id.* para. 146.

Similarly, the *Sempra* annulment committee declared that the tribunal had made a manifest error of law when it applied Article 27 of the ILC to Article XI of the BIT, as discussed above, to annul the entire award.⁷⁴⁰ The question of how liability and the duty to compensate will be affected eventually requires an appreciation of how each source of international law can apply in an investor-State arbitration.

III. Concluding Remarks

This Chapter discussed the interpretative methods used by the Argentine ICSID tribunals to demonstrate the intricacies of interpreting the public order carve-out as used in Article XI of the U.S.-Argentina BIT and ILC Article 25. The problem with the public order carve-out is that even if the general rule of interpretation provided for in Article 31(1) of the Vienna Convention on the Law of Treaties commands a treaty to be interpreted according to its “ordinary meaning,” the reality is that the term “public order” is subject to debatable meanings as previously discussed in this Dissertation.⁷⁴¹ Furthermore, the application of the necessity standard is also an unsettled area of international investment law whether in the context of an investment treaty or under customary international law, therefore creating a degree of interpretative uncertainty when analyzing the public order carve-out. From a tribunal perspective, proper application of Article 25 of the ILC is difficult because one condition is that the necessity defense may not be invoked if a State has contributed to the situation of necessity.⁷⁴²

⁷⁴⁰ *Sempra Annulment*, *supra* note 685, para. 120.

⁷⁴¹ *See* ch. 2 of this Dissertation.

⁷⁴² State Responsibility Draft with Commentaries, *supra* note 367, art. 25, para. 2(b).

Overcoming the no contribution requirement of ILC Article 25 creates an unreasonably high burden of proof because it is actually difficult to think of a context where the State invoking the necessity defense is completely isolated from that situation.⁷⁴³ An economic crisis does not fall into the category of *force majeure*, but is the result of “a chain of Government acts or omissions”⁷⁴⁴ that culminate to produce a negative effect on a country’s economy.⁷⁴⁵ But it is at this precise point that a host State may choose to intervene by taking regulatory action in response to a collapse in its economic, political, and/or social structure even in violation of an international investment agreement. In an extreme situation, the concept of public order may be limited to the exercise of police power at the expense of the societal, cultural, and political values of a State, thus disregarding the reality that public order varies in time and space.⁷⁴⁶ The more suitable option would be to allow an investment treaty public order carve-out that can operate to meet the emergency and non-emergency regulatory demands of a State.

The first right to regulate exception appeared in Article 11 of the China-Singapore BIT.⁷⁴⁷ However, this regulatory space preserving

⁷⁴³ See Luzi, *supra* note 46, at 16.

⁷⁴⁴ *Id.*

⁷⁴⁵ TITI, *supra* note 79, at 254 (“It is difficult to imagine that a state will not have *any* [emphasis supplied] contribution to a situation of necessity; in the case of an economic crisis, as in the case of an ecological disaster, an epidemic, etc., the state will often have contributed, for example by delaying in taking appropriate action.”).

⁷⁴⁶ See *U.S. – Gambling*, *supra* note 269, para. 6.461 & ch. 2.II.B.2 of this Dissertation.

⁷⁴⁷ China-Singapore BIT, art. 11, Nov. 21, 1985. Under the heading, “Prohibitions

exception did not become a model for the majority of the BITs concluded thereafter. Even though the regulatory exception became common in BITs concluded between the developing States, particularly among the Southeast Asian and African countries, Article 11 of the China-Singapore BIT was a creation of the developing States and consequently lacked the support of the developed States in a BIT universe primarily designed by the developed States. Although it can be argued that exceptions for exercise of regulatory authority were not included in investment treaties to prevent abuse by the host States which already had the advantage over investors since an investor's business is established in the territory of the host States and therefore inevitably more likely to be exposed to the risk of a host State's regulatory acts, it is to the advantage of both home and host States to explicitly include regulatory space exceptions in IIAs. Such a practice would place the home State in a better position to control for uncertainties arising from the regulatory space context consistent with its investors' legitimate expectations. Likewise, the host State can benefit from including an exception provision that preserves the right to regulate since it can control its risk of being exposed to an unexpected, high compensation payout by demanding in advance the areas of regulatory space to be excluded from the scope of the IIA. Concerns that regulatory space exceptions would undermine the international investment law system may be alleviated by the

and Restriction," provision states that:

The provisions of this Agreement shall not in any way limit the right of either Contracting Party to apply prohibitions or restrictions of any kind or take any other action which is directed to the protection of its essential security interests, or to the protection of public health or the prevention of diseases and pests in animals or plants.

checks afforded by investment treaty standards such as the fair and equitable treatment, legitimate expectations, and expropriation principles. This approach was observed in the recent ICSID decision in *Philip Morris v. Uruguay*.⁷⁴⁸ Moreover, some model BITs have undergone revisions that focus on improving the investor-State dispute settlement system and safeguarding the right to regulate. Colombia is revising its 2011 version of the model BIT to better preserve its regulatory authority. As previously mentioned in Chapter 3 of this Dissertation, the model BITs of Norway and India also reflect this trend. The absence of an explicit regulatory space exception in IIAs is an Achilles' heel that can be avoided by including a standard public order carve-out as explained in greater detail in the following Chapter 5.

⁷⁴⁸ *Philip Morris v. Uruguay*, ICSID Case No. ARB/10/7, Award (July 8, 2016).

Chapter 5: A Standard Public Order Carve-out in IIAs to Balance Stakeholders' Interests

I. Proposal of a Sample Standard Public Order Carve-out

As previously examined in Chapters 1 and 2 of this Dissertation, publications including annual reports and guiding principles authored by international organizations use the term “right to regulate” to describe the preservation of regulatory space by host States in a general sense. Modern IIAs such as the TPP and TTIP proposal similarly use the right to regulate language in an abstract fashion that leaves the interpretative scope wide open. However, the right to regulate principle would be difficult to sustain without a concrete concept and create further problems of inconsistencies that would once again put into question the legitimacy of the international investment law system. This Dissertation proposes expanding the NPM public order carve-out to form a standard public order carve-out provision as a cohesive place where exceptions regarding the right to regulate may be found. Similar to how a section is typically devoted to ISDS in IIAs, an exceptions section should be demarcated so that the standard public order carve-out provision can be placed therein. The exceptions section of the IIA can provide a single place for pulling together other regulatory exceptions. One possible structure of an exceptions section may include carve-outs that address the following areas: emergencies and national and/or essential security interests; non-emergencies affecting public interest matters; and, financial regulations. Alternatively, under the scenario that a single exceptions provision is implemented to include all facets of a State’s regulatory act, an investment tribunal may interpret the provision to

provide an exhaustive list, in which case, a previously unconceived measure may fall out of the scope of the exceptions provision or, in a worst-case scenario, lose effect for being casting an overly, unworkable broad scope. The cost-benefit of each type of exceptions provision should be something for each State to consider so that its regulatory needs are best addressed in light of its investment treaty obligations.

The following standard public order carve-out may provide a template for when the contracting States draft their provision allowing for the right to regulate:

Subject to the requirement that such measures are *bona fide* and not applied as a disguised restriction on international investment, this Treaty shall not preclude the application by a Party of measures adopted, maintained, or enforced by a government in pursuance of legitimate policy objectives when the measure taken for public interest bears an objectively reasonable and proportionate relationship to important rational policies that [are limited to/not limited to] the following regulatory measures:

- i. to maintain public order or to protect public morals or public safety;
- ii. to protect human, animal, or plant life or other areas of public health;
- iii. to protect the environment;
- iv. to promote or protect cultural diversity or cultural assets such as national treasures of artistic, historic, or archaeological value; or

- v. to secure compliance with laws and regulations that are not consistent with the provisions of this Agreement.

In the absence of a central institution bound by a multilateral agreement, it could be difficult to realistically persuade the contracting States to accept a standard public order carve-out containing a fixed list of legitimate policy objectives. For this reason, the standard public order carve-out suggests that the determination of an illustrative or exhaustive list should be decided between the contracting States which are in a better position to judge the different implications of adopting an illustrative or exhaustive list. The following sections provide an in-depth consideration of the proposed standard public order carve-out by analyzing the differences between it and the existing approaches to the right to regulate in investment treaties.

A. Evolving Object and Purpose of IIAs

The perspectives of the IIA stakeholders continuously challenge the purpose of IIAs. The gradual textual transformation presented in Chapter 3 of this Dissertation is a testament to the kinds of concerns affecting States. During the era that FCNs prevailed, the public order carve-out was included to address religious concerns or to restrict the right to travel and the right to assemble. By the 1950s and 1960s, the term “necessary” was included in the public order carve-out although the intent of its operation has not been readily apparent. During the peak years of the BITs in the 1990s, the public order carve-out was considered to be a potential source of threat for the United States. It was during this period in the 1990s when BITs flourished that the United States decided to exclude the public order carve-out. The mood rapidly plunged in the 2000s, which was when the NAFTA was

criticized and the ICSID tribunals made exorbitant awards against Argentina. Modern IIAs concluded since the 2000s have experimented with various ways of balancing interests in the investment treaties. During the course of this evolution, the overall purpose of IIAs has changed to engage the aggregate community interests of the IIA stakeholders. One consequence of this effort has been to attempt to secure regulatory space for host States through the right to regulate concept in the preambles of the investment treaties. To better meet the changing needs of the IIA stakeholders, the proposed standard public order carve-out suggests a list of legitimate policy objectives from which the contracting States can flexibly use to negotiate the standard public order carve-out according to the demands of their regulatory interests.

Although an undefined concept in international investment law, an idea of what the right to regulate concept entails may be illustrated in the preambles of modern IIAs, which international investment tribunals interpret according to the generally established rules of treaty interpretation. The Vienna Convention on the Law of Treaties (VCLT) provides the seminal interpretative authority for international investment agreements. Article 31(1) of the VCLT instructs that “[a] treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose.”⁷⁴⁹ Many investment tribunals refer to Article 31 of the VCLT as the “first point of reference”⁷⁵⁰ to determine the ordinary meaning of the words contained in

⁷⁴⁹ Vienna Convention on the Law of Treaties, art. 31(1), May 23, 1969, 1155 U.N.T.S. 331 [hereinafter Vienna Convention].

⁷⁵⁰ See, e.g., *Sempra Annulment*, *supra* note 685, paras. 188-89

the treaty. Moreover, Article 31(2) of the VCLT states that the preamble may be used to identify the object and purpose of a treaty. This may leave investment tribunals to consider the extent of the binding force of the preamble when interpreting the preambles in the more recent generation of IIAs that contain statements on safeguarding certain public interests.⁷⁵¹ On one hand, the preamble is said to be without any actual binding authority and that its function is to set the contextual stage for the rest of the treaty agreement.⁷⁵² In contrast, tribunals may place greater weight on the preamble to fill interpretative gaps in the treaty. In 1952, the ICJ dealt with a similar issue to conclude that the language used in the preamble was clearly intended to be binding.⁷⁵³ The question of whether the preamble language in an IIA has a legally binding effect may arise given that the preambles of recent IIAs increasingly provide specified regulatory interests. But, more importantly, the right to regulate language in the preambles of investment treaties invites investor-State tribunals to consider investment protection together with other competing values that arise out of the regulatory interests of a host State.

In the case of international investment law, arbitrators of investor-

⁷⁵¹ See ch. 3.B.1 of this Dissertation.

⁷⁵² See Peter Muchlinkski, *Negotiating New Generational International Investment Agreements: New Sustainable Development Oriented Initiatives*, in SHIFTING PARADIGMS IN INTERNATIONAL INVESTMENT LAW: MORE BALANCED, LESS DIVERSIFIED 41, 46 (Steffen Hindelang & Markus Krajewski eds., 2016).

⁷⁵³ *Rights of Nationals of the United States of America in Morocco (France v. U.S.)*, 1952 I.C.J. 176, 184 (Aug. 27) (concluding on the basis that the preamble of the Algeiras Act provided for the guarantee of equality of treatment in the preamble that “it seems clear that the principle was intended to be of a binding character and not merely an empty phrase”).

State tribunals and foreign investors may be pressed to acknowledge the changing purpose of IIAs by giving serious consideration to the right to regulate language when the preamble expressly provides for various regulatory interests relating to legitimate public welfare objectives, environment, public health and safety, culture, human rights, and sustainable development. It is a noticeable departure from the single-minded goal of IIAs on investment protection.⁷⁵⁴ Contracting States attempt to preserve regulatory space via the preamble to prevent the investment treaty from narrowly focusing on investment protection. Without such an explicit expression, a host State may not be able to secure its regulatory space when put to test against the object and purpose of investment treaties. This may occur particularly when an investment tribunal engages in a teleological method of interpretation that overly emphasizes the “object and purpose” element of Article 31(1) of the VCLT.⁷⁵⁵ For example, the ICSID tribunal in *Siemens v. Argentina* sought to know the object and purpose of the Germany-Argentina BIT by examining the preamble to conclude that the parties’ intention “to create favorable conditions for investments and to stimulate

⁷⁵⁴ See VanDuzer, *supra* note 418, at 172; Suzanne A. Spears, *The Quest for Policy Space in a New Generation of International Investment Agreements*, 13 J. INT’L ECON. L. 1037, 1065 (2010). *But see* Anthea Roberts, *Triangular Treaties: The Extent and Limits of Investment Treaty Rights*, 56 HARV. INT’L L.J. 353, 373 (identifying investor protection and the de-politicization of investor-State disputes as the two main objectives of IIAs).

⁷⁵⁵ *Plama Consortium*, *supra* note 238, para. 193 (quoting Sir Ian Sinclair’s cautionary statement that the “risk that the placing of undue emphasis on the ‘object and purpose’ of a treaty will encourage teleological methods of interpretation [which], in some of its more extreme forms, will even deny the relevance of the intentions of the parties”). *See also* NEWCOMBE & PARADELL, *supra* note 43, at 115.

private initiative”⁷⁵⁶ was clear. Based on the preamble language that the parties agreed to create and maintain favorable conditions for investments, the ICSID tribunal in *SGS v. Philippines* concluded that “[i]t is legitimate to resolve uncertainties in its interpretation so as to favor the protection of covered investments.”⁷⁵⁷ In both of these cases, the narrowly drafted object and purpose of the investment treaty operated to tip the balance in favor of investors since regulatory objectives were not specified in the preamble. When regulatory interests are established in the preamble of investment treaties, the preamble language sets the tone for the rest of the agreement and may also direct the investor-State tribunal to interpret the object and purpose of the treaty with regards to the regulatory space carved out by the host State. Without such a right to regulate language in the preamble, investment tribunals may be inclined to follow the presumption created in favor of investment protection so that the substantive obligations of the IIAs are broadly applied while exceptions are restrictively reviewed.⁷⁵⁸ However, language aimed to preserve regulatory space must also be present as a substantive provision of the IIA to become a legally enforceable right since the preamble merely offers an “interpretative device.”⁷⁵⁹ A standard public order carve-out can minimize the hortatory nature of the right to regulate language in the preambles of investment treaties to provide more consistent

⁷⁵⁶ *Siemens A.G. v. Argentina*, ICSID Case No. ARB/02/8, Decision on Jurisdiction, para. 81 (Aug. 3, 2004).

⁷⁵⁷ *SGS v. Philippines*, ICSID Case No. ARB/02/6, Decision of the Tribunal on Objections to Jurisdiction, para. 116 (Jan. 29, 2004).

⁷⁵⁸ *See, e.g., Enron v. Argentina*, *supra* note 179, para. 331; *Sempra v. Argentina*, *supra* note 179, para. 373.

⁷⁵⁹ *TITI*, *supra* note 79, at 122.

results than what has been observed in the ICSID cases against Argentina discussed in this Dissertation.

If the traditional application of the NPM provision was usually confined to protecting essential security interests, the Argentine ICSID awards introduced a new era of interpretation that permitted economic necessity as a viable defense under the NPM provision of the BIT. However, was it foreseeable that Article XI of the U.S.-Argentina BIT would be susceptible to greater degrees of interpretation? Although the plain text meaning of Article XI does not prohibit situations of economic necessity, in a parallel comparison discussing the other prong of the NPM provision on essential security interests, Professor Vandeveldelde confidently explains that the drafters did not envision a broad application of the essential security interest exception and that there is “no evidence... to broaden its application to include economic crises.”⁷⁶⁰ To support his view, Vandeveldelde explains that when the International Trade Organization (ITO) Charter was being negotiated during the 1940s, a period characterized by great economic slump in Europe, the United States recognized that it could be adversely affected by economic crises and therefore formulated certain carve-out provisions that would permit it to balance domestic economic interests against the international obligations arising from treaties.⁷⁶¹ For example, the United

⁷⁶⁰ Vandeveldelde, *Rebalancing*, *supra* note 188, at 456 (stating “history of exception suggests that the drafters did not contemplate its [essential security interests clause] exception to economic crises”).

⁷⁶¹ The purpose of the ITO Charter was to establish the ITO in 1948 as a special agency of the United Nations, but it never entered into force. For more background on the ITO, see, e.g., DAVID A. DEESE, *WORLD TRADE POLITICS: POWER, PRINCIPLES, AND LEADERSHIP* 41-50 (Routledge 2008). At the time, multilateral trade was handled through the GATT and eventually replaced by the

States prepared for bad economic situations by including in the U.S. FCN treaties exception provisions that would allow foreign exchange restrictions to be imposed “to the extent necessary to prevent its monetary reserves from falling to a very low level or to effect a moderate increase in very low monetary reserves.”⁷⁶² The United States may have also enabled its contracting States to derogate from national treatment obligations to manage adverse economic situations that can arise in the host State.⁷⁶³ The U.S.-China FCN treaty effectively subjected the national treatment obligations to the laws of the host State⁷⁶⁴ whereas the U.S.-Ethiopia FCN treaty flatly excluded the national treatment provision.⁷⁶⁵ Critiquing that the essential security interests clause does not bear any resemblance to the provisions typically drafted to address economic crises, Professor Vandeveldé’s comment that the essential security interests exception “is an exception that

formal establishment of the WTO. See WTO, *The GATT Years: From Havana to Marrakesh*, https://www.wto.org/english/thewto_e/whatis_e/tif_e/fact4_e.htm. See generally Peter Neumann, *The Relationship between GATT and the United States*, 3 CORNELL INT’L L.J. 63 (1970).

⁷⁶² U.S.-Greece FCN Treaty, art. XV(2), Aug. 3, 1951; U.S.-Pakistan FCN Treaty, art. XII(2), Nov. 12, 1959; U.S.-Japan FCN Treaty, *supra* note 393, art. XII(2); U.S.-Nicaragua FCN Treaty, art. XII(2), Jan. 21, 1956. Another variation of the balance-of-payments exception permitted the restriction “to the extent necessary to maintain or restore adequacy to its monetary reserves....” U.S.-Luxembourg FCN Treaty, *supra* note 394, art. XI(2); U.S.-Belgium FCN Treaty, *supra* note 393, art. X(2); U.S.-Netherlands FCN Treaty, *supra* note 391, art. XII(2). See Kenneth J. Vandeveldé, *The Bilateral Investment Treaty Program of the United States*, 21 CORNELL INT’L L.J. 201, 245 (1988).

⁷⁶³ Vandeveldé, *Rebalancing*, *supra* note 188, at 457.

⁷⁶⁴ U.S.-China FCN Treaty, art. III(3), Nov. 4, 1946. See Vandeveldé, *Rebalancing*, *supra* note 188, at 457, n. 46 (stating that this FCN “subordinated the right of corporations to national treatment to local law”).

⁷⁶⁵ U.S.-Ethiopia FCN Treaty, *supra* note 385, art. VIII.

overbalances all BIT obligations when it applies and the scope of its application is not carefully defined”⁷⁶⁶ may be similarly noted when considering how economic crises can affect the public order exception. However, the scope of the standard public order carve-out being proposed in this Dissertation should not be narrowly tailored to exclude unexpected economic events of a grave degree but cover a slightly broader range of legitimate policy objectives that are important to the State, which may have to be identified on a case-by-case basis.

In general, BITs were concluded to attract investments by providing certain protections to foreign investors. Consistent with this spirit, a large majority of the Argentine BITs including the U.S.-Argentina BIT were concluded as a reaction to the 1989 Argentine economic crisis to attract capital.⁷⁶⁷ Moreover, the riots, shutdowns, hyperinflation, and successive presidential resignations described in the ICSID cases against Argentina were similarly evident in the economic crisis of 1989. Given this context as well as the tumultuous economic history that has been occurring in Argentina at least since the 1930s,⁷⁶⁸ it would be reasonable to argue that Article XI of the U.S.-Argentina BIT was precisely intended to operate as a treaty exception situations of economic crisis so that the host State can avoid committing an international breach of an investment treaty. The United

⁷⁶⁶ *Id.*

⁷⁶⁷ *See, e.g.,* Luzi, *supra* note 47, at 15.

⁷⁶⁸ Sarah Marsh & Brian Winter, Chronology: Argentina’s Turbulent History of Economic Crises, REUTERS (July 30, 2014), <http://www.reuters.com/article/2014/07/30/us-argentina-debt-chronology-idUSKBN0FZ23N20140730> (describing some of Argentina’s economic crises throughout history).

States concluded the BIT with Argentina, a country with known economic troubles, in an effort “to protect U.S. investment and encourage private sector development in Argentina and to support the economic reforms taking place there.”⁷⁶⁹ The CMS tribunal explicitly stated that while some treaties like those covering humanitarian rules for armed conflicts are enacted to specifically apply in the case of necessity, the U.S.-Argentina BIT was “clearly designed to protect investments at a time of economic difficulties or other circumstances leading to the adoption of adverse measures by the Government.”⁷⁷⁰ Furthermore, what if, as contended by Argentina, its economic crisis was truly attributable to external factors that made it a victim of a globalized economy? In a highly intertwined global community, determining the origin of an economic crisis for a particular State is probably an impossible task which makes it even more urgent for IIAs to include a standard public order carve-out that can adjust for the important regulatory issues that arise in both emergency and non-emergency situations of a State.

B. Scope of a Standard Public Order Carve-out

Determining the scope of the standard public order carve-out is crucial to the interpretative process of the investment tribunals because it helps to reduce the adjudicative burden for international investment tribunals while enabling host States to preserve their regulatory space in a consistent manner. Under the proposed standard public order carve-out, a

⁷⁶⁹ Letter from George Bush, U.S. President, to U.S. Senate (Jan. 19, 1993), *available at* http://tcc.export.gov/trade_agreements/all_trade_agreements/exp_000897.asp.

⁷⁷⁰ CMS, *supra* note 179, para. 354.

standard of review is expressly embedded in the provision by including the language “when the measure bears a reasonable relationship to important rational policies.” The role of the phrase “important rational policies” is to emphasize that the State policy must be important and rational to prevent abusive practice of the standard public order carve-out as well as to discourage an overly broad application of the standard public order carve-out.

Broadening the scope of interpretation of the standard public order carve-out may certainly have some benefits like allowing States to preserve their regulatory power, but this approach can be problematic because the public order carve-out in BITs, along with the newer textual variations in the comprehensive FTAs with investment chapters,⁷⁷¹ cannot account for the myriad legitimate policy objectives which could be excused as a legitimate exercise of regulatory State power under IIAs.⁷⁷² Moreover, whether the public order carve-out should function as a catch-all basket that justifies every sort of regulatory act is beyond the intended scope of the proposed standard public order carve-out provision. Scholars such as Professor Alvarez cautions that permitting an overly broad reading of the public order clause may create the undesired assumption that “its object and purpose now includes the right of host states to regulate as they please.”⁷⁷³ Professor Sourgens hypothesizes that moving towards such a liberal direction would destabilize the investment treaty regime by shifting the jurisdiction of

⁷⁷¹ See ch. 4.II of this Dissertation.

⁷⁷² DI BENEDETTO, *supra* note 563, at 212.

⁷⁷³ José E. Alvarez, *The Return of the State*, 20 MINN. J. INT’L L. 223, 237 (2011).

investor-State tribunals into the domestic space of a host State.⁷⁷⁴ While broadening the public order carve-out can more widely capture the right to regulate concept, too much broadening of the public order carve-out can also create an adverse effect that fails to balance the interests of the IIA stakeholders. Therefore, the proposed standard public order carve-out recommends the inclusion of the words “important” and “rational” to describe and limit the type of regulatory policies to be pursued by the States to provide a safety feature against overly broad interpretation that can undesirably water down the goal of investment protection.

Alternatively, the proposed standard public order carve-out can be given a restrictive interpretation similar to the narrowly constructed reading of Article XI of the U.S.-Argentina BIT by a few of the ICSID tribunals. In the worst case, investment tribunals may completely exclude the application of the standard public order carve-out. In fact, during the process of interpreting the NPM provision in Article XI of the U.S.-Argentina BIT, the ICSID tribunals did not analyze the public order clause in isolation instead letting it be overshadowed by the more familiar essential security interest clause. Without fully evaluating the ramifications of combining two distinct carve-outs, the possibility that the public order carve-out may yield different results when interpreted as a stand-alone carve-out with its own set of requirements was dismissed. However, such an approach would undermine the potential of the public order carve-out to operate as a balancing tool for

⁷⁷⁴ FRÉDÉRIC GILLES SOURGENS, *A NASCENT COMMON LAW: THE PROCESS OF DECISIONMAKING IN INTERNATIONAL LEGAL DISPUTES BETWEEN STATES AND FOREIGN INVESTORS* 39-40 (Brill Nijhoff 2015).

the host States.⁷⁷⁵

Moreover, as seen from the examples of the public order carve-out in BITs and investment chapters of comprehensive FTAs,⁷⁷⁶ the States' understanding of the concept of public order is difficult to know and the concept is inherently open-ended. It was this interpretive crevice that Argentina used to appeal to the tribunals that its civil law understanding of public order is distinguishable from the way the term is understood under the common law tradition of the United States. Even if a note is appended to the public order carve-out stating that public order can be invoked only for a genuine and sufficiently serious threat against the fundamental interests of society, the ability of the note to clarify is limited because the element of indeterminacy cannot be completely eliminated from the interpretive process. Subjecting the public order clause to only a narrow scope of interpretation would be a disservice to the international investment regime since conflicting rules and decisions would be prematurely concluded as a "scandal or... structural 'deficiency'" when, in fact, it is a phenomenon that occurs because each of the actors in the international investment regime have purposes that are conflicting and unstable.⁷⁷⁷ Rather than thinking that derogation provisions like the public order clause presents a problem of indeterminacy or exacerbates what is unknown to lessen the legitimate expectations of investors, Professor Di Benedetto

⁷⁷⁵ See Kurtz, *Adjudging Security*, *supra* note 183, at 35 (describing the primary/secondary and conflated approaches).

⁷⁷⁶ See ch. 2.II.C of this Dissertation.

⁷⁷⁷ KOSKENNIEMI, *supra* note 566, at 591.

concludes that the better alternative for the international investment regime would be to structurally recognize that a rule-exception relationship exists from which a general model of exception should be formulated.⁷⁷⁸ While concerns relating to the coherence of international investment law are certainly valid, the conflicting rules, purposes, and principles do serve as an important feature of the international investment regime that foster the growing body of international investment law and recognize the various purposes and different interaction points of the actors.⁷⁷⁹

When considering the issue of scope, the difficulty lies in determining the degree of interpretive scope to give it. A jurisprudence that expansively widens the interpretation of the public order carve-out may set the clock backwards by removing the substantive guarantees of IIAs aimed at providing investment protection. However, an overly narrow interpretation of the public order carve-out may bar host States from taking regulatory acts during times of non-emergencies, but which deal with important issues like the phasing out of nuclear plants in the *Vattenfall* case, legislating for public health in the *Philip Morris* case, protecting an ecological coastal system in the *Bilcon* case, or even observing international climate change commitments as in the pending *TransCanada* case where the claimant

⁷⁷⁸ DI BENEDETTO, *supra* note 563, at 224.

⁷⁷⁹ See UNCTAD, *International Investment Arrangements: Trends and Emerging Issues*, in UNCTAD SERIES ON INTERNATIONAL INVESTMENT POLICIES FOR DEVELOPMENT 57 (2006). See also Jonathan Ketcheson, *Investment Arbitration: Learning from Experience*, in SHIFTING PARADIGMS IN INTERNATIONAL INVESTMENT LAW: MORE BALANCED, LESS ISOLATED, INCREASINGLY DIVERSIFIED 97, 121 (Steffen Hindelang & Markus Krajewski eds., 2016) (stating that although the higher goal of attaining greater consistency in the investment treaty regime should be aspired to, a “limited amount of inconsistency may not be a negative feature of a system”).

has demanded more than fifteen billion dollars.⁷⁸⁰ These are problems that the Vienna Convention cannot answer straightforwardly since Article 31 of the Vienna Convention does not require that the public order carve-out be interpreted either narrowly or broadly.⁷⁸¹ Thus, when interpreting the public order carve-out, investment tribunals have to avoid imposing an exaggerated sense of equilibrium that includes cases which should have been excluded and *vice versa*. Such an interpretative approach ultimately weakens rules and “compels the move to ‘discretion’ which it was the very purpose to avoid.”⁷⁸² The interpretative goal of the standard public order carve-out requires that investment tribunals utilize their decision-making competencies to adjust for a certain level of balance that is neither overly restrictive as seen in Article XI of the U.S.-Argentina BIT nor broad as used in the recently emerging concept on the right to regulate.⁷⁸³

⁷⁸⁰ See *Bilcon v. Canada*, UNCITRAL, PCA Case No. 2009-04, Dissenting Opinion of Donald McRae (Mar. 10, 2015); *TransCanada v. U.S.*, NAFTA, Notice of Intent to Submit a Claim to Arbitration under Chapter 11 of NAFTA (Jan. 6, 2016). See, e.g., Marc Bungenberg & Catherine Titi, *Developments in International Law*, in EUROPEAN YEARBOOK OF INT’L LAW 2013 441, 453 (Christoph Herrmann et al. eds., 2013); Kate Miles, *Investor-State Dispute Settlement: Conflict, Convergence, and Future Directions*, in EUROPEAN YEARBOOK OF INT’L LAW 2016 273, 277 (Marc Bungenberg et al. eds., 2016).

⁷⁸¹ See, e.g., *Siemens*, *supra* note 756, para. 81 (“The Tribunal considers that the Treaty has to be interpreted neither liberally nor restrictively, as neither of these adverbs is part of Article 31(1) of the Vienna Convention.”).

⁷⁸² KOSKENNIEMI, *supra* note 566, at 591-92.

⁷⁸³ See NEWCOMBE & PARADELL, *supra* note 43, at 116 (stating that no principle of restrictive interpretation of treaties exists based on the classic authority established in the *Wimbledon Case*).

C. Distinguishing the Standard Public Order Carve-out from the WTO/GATS-inspired General Exceptions Clause

In whichever manner drafted by the State parties and subsequently interpreted by investment tribunals, the adoption from the NPM public order carve-out to the proposed standard public order carve-out being proposed in this Dissertation must occur without diminishing the purpose of IIAs. After all, the milestones made in favor of investor protection must not regress.⁷⁸⁴ The explicit presence of general exception clauses in IIAs can provide a kind of safety feature that deters investment tribunals from forming sweeping interpretations of IIA obligations and may also encourage tribunals to be more deferential to the policy objectives of the State. Whereas in *Continental Casualty*⁷⁸⁵ Argentina had defended its regulatory measure on the basis of maintaining public order and protecting essential security interests as provided for in Article XI of the U.S.-Argentina BIT, the ICSID tribunal in *Total v. Argentina*⁷⁸⁶ decided against Argentina because an exception provision did not exist in the underlying BIT with France. Investment tribunals may be better encouraged to weigh in policy objectives when an investment treaty explicitly contains an exceptions provision to prevent a hard interpretation of the purpose of IIAs.⁷⁸⁷ In this regards, the

⁷⁸⁴ See UNCTAD, SUSTAINABLE DEVELOPMENT FRAMEWORK, *supra* note 76, at 213 (stating that “such a reversion would seriously impair the essential aim of [international investment law], which is to limit the domestic jurisdiction of states to the protection of foreign investors and to enhance the free global market”).

⁷⁸⁵ *Continental Casualty v. Argentina*, *supra* note 179, paras. 231-33.

⁷⁸⁶ *Total S.A. v Argentina*, ICSID Case No. ARB/04/1, Decision on Liability, paras. 224-30 (Dec. 27, 2010).

⁷⁸⁷ Mavluda Sattorova, *International Investment Law, Renewable Energy, and National Policy-making: On ‘Green’ Discrimination, Double Regulatory Squeeze, and the Law of*

need to balance investment protection with a standard public order carve-out that identifies some of the policy objectives can contribute to the further development of international investment law. However, the recent practice of including WTO/GATS-type of general exceptions into IIAs should be scrutinized for several reasons⁷⁸⁸ and distinguished from the standard public order carve-out being proposed in this Dissertation.

The first concern relates to the status of exception as understood in the public order carve-out of an investment treaty – that is, whether the act conducted under the public order carve-out is outside the scope of the IIA or is a justification to an otherwise unlawful conduct. The proposed standard public order carve-out would operate as a treaty exception. Apart from the “symbolic difference” between the two types of conduct, Professor Henckels argues that it is hard to comprehend why States would agree to the latter situation given that the contracting States are explicitly preserving their regulatory space to rebalance IIAs.⁷⁸⁹ The WTO/GATS general exceptions clause operates as an affirmative defense that puts the burden of proof on the host State to prove that its *prima facie* breach should be exempted under

Exceptions, in YEARBOOK ON INT’L INVESTMENT L. & POL’Y 2012–2013 415, 442 (Andrea K. Bjorklund ed., 2014) (contending that an expressly written exceptions clause “would prevent the interpretation of certain investment treaty obligations as absolute, non-derogable standards that always entail a form of compensatory or restitutionary redress”).

⁷⁸⁸ See Newcombe, *General Exceptions*, *supra* note 288, 357 (stating the “significant uncertainty” surrounding how investment tribunals would interpret WTO/GATS-inspired general exception clauses).

⁷⁸⁹ Caroline Henckels, *When the “Exception” is an Element of the Rule: The Structural Status of Investment Treaty Exception Clauses*, in EXCEPTIONS IN INTERNATIONAL LAW (Lorand Bartels & Federica Paddeu eds., forthcoming 2017), available at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2801950.

Article XX of the GATT.⁷⁹⁰ The defending State has the initial burden of showing that the measure being challenged is justified because it falls within one of the exceptions enumerated under Article XX. The respondent State makes the *prima facie* case based on the weighing and balancing test formulated in the *Korea – Beef* to argue that it took the least restrictive means available.⁷⁹¹

The mechanic and structure of the exception provided in Article XX of the GATT should be viewed differently from the way the public order carve-out should apply in investment treaties. The proposed standard public order carve-out should not operate as an affirmative defense. The function of the standard public order carve-out is to allow an exception in a specific area of the investment treaty to stipulate that measures necessary for the maintenance of public order shall not be unlawful since it lies outside the scope of IIA obligations. Accepting the view held by the *CMS* annulment committee,⁷⁹² the *Continental Casualty* tribunal held that a State does not commit a breach for measures properly taken to maintain public order under Article XI of the U.S.-Argentina BIT.⁷⁹³ Likewise, the *Sempra* annulment committee also shared the view that the substantive obligations of the U.S.-Argentina BIT does not apply where Article XI applies.⁷⁹⁴

⁷⁹⁰ See Emily C. Barbour, *Trade Law: An Introduction to Selected International Agreements and U.S. Laws*, CRS Report for Congress, June 29, 2010, available at <http://nationalaglawcenter.org/wp-content/uploads/assets/crs/R41306.pdf>

⁷⁹¹ See ch. 3 of this Dissertation.

⁷⁹² *CMS Annulment*, *supra* note 658, para. 129.

⁷⁹³ *Continental Casualty v. Argentina*, *supra* note 179, para. 164.

⁷⁹⁴ *Sempra Annulment*, *supra* note 685, para. 200.

Unlike an affirmative defense which places the burden of proof on the host State, the claimant would have the burden of proving that the State's measure was not necessary to maintain public order. The placement of the burden of proof on the claimant is consistent with the position long established in international law.⁷⁹⁵ The proposed standard public order carve-out may contribute to the balancing of interests between foreign investors and their host States by placing the initial burden of proof on the claimant. However, the burden would then shift to the host State who will carry a significant portion of the burden of raising the exception. The burden of production would be borne by both the host State and claimant while the burden of persuasion would remain with the host State. Specifying who bears the burden at each phase of the arbitration when applying the proposed standard public order carve-out can achieve the important objective of balancing interests among the IIA stakeholders by increasing awareness of the regulatory concerns particularly among the arbitrators sitting in an investor-State dispute – a perspective that has not been traditionally stressed in investor-State arbitration cases. As a related matter,

⁷⁹⁵ See MOJTABA KAZAZI, *BURDEN OF PROOF AND RELATED ISSUES: A STUDY ON EVIDENCE BEFORE INTERNATIONAL TRIBUNALS* 86 (Kluwer Law Int'l 2006) (stating that the rule with respect to the burden of proof applied by the ICJ has been the "basic rule according to which the party who asserts a fact is responsible for providing proof thereof"). For more international law case examples, see *id.* See, e.g., *Corfu Channel Case (United Kingdom v. Albania)*, 1949 I.C.J. 4 (Apr. 9) (stating that Britain owed the burden of proof since it asserted the claim); *Military and Paramilitary Activities (Nicaragua v. U.S.)*, 1984 I.C.J. 437, *Jurisdiction of the Court and Admissibility of the Application*, para. 101 (Nov. 26, 1984) ("Ultimately, however, it is the litigant seeking to establish a fact who bears the burden of proving it..."). See generally ROBERT KOLB, *THE ELGAR COMPANION TO THE INTERNATIONAL COURT OF JUSTICE* 235 (Edward Elgar Pub. 2014); NAGENDRA SINGH, *THE ROLE AND RECORD OF THE INTERNATIONAL COURT OF JUSTICE* 196 (Martinus Nijhoff 1989).

it may be helpful to the claimant and host State when an investment tribunal expressly identifies each phase of the burden of proof to make the decision-making process more predictable and transparent for the disputing parties as well as the observers of the case.

The second concern relates to the remedies available under the two systems. Differences between the two systems should be taken into consideration so that investment tribunals do not transplant jurisprudence from the WTO system without regard to international investment law⁷⁹⁶ since the remedies available in the WTO system do not necessarily share the same type of application in the international investment regime.⁷⁹⁷ Although “strong textual affinities”⁷⁹⁸ between the language in the WTO/GATS exceptions and the exceptions chapter from IIAs have led some to suggest that the general exceptions jurisprudence established by the WTO regime should be applied even for interpreting international investment obligations,⁷⁹⁹ how would investor-State tribunals actually interpret the

⁷⁹⁶ See Jürgen Kurtz, *On the Evolution and Slow Convergence of International Trade and Investment Law*, in GENERAL INTERESTS OF HOST STATES IN INTERNATIONAL INVESTMENT LAW 104, 127 (Giorgio Sacerdoti et al. eds., 2014) (stating that it would be premature to conclude without any testing that “the (usually) older WTO jurisprudence on common norms is necessarily superior select approaches on investment arbitration”).

⁷⁹⁷ See Daniel Kalderimis, *Exploring the Differences between WTO and Investment Treaty Dispute Resolution*, in TRADE AGREEMENTS AT THE CROSSROADS 46, 57 (Susy Frankel & Meredith Kolsky Lewis eds., 2014) (providing a detailed account of the differences in remedies available in the WTO and investment regime).

⁷⁹⁸ Newcombe, *Use of General Exceptions in IIAs*, *supra* note 286, at 275.

⁷⁹⁹ See *Continental Casualty v. Argentina*, *supra* note 179, para. 192 (stating that “the Tribunal finds it more appropriate to refer to the GATT and WTO case law which has extensively dealt with the concept and requirements of necessity”). Cf. Jürgen Kurtz, *The Use and Abuse of WTO Law in Investor-State Arbitration: Competition and its Discontents*, 20 EJIL 749 (2009) (arguing that the use of WTO law

exceptions chapter in connection to the investment chapter of the FTA? Unlike in the WTO where the breaching State can be made to either modify or withdraw its measure, neither investment tribunals nor investors can compel the offending State government to change or withdraw its regulatory act.⁸⁰⁰ Moreover, the meaning of the term “public order” and the concept of the necessity of a measure has already been addressed in WTO decisions. For example, after noting the tension between international trade and regulatory interests pertaining to public health and environment, the Appellate Body in *Brazil – Retreaded Tyres* declared that the WTO member States have a fundamental right to decide on the level of protection to give in order to protect such regulatory interests so long as there is a genuine relationship between the means taken and the objective sought.⁸⁰¹ Furthermore, this Appellate Body stated that the measure does not have to be indispensable to be necessary as stated in Article XX of the GATT. Under the international investment regime, however, such a provision is included because, without it, a host State would not be able to implement a measure that potentially violates the investment treaty. Furthermore, if a host State is found to be in violation of the investment treaty, then a duty to compensate would arise. Therefore, the treatment of governmental acts is significantly different under the two international economic regimes,⁸⁰² and despite

by investor-State tribunals contribute to inconsistent jurisprudence on national treatment in the field of international law).

⁸⁰⁰ DI BENEDETTO, *supra* note 563, at 200.

⁸⁰¹ E.g., Appellate Body Report, *Brazil – Measure Affecting Imports of Retreaded Tyres*, para. 210, WT/DS332/AB/R (Dec. 3, 2007).

⁸⁰² See Simon Lester, *Improving Investment Treaties through General Exceptions Provisions: The Australian Example*, INVESTMENT TREATY NEWS (May 14, 2014),

thematic similarities, such a phenomenon occurs because the meaning meant to be embodied under the investment regime differs from other international economic agreements such as the WTO agreements due to the fact that “[e]ach agreement has its own architecture, objectives and cultural and legal specificity”⁸⁰³ which produce across different IIAs multiple interpretations even of the similar substantive obligations.⁸⁰⁴ The proposed standard public order carve-out is intended to provide an exception in IIAs so that important and rational regulatory acts are placed outside the scope of the investment treaty enabling States to take certain measures without breaching international obligations. The duty to compensate should not arise when the standard public order carve-out applies. However, to what extent the compensation duty does not apply due to a regulatory act (as defined under the standard public order carve-out) is a closely related, but separate issue best left for investment tribunals.

The third concern takes issue with the language used in the WTO/GATS-style general exception clauses, which the proposed standard public order carve-out attempts to minimize such linguistic influence from the WTO/GATS general exceptions provisions. The general exceptions provision in IIAs may use at verbatim or be closely modeled after the GATT

<https://www.iisd.org/itn/2014/05/14/improving-investment-treaties-through-general-exceptions-provisions-the-australian-example>.

⁸⁰³ Marie-France Houde & Katia Yannaca-Small, *Relationships between International Investment Agreements* (OECD Working Papers on Int’l Investment 2004/01, 2004), available at http://www.oecd.org/investment/internationalinvestmentagreements/WP-2004_1.pdf.

⁸⁰⁴ *Id.*

Article XX,⁸⁰⁵ GATS Article XIV,⁸⁰⁶ or provide a combination⁸⁰⁷ of those two articles. The last method is peculiar not only because of the obvious difference that GATT relates to goods whereas GATS covers services, but also because the objectives of the WTO/GATS agreements is to ensure that discrimination does not occur on the basis of national origin while IIAs obligate parties to certain substantive obligations to protect investments whether it is against discrimination, expropriation, or another factor. Moreover, certain exceptions enumerated in GATS like the provision allowing for the maintenance of public order are not included in GATT and *vice versa* while some of the legitimate policy objectives enumerated under Article XX of the GATT and Article XIV of the GATS may not always be useful for preserving the regulatory power of a host State under IIAs. Although the GATT and GATS may share a similar structure,⁸⁰⁸ this raises an interpretive issue for investment tribunals who must now grapple with fairly new and complex questions like whether to borrow from WTO jurisprudence, and if so, to what extent, and how to make it work in the international investment regime.⁸⁰⁹ While adopting Article XIV of the GATS

⁸⁰⁵ E.g., ASEAN Comprehensive Investment Agreement, *supra* note 504, art. 17.

⁸⁰⁶ E.g., Korea-Singapore FTA, *supra* note 288, art. 21.2; Panama-Taiwan FTA, art. 20.02(2), Aug. 21, 2003.

⁸⁰⁷ E.g., Korea-Australia FTA, *supra* note 521, art. 22.1; China-New Zealand FTA, art. 200, Apr. 7, 2008.

⁸⁰⁸ PETER VAN DEN BOSSCHE & WERNER ZDOUC, *THE LAW AND POLICY OF THE WORLD TRADE ORGANIZATION* (Cambridge Univ. Press 3rd ed. 2013)

⁸⁰⁹ See Roberts, *supra* note 82, at 46 (“Investment treaties have traditionally been short and vaguely worded, while the system as a whole is new and undertheorized. As a result, participants routinely draw on comparisons with other legal fields when seeking to fill gaps, resolve ambiguities, or understand the

at verbatim, recently concluded IIAs like the Canada-EU CETA attempt to reduce the interpretation burden for investment tribunals by appending a clarification note so that measures necessary to protect human, animal or plant life or health as provided for in Article XIV of GATS also extends to environmental measures that are necessary to protect human, animal or plant life or health.⁸¹⁰ Scholars like Sabanogullari optimistically believe that modifying the WTO/GATS general exceptions provision to accommodate the State's needs "exemplify how treaty drafters can not only custom tailor the WTO exceptions to their regulatory needs in the investment realm, but also codify and thereby endorse WTO jurisprudence in the IIA drafting process."⁸¹¹ In practice, however, the effect of adding such clarification language to better reconcile the two jurisdictional bodies is yet to be elucidated and literature on this topic is sparse.⁸¹² Rather than relying on footnotes, the proposed standard public order carve-out strives to clearly express the elements required to encourage consistent investor-State arbitral outcomes.

In a substantive examination of the general exceptions provision, Lester refers to Article 22.1.3 of the Korea-Australia FTA to express skepticism towards the clarity of the scope of general exceptions in IIAs particularly because of the language in the chapeau stating that "nothing in

system's nature.").

⁸¹⁰ Canada-EU CETA, *supra* note 18, n. 32.

⁸¹¹ Sabanogullari, *supra* note 286.

⁸¹² Brooks E. Allen & Tommaso Soave, *Jurisdictional Overlap in WTO Dispute Settlement and Investment Arbitration*, 30 J. LONDON CT. INT'L ARB. 1, 3 (2014).

this Agreement shall be construed to prevent a Party from adopting or enforcing measures.” The criticism is that such a language may be ineffective for *preventing* measures that violate international investment obligations.⁸¹³ Even under WTO practice, a measure is not prevented, but can be remedied by either modifying or withdrawing it whereas an investment treaty breach may obligate the host State to either pay full compensation or no compensation without compelling the host State to modify or withdraw the challenged measure.⁸¹⁴ For this reason, other scholars like Professor Di Benedetto also believes that the above chapeau language from the WTO general exceptions provisions poses certain adaptive difficulties within the IIA context because investors usually do not demand that the challenged measure be modified or withdrawn since it is not a remedy that investor-State tribunals can require in their awards against the host State.⁸¹⁵ Moreover, borrowing WTO language presents interpretation issues within the investment context. Furthermore, the requirement in the chapeau language of the general exceptions provision in the Canada Model FIPA that

⁸¹³ Lester, *supra* note 802.

⁸¹⁴ DOLZER & SCHREUER, *supra* note 41, at 293-94 (“In investment arbitration, the remedy nearly always consists of monetary compensation. Satisfaction plays a subordinate role in investment law. Restitution in kind or specific performance is ordered infrequently.”). Cf. *Enron Corp. Ponderosa Asset, L.P. v. Argentina*, ICSID Case No. ARB/01/3, Decision on Jurisdiction, para. 76 (Jan. 14, 2004) (Argentina contending that the proper role of the *Enron* tribunal was to determine whether an expropriation had occurred and, if so, the compensation; but, the tribunal claimed that “the power of international courts and tribunals to order measures concerning performance or injunction” was also available to this tribunal).

⁸¹⁵ DI BENEDETTO, *supra* note 563, at 198. See *id.* n. 134 (noting that only a minute number of cases have involved investment tribunals ordering restitution or specific performances).

“such measures are not applied in a manner that could constitute arbitrary or unjustifiable discrimination between investments or between investors”⁸¹⁶ may bear a more difficult standard in IIAs than in the WTO context where discriminatory measures are prohibited between “countries where the same conditions prevail.”⁸¹⁷ The impact of the enumerated list of exceptions also sits curiously with Professors DiMascio and Pauwelyn who contend that when IIAs do not include express exceptions, the outcome is “a list far broader than the exceptions in GATT Article XX.”⁸¹⁸ Unlike the public order carve-out provided in NPM provisions like Article XI of the U.S.-Argentina BIT, the proposed standard public order carve-out strives to maintain regulatory flexibility for the States by providing an enumerated, but non-exhaustive list of possible legitimate policy objectives to offset the potentially broad scope of an open-ended public order carve-out.⁸¹⁹

On the other hand, scholars such as Professor Collins argues that despite the lack of commentary from academics and practitioners on the inclusion of general exceptions in IIAs, this method would “offer a plausible means of resolving the criticism that arbitrators do not appreciate the essential public dimension of treaty-based disputes” because it can balance

⁸¹⁶ Canada Model FIPA, *supra* note 505, art. 10.

⁸¹⁷ GATT, *supra* note 270, art. XX.

⁸¹⁸ Nicholas A. DiMascio & Joost Pauwelyn, *Nondiscrimination in Trade and Investment: Worlds Apart or Two Sides of the Same Coin?*, 102 AM. J. INT’L L. 48, 82-83 (2008).

⁸¹⁹ See Newcombe, *General Exceptions*, *supra* note 288, at 368 (having an enumerated list of exceptions may demand “a stricter review of State measures than currently suggested by IIA jurisprudence”).

the “regulatory intrusion” against IIA obligations on investor protection.⁸²⁰ To a certain extent, including general exceptions in IIAs may act as a catalyst for helping public interest objectives to become a firm part of the investment regime similar to how the initial inclusion of GATT/GATS general exceptions eventually contributed to the building of a relationship between social interests and international trade obligations.⁸²¹ As previously discussed, the general exceptions provision in the TPP is for performance requirements only and the chapter on exceptions using GATT Article XX language does not cover the investment chapter of the TPP; instead, a footnote appended to the national treatment provision reserves the right of the host State to enact discriminatory measures in pursuit of “legitimate public welfare objectives.”⁸²² Due partially to the fact that the inclusion (or exclusion) of the general exceptions provisions has not yet taken place as a coherent investment treaty practice, this abridged form of drafting to carve-out regulatory space in a footnote to an often contested provision of an IIA may be less desirable than having an enumerated list that could, at the minimum, limit the scope of inquiry for the tribunals to avoid “re-cast[ing] the arbitrator’s role as one tied to the interpretation of domestic laws.”⁸²³

⁸²⁰ David Collins, *The Line of Equilibrium: Improving the Legitimacy of Investment Treaty Arbitration through the Application of the WTO’s General Exceptions*, 32 *ARBITRATION INT’L* 575, available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2487778.

⁸²¹ *Id.*

⁸²² TPP, *supra* note 11, art. 9.4, n. 14.

⁸²³ See Collins, *supra* note 820, at 12 (observing that the general exceptions provisions in IIAs used “a very minimal format that is unfortunately lacking in guidance to adjudicators”).

Furthermore, Collins argues that not including the general exceptions provision in IIAs “places significant pressure on tribunals to strike the correct balance between legal restraint and flexibility” especially when the investment regime does not support an appeals system and the compensation awards are potentially significant.⁸²⁴ The public order carve-out going forward must be distinguished from the WTO/GATS general exceptions provisions. By aiming towards the elimination of the influence from the WTO/GATS general exceptions provisions, the proposed standard public order carve-out can provide a uniform provision from which States can further negotiate to make the proposed standard public order carve-out most applicable to their regulatory demands.

The proposed standard public order carve-out aims to reduce a fourth concern which arises due to the inconsistent IIA practice of including WTO/GATS-inspired general exception clauses in investment treaties. Contracting parties such as Australia, Canada, China, India, Korea, Japan, and Singapore include the general exceptions provision in the investment chapter of FTAs on a sporadic basis resulting in inconsistent treaty practice. The FTAs between Korea-Singapore⁸²⁵ and Panama-Taiwan⁸²⁶ contain a separate exceptions chapter modeled after Article XIV of GATS and applicable to their respective investment chapters. The exceptions chapter

⁸²⁴ *Id.* See also Razeen Sappideen & Ling Ling He, *Dispute Resolution in Investment Treaties: Balancing the Rights of Investors and Host States*, 49 J. WORLD TRADE 85, 112 (2015) (arguing for the creation of a public interest exceptions clause).

⁸²⁵ Korea-Singapore FTA, *supra* note 288, art. 21.2, Aug. 4, 2005.

⁸²⁶ Panama-Taiwan FTA, *supra* note 806, art. 20.02(02).

in the China-New Zealand FTA⁸²⁷ uses a combination of both the GATT and GATS exceptions provisions and also pertains to the investment chapter. In the Korea-Australia FTA, the general exceptions chapter, which closely resembles the GATT Article XX, essentially states that a party will not be prevented from adopting or enforcing necessary measures unless done in an arbitrary or discriminatory manner.⁸²⁸ Although the examples cited here are not exhaustive, they offer a glimpse into the inconsistent manner in which the States have drafted the exceptions chapter. Inconsistency is further aggravated because participants in the international investment regime embody different views towards the adoption of WTO/GATS-inspired general exceptions in IIAs. Professor Newcombe predicts that including general exceptions “is unlikely to have much practical significance” and that the apparent merit for importing it into investment treaties is because they explicitly identify the legitimate objectives in IIA jurisprudence and provide a check on the tribunals’ interpretive scope.⁸²⁹ However, other commentators are more optimistic about the contributory role that WTO/GATS general exceptions can have in shaping the exceptions model in IIAs. Professors Sappideen and He believe that States can reduce the cost of negotiation and improve the efficiency of negotiations when a “modified GATT Article XX and GATS Article XIV that will apply specifically to investment” is considered during the IIA negotiation phase.⁸³⁰ Other

⁸²⁷ China-New Zealand FTA, *supra* note 807, art. 200(1).

⁸²⁸ Korea-Australia FTA, *supra* note 521, art. 22.1.3.

⁸²⁹ Newcombe, *General Exceptions*, *supra* note 288, at 357.

⁸³⁰ Sappideen & He, *supra* note 824, at 114-15.

commentators acknowledge the interaction that occurs between trade and investment for substantive provisions on general exceptions, but maintain a bystander perspective stating that this is a “fairly limited,”⁸³¹ “not common”⁸³² practice that remains to be seen. An important objective of the proposed standard public order carve-out is to have it become an established feature of IIAs and provide a template for exceptions relating to regulatory interests which the contracting States can use when negotiating investment treaties.

D. The Public Order Carve-out is not a *Lex Specialis* Rule

The theory that BIT rules are a *lex specialis* may have legal grounding in Article 55 of the ILC Articles on State Responsibility which provides that:

These articles do not apply where and to the extent that the conditions for the existence of an internationally wrongful act or the content or implementation of the international responsibility of a State are governed by special rules of international law.⁸³³

Except for *jus cogens* norms, parties may agree to override the ILC Articles on State Responsibility with a *lex specialis*.⁸³⁴ Whereas WTO/GATT law is a prominent example of the special rules of international law referred to in

⁸³¹ Mark Wu, *The Scope and Limits of Trade’s Influence in Shaping the Evolving International Investment Regime*, in THE FOUNDATIONS OF INTERNATIONAL INVESTMENT LAW: BRINGING THEORY INTO PRACTICE 169, 201 (Zachary Douglas et al. eds., 2014).

⁸³² NEWCOMBE & PARADELL, *supra* note 43, at 500.

⁸³³ State Responsibility Draft with Commentaries, *supra* note 367, art. 55, at 140.

⁸³⁴ James Crawford, *Third Report on State Responsibility*, 2 YEARBOOK OF INT’L LAW COMM’N, pt. 1, at 3, para. 416, UN Doc. A/CN.4/507/Add.4 (2000).

Article 55, “specific treaty provisions on a single point” are also within the accepted purview of ILC Article 55.⁸³⁵ According to the ILC Commentary, there must be either an “actual inconsistency” or “a discernible intention that one provision is to exclude the other” between the general rule and the alleged *lex specialis* for Article 55 to apply. Another caveat is that if applying the *lex specialis* over the general provision would lead to an absurd outcome or defeat the objective of the parties’ agreement, then the *lex specialis* may not apply meaning that whether a rule alleging to be a *lex specialis* can trump a general principle “is essentially one of interpretation.”⁸³⁶

However, regarding Article XI of the U.S.-Argentina BIT as a *lex specialis* that displaces the customary law on necessity needs to be approached with some caution. The *lex specialis derogate generali* principle is not provided under the Vienna Convention, but is used in investment treaty interpretation because customary international rule can co-exist alongside a treaty⁸³⁷ and, if a conflict arises between the two legal sources, an investment treaty provision may operate as the *lex specialis* that sets the general rules of customary international law aside.⁸³⁸ In the Argentine ICSID cases, the

⁸³⁵ State Responsibility Draft with Commentaries, *supra* note 367, para. 5, at 140 (“Article 55 is designed to cover both ‘strong’ forms of *lex specialis*, including what are often referred to as self-contained regimes, as well as ‘weaker’ forms such as specific treaty provisions on a single point, for example, a specific treaty provision excluding restitution.”).

⁸³⁶ *Id.* para. 4, at 140.

⁸³⁷ Nicaragua case, *supra* note 660, para. 175.

⁸³⁸ ADC Affiliate Ltd. & ADC & ADMC Management Ltd. v. Hungary, ICSID Case No. ARB/03/16, Award, para. 481 (Oct. 2, 2006) (“There is general authority for the view that a BIT can be considered as a *lex specialis* whose provisions will prevail over rules of customary international law”). See Rahim Moloo, *The Source for Determining Standards of Review in International Investment Law*, INVESTMENT

tribunals in *CMS*, *Enron*, and *Sempra* were criticized for not interpreting the NPM provision of the U.S.-Argentina BIT as the *lex specialis* to the customary law of necessity. But the *LG&E* tribunal, which did identify Article XI as a *lex specialis*, has also been criticized for failing to reason out how “Article XI establishes the state of necessity as a ground for exclusion from the wrongfulness of an act of the State”⁸³⁹ that exempts Argentina also from the duty to compensate.⁸⁴⁰ Likewise, the *CMS* annulment committee also identified Article XI as a *lex specialis* without engaging in a satisfying discussion of why it should be treated as a *lex specialis*. The proposed standard public order carve-out aims to resolve the unclear relationship between Article XI of the BIT and the customary international law on necessity by denying this kind of association.

For hypothetical purposes, we may consider treating Article XI of the U.S.-Argentina BIT as the *lex specialis*. The advantage of this approach is that it avoids directly competing with the customary rule on necessity, but academic opinions widely vary on this point.⁸⁴¹ Already discussed in

TREATY NEWS (July 19, 2012), https://www.iisd.org/itn/2012/07/19/the-source-for-determining-standards-of-review-in-international-investment-law/#_ftn7 (reiterating the general view that “the *lex specialis* is the investment treaty being applied”). See also Nicholas J. Birch, *Calculating Damages in Energy Disputes: The Restoration of Indexing Clauses*, in INVESTMENT TREATY ARBITRATION AND INTERNATIONAL LAW 313, 315 n. 6 (Ian A. Laird et al. eds., 2014) (citing Phillips Petroleum Co. Iran v. Iran, 21 Iran-U.S. Cl. Trib. Rep. at 121 to state the accepted proposition that a BIT may trump over international customary law when considered a *lex specialis*).

⁸³⁹ *LG&E v. Argentina*, *supra* note 179, para. 261

⁸⁴⁰ Sloane, *supra* note 331, at 501.

⁸⁴¹ See Andrea K. Bjorklund & Sophie Nappert, *Beyond Fragmentation*, in NEW DIRECTIONS IN INTERNATIONAL ECONOMIC LAW: IN MEMORIAM THOMAS WÄLDE 439, 469 n. 108 (Todd Weiler & Freya Baetens eds., 2011) (listing the articles of

Chapter 4 of this Dissertation, this approach does not designate the scope of priority to be given to the public order carve-out but two possible scenarios may be considered to elucidate this issue.⁸⁴² Under the first approach, the customary law of necessity may be applied residually to provide content to the public order carve-out so that the task of the adjudicator is to determine the interpretative relationship, which would occur by recognizing the legitimacy and applicability of the two norms arising from two different sources of law so that one norm aids the interpretation of the other norm to clarify, modify, or apply the latter norm.⁸⁴³ This is in contrast to the second approach which assumes a relationship of conflict so that even if the two norms are applicable, the *lex specialis* would have to displace the inconsistency brought on by the customary international law to avoid having two different outcomes.⁸⁴⁴

In recent years, the discussion on the relationship between treaties and customary law has evolved to the point where commentators have been compelled to consider it from various angles. Although well-established that customary international law is composed of two elements – state practice and *opinio juris* – international investment arbitral tribunals have neither uniformly explored nor demanded evidence of state practice and *opinio juris* when applying the customary law standard of necessity to the

authors covered in this Dissertation with diverging views).

⁸⁴² Kurtz, *Adjudging Security*, *supra* note 183, at 35.

⁸⁴³ U.N. GAOR, 58th Sess., Int'l L. Comm., U.N. Doc. A/CN.4/L.702, at 7 (July 18, 2006).

⁸⁴⁴ *Id.* at 8.

public order clause.⁸⁴⁵ Scholarly debate on this very question of whether BITs serve as evidence of state practice is intense and without a single answer. On one hand, an ICSID tribunal declared that “there is no obstacle in international law to the expression of the will of States through treaties being at the same time an expression of practice and of the *opinio[] juris* necessary for the birth of a customary rule if the conditions for it are met.”⁸⁴⁶ This position stands in contradiction to the principle established by the influential International Law Association Committee on the Formation of Customary International Law which concluded that “[s]o far as concerns a *succession* of bilateral treaties, again there is certainly no presumption that they will have assisted in the crystallization of an emerging norm”⁸⁴⁷ and reiterated its firm belief that “there is no presumption that a series of treaties gives rise to a new rule of customary law” unless evidence can be found that the provisions are generally accepted “*outside the treaty framework*.”⁸⁴⁸ Unlike the WTO regime where the role of customary international law is minimal and more reliant on codification and treaty law, customary international law was originally

⁸⁴⁵ David Sahargun, *Investor-State Arbitration and Argentina: A State of Necessity at the ICSID*, INT’L LEGAL STUDIES PROG. L.J. 219, 221 (2012) (stating that customary international law is a principal part of the international legal system and a source of law that “derives from the practice of states and is accepted by them as legally binding”).

⁸⁴⁶ Camuzzi International S. A. v. Argentina, ICSID Case No. ARB/03/2, Decision on Objections to Jurisdiction, para. 144 (May 11, 2005).

⁸⁴⁷ INT’L L. ASS’N COMM. ON FORMATION OF CUSTOMARY (GEN.) INT’L L., Final Report, *Statement of Principles Applicable to the Formation of General Customary International Law* 50 (2000), <http://www.ila-hq.org/download.cfm/docid/A709CDEB-92D6-4CFA-A61C4CA30217F376>.

⁸⁴⁸ *Id.* at 48.

thought to be the “natural source of the law of investment protection”⁸⁴⁹ for its ability to “withstand the wide-ranging dissonance echoed in the world stage as to which protection foreign investors ought to be offered.”⁸⁵⁰

However, in another perspective, international investment law scholars and practitioners have increasingly observed the trends towards treatification; that is, favoring the lawmaking process through treaties rather than customary international law.⁸⁵¹ In an arbitration where former ICJ president Judge Schwebel and Professor Brownlie sat, the tribunal observed that BITs have “reshaped the body of customary international law itself.”⁸⁵² In another arbitration where Judge Schwebel was present along with Professor Crawford, the tribunal affirmed that customary international law is “shaped by the conclusion of more than two thousand bilateral investment treaties and many treaties of friendship and commerce.”⁸⁵³ For those proponents who concur that the codification of international rules through treaties is lessening the effective power of customary international law, Professor Trachtman recently argued that customary international law

⁸⁴⁹ Jean d’Aspremont, *International Customary Investment Law: Story of a Paradox*, in INTERNATIONAL INVESTMENT LAW: THE SOURCES OF RIGHTS AND OBLIGATIONS 5, 12 (Tarcisio Gazzini & Eric De Brabandere eds., 2012).

⁸⁵⁰ *Id.*

⁸⁵¹ For discussion on the treatification trend, see Jeswald W. Salacuse, *The Treatification of International Investment Law*, 13 LAW & BUS. REV. AM. 155 (2007).

⁸⁵² CME Czech Republic v. Czech Republic, UNCITRAL, Final Award, para. 498 (Mar 14, 2003) (stating that BITs, and not the domestic law of the host State or the demands of its internal circumstances, have prevailed on the matter of payment of compensation).

⁸⁵³ *Mondev Int’l V. U.S.*, ICSID Case No. ARB(AF)/99/2, Award, para. 125 (Oct. 11, 2002).

inevitably falls short of addressing the “great modern challenges” of the international community which may arise in the context of global environment protection, international public health, cybersecurity, financial cataclysm, and liberalization of the movement of goods, services, and people.⁸⁵⁴ While recognizing the strengths of customary international law such as its informal nature which may be more suitable in certain situations and the decentralized structure which can by-pass parliamentary control and bureaucratic red tape but nonetheless bind states without obtaining actual consent, Trachtman emphasizes the obsolescence of customary international law.⁸⁵⁵ That is, from a lawmaking standpoint, customary international law is not created in coordination with the States of the international community before certain events occur. Moreover, States cannot be assumed to embrace the same set of symmetric interests and customary international law is too rigid to allow for the comparisons and preferences that inevitably occur due to the different situations and

⁸⁵⁴ Joel P. Trachtman, *The Growing Obsolescence of Customary International Law*, in *CUSTOM’S FUTURE: INTERNATIONAL LAW IN A CHANGING WORLD* 172 (Curtis A. Bradley ed., 2016). See Roger Alford, *Customary International Law is Obsolete*, *OPINIO JURIS* (Nov. 29, 2014), <http://opiniojuris.org/2014/11/29/customary-international-law-obsolete> (commenting on Trachtman’s latest provocative conclusion and agreeing that “critics will [not] be able to... refute [Trachtman’s] general thesis that the codification of international rules through treaties has made CIL increasingly obsolete”). See also Laurence R. Helfer & Ingrid B. Wuerth, *An Instrument Choice Perspective on Customary International Law*, 37 *MICH. J. INT’L L.* (forthcoming 2016), available at http://scholarship.law.duke.edu/cgi/viewcontent.cgi?article=6224&context=faculty_scholarship (addressing the complementary and competitive relationship between treaties and soft law *i.e.* custom).

⁸⁵⁵ Trachtman, *supra* note 854, at 173.

capabilities of each State.⁸⁵⁶ Additionally, from an implementation point of view, customary international law is not subject to the domestic legislative process of a State and may have a binding effect on those States that did not expressly consent but failed to object to its formation.⁸⁵⁷ Finally, from an enforcement perspective, customary international law is usually too vague even though greater specificity may lead to better compliance⁸⁵⁸ or may grant too much discretion for “auto-interpretation by [S]tates, or for sometimes insufficiently disciplined interpretation by judges.”⁸⁵⁹

Some IIAs try to avoid vagueness by including an explicit reference to the phrase “customary international law.” Although this phrase is absent in the U.S.-Argentina BIT, this omission should not be treated as an intentional disregard for customary international law. An additional, but related concern relates to whether the mere presence of the word “necessary” in the public order carve-out (“measures necessary for the maintenance of public order”) invokes customary international law even when the U.S.-Argentina BIT does not make a specific reference to it.⁸⁶⁰ For example, in the 2004 Canada Model FIPA, the fair and equitable treatment clause is explicitly linked to the customary rule on minimum standard in the following manner: “Each Party shall accord to covered investments treatment in accordance

⁸⁵⁶ *Id.* at 185.

⁸⁵⁷ *Id.* at 187-88.

⁸⁵⁸ *Id.* at 184.

⁸⁵⁹ *Id.* at 173.

⁸⁶⁰ TITI, *supra* note 79, at 193 (referring to ILC art. 25 as “the substance of another provision”).

with the customary international law minimum standard of treatment of aliens, including fair and equitable treatment and full protection and security.”⁸⁶¹ The absence of an explicit reference to customary international law in investment treaties has been questioned with one scholar bluntly asking “why BITs should refer to custom at all”⁸⁶² when customary international law is merely one of the other sources mentioned in ICJ Article 38 along with international conventions, general principles of law, and judicial decisions and teachings of the most highly qualified publicists.⁸⁶³ Even if an investment treaty does not explicitly establish a link with customary international law, the latter may nevertheless be used to fill in the *lacuane* of a treaty and play a supportive role to add further integrity to the treaty interpretive process.⁸⁶⁴ In fact, it was on this basis that the *Sempra*

⁸⁶¹ Canada Model FIPA, *supra* note 505, art. 5.1. See IOANA TUDOR, THE FAIR AND EQUITABLE TREATMENT STANDARD IN THE INTERNATIONAL LAW OF FOREIGN INVESTMENT 57 (2008) (“The minimum standard provides a ‘floor’ to ensure that the treatment of an investment cannot fall below treatment considered as appropriate under generally accepted standards of customary international law.”). See generally Matthew C. Porterfield, *A Distinction Without a Difference? The Interpretation of Fair and Equitable Treatment Under Customary International Law by Investment Tribunals*, INVESTMENT TREATY NEWS (Mar. 22, 2013), https://www.iisd.org/itn/2013/03/22/a-distinction-without-a-difference-the-interpretation-of-fair-and-equitable-treatment-under-customary-international-law-by-investment-tribunals/#_ftn13; OECD, INTERNATIONAL INVESTMENT LAW: A CHANGING LANDSCAPE: A COMPANION VOLUME TO INTERNATIONAL INVESTMENT PERSPECTIVES 73 (2005) (describing the relationship between the treaty standard of FET with the minimum standard of international customary law).

⁸⁶² Patrick Dumberry, *Are BITs Representing the “New” Customary International Law in International Investment Law?*, 28 PENN STATE INT’L L. REV. 675, 684 (2010).

⁸⁶³ Statute of the International Court of Justice, art. 38(1), June 26, 1945, 33 U.N.T.S. 993.

⁸⁶⁴ *Amoco Int’l Finance Corp. v. Iran*, Iran-U.S. Claims Tribunal, Award No. 310-56-3, para. 112 (July 24, 1987). See Dumberry, *supra* note 862, at 697.

tribunal was perhaps compelled to refer to customary international law; that is, to fill the gap that existed because the U.S.-Argentina BIT did not detail the legal elements necessary for the application of the necessity standard.⁸⁶⁵ Although various drafting techniques may be used to reduce uncertainties regarding the relationship between an IIA carve-out and customary international law, the intent behind the proposed standard public order carve-out is to prevent the necessity doctrine under the customary international law from being conjured when investment tribunals interpret the standard public order carve-out.

The public order carve-out as expressed in Article XI of the U.S.-Argentina BIT or as proposed in this Dissertation is not a *lex specialis* to the necessity doctrine, but can gain legitimacy from the police powers doctrine derived from the customary international law principle of State sovereignty. In fact, it was on this basis that the host State of Uruguay argued that its tobacco control measures on cigarette packing were a legitimate exercise of sovereign police powers aimed at the protection of public health since the underlying Switzerland-Uruguay BIT did not contain a NPM provision such as Article XI of the U.S.-Argentina BIT.⁸⁶⁶ The police powers doctrine is not explicitly stated for in the Switzerland-Uruguay BIT, but the ICSID tribunal found Uruguay's tobacco control measures to be a legitimate exercise of its police powers under customary international law.⁸⁶⁷ A technical issue that may need to be sorted out is the fine distinction between the proposed

⁸⁶⁵ *Sempra v. Argentina*, *supra* note 179, para. 378.

⁸⁶⁶ *Philip Morris v. Uruguay*, *supra* note 748, paras. 181 & 216.

⁸⁶⁷ *Id.* para. 290.

standard public order carve-out and the police powers doctrine. The outcome under the two legal sources may not show a significant difference, but when the police powers doctrine under customary international law fails, the proposed standard public order carve-out should apply. Even if there exists a police powers doctrine, the conditions that allow for the application of a State's right to regulate can be better identified through a standard public order carve-out.

E. Preserving Regulatory Space in the Absence of the Public Order Carve-out

Not all recently concluded IIAs contain the public order carve-out or an explicit right to regulate provision to preserve policy space. In fact, because the IIA universe is comprised of agreements concluded especially during the 1990s, most investment treaties do not explicitly contain the public order carve-out or similar provisions aimed at preserving regulatory space. As previously examined in discussion on the perspectives of each of the IIA stakeholders in Chapter 1, the need for a public order carve-out in investment treaties was minimal for at least two reasons. First, BITs were usually concluded between a developing country/host State and a developed country whose nationals it had to protect when doing business in a foreign country. Second, although the United States intended to wield certain economic behavior from its contracting States through the public order carve-out, it realized that those contracting States as host States could just as easily reverse the situation by using the same exception provision to the detriment of its nationals. However, given that the traditional roles are no longer distinct and that States often take on both roles as provider and recipient of foreign investment, the omission of a standard public order

carve-out that enables the contracting States to take certain act regulatory acts is no longer recommendable.

In the absence of an explicit public order carve-out, it may be contended that IIAs implicitly contain the right to regulate since treaties must be interpreted in accordance to general international law, which recognizes the sovereign right to regulate, or that IIAs must be interpreted together with any relevant rules of international law so that obligations arising out of international human rights and environmental law would require States to regulate for society and the environment.⁸⁶⁸ However, the absence of an express provision like the public order carve-out may prevent the balancing of the stakeholders' interests slowing down the development process of IIAs in the current investment climate.⁸⁶⁹ Moreover, without a public order provision that carves out regulatory space, investment tribunals may be inclined to rely on the familiar, but strict conditions set forth in ILC Article 25. Intended or not, this may prompt a situation of "universal privileging"⁸⁷⁰ where the purpose of investor protection is treated as if it has

⁸⁶⁸ See Spears, *supra* note 754, at 1046.

⁸⁶⁹ See Markus Gehring & Dimitrij Euler, *Public Interest in Investment Arbitration*, in *TRANSPARENCY IN INTERNATIONAL INVESTMENT ARBITRATION: A GUIDE TO THE UNCITRAL RULES ON TRANSPARENCY IN TREATY-BASED INVESTOR-STATE ARBITRATION* 7, 11 (Dimitrij Euler et al. eds., 2015) (stating that "[f]rom a sustainable development perspective, the main challenge faced by treaty negotiators is to balance the conflict interests present in the essence of foreign investments").

⁸⁷⁰ CHRISTINA VOIGT, *SUSTAINABLE DEVELOPMENT AS A PRINCIPLE OF INTERNATIONAL LAW: RESOLVING CONFLICTS BETWEEN CLIMATE MEASURES AND WTO LAW* 336 (Brill 2009); Jeffrey L. Dunoff, *Reconciling International Trade with Preservation of the Global Commons: Can We Prosper and Protect?*, 49 *WASH. & LEE L. REV.* 1407, 1449 (1992) (author coining the term "universal privileging").

the power to override other competing interests related to the preservation of a host State's regulatory space. The effect may be to degrade important social values.⁸⁷¹ Such an application of the customary necessity standard in the absence of the public order carve-out would overwhelm the stakeholders in the international investment law system.

Apart from the newer generation of IIAs, the vast number of agreements in the 3,000-plus IIA universe does not contain explicit provisions that permit States to derogate from their international commitments for policy reasons.⁸⁷² Then, how should investment tribunals interpret a public order carve-out from an earlier BIT when a later IIA does not include a public order carve-out? Although investment tribunals usually only refer to Article 31 of the Vienna Convention to guide treaty interpretation,⁸⁷³ Articles 30 and 50 which addressing the principles to be applied for successive treaties of the same subject matter may offer some initial guidance. Article 30 of the Vienna Convention is titled "Application of Successive Treaties Relating to the Same Subject Matter" and stated as follows:

⁸⁷¹ VOIGT, *supra* note 870, at 336.

⁸⁷² See UNCTAD, SUSTAINABLE DEVELOPMENT FRAMEWORK, *supra* note 76, at 211 ("No general model of exception has thus been developed in state and tribunal practice.").

⁸⁷³ Moshe Hirsch, *Interactions between Investment and Non-investment Obligations*, in THE OXFORD HANDBOOK OF INTERNATIONAL INVESTMENT LAW 154, 162 (Peter Muchlinski et al. eds., 2008) ("This practical disregard may appear even more puzzling in light of the fact that contemporary international investment law does not include a coherent body of rules in this sphere."). See generally Houde & Yannaca-Small, *supra* note 833.

1. Subject to Article 103 of the Charter of the United Nations, the rights and obligations of States parties to successive treaties relating to the same subject-matter shall be determined in accordance with the following paragraphs.
2. When a treaty specifies that it is subject to, or that it is not to be considered as incompatible with, an earlier or later treaty, the provisions of that other treaty prevail.
3. When all the parties to the earlier treaty are parties also to the later treaty but the earlier treaty is not terminated or suspended in operation under article 59, the earlier treaty applies only to the extent that its provisions are compatible with those of the later treaty.
4. When the parties to the later treaty do not include all the parties to the earlier one:
 - (a) As between States parties to both treaties the same rule applies as in paragraph 3;
 - (b) As between a State party to both treaties and a State party to only one of the treaties, the treaty to which both States are parties governs their mutual rights and obligations.
5. Paragraph 4 is without prejudice to article 41, or to any question of the termination of suspension of the operation of a treaty under article 60 or to any question of responsibility which may arise for a State from the conclusion or application of a treaty the provisions of

which are incompatible with its obligations towards another State under another treaty.⁸⁷⁴

Under the heading “Termination or Suspension of the Operation of a Treaty Implied by Conclusion of a Later Treaty,” Article 59 of the Vienna Convention provides that:

1. A treaty shall be considered as terminated if all the parties to it conclude a later treaty relating to the same subject-matter and:
 - (b) It appears from the later treaty or is otherwise established that the parties intended that the matter should be governed by that treaty; or
 - (c) The provisions of the later treaty are so far incompatible with those of the earlier one that the two treaties are not capable of being applied at the same time.
2. The earlier treaty shall be considered as only suspended in operation if it appears from the later treaty or is otherwise established that such was the intention of the parties.⁸⁷⁵

Along with the existing BITs, some States have also subsequently entered into regional and/or bilateral comprehensive FTAs creating the problem of how the public order carve-out will be interpreted. In the relatively straightforward circumstance that the parties to the earlier and

⁸⁷⁴ Vienna Convention, *supra* note 749, art. 30.

⁸⁷⁵ *Id.* art. 59.

successive treaty are identical, two scenarios would be possible. Article 59(1) of the Vienna Convention provides that the earlier treaty will be terminated based on the parties' intent to do so or if the two treaties cannot be reconciled. For the parties that overlap in both treaties, Article 30(4)(a) of the Vienna Convention redirects the parties to the rule described above in paragraph 3. But if the parties to a later treaty do not include the same member States, "the treaty to which both States are parties govern their mutual rights and obligations."⁸⁷⁶ Where the treaties are incompatible, the State which is a party to both treaties may owe an obligation towards the other party State which is a member to the later treaty. Further complications arise because the Vienna Convention does not instruct how the incompatible treaties should be prioritized with respect to each other. A rigorous interpretation of this situation may compel the party that undertook legal duties in the inconsistent treaties to breach one treaty in favor of another. Alternatively, this situation might be avoided if the treaties deemed to be incompatible are interpreted so that one treaty does not override the other.⁸⁷⁷ Even under a harmonious approach, the practical effect of applying one rule to the exclusion of the other incompatible treaties may, however, remain the same.⁸⁷⁸

The situation of where an earlier, but not later concluded IIA contains the public order carve-out is conceivable given the recent trend

⁸⁷⁶ *Id.* art. 30.4(b).

⁸⁷⁷ Hirsch, *supra* note 873, at 162 ("Such an approach strives to interpret one treaty in light of the other treaty....").

⁸⁷⁸ *Id.*

towards mega-regional trade agreements.⁸⁷⁹ The TPP includes the MFN clause,⁸⁸⁰ but not a public order clause, which may allow foreign investors to challenge a State that has enacted a public order measure under different playing grounds.⁸⁸¹ The public order carve-out is explicitly provided for in the investment chapter of the Japan-Singapore New-Age Economic Partnership Agreement,⁸⁸² the Agreement between New Zealand and Singapore on a Closer Economic Partnership,⁸⁸³ and alluded to in the Malaysia-Japan Economic Partnership Agreement.⁸⁸⁴ Moreover, these

⁸⁷⁹ Policy institutes around the world including Korea have already initiated studies on the rise of mega-FTAs. See, e.g., Ruben van den Hengel, *The Rise of Mega-FTAs*, EU CENTRE FACT SHEET (Oct. 2013), <http://www.eucentre.sg/wp-content/uploads/2013/10/Fact-Sheet-Mega-FTAs-October-2013.pdf>; *Seoul Int'l Trade Conference to Examine the Rise of Mega FTAs*, KOREA HERALD (Nov. 10, 2015), <http://www.koreaherald.com/view.php?ud=20151110000234>.

⁸⁸⁰ TPP, *supra* note 11, art. 9.5 (providing the MFN provision).

⁸⁸¹ Jess Hill, *TPP's Clauses that Let Australia be Sued are Weapons of Legal Destruction, Says Lawyer*, GUARDIAN (Nov. 10, 2015), <http://www.theguardian.com/business/2015/nov/10/tpps-clauses-that-let-australia-be-sued-are-weapons-of-legal-destruction-says-lawyer> (lawyer for the Australian government arguing that including the MFN clause in the TPP was a “major mistake” because it still leaves Australia susceptible to being sued under the ISDS system even if Australia had opted out of ISDS under the TPP); Alicia Nicholls, *Trans-Pacific Partnership Agreement in Review Part I: The Investment Chapter*, CARIBBEAN TRADE LAW & DEVELOPMENT (Nov. 10, 2015), <https://caribbeantradelaw.wordpress.com/category/trans-pacific-partnership-agreement/> (“The biggest concern is the MFN clause which if a liberal interpretation by an arbitral tribunal is given may ultimately undo a lot of the improvements made in the TPP by allowing investors to rely on more favourable provisions in other agreements concluded by the host state.”).

⁸⁸² Japan-Singapore New Age Economic Partnership Agreement, *supra* note 288, art. 83.1.

⁸⁸³ New Zealand-Singapore CEPA, *supra* note 458, art. 71.

⁸⁸⁴ Malaysia-Japan Economic Partnership Agreement, art. 10, Dec. 13, 2005.

contracting States also happen to be parties to the TPP. However, the public order carve-out is not specifically provided for in the investment chapter of the TPP but instead covered by a more general provision titled “Investment and Environmental, Health and other Regulatory Objectives.” The relevant Article 9.16 of the TPP investment chapter states the following:

Nothing in this Chapter 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, health or other regulatory objectives.⁸⁸⁵

Article 9.16 of the TPP does not provide reference to a public order carve-out. However, Chapter 25 titled “Regulatory Coherence”⁸⁸⁶ allows TPP States to preserve their right to regulate for “covered regulatory measures” publicly identified within one year after entry into force.⁸⁸⁷ The term “regulatory coherence” is to be understood as the States’ “use of good regulatory practices in the process of planning, designing, issuing,

⁸⁸⁵ TPP, *supra* note 11, art. 9.15.

⁸⁸⁶ However, the investment chapter of the TPP contains a provision on relation to other chapters in Article 9.3 that would permit the chapter on regulatory coherence to prevail in the case of an inconsistency between it and the investment chapter.

⁸⁸⁷ TPP, *supra* note 11, art. 25.3 providing for the scope of covered regulatory measures states that:

Each Party shall promptly, and no later than one year after the date of entry into force of this Agreement for that Party, determine and make publicly available the scope of its covered regulatory measures. In determining the scope of covered regulatory measures, each Party should aim to achieve significant coverage.

implementing and reviewing regulatory measures” so that domestic policy goals may be realized while being mindful of the international effort “to enhance regulatory cooperation in order to further those objectives and promote international trade and investment, economic growth and employment.”⁸⁸⁸ This chapter grants considerable leeway to the Parties in that each TPP State is entitled by sovereign right to determine its regulatory priorities and establish and implement measures to give effect to those priorities “at the levels that the Party considers appropriate,”⁸⁸⁹ but also encourages that regulatory proposals undergo an impact assessment during the development phase.⁸⁹⁰ A regulatory impact assessment should ideally evaluate the need for the proposed regulation, perform due diligence to find feasible alternatives, and justify how the selected regulatory proposal efficiently achieves the desired policy objective.⁸⁹¹ The implementing State should ensure that the covered regulation uses easy-to-understand language that is clear and concise and accessible to the public, and if possible, make the information viewable online.⁸⁹² Moreover, the TPP States should review their covered regulatory measures at intervals specified by the implementing State to determine the continued effectiveness in achieving the State’s policy goals.⁸⁹³ The States are also encouraged to provide annual public notice of

⁸⁸⁸ *Id.* art. 25.2.1.

⁸⁸⁹ *Id.* art. 25.2.2(b).

⁸⁹⁰ *Id.* art. 25.5.1.

⁸⁹¹ *Id.* art. 25.5.2.

⁸⁹² *Id.* arts. 25.5.4 & 25.5.5.

⁸⁹³ *Id.* art. 25.5.6.

the regulatory measures it expects to enact for the following year.⁸⁹⁴

To a certain extent, the TPP expands the public order carve-out seen in previous BITs. Rather than providing an enumerated list of what would fall under a public order carve-out, the Regulatory Coherence chapter focuses on developing a process that could later be established as a firm practice that balances the domestic regulatory space of the States with their international investment obligations. However, the concern remains that the chapter on regulatory coherence is generally laden with soft language like “in a manner [the Party] deems appropriate,”⁸⁹⁵ “each Party shall endeavor to ensure,”⁸⁹⁶ and “should generally have as overarching characteristics.”⁸⁹⁷ Some critics of the TPP also contend that the essence of Article 9.16 has been eliminated due to the inclusion of the phrase “[unless] otherwise consistent with this chapter.”⁸⁹⁸ So while the TPP features a promising system through which the States can retain a flexible degree of regulatory power, the actual impact of this chapter remains to be tested.

The newly concluded Canada-EU CETA completely avoids this issue by permitting the CETA to replace the existing BITs between the individual EU member States and Canada. For previous BITs that did not provide for the public order carve-out, the investment chapter of the Canada-EU CETA

⁸⁹⁴ *Id.* art. 25.5.7.

⁸⁹⁵ *Id.* art. 25.5.7.

⁸⁹⁶ *Id.* art. 25.4.1.

⁸⁹⁷ *Id.* art. 25.4.2.

⁸⁹⁸ Hill, *supra* note 881. Nicholls, *supra* note 881 (“loophole which potentially negates the efficacy of this carve-out”).

provides a modified right to regulation framework. The preamble “preserve[s] the right of the Parties to regulate within their territories and the Parties’ flexibility to achieve legitimate policy objectives, such as public health, safety, environment, public morals and the promotion and protection of cultural diversity.”⁸⁹⁹ This commitment is reaffirmed in the article covering “Investment and regulatory measures,” which contains three paragraphs that further explain the scope of a State’s right to regulate.⁹⁰⁰ Moreover, the Canada-EU CETA provides for sustainable development in the context of trade⁹⁰¹ and specifically creates a linkage with the environment by stating that “the environment is a fundamental pillar of sustainable development and recognize the contribution that trade could make to sustainable development.”⁹⁰² Given that foreign investment can have a significant role on sustainable development, the next step may be to draft a similar chapter dedicated to establishing the linkage between investment and sustainable development so that the traditional purpose of IIAs continues to be promoted.⁹⁰³ However, creating a linkage between investment and sustainable development in IIAs will be an arduous task

⁸⁹⁹ Canada-EU CETA, *supra* note 18, preamble.

⁹⁰⁰ *Id.* art 8.9.

⁹⁰¹ *Id.* preamble (“Reaffirming their commitment to promote sustainable development and the development of international trade in such a way as to contribute to sustainable development in its economic, social and environmental dimensions...”) & ch. 22 (Trade and Sustainable Development).

⁹⁰² *Id.* art. 24.2.

⁹⁰³ Markus Gehring & Andrew Newcombe, *An Introduction to Sustainable Development in World Investment Law*, in *SUSTAINABLE DEVELOPMENT IN WORLD INVESTMENT LAW* 3, 9-10 (Marie-Claire C. Segger et al. eds., 2011).

since a balance needs to be struck among providing a favorable investment climate, carving out a sufficient amount of policy space, and creating incentives that promote sustainable development goals.⁹⁰⁴ An investment treaty that aggressively preserves policy space for sustainable development regulations could revert the original purpose of investment treaties, which is to protect investors.⁹⁰⁵ Moreover, pursuing sustainable development goals will probably not permit a State to derogate from its obligations when subject to the “deliberately stringent” requirements of the necessity doctrine. Nor should this be a substitute for the concept of having a public order carve-out. Professor Bjorklund points out that tribunals would be reluctant to allow a host State to derogate from its specific treaty obligations so that it could realize its sustainable development goals, which are broad policies of a general nature.⁹⁰⁶ Alternatively, even if a State bases its derogation of an IIA obligation upon a specific sustainable development regulation, tribunals would still have a hard time finding that the perceived threat put the State in a grave and imminent peril, a criterion that is very difficult to prove under the necessity doctrine.⁹⁰⁷ Therefore, this Dissertation recommends that

⁹⁰⁴ *Id.* at 5. See BONNITCHA, *supra* note 82, at 38 (“In practice, the phrase ‘sustainable development’ functions either as a portmanteau for a collection of incommensurable norms that include environmental conservation, economic growth, realization of human rights and distributive justice; an interstitial principle – a secondary norm governing the balancing of competing primary norms such as these; or as both a portmanteau and an interstitial norm.” [footnotes omitted]).

⁹⁰⁵ See Andrea K. Bjorklund, *The Necessity of Sustainable Development?*, in SUSTAINABLE DEVELOPMENT IN WORLD INVESTMENT LAW 373, 377 (Marie-Claire C. Segger et al. eds., 2011).

⁹⁰⁶ *Id.*

⁹⁰⁷ *Id.*

future investment treaties include a standard public order carve-out.

II. The Legitimate Policy Objectives in the Proposed Standard Public Order Carve-out as Explained by Existing Cases

The proposed standard public order carve-out strives to produce a convincing model by relying on a reasonableness test where the task of the tribunal is to determine if the regulatory measure can be supported by coherent reasonable and respectable evidence that is objectively justifiable.⁹⁰⁸ A key feature of the proposed standard public order carve-out is the inclusion of a review standard which is contrary to the typically silent nature of investment treaties regarding the appropriate standard of review.⁹⁰⁹ This perspective changes the way investor-State tribunals are viewed since, traditionally, investment arbitration has been strongly associated with international commercial arbitration involving disputes between private parties. However, with foreign investors challenging the regulatory measures of a host State, investment tribunals have begun to embrace the fact that investment arbitration can impact matters of a State public law and public international law. The aim of this section is to reduce the abstractness of the proposed standard public order carve-out by referring to previous

⁹⁰⁸ Valentina Vadi, *Proportionality, Reasonableness, and Standards of Review in Investment Treaty Arbitration*, in YEARBOOK ON INT'L INVESTMENT LAW & POLICY 2013-2014 201, 216 (Andrea K. Bjorklund ed., 2015). See ALISTAIR RIEU-CLARKE, INTERNATIONAL LAW AND SUSTAINABLE DEVELOPMENT: LESSONS FROM THE LAW OF INTERNATIONAL WATERCOURSES 108 (IWA 2005) (stating that the meaning of reasonableness "may [] vary depending on the stage of development of a State"); Juan Felipe Merizalde Urdaneta, *Proportionality, Contributory Negligence and other Equity Considerations in Investment Arbitration*, in INVESTMENT TREATY AND ARBITRATION LAW 301, 314 (Ian A. Laird et al. eds., 2015).

⁹⁰⁹ Julian Arato, *The Margin of Appreciation in International Investment Law*, 54 VA. J. INT'L L. 545, 555 (2014).

cases and current trends that can elucidate how the legitimate policy objectives might be understood as set forth in the proposed standard public order carve-out.

In the first and second paragraphs of the proposed standard public order carve-out respectively providing for, in relevant parts, the protection of public safety and human, animal, or plant life or public health as well as the third paragraph on the protection of the environment, the recent decision by the German Constitutional Court in the *Vattenfall* case at the end of 2016 is foretelling of how future investment tribunals may address such regulatory issues. The German Constitutional Court acknowledged that the government's decision to completely shut down the operation of nuclear plants without any compensation came as a response to the Fukushima nuclear disaster brought upon a tsunami in 2011.⁹¹⁰ It then affirmed the regulatory authority of the State to determine whether the nuclear plants pose a safety risk to the public even if the measure was adopted shortly after the government had significantly extended the existing nuclear plant permits.⁹¹¹ This approach taken by the German Constitutional Court is

⁹¹⁰ Federal Const. Ct. (Germany), *The Thirteenth Amendment to the Atomic Energy Act is for the Most Part Compatible with the Basic Law* (Dec. 6, 2016), http://www.bundesverfassungsgericht.de/SharedDocs/Pressemitteilungen/EN/2016/bvg16-088.html;jsessionid=D6A15080C9CF34604A8541E39DB17146.2_cid361 ("As a result of the tsunami of 11 March 2011 and of the meltdown of three reactor cores this brought about at the Fukushima nuclear power plant in Japan, the legislature, for the first time, statutorily set down fixed end dates for the operation of nuclear power plants in the 13th AtG Amendment....").

⁹¹¹ *Id.* ("The legislature is pursuing a legitimate regulatory objective in accelerating the nuclear phase-out with the underlying intent of thus minimising, in time and scope, the residual risk associated with nuclear energy, and thereby protecting the life and health of the people as well as the natural foundations of life.").

consistent with the recent investment arbitration awards which reveal a trend towards recognizing a host State's right to regulate.

In an ICSID arbitration dealing with public health, the tribunal in *Philip Morris v. Uruguay* found that Uruguay possessed the regulatory authority to enact tobacco control measures under the State's sovereign police power to protect health and also owed a duty to protect public health under both domestic and international laws.⁹¹² Although each of the adjudicative bodies mentioned above found that the challenged measure fell within the scope of the host State's regulatory power, this dispute is differentiable from the *Vattenfall* case where the German parliament exercised regulatory authority to address a purely domestic concern. This is unlike the case in *Philip Morris v. Uruguay* where Uruguay enacted the domestic measures on tobacco control in compliance with the international obligations arising out of Uruguay's ratification of multilateral conventions like the World Health Organization (WHO) Framework Convention on Tobacco Control and the ICESCR.⁹¹³ Furthermore, crucial details can be set apart to explain their different outcomes regarding the expropriation issue. The German Constitutional Court, which was faced with the task of

⁹¹² *Philip Morris v. Uruguay*, ICSID Case No. ARB/10/7, Concurring and Dissenting Opinion Co-Arbitrator Gary Born, paras. 89-90 (July 8, 2016) (making clear that nothing in the award or the dissenting opinion challenges Uruguay's sovereign authority).

⁹¹³ The WHO Framework Convention on Tobacco Control was adopted on May 21, 2003, which Uruguay ratified on September 9, 2004. ICESCR art. 12.1 ("The States Parties to the present Covenant recognize the right of everyone to the enjoyment of the highest attainable standard of physical and mental health."). Moreover, the *amicus curiae* submissions by major international organizations like the WHO, the Pan American Health Organization, FCTC Secretariat strengthened the case on behalf of Uruguay.

determining the constitutionality of a measure that would require the shutdown of nuclear plants without any compensation, held that the measure violated the constitutional right to property. However, in *Philip Morris v. Uruguay*, the ICSID tribunal specified that regulatory measures are not expropriatory, but legitimate exercises of police powers if they are “taken *bona fide* for the purpose of protecting the public welfare, [...] non-discriminatory and proportionate.”⁹¹⁴ This clear expression of the non-expropriatory nature of regulatory measures can be traced back to award in *Saluka v. Czech Republic* where the UNCITRAL tribunal affirmed that:

It is now established in international law that States are not liable to pay compensation to a foreign investor when, in the normal exercise of their regulatory powers, they adopt in a non-discriminatory manner *bona fide* regulations that are aimed at the general welfare.⁹¹⁵

Similar to how the tobacco control measures were enacted in Uruguay to meet its international obligations, regulatory measures aimed at the protection of the environment will no longer be a domestic matter but be enacted to meet international commitments such as those arising from the Paris Agreement within the UN Framework Convention on Climate Change (“Paris Agreement”) signed by 195 States and the EU in December 2015.⁹¹⁶ The Paris Agreement is expected to produce a collection of new regulatory

⁹¹⁴ *Philip Morris v. Uruguay*, *supra* note 748, para. 303 (citing *Tecmed*, *supra* note 96, para. 122).

⁹¹⁵ *Saluka Investments v. Czech Republic*, UNCITRAL, Partial Award, para. 255 (Mar. 17, 2006).

⁹¹⁶ Paris Agreement to the United Nations Framework Convention on Climate Change, Dec. 12, 2015, FCCC/CP/2015/L.9/Rev.1 (2015).

measures that will be adopted to meet emission reduction targets like those on carbon dioxide and methane. Climate change action may also be further facilitated through the adoption of fiscal policy measures like carbon tax. These new regulatory measures may even place a higher environmental standard than what had existed at the time of initial investment. In fact, in the pending interim decision in *Perenco v. Ecuador*, the ICSID tribunal held that more stringent environmental regulations may be adopted so long as it does not apply retrospectively.⁹¹⁷

Investment arbitration cases regarding the fourth paragraph of the proposed standard public order carve-out on the protection of cultural diversity or assets can be expected to follow suit as exemplified above towards allowing a host State to exercise its sovereign right to regulate. In *Parkerings-Compagniet v. Lithuania*, a city of Lithuania rejected the foreign investor's proposal to develop car parks in the Old Town, a UNESCO historical site. The ICSID tribunal held that Lithuania's refusal of the car park proposal was justified for reasons of historical and archaeological preservation. In affirming the State's "undeniable right and privilege to exercise its sovereign legislative power," the *Parkerings* tribunal also expressed that the "State has the right to enact, modify or cancel a law at its own discretion"⁹¹⁸ since any investor would know that laws evolve over time.

⁹¹⁷ *Perenco v. Ecuador*, ICSID Case No. ARB/08/6, Interim Decision on the Environmental Counterclaim, para. 357 (Aug. 11, 2015) ("... the basic legal standards against which Perenco was to conduct itself cannot later be changed and applied retroactively to impose liability where none existed under the then-applicable standard.").

⁹¹⁸ *Parkerings-Compagniet v. Lithuania*, ICSID Case No. ARB/05/8, Award, para. 332 (Sep. 11, 2007).

The caveat is that the State must not have acted “unfairly, unreasonably or inequitably in the exercise of its legislative power.”⁹¹⁹ Moreover, another consideration for the legitimate policy objective on cultural protection is that it may be broadly interpreted to include the promotion of cultural diversity to expansively cover the distribution of publications and the publications themselves.⁹²⁰

However, regardless of the legitimate policy objective being pursued under the proposed standard public order carve-out, the common overlap of these arbitration cases is that while investment tribunals and foreign investors increasingly have to respect a host State’s “inherent right to regulate,” the exercise of such a right is not without limits.⁹²¹ Under international investment law, the State’s sovereignty is curbed when the government concludes international investment agreements, which embody international law principles that demand sovereignty to be balanced with the IIA goal of investment treaty by requiring the legitimate expectations of investors to be upheld while also ensuring that the FET and expropriation standards properly operate to prevent the unfair, discriminatory, or grossly inequitable nature of the State regulatory act.⁹²²

⁹¹⁹ *Id.*

⁹²⁰ UPS v. Canada, *supra* note 702, paras. 156-72.

⁹²¹ ADC v. Hungary, *supra* note 838, para. 423.

⁹²² See, e.g., Todd Weiler, PHYSICIANS FOR A SMOKE FREE CANADA, *Philip Morris vs. Uruguay: An Analysis of Tobacco Control Measures in the Context of International Investment Law* (July 28, 2010) (“The FET standard was never meant to prevent the good faith and non-discriminatory exercise of regulatory (aka ‘police’) powers by the Host State unless the adoption, implementation or effects of a measure are manifestly arbitrary, grossly inequitable or patently unfair.”). E.g., *Methanex v. U.S.*, UNCITRAL, Final Award of the Tribunal on Jurisdiction and Merits, para. 32

III. Concluding Remarks

Chapter 5 investigated the potential of the public order carve-out to meet the stakeholders' demands in international investment law through the proposed standard public order carve-out to emphasize the point that a standard public order carve-out should be legitimized as an IIA-based exception provision that can help preserve the regulatory space of host States. To consider the feasibility of the standard public order carve-out proposed in this Chapter, the changing nature of international investment agreements should be better recognized to minimize practice that egregiously tips the balance to one group of stakeholders over other stakeholders. The public order carve-out should not be simplistically regarded as a *lex specialis* as it is not a provision intended to fill the gaps in customary international law.

An important finding of this Dissertation is that evidence is generally lacking that the public order carve-out or the NPM provision was intended to operate as the *lex specialis* to the customary defense of necessity. The proposed standard public order carve-out seeks to form its own identity apart from the WTO/GATS-style general exceptions to provide a cautionary remark against blindly importing GATT Article XX and/or GATS Article XIV. This Chapter also considered the absence of the public order carve-out provision in investment treaties.

The legitimate policy objectives of the proposed standard public order carve-out may be negotiated as an exhaustive or illustrative list. In the case of the former, other exceptions to the IIA should be explicitly provided

(Aug. 3, 2005) (interpreting the expropriation standard as "incorporating the principle" that States usually do not owe compensation to foreign investors if measure taken for public interest is non-discriminatory).

for within the investment treaty exceptions section previously mentioned in this Dissertation. However, in the case that the proposed standard public order carve-out is envisioned as an illustrative list, other policy objectives that can plausibly arise in the regulatory context, such as those on tax, sustainable development, and human rights, would not have to be explicitly specified but would leave a degree of uncertainty that would have to be resolved by the investment tribunal.

Under the current environment where investment treaties are being rebalanced to better represent the interests of a diverse range of IIA stakeholders, the recommendation that this Dissertation offers is to include a public order carve-out so that a State's right to regulate can also be provided for in the IIA, even if it is provided for under the police powers doctrine under customary international law. On a related note, the goal of sustainable development is an important one, but investment tribunals cannot impose that presumption into IIAs in lieu of the public order carve-out; even if it could, the discourse concerning the relationship between the public order carve-out and sustainable development is very limited. However, an investment treaty that explicitly contains the legitimate policy objectives under a standard public order carve-out will publicize the intent of the States to limit the scope of some IIA obligations in order to preserve their regulatory space to foreign investors and investment tribunals.

Chapter 6: Conclusion

Under international investment law, the policy of preserving regulatory space should be defined to meet the changing times and needs of its stakeholders. Current efforts toward reinforcing the right to regulate in international investment law occur on an *ad hoc* basis and is not a consistently established IIA drafting practice among States. Just like how the provisions on expropriation and minimum standard of treatment, for example, have become a core part of investment treaties, consistently including a standard public order carve-out specifically tailored for investment treaties can contribute to the promotion of international investment agreements without distorting the original purpose of IIAs, which is to provide investment protection. However, in order for the proposed standard public order carve-out to emerge as a consistent and uniform IIA treaty-making practice that is capable of adding substance to the broadly conceived right to regulate notion, support is needed from all of the IIA stakeholders including the States, international organizations, and civil societies. The newfound equilibrium between the host States, foreign investors, and investment tribunals can contribute to a healthy improvement in the predictability and legitimacy of the international investment environment without regressing the advancements made for the protection of foreign investors and investments.

Of course, other ways of providing regulatory space for States are available. The UNCTAD identifies “four paths of actions” that can be taken to achieve reform of the international investment law system. The EU’s proposal of an investment court, which is stipulated in the Canada-EU CETA, the Vietnam-EU FTA, and the draft of the EU TTIP proposal is intended to replace the *ad hoc* investment arbitration system with a permanent court

system,⁹²³ might be an example of a systematic reform that includes multilateral efforts to “create proactive sustainable-development-oriented IIAs” for the preservation of a State’s policy space.⁹²⁴ Another reform may be pursued selectively to “add a sustainable development dimension to IIAs” such as by providing the right to regulate language in preambles or in the text of the treaty. Other options that maintain the status quo or completely disengage the IIA system might also be considered. However, the fundamental problem with all of these proposals is that vague principles like sustainable development persist as an undefined concept, thus recycling the age-old problem of where to pin concepts like sustainable development or the right to regulate in the public international law body to make them have better applicability when an investment tribunal decides on the outcome of an award.

Even the more seemingly concrete proposal of a permanent investment court possesses its own set of problems. The first problem is the establishment of a permanent institution is trying to be achieved through the conclusion of IIAs among a select group of the world’s countries under circumstances that may exploit an imbalance in powers among the States. The second problem is that an investment court merely provides an exterior shell to a body of international investment law jurisprudence that has yet to determine the appropriate review standard for deciding a State’s right to regulate. A sturdier foundation needs to be formed to reorient the

⁹²³ See EUROPEAN COMM’N, THE MULTILATERAL INVESTMENT COURT PROJECT (Dec. 21, 2016), <http://trade.ec.europa.eu/doclib/press/index.cfm?id=1608>.

⁹²⁴ UNCTAD, *Reform of the IIA Regime: Four Paths of Action and a Way Forward*, 3 IIA ISSUES NOTE (June 2014), http://unctad.org/en/PublicationsLibrary/webdiaepcb2014d6_en.pdf.

international investment law system so that investment protection is balanced alongside a State's right to regulate. It is this meaningful gap that this Dissertation strives to fill by arguing that IIA stakeholders must know what public interests will be carved out and what standard of review will be applied in case of an investment arbitration.

One of the major themes of this Dissertation has been to identify that the rule-exception structure is not firmly established in international investment agreements, even though treaty-based exceptions implemented for the purpose of preserving regulatory freedom has existed as early as in the FCN treaties and in the other international law systems examined in this Dissertation. The ILC Articles on State Responsibility, which is widely accepted as the codification of customary international law, permits wrongdoings under the justification rather than an exception concept. This is fundamentally different from the approach taken in the public order carve-out of IIAs, which ought to operate as a treaty exception that lies outside the scope of the investment treaty containing substantive obligations. Despite the potential of the proposed standard public order carve-out to serve as a tool for preserving regulatory freedom in international investment law, the same cannot be said for the necessity defense of customary international law. Furthermore, the relationship between the public order carve-out as provided in IIAs and the necessity defense arising out of customary international law appears to be under analyzed by any particular IIA stakeholder. This has resulted in Argentina raising the necessity defense because no other means of exculpation existed under customary international law. As examined in Chapter 4, the defenses available under customary international law are unlikely to provide host States with the

needed regulatory freedom to sustain the legitimacy of IIAs. Unlike the potential of the proposed standard public order carve-out to help host States act for their public interest, the necessity doctrine in customary international law contains impractical limitations that render it unusable as a means for preserving regulatory space.

Investment protection is not the only goal to be upheld in international investment law. The goals of providing legitimacy, predictability, and consistency must be achieved through the investor-State arbitration mechanism. These objectives are as important as providing investment protection and may be better achieved instead of placing the burden of preserving regulatory space only on the host State or the investment tribunals that have to determine whether a host State's measure is within the carve-out. An examination of the textual evolution of the public order carve-out has revealed that the function of the carve-out can vary according to where it is placed within the IIA. These nuances may work to the benefit of the States if they can control the amount of regulatory space needed in their investment treaties, which is one of the objectives to be achieved through the proposed standard public order carve-out. The placement of the standard public order carve-out with respect to the rest of the investment treaty is an important consideration that must be made by the contracting States. Including the standard public order as a consistent IIA-making practice of the States can provide a powerful, express indication of their intention to maintain regulatory power for certain public interest matters even after committing themselves to international treaty obligations, but must be expressed in the substantive body of the IIA since mere preambular language of the public order carve-out will most likely be treated

as hortatory language. The TPP presents its right to regulate provision by using positive language that establishes the provision titled “Investment and Regulatory Measures/Objectives” as one of the substantive obligations of the investment treaty. Special attention was given to the variant uses of the public order carve-out in IIAs, which may appear in relation to national treatment and most favored nation clauses or the WTO/GATS general exceptions provisions. Other IIAs provide in their consultations provision that issues relating to public order will be non-justiciable. To be fair, investment treaties have allowed derogations that can also raise into question their relationship with the public order carve-out. Legitimate public welfare objectives are usually discussed in the context of indirect expropriation, but may lie on the periphery of the public order carve-out. The Canada-EU CETA defines that legitimate policy objectives may include public health, safety, environment, public morals and the promotion and protection of cultural diversity – regulatory areas that may be a part of the public order concept in international investment law. How much regulatory space this use of positive language will deliver to host States remains a question and appears to be an extension of the hortatory language made in the preamble. The proposed standard public order carve-out aims to strengthen the States’ intent to preserve their regulatory power by existing as a clear exception to the obligations set forth in the IIA.

In the Argentine ICSID tribunals’ discussion of Article XI, which contained the public order carve-out, the required nexus between the regulatory act and its objective came into question. The public order carve-out may include a self-judging language to indicate the level of arbitral intervention that it is obligated to receive. The absence of the self-judging

language in the public order carve-out would bestow full interpretative authority to the investment tribunal although the adjudicative body must take care not to tread too deeply into the policy space of the host State. The CMS tribunal was heavily criticized for conflating the treaty standard of the public order carve-out with the necessity defense under customary international law. Subsequent ICSID arbitration cases against Argentina attempted to reconcile the two sources of law by treating the public order carve-out as a *lex specialis* that would apply where there is a lacuna in customary international law. While understandable that the majority of the earlier BITs did not contain the public order carve-out, some of the current IIAs continue to exclude the public order carve-out (or provide any language that could be interpreted to preserve regulatory space). But the literal application of the necessity standard and the defenses provided under customary international law would defeat the purpose of an IIA-based public order carve-out and still leave unresolved related questions of compensation when analyzed in connection with the ILC articles on circumstances precluding wrongfulness. For this reason, the standard public order carve-out has been drafted in a way to prevent application of the necessity defense under customary international law.

In conclusion, the proposed standard public order carve-out provides a starting point for increased discussion among IIA stakeholders, and the future generation of IIAs may benefit from its further development. Regulatory interests relating to public health, safety, the environment, and human rights are directly or indirectly associated with the concept of public order. Similar to what Argentina argued in the ICSID cases, a financial catastrophe may become increasingly difficult to treat as an isolated event

attributable to a specific country due to the interconnectedness of the world economy. The necessity standard under customary international law lacks the sensitivity to meet the dynamic demands of IIA stakeholders. Meaningful progress is being made in this regards in the recently concluded investment treaties that include novel attempts to better balance competing interests through right to regulate provisions. The EU, United States, and Canada have generally been at the forefront of this progress, with the EU attempting a bolder move in the not yet concluded TTIP. Where the correct equilibrium lies at the moment is not obvious and will most likely evolve in the coming generations of IIAs, but a carefully defined formulation of a standard public order carve-out can provide what has been missing in international investment law – an overarching concept on IIA exceptions that can serve as the basis of the right to regulate interest of States.

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국문초록

1960년대에 BIT 프로그램이 시작되면서, BIT의 목적은 외국인 투자를 보호하여 대체로 자본을 수출하는 선진국에게 이득이 돌아가게 한다는 한 가지 목표에 의해 지배적으로 영향을 받았다. BIT의 법적인 과급 효과를 총체적으로 인지하지 못하고 외국 투자를 유치하기 위해 BIT에 참여한 자본을 수입하는 개발도상국들과는 달리, 이 자본을 수출하는 선진국들은 BIT의 목적이 투자자의 투자를 보호하는 것이라는 점을 명확하게 이해하고 있었다.

하지만, NAFTA 등의 투자 조항을 포함하는 FTA가 체결되면서 BIT의 투자 보호 목표가 확대되어 투자 촉진이나 자유화 같은 목표를 포함하게 되었다. NAFTA 이전에는 국제 투자 협정 (IIA)에 정책 공간 확보가 우려의 대상이 되지 않았으나, 후일 NAFTA에서 얻은 경험으로 개발도상국뿐만 아니라 선진국도 투자 분쟁원에서 피고국이 될 수 있다는 게 입증되면서 상황이 바뀌게 되었다. 이와 같은 선례, 그리고 아르헨티나와의 국제투자분쟁해결기구 (ICSID) 사례들이 소재국이 규제권을 행사할 필요성에 관심을 가지게 하는데 중요한 역할을 했으며, IIA 체결로 인한 유의한 법적 결과는 공익의 다양한 측면을 규제하기 위해 주권적 조치를 취할 시, IIA의 조항을 위반하게 될 수 있다는 사실을 선진국과 개발도상국이 모두 이해하는데 도움이 되었다.

이 연구의 목적은 국제 투자에 존재하는 의미 있는 빈틈을 메꾸어 국가들이 미국-아르헨티나 BIT의 non-precluded measure 규정에 나오는 공공 질서 조항을 시작점으로 사용하여 규제하는데 주권을 더 잘 행사할 수 있게 하는 것이다. 이 연구에서는 국제 투자 법에 공공 질서 개념이 정의되어 있지 않아 투자자소송 임의중재가 공공 질서 제외 조항 (carve-out)을 일관성 있고 예측 가능한 방식으로 해석하기 어렵다는 사실을 알게 된다. 이 연구에서 묻는 질문에는 공익 정책을 위한 공공 질서 제외 조항이 나타나고 있는지, 그리고 만

일 나타나고 있다면, 공공 질서 제외 조항은소재국이 규제 권한을 행사하는데 필요한 유연성을 갖출 수 있는지 여부가 포함된다.

어떤 면에서는, 규제권 개념이 아르헨티나에 맞서 ICSID 중재원에서 예시된 교훈에도 불구하고, 국제 투자 법에서 규제권을 적용하는 방법은 고려하지 않고 IIA의 최신 견해에 포함되고 있다.. 또 다른 면에서 보면, BIT는 일반적으로 실증적 의무 (substantive obligation)만 담도록 구성되었다. IIA의 최근 추세는 실증적 의무의 범위를 제한하는 몇 가지 변형된 일반적인 예외 조항을 포함하는 것이지만, 실무 방식은 여전히 대체로 일관성이 없고 WTO/GATS 법학 이론에서 빌려온 것이다. 하지만, 이 연구에서는 구체적으로 정부의 규제 영역을 보존하려는 목표의 표준 공공 질서 제외 조항을 포함하는 것이 미래의 IIA 조약의 고정된 요소가 되어야 IIA 이해관계자들의 증가하는 집합적 공동체 이익을 더 잘 처리할 것이라고 결론을 내린다. 이렇게 되면 궁극적으로 국제 투자 법 참여자들의 기준 가치 및 우려하는 점을 평가해야 한다.

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주요어: 공공 질서, 표준 제외 조항, 규제권 개념, 필요성 원칙, 공동체 이익, 아르헨티나

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