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Towards a Convergence of Trade and Investment Law? A Right to Take Prudential Measures for the Preservation of Financial Stability

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I. Introduction

The legal and political-economic literature has widely debated whether and to what extent States should be allowed to take "prudential" regulatory measures in order to safeguard their financial systemic interests from serious threats of financial crisis. In the main, most commentators agree that States should have the right to take prudential measures in derogation of their trade commitments. But disagreements have emerged over the conditions, necessity, timing, and length of such measures because there has been virtually no case law applicable to the subject matter.[1] A recent dispute involving financial services at the World Trade Organization (WTO) provides an opportunity for this article to contribute to the doctrinal debate on prudential measures by drawing a parallel between trade and investment perspectives on the matter.[2] Indeed, investment cases relating to regulatory measures taken in a "state of necessity" following the Argentinean economic crisis of 2001 have briefly touched upon prudential measures in investment tribunals.[3]

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1. For background information on this debate, *see* IMF, *Reference Note on Trade in Financial Services*, (Sept. 2010); Sydney J. Key, The Doha Round and Financial Services Negotiations (2003); Inu Barbee & Simon Lester, *Financial Services in the TTIP: Making the Prudential Exception Work*, 45 GEO. J. INT'L L. 953 (2014); Thomas Cottier & Markus Krajewski, *What Role for Non-Discrimination and Prudential Standards in International Law?*, 13 J. INT'L ECON. L. 817, 817-835 (2010).

2. Appellate Body Report, *Argentina – Measures Relating to Trade in Goods and Services*, WTO Doc. WT/DS453/AB/R (adopted Apr. 14, 2016) [hereinafter *Argentina – Financial Services Appellate Body Report*]; Panel Report, *Argentina – Measures Relating to Trade in Goods and Services*, WTO Doc. WT/DS453/R (adopted Sept. 30, 2015) [hereinafter *Argentina – Financial Services Panel Report*].

3. *See* Urbaser S.A. v. Argentine Republic, ARB/07/26, Award (ICSID 2016); Cont'l Cas. Co. v. Argentine Republic, ARB/03/9, Award (ICSID 2008); Sempra Energy Int'l v. Argentine Republic, ARB/02/16, Award (ICSID 2007); Enron Corp. Ponderosa Assets, LP v. Argentine Republic, ARB/01/03, Award (ICSID 2007); LG&E Energy Corp. v. Argentine Republic, ARB/02/1, Decision on Liability (ICSID 2006); CMS Gas Transmission Co. v. Argentine Republic, ARB/01/8, Award (ICSID 2005).

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While this article is not the first to focus on prudential measures, the literature to date has largely focused on trade-related aspects and only lightly touched upon the important contribution made by investment tribunals.[4] Moreover, no article to date discusses the potential convergence between WTO case law and investment arbitral law on the issue of measures taken for prudential reasons relating to economic duress. In this regard, this article fills a gap in the literature by assessing and, in many respects, linking the contribution of the recent WTO jurisprudence *and* the relevant investment cases pertaining to the notion of prudential measures aimed at ensuring the security and predictability of their financial system.

The article proceeds as follows: Part I provides background on prudential measures in the GATS before reviewing the text and doctrinal debate on the effectiveness of prudential measures.

Part II examines the recent and first WTO dispute which raises and discusses a range of trade-related issues regarding prudential measures. *Argentina – Measures Relating to Trade in Goods and Services (Argentina – Financial Services)* is instructive in establishing the parameters of a wider framework for financial regulatory intervention, particularly in times of economic and systemic duress.[5] Discussions on necessity at the WTO have not traditionally focused on prudential measures justified by economic duress. Of course, the WTO Appellate Body is well-versed in the concept of necessity as it relates to trade restrictiveness[6] and the scholarship has focused accordingly on analysing whether a measure is necessary to obtain particular objectives and meet the tests established and applied by the Appellate Body.[7] In contrast, the September 2015 WTO Panel Report in *Argentina – Financial Services* and, more recently, the additional findings by the Appellate Body in April 2016 have provided substance to what has been largely an academic debate relating to financial services.[8] More specifically, the Panel and Appellate Body reports in *Argentina – Financial Services* provided a

4. *See, e.g.*, Andrew D. Mitchell, Jennifer K. Hawkins & Neha Mishra, *Dear Prudence: Allowances under International Trade and Investment Law for Prudential Regulation in the Financial Services Sector*, 9 J. INT'L ECON. L. 787, 787–820 (2016).

5. *See Argentina – Financial Services Appellate Body Report*, *supra* note 2; *Argentina – Financial Services Panel Report*, *supra* note 2.

6. *See* Appellate Body Report, *Brazil – Measures Affecting Imports of Retreaded Tyres*, WTO Doc. WT/DS332/AB/R (adopted Dec. 3, 2007); Appellate Body Report, *United States – Measures Affecting the Cross-Border Supply of Gambling and Betting Services*, WTO Doc. WT/DS285/AB/R (adopted Apr. 7, 2005) [hereinafter *United States – Gambling Appellate Body Report*]; Appellate Body Report, *European Communities – Measures Affecting Asbestos and Asbestos-Containing Products*, WTO Doc. WT/DS135/AB/R (adopted Mar. 12 2001) [hereinafter *European Communities – Asbestos*]; Appellate Body Report, *Korea – Measures Affecting Imports of Fresh, Chilled and Frozen Beef*, WTO Doc. WT/DS161/AB/R – WT/DS169/AB/R (adopted Dec. 11, 2000) [hereinafter *Korea – Frozen Beef*].

7. In relation to SPS issues, *see* Andrew D. Mitchell and Caroline Henckels, *Variations on a Theme: Comparing the Concept of "Necessity" in International Investment Law and WTO Law*, 14(1) CHI. J. INT'L L. 93, 93-164 (2013).

8. *See Argentina – Financial Services Appellate Body Report*, *supra* note 2; *Argentina – Financial Services Panel Report*, *supra* note 2.

landmark contribution to the WTO's approach to the handling of financial services issues generally and more particularly prudential regulatory initiatives taken for reasons of emergency or in a "state of necessity".[9]

Part III focuses on the investment perspective. The trade and investment regimes are of course different and should not be read as interchangeable, but it is nonetheless interesting to note that a certain degree of convergence can be found between the trade and investment jurisprudence in regard to prudential measures. At the same time, it must also be noted that important gaps appear in the methodology and reasoning between the two regimes. In more practical terms, while investment cases have tended to preserve the right of host governments to regulate so as to preserve domestic financial and economic stability over foreign corporate interests, the tribunals and Annulment Committees have not been able to formulate a coherent and robust legal reasoning as to what measures taken for prudential reasons ought to be considered as valid.[10]

Part IV concludes with a set of general remarks drawing upon recent jurisprudence and offers confidence to governments wishing to preserve a high degree of freedom in times of financial instability.

II. Background on Prudential Measures

Provisions allowing for the taking of exceptional measures—particularly for prudential reasons—have long been part of international investment and trade agreements. The language used and construction of such clauses rarely differ much between various agreements, however, the structure and wording of such clauses have raised questions as to the scope of their applicability (with some viewing the language as self-cancelling and without any practical effect). To date, the point has mainly been debated in academic literature, but has only rarely been a point of issue in any international dispute settlement forum. This section reviews the textual language of the General Agreement on Trade in Services (GATS) and other agreements before considering the differing interpretive positions on the practical effect of such clauses.

A. The Textual Language of Prudential Provisions in GATS

The GATS provides several general and specific carve-outs and exceptions to liberalization commitments. This begins with the language of the Preamble which protects and promotes "the right of Members to regulate, and to introduce new regulations, on the supply of services within their

9. *Id.*

10. *See infra* Section III. For a similar conclusion, *see* Mitchell and Henckels, *supra* note 7, at 93-164.

territories in order to meet national policy objectives."[11] The Preamble is supplemented by hard law provisions including, most notably, Article VI, which stipulates that domestic measures of general application should be conducted "in a reasonable, objective and impartial manner."[12] In addition, Article XII on Restrictions to Safeguard the Balance of Payments also grants Members a right act in a manner contrary to its liberalization commitments in cases of "serious balance-of-payments and external financial difficulties or threat," provided that "such restrictions shall not be adopted or maintained for the purpose of protecting a particular service sector" and as long as the involved government submits to a balance of payment assessment procedure.[13] These obligations, furthermore, are accompanied by the well-known and important General Exceptions clause of Article XIV, which allows for the adoption of certain measures such as those "necessary to protect human, animal or plant life or health" or "to protect morals or to maintain public order."[14]

More relevant to financial stability and to financial services liberalization more generally is the GATS Annex on Financial Services, which contains a Domestic Regulation provision allowing for the taking of regulatory measures "for prudential reasons" related to the protection of investors or to the preservation of economic and financial stability.[15] More specifically, the Annex states that:

> [n]otwithstanding any other provisions of the Agreement, a Member shall not be prevented from taking measures for prudential reasons, including for the protection of investors, depositors, policy holders or persons to whom a fiduciary duty is owed by a financial service supplier, or to ensure the integrity and stability of the financial system.[16]

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11. General Agreement on Trade in Services, Apr. 15, 1994, Marrakesh Agreement Establishing the World Trade Organization, Annex 1B, 1869 U.N.T.S. 183, 33 I.L.M. 1167 (1994) [hereinafter GATS].

12. *Id.* art. VI, § 1.

13. *Id.* art. XII, §§ 1, 3, 5.

14. *Id.* art. XIV. The Panel in *United States – Gambling* associated public morals with "the preservation of the fundamental interests of a society, as reflected in public policy and law" in a case concerning issues relating to money laundering. *United States – Gambling Appellate Body Report* at ¶ 296 (discussing Panel Report, *United States - Measures Affecting the Cross-border Supply of Gambling and Betting Services*, WT/DS285/R, ¶ 6.467 (adopted Nov. 10, 2004)). "Hence, in our view, the dictionary definition of the word 'order', read together with [Article XIV] footnote 5, suggests that 'public order' refers to the preservation of the fundamental interests of a society, as reflected in public policy and law. These fundamental interests can relate, *inter alia*, to standards of law, security and morality." *Id.* Unsurprisingly, the point was relied on by the Panel in Argentina – Financial Services. *Argentina – Financial Services Panel Report*, at para 7.870.

15. GATS, *supra* note 11, at Annex on Financial Services, para. 2.

16. *Id.*

B. Other Investment and Trade Agreements

Similar prudential provisions are included in a broad range of regional and bilateral trade and investment agreements. Referred to by a host of names, including Exceptions, Domestic Regulation, or Carve-Out provisions, such prudential provisions are commonly included in every free trade agreement (FTA) entered into by the United States (except the Jordan agreement),[17] including the widely publicized (and, it appears, failed) US-led mega-regional Trans-Pacific Partnership (TPP).[18] Likewise, recent EU treaties such as the EU – Singapore FTA and Canada – EU FTA (CETA) include such provisions.[19]

Looking at the fifty-nine agreements listed by the UNCTAD Investment Policy Hub as being negotiated in 2014 and 2015 a similar trend emerges.[20] Of the twenty-seven most recently negotiated agreements listed in the UNCTAD Investment Policy Hub (available in English) the vast majority include exceptions through a variety of wordings and methods.[21] Of the twenty-seven agreements, seventeen contain a Prudential Reasons clause,[22] a Domestic Regulations clause[23] and/or a General Exceptions provision[24] expressly allowing for the taking of regulatory measures "for prudential reasons." An additional two agreements alternatively incorporate the previously mentioned GATS Annex on Financial Services into their text so as to provide parties with prudential exceptions,[25] while six agreements

17. *See* Office of the United States Trade Representative, *United States Free Trade Agreements*, https://ustr.gov/trade-agreements/free-trade-agreements (last visited Dec. 5 2015).

18. Trans-Pacific Partnership Agreement § 11.11.1, Feb. 4, 2016, Office of the United States Trade Representative, https://ustr.gov/trade-agreements/free-trade-agreements/trans-pacific-partnership/tpp-full-text.

19. *See* Comprehensive Economic and Trade Agreement Between Canada, of the One Part, and the European Union, Can.-EU, art. 13.16, Oct. 30, 2016, http://trade.ec.europa.eu/doclib/docs/2016/february/tradoc_154329.pdf [hereinafter CETA]; Free Trade Agreement Between the European Union and the Republic of Singapore, EU-Sing., art. 8.50, May, 2015, http://trade.ec.europa.eu/doclib/press/index.cfm?id=961.

20. *See* UNCTAD, *Investment Policy Hub*, http://investmentpolicyhub.unctad.org/IIA/MostRecentTreaties#iiaInnerMenu (last visited June 11, 2018).

21. *See id.*

22. *See, e.g.*, Agreement Between Japan and the Sultanate of Oman for the Reciprocal Promotion and Protection of Investment, Japan-Oman art. 18, June 19, 2015, http://investmentpolicyhub.unctad.org/Download/TreatyFile/3481.

23. *See* Free Trade Agreement Between the Government of Australia and the Government of the People's Republic of China, Austl.-China, art. 3, Aus. Gov. Dept. of Foreign Affairs and Trade, http://dfat.gov.au/trade/agreements/in-force/chafta/official-documents/Documents/chafta-agreement-text.pdf.

24. *See, e.g.*, Agreement between the Government of Canada and the Government of Burkina Faso for the Promotion and Protection of Investments, Can. Burk. Faso, art. 18, May 20, 2015, UNCTAD, http://investmentpolicyhub.unctad.org/Download/TreatyFile/3460.

25. *See* Agreement on Investment under the Framework Agreement on Comprehensive Economic Cooperation between Association of Southeast Asian Nations and the Republic of India, ASEAN-India, art. 21, Dec. 11, 2014, UNCTAD, http://investmentpolicyhub.unctad.org/Download/TreatyFile/3337; Agreement between Canada and the Republic of

provide no specific prudential exception but rather rely on general security interest protection, serious balance-of-payment, external financial difficulties,[26]or investment transfer provisions[27] to justify what other agreements refer to as measures taken for prudential reasons, provided that these measures remain temporary. Of the twenty-seven, only two agreements fail to explicitly and clearly provide visible prudential exceptions. One of these two, the 1314 page-long FTA between the Eurasian Economic Union and Viet Nam allows for General and Security Exceptions and incorporates Article XIV of the GATS but makes no reference to the preservation of financial stability.[28] The other, the Malaysia – Turkey FTA, exclusively incorporates GATS XX exceptions relating to public order and security but ignores the possibility of financial stability-related action.[29]

C. Doctrinal Debate

Despite prudential or carve-out provisions being included in multiple agreements, a doctrinal debate on whether such provisions are useful and applicable in practice has emerged in the literature. This debate essentially relates to the wording of the clauses. Paragraph 2 of the GATS Annex on Financial Services can be used, for illustration purposes, as a standard carve-out provision:

> Notwithstanding any other provisions of the Agreement, a Member shall not be prevented from taking measures for prudential reasons,

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Cameroon for the Promotion and Protection of Investments, Cameroon-Can., art. 17, Mar. 03, 2016, UNCTAD, http://investmentpolicyhub.unctad.org/Download/TreatyFile/3163.

26. *See, e.g.*, Agreement between Japan and the Oriental Republic of Uruguay for the Liberalization, Promotion and Protection of Investment, Japan-Uru., arts. 22–23, Jan. 01, 2015, UNCTAD, http://investmentpolicyhub.unctad.org/Download/TreatyFile/3284.

27. *See* Investment Cooperation and Facilitation Agreement between the Federative Republic of Brazil and the Republic of Malawi, Braz.-Malawi, art. 12, UNCTAD, http://investmentpolicyhub.unctad.org/Download/TreatyFile/4715; Agreement between the Government of the State of Israel and the Government of the Republic of the Union of Myanmar for the Reciprocal Promotion and Protection of Investments, Isr.-Myan., arts. 6–7, Oct. 05, 2014, UNCTAD, http://investmentpolicyhub.unctad.org/Download/TreatyFile/3161; Agreement between the Government of the Republic of Colombia and the Government of the Republic of Turkey concerning the Reciprocal Promotion and Protection of Investments, Colom.-Turk., art. 9, July 28, 2014, UNCTAD, http://investmentpolicyhub.unctad.org/Download/TreatyFile/3249; The Investment Promotion Act, Egypt-Mauritius, art. 8.4, June 25, 2014, UNCTAD, http://investmentpolicyhub.unctad.org/Download/TreatyFile/3285; Korea – Australia Free Trade Agreement, Austl.-S. Kor., Annex 11–C, Apr. 08, 2014, Aus. Gov. Dept. of Foreign Affairs and Trade, http://dfat.gov.au/trade/agreements/in-force/kafta/official-documents/Pages/full-text-of-kafta.aspx.

28. Free Trade Agreement between the Eurasian Economic Union and Its Member States, of the one part, and the Socialist Republic of Viet Nam, of the other part, E.E.U.-Viet., art. 1.9, May 29, 2015, UNCTAD, http://investmentpolicyhub.unctad.org/Download/TreatyFile/3455.

29. Free Trade Agreement between the Government of Malaysia and the Government of the Republic of Turkey, Malay-Turk., ch. 13, Apr. 17, 2014, Malaysia Ministry of Int'l Trade and Indus., http://fta.miti.gov.my/miti-fta/resources/Malaysia%20-%20Turkey/MTFTA_Main_Agreement.pdf.

> including for the protection of investors, depositors, policy holders or persons to whom a fiduciary duty is owed by a financial service supplier, or to ensure the integrity and stability of the financial system. Where such [prudential] measures do not conform with the provisions of the Agreement, they shall not be used as a means of avoiding the Member's commitments or obligations under the Agreement.[30]

As previously mentioned, the first part of the provision suggests that WTO Members retain a wide degree of autonomy to control financial services in case of financial instability or threat thereof. In what some have put down to poor drafting, however, the last sentence of Article 2(a) implies that such prudential measures cannot contradict existing GATS obligations, which leads some to question on whether the prudential provision could ever permit governmental action in practice.[31] More specifically, those commentators contend that the last sentence has a self-cancelling effect that prevents WTO Members from taking measures inconsistent with their WTO obligations.[32] Thus, to those commentators, the prudential carve-out does not actually allow a WTO Member to address systemic risks, because attempting to do so would breach their WTO commitments.[33]

Reading the provisions with state regulatory needs in mind and with a view to avoiding contradictions within the same treaty, as required by Article 31 of the Vienna Convention on the Law of Treaties,[34] this article contends that where threats are identified, prudential measures may legitimately contradict WTO obligations, provided that they are not used as pretext to initiate protectionist measures and escape general obligations under the Agreement. In other words, the last sentence of Article 2(a) is not self-cancelling, but rather constitutes a good faith clause or safeguard against abuse in a similar fashion to the chapeau of Article XIV of the GATS and Article XX of the General Agreement on Tariffs and Trade (GATT).[35] Support for this interpretation has been expressed in various doctrinal

30. GATS, *supra* note 11, at Annex on Financial Services, § 2(a).

31. *See, e.g.*, Lori Wallach & Todd Tucker, *Answering Critical Questions about Conflicts Between Financial Regulation and WTO Rules Hitherto Unaddressed by the WTO Secretariat and other Official Sources*, PUBLIC CITIZEN (June 22, 2010), 3, https://www.citizen.org/sites/default/files/memo_-_unanswered_questions_memo_for_geneva.pdf. (stating that "[a]s the second sentence makes clear, prudential measures *are only allowed* under GATS *if they don't violate any of the GATS rules*, which are very expansive, or operate to reduce a member country's commitments or obligations."); *To Promote Economic Stability, Nations Must Free Themselves from WTO Financial Deregulation Dictates*, PUBLIC CITIZEN (Oct. 2009), 8, https://www.citizen.org/sites/default/files/introductiontowtoderegulation.pdf (stating that "the provision may only be used to defend regulatory policies if such policies do not undermine the commitments and obligations established through the other WTO rules. This effectively eviscerates the use of the provision . . . self-cancelling second sentence").

32. *See, e.g., id.*

33. *See, e.g., id.*

34. Vienna Convention on the Law of Treaties, art. 31, May 23, 1969, 1155 U.N.T.S. 18232.

35. GATS, *supra* note 11, at art. XIV; General Agreement on Tariffs and Trade, art. XX, Oct. 30, 1947, 61 Stat. A-11, 55 U.N.T.S. 194 [hereinafter GATT].

discussions and carries the weight of the commentaries. For instance, a 2010 note by the International Monetary Fund concluded that "[t]he Annex on Financial Services includes a 'prudential carve out' clause that recognizes the right of WTO members to introduce and maintain prudential measures . . . regardless of any other provisions of the GATS" and suggests that "[s]ince the Annex on Financial Services does not provide any definition or indicative list of prudential measures that would be covered by this provision, governments have considerable leeway in introducing prudential measures that fit their needs."[36] Other commentators have noted that the prudential provision allows financial regulatory authorities to "take measures to ensure the integrity and stability of the financial system or to protect consumers of financial services even if these measures are inconsistent with other provisions of GATS."[37] In this regard, Key notes that "[t]he only issues are whether the measure is, in fact, prudential, and whether it is being used to avoid a country's obligations or commitments under the GATS."[38] Similarly, Cottier and Krajewski find that WTO Members may adopt prudential measures without interference from the WTO because the system "preserves national regulatory autonomy and enables each country to adopt those rules which [it] deems appropriate."[39] Finally, in an extensive analysis of prudential provisions, Barbee and Lester concluded that although the wording of the prudential regulatory clauses have raised concerns over effectiveness, the concerns are only "speculative and have been overstated."[40] The prudential carve-out provides considerable policy space for regulators to safeguard the integrity and stability of the financial system, provided "the non-protectionist purposes offered to justify the measure [is] authentic and real."[41]

Perhaps even more importantly, several governments have also come to similar conclusions on the role and efficiency of prudential measures. This includes direct statements on the high degree of autonomy granted to the WTO Members, notwithstanding the inclusion of the last sentence in Article 2(a) of the Annex. For instance, former US Treasury Secretary Timothy Geithner once stated that the controversial part of prudential provision was to be read as a guard against abuse and concluded that US investment treaties and FTAs provided "very substantial and adequate flexibility for government policy makers to mitigate such risks, including through the so-called prudential exception and through the monetary and exchange rate policy exception."[42] The effectiveness of the prudential carve-

36. *Reference Note on Trade in Financial Services*, *supra* note 1, at para. 14.

37. *See* Key, *supra* note 1, at 47.

38. *Id.* at 50.

39. Cottier & Krajewski, *supra* note 1, at 827.

40. Barbee & Simon, *supra* note 1, at 954.

41. *Id.* at 954, 961.

42. *Id.* at 962 (quoting Letter from Timothy Geithner, Treasury Secretary, to Rep. Barney Frank, Inside U.S. Trade (July 19, 2012), http://insidetrade.com/iwpfile.html?file??dec2012%2Fwto2012_2846a. pdf).

out provisions have also been confirmed by jurisdictions as diverse as Macao, Costa Rica, and the EU.[43]

The recently negotiated CETA goes even further and contains unique and noteworthy provisions demonstrating solid political intent to strengthen the prudential carve-outs. For example, Annex 13–C of the agreement unquestionably demonstrates the parties' commitment to strengthening financial stability through a "dialogue on the regulation of the financial services sector," while adding that discussions "shall be based on the principles and prudential standards agreed at multilateral level."[44] Moreover, Annex 13–B makes clear that prudential measures are acceptable where the parties act in good faith and provides a list of non-exhaustive "High-Level Principles" including a right of each party to "determine its own appropriate level of prudential regulation . . . and enforce measures that provide a higher level of prudential protection than those set out in common international prudential commitments[.]"[45] The article also defines a valid prudential measure as having a non-manifestly disproportionate prudential objective in the pursuance of the resolution of matters involving the recovery of non-viable financial institutions and "the preservation or the restoration of financial stability in response to a system-wide financial crisis."[46]

Canada and the US have likewise made their intentions clear in a declaration on the Energy Charter Treaty:

> Legitimate policy objectives may justify differential treatment of foreign Investors or their Investments in order to reflect a dissimilarity of relevant circumstances between those Investors and Investments and their domestic counterparts. For example, the objective of ensuring the integrity of a country's financial system would justify reasonable prudential measures with respect to foreign Investors or Investments, where such measures would be unnecessary to ensure the attainment of the same objectives insofar as domestic Investors or Investments are concerned. Those foreign Investors or their Investments would thus not be "in similar circumstances" to domestic Investors or their Investments.[47]

In light of the above, and in line with the prevailing view of commentators and governments, we therefore disagree with the vocal commentators who question the applicability and feasibility of the prudential provision. To the

43. *See* KH Lei, *Financial Services in the Current WTO Framework*, Monetary Authority of Macao (2006), available at http://docplayer.net/5989501-Financial-services-in-the-current-wto-framework.html (accessed June 2018).

44. CETA, *supra* note 19, at Annex 13–C.

45. CETA, *supra* note 19, at Annex 13–B § 8(a). In addition, the article provides that "[r]elevant considerations in determining whether a measure meets the requirements of Article 13.16.1 include the extent to which a measure may be required by the urgency of the situation and the information available to the party at the time when the measure was adopted." *Id.* § 8(b).

46. *Id.* § 8(d) – (e).

47. Consolidated Energy Charter Treaty, art. 10, Dec. 17, 1994, 2080 U.N.T.S. 95.

contrary, the provisions contained in the GATS Agreement and relevant Annex and their FTA counterparts provide ample scope for WTO Members and FTA signatories to utilise the prudential carve-out as a safeguard in times of financial instability and crisis.

III. Recent WTO Interpretation of Prudential Measures

The limitation of the above conclusion is that governments and commentators base their conclusions on the effectiveness of the prudential carve-out provisions simply on a textual analysis of treaty language, if only because most did not see any relevant case law from which to draw upon.[48]

The recent WTO panel and Appellate Body reports in *Argentina – Financial Services*, however, allow us to supplement doctrinal analysis with relevant trade jurisprudence. Ignored in this debate, also, is the contribution of jurisprudence of investment tribunals that have considered the issue of regulations taken during a state of necessity so as to protect a country's essential interest.

As previously mentioned, Panama's WTO dispute stemmed from the Argentine economic crisis. The claim challenged a set of prudential regulations—in this case in relation to transparency towards remuneration and interest, control over doubtful increases in wealth, financial intermediaries pre-market access, operational and foreign exchange trading requirement, etc.—to which Argentina justified by a state of necessity claim.[49] In this dispute, however, the legal text was not a Bilateral Investment Treaty (BIT) but the GATS and the Annex on Financial Services.

In *Argentina – Financial Services*, the necessity debate considered focused on both regulatory exceptions and prudential measures for eight financial, taxation, foreign exchange, and business registration measures.[50] According to Argentina, the regulations constituted "anti-abuse measures which [were] essential tools for enforcing national tax laws, guaranteeing taxation and tax collection, preventing fraudulent practices, tax evasion and tax avoidance, as well as the erosion of national tax bases."[51] At stake was also a financial information exchange agreement between Argentina and various tax-cooperative countries which Argentina preventively extended to Panama prior to the effective signing of an agreement.[52] To Panama, however, Argentina's measures and corresponding restrictions infringed upon its market access commitment in the financial services sector.[53] The remainder

48. *See, e.g.*, Barbee & Lester, *supra* note 1, at 954; U.N. Conference on Trade and Development, *Policy Space to Prevent and Mitigate Financial Crises in Trade and Investment Agreements*, 8, UNCTAD/GDS/MDP/G24/2010/1 (May 2010).

49. *See Argentina – Financial Services Panel Report*, *supra* note 2.

50. *Id.* at ¶ 2.9.

51. *Argentina – Financial Services Panel Report*, *supra* note 2, ¶ 2.

52. *See id.*

53. *Id.* ¶¶ 3.1 – 3.3.

of this sub-section reviews the claims made and decision taken in relation to both the regulatory exceptions and prudential measures.

A. Regulatory Exceptions under Article XIV of the GATS

The Panel in *Argentina – Financial Services* first considered whether the allegedly prudential measures taken by Argentina qualified as relevant exceptions under Article XIV of the GATS.[54] Article XIV is the general exception clause (akin to Article XX of the GATT) which in this case would allow measures necessary to secure compliance with laws aiming at preventing fraudulent practices, subject of course to satisfaction of the chapeau.[55] The relevant portion of Article XIV reads as follows:

> 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:
>
> (c) necessary to secure compliance with laws or regulations which are not inconsistent with the provisions of this Agreement including those relating to:
>
> (i) the prevention of deceptive and fraudulent practices or to deal with the effects of a default on services contracts[.]

An important question remains, therefore, regarding what constitutes a necessary measure compatible with the exception clause.

B. Identifying "Necessary Measures"

The WTO has a long line of jurisprudence on the general exceptions clause, and while the majority of the cases consider Article XX of GATT,[56] this jurisprudence is relevant to Article XIV of GATS.[57] When analysing

54. *Id.* ¶ 7.61.

55. GATS, *supra* note 11, at art. XIV.

56. Prominent disputes in which the Appellate Body has considered Article XX include Appellate Body Report, *European Communities – Measures Prohibiting the Importation and Marketing of Seal Products*, WTO Doc. WT/DS400/AB/R – WT/DS401/AB/R (May 22, 2014) [hereinafter *EC – Seal Products*]; Appellate Body Report, *China – Measures Related to the Exportation of Various Raw Materials*, WTO Doc. WT/DS394/AB/R – WT/DS395/AB/R –WT/DS398/AB/R (adopted Jan. 30, 2012); Appellate Body Report, *Thailand – Customs and Fiscal Measures on Cigarettes from the Philippines*, WTO Doc. WT/DS371/AB/R (adopted June 17, 2011); Appellate Body Report, *Brazil – Measures Affecting Imports of Retreaded Tyres*, WTO Doc. WT/DS332/AB/R (adopted Dec. 3, 2007); *Korea – Frozen Beef*; Appellate Body Report, *United States – Import Prohibition of Certain Shrimp and Shrimp Products*, WTO Doc. WT/DS58/AB/R (adopted Oct. 12, 1998); Appellate Body Report, *United States – Standards for Reformulated and Conventional Gasoline*, WTO Doc. WT/DS2/AB/R (adopted Apr. 29, 1996).

57. *See, e.g.*, *United States – Gambling Appellate Body Report*, *supra* note 6, ¶ 291 (stating that "Article XIV of the GATS sets out the general exceptions from obligations under that

whether a measure conforms to the general exception clause the first task of a panel is to determine whether the challenged measure falls within the scope of the clause as set out in the enumerated list (i.e. is a measure "necessary to secure compliance with laws or regulations which are not inconsistent with the provisions of this Agreement").[58] When this has been established, the panel then ascertains whether the measure has been applied appropriately—that is, it does not fall afoul of the requirements of the chapeau.[59]

In regards to the first part of the test, the Panel referred to Appellate Body decisions interpreting the equivalent GATT Article XX general exceptions—in particular *Brazil – Retreaded Tyres* and *EC – Seal Products*—and followed the precedent that in order for a measure to be necessary the respondent must establish that the measure contributed to the goal pursued and that the design, structure and operation of the measures offered an "ends and means relationship with the objectives pursued."[60] After a

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Agreement in the same manner as does Article XX of the GATT 1994. Both of these provisions affirm the right of Members to pursue objectives identified in the paragraphs of these provisions even if, in doing so, Members act inconsistently with obligations set out in other provisions of the respective agreements, provided provisions of the respective agreements, provided that all of the conditions set out therein are satisfied. Similar language is used in both provisions, notably the term 'necessary' and the requirements set out in their respective chapeaux. Accordingly, like the Panel, we find previous decisions under Article XX of the GATT 1994 relevant for our analysis under Article XIV of the GATS."). For a brief summary of the general interpretative principles of Article XX, *see* SIMON LESTER, ET AL., WORLD TRADE LAW: TEXT, MATERIALS AND COMMENTARY 363–74 (Oxford, 2nd ed. 2012).

58. GATS, *supra* note 11, at art. XIV § (c)

59. The chapeau of Article XX reads "[s]ubject 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[.]" GATT, *supra* note 35, at art. XX. "Article XIV of the GATS, like Article XX of the GATT 1994, contemplates a 'two-tier analysis' of a measure that a Member seeks to justify under that provision. A panel should first determine whether the challenged measure falls within the scope of one of the paragraphs of Article XIV. This requires that the challenged measure address the particular interest specified in that paragraph and that there be a sufficient nexus between the measure and the interest protected. The required nexus—or 'degree of connection'—between the measure and the interest is specified in the language of the paragraphs themselves, through the use of terms such as 'relating to' and 'necessary to'. Where the challenged measure has been found to fall within one of the paragraphs of Article XIV, a panel should then consider whether that measure satisfies the requirements of the chapeau of Article XIV." *United States – Gambling Appellate Body Report*, *supra* note 6, ¶ 292.

60. *See Argentina – Financial Services Panel Report supra* note 2, ¶¶ 7.684 – 7.688. "We first examine the design, structure and operation of the measures in question. We shall focus in particular on determining whether there is an ends and means relationship between the objective pursued and the measures in question." *Id.* ¶ 7.688. The panel also made reference to *EC – Seal Products*. "A measure's contribution is thus only one component of the necessity calculus under Article XX. This means that whether a measure is "necessary" cannot be determined by the level of contribution alone, but will depend on the manner in which the other factors of the necessity analysis, including a consideration of potential alternative measures, inform the analysis . . . . Indeed, the very utility of examining the interaction between the various factors of the necessity analysis, and conducting a comparison with potential

thorough review, the Panel concluded that, given OECD and G20 efforts against harmful tax practices, most of the measures at issue individually and conjunctively contributed to achieving the anti-abuse goal.[61] The protection of the tax system against the risks posed by harmful tax practices and money laundering constituted a primordial goal "of the utmost importance,"[62] had a "limited restrictive effect on international trade in services" and were overall "necessary to secure compliance with laws or regulations which [were] not inconsistent" with GATS Article XIV.[63]

As to the second part of the test, the panel, somewhat surprisingly, found that the measures provided unequal treatment amongst countries because Panama—which had not yet exchanged tax information and initiated the case as the complainant—had been given cooperative country status.[64] By so doing, the panel held that Argentina distorted competition and provided "unequal treatment" to services and service providers from countries that did effectively provide such information to Argentina.[65] The panel, in other words, found that Argentina's inclusion of Panama on the list of cooperating countries, in anticipation of and in order to encourage the rapid conclusion of a tax treaty between the two countries (but without any exchange of information taking place), was not detrimental to Panama but was discriminatory to the other countries effectively cooperating with Argentina.[66] The privilege granted to Panama, in turn, was held to generate counterproductive distortions, i.e. the creation of an unfair burden on the services and service providers from effectively-cooperating countries,[67] and thus considered as "arbitrary and unjustifiable discrimination within the meaning of the chapeau of Article XIV of the GATS."[68]

The Appellate Body agreed that the measures fell within the scope of Article XIV, and thus were

> designed to secure compliance with the laws or regulations identified by Argentina[,] . . . discourage harmful tax practices and enable the authorities to ensure that Argentine residents are taxed on all their earnings . . . and that earnings from activities performed in Argentina

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alternative measures, is that it provides a means of testing these factors as part of a holistic weighing and balancing exercise, whether quantitative or qualitative in nature." *Id.* ¶ 7.686 (quoting *EC – Seal Products*, ¶ 5.215).

61. *See Argentina – Financial Services Panel Report supra* note 2, ¶ 7.713.

62. *Id.* ¶ 7.738. "The Panel has found that the protection of its tax collection system and the fight against harmful tax practices and money laundering are interests or values of the utmost importance for Argentina." *Id.*

63. *Id.* ¶ 7.739. Panama, in addition, failed to identify alternative less trade-restrictive measures reasonably available to Argentina. *Id.*

64. *Id.* ¶¶ 7.278 – 7.289.

65. *Id.* ¶¶ 7.292 – 7.293.

66. *See id.*

67. *Id.* ¶¶ 7.752 – 7.753.

68. *Id.* ¶ 7.762.

> by domestic or foreign service suppliers are subject to taxation in Argentina . . . ."[69]

This was to be done in a GATS-consistent manner so that they "contribute[d] to achieving the objectives pursued."[70] The Appellate Body began its analysis by reviewing the Panel's approach in terms of trade restriction impacts, taking note of the Panel's conclusion that the measures did not prevent the supply of services by service suppliers of non-cooperative countries[71] and reiterating the Panel's reasoning that Argentina's measures overall had to be designed broadly so as to cover all harmful transactions.[72] The Appellate Body then reiterated that an Article XIV(c) analysis of necessity requires a panel "to assess, in a qualitative or quantitative manner, the extent of the measure's contribution to the end pursued" and found that the Panel had "in fact included an appropriate analysis of the contribution made by [the measures] to securing compliance with specific rules, obligations, or requirements."[73] But whilst the Panel had justified part of its analysis by making reference to OECD and G-20 initiatives,[74] the Appellate Body questioned recourse to "concepts that are not defined in the WTO-context"—including the creation of "'a level playing field', and 'unintended competitive advantages'"—to legitimise GATS-inconsistent measures.[75]

C. "Prudential Measures" under the Annex on Financial Services

The Panel and Appellate Body reports in *Argentina – Financial Services* also considered whether certain Argentine measures—including requirements relating to reinsurance services and requirements for access to the Argentine capital market—could, furthermore, qualify under paragraph 2 (Domestic Regulations) of the GATS Annex on Financial Services as measures taken for prudential reasons, i.e. to protect investors, financial service suppliers or, more generally, the integrity and stability of the financial system.[76] The Panel began its analysis by stating:

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69. *Argentina – Financial Services Appellate Body Report supra* note 2, ¶ 6.185.

70. *Id.* ¶ 6.194 (quoting *Argentina – Financial Services Panel Report*, ¶ 7.717). The Appellate Body did have some points of contention with the Panel's analysis. *See id.* ¶ 6.221.

71. *Id.* ¶¶ 6.195 – 6.197.

72. *Id.* ¶ 6.214 (referring to *Argentina – Financial Services Panel Report*, ¶ 7.726).

73. *Id.* ¶¶ 6.233 – 6.234.

74. *Argentina – Financial Services Panel Report, supra* note 2, ¶¶ 7.511 – 7.521.

75. *Argentina – Financial Services Appellate Body Report, supra* note 2, ¶¶ 6.139 – 6.141. "[A] measure either modifies the conditions of competition in the marketplace, thus according less favourable treatment, or it does not. However, . . . the Panel effectively employed a standard whereby certain regulatory aspects, as alleged by a Member in a particular dispute, could "convert" a measure that accords less favourable treatment, and is therefore inconsistent with Article XVII of the GATS, into a measure that is GATS-consistent." *Id.*

76. *Argentina – Financial Services Panel Report, supra* note 2, ¶ 7.821.

> it can be inferred from the wording of paragraph 2(a) of the Annex on Financial Services that Argentina must demonstrate that two requirements have been met in order to avail itself of the exception, namely: (i) that the measure in question was taken for prudential reasons and (ii) that the measure is not being used as a means of avoiding its commitments or obligations under the GATS.[77]

It then proceeded to analyse the Argentina measures under both prongs of the test.[78]

In analysing whether the measures in question were taken for prudential reasons, the Panel drew a firm distinction between "prudential measures" and "measures taken for prudential reasons" and concluded that in order to fall within the provision "it is the reason which must be "prudential" and not the measure *per se*."[79] In other words, the prudential factor does not relate to a certain type of measure but to the circumstances justifying the measure.[80] In explaining the concept of prudential reasons, the Panel then considered the circumstances characteristic of prudential decisions.[81]

1. *Prevention Role*

Using a dictionary definition, the Panel determined that prudential measures are "preventive or precautionary" in nature[82] and could thus include an "extremely broad" number of measures in quantitative terms.[83] In this regard, the Panel found the prudential reasons listed in paragraph 2(a) to be indicative rather than exhaustive (in contrast to that of GATS Article XIV).[84] Following the jurisprudence of the GATT/GATS General Exception clause the Panel concluded that prudential measures under Paragraph 2 of the GATS Annex on Financial Services should be read in a broad manner and, in so doing, also expressed concerns as to the "serious systemic implications of the narrow interpretation" of such provisions.[85] Hence, the Panel found that Members "are entitled to determine the level of protection they consider appropriate"[86] and that the "nature and scope of financial regulation at different times reflect the knowledge, experience and scales of values of governments at the moment in question."[87] In this regard, the Panel stated that Members

77. *Id.*
78. *Id.* ¶ 7.822.
79. *Id.* ¶ 7.861.
80. *Id.* "[T]he exception makes it possible to exempt or exonerate any measure affecting the supply of financial services that has been taken '*for prudential reasons*.'" *Id.*
81. *See id.* ¶¶ 7.864 – 7.945.
82. *Argentina-Financial Services Panel Report*, *supra* note 2, ¶ 7.868
83. *Id.* ¶ 7.869.
84. *Id.*
85. *Id.* ¶ 7.848.
86. *Id.* ¶ 7.870 (citing *United States – Gambling Panel Report*, at para. 6.461; *European Communities – Asbestos*, at para. 168; *Korea – Frozen Beef*, at para. 176).
87. *Id.* ¶ 7.871.

> should have sufficient freedom to define the prudential reasons that underpin their measures, in accordance with their own scales of values . . . such as "the protection of investors, depositors, policy holders or persons to whom a fiduciary duty is owed by a financial service supplier" or "the integrity and stability of the financial system[.]"[88]

2. *Prudential Cause*

In a related manner, the Panel made an important distinction between a prudential measure and a measure taken for prudential reasons.[89] Analysing the text of paragraph 2(a) of the Annex on Financial Services on the basis of the ordinary meaning of its terms as provided under the Vienna Convention on the Law of Treaties, the Panel again resorted to the dictionary and found that a "measure taken 'for' prudential reasons would . . . be a measure with a prudential cause."[90] Accordingly, it came to the conclusion that a rational relationship must exist between "the measure and its prudential objective" and that "the measure must be fit for the purpose of preventing the event, or the effects resulting therefrom, which the measure is intended to avoid" is in line with the notion that in "the measure's design, structure and architecture there must be a rational relationship of cause and effect between the measure and the prudential reason for it."[91] The Panel concluded:

> the word "for" in the phrase "measures for prudential reasons" denotes a rational relationship of cause and effect between the measure and the prudential reason. Thus, the Member taking the measure in question must demonstrate that in its design, structure or architecture there is a rational relationship of cause and effect between the measure it seeks to justify under paragraph 2(a) and the prudential reason provided. A central aspect of this rational relationship of cause and effect is the adequacy of the measure to the prudential reason, that is, whether the measure, through its design, structure and architecture, contributes to achieving the desired effect.[92]

The Panel, accordingly, went on to state that whether a measure has been taken "for prudential reasons" (i.e. whether there is a rational relationship of cause and effect between the measure and the reason), must be determined "on a case-by-case basis, taking into account the particular characteristics of

88. *Argentina-Financial Services Report*, *supra* note 2, ¶ 7.871. Such an interpretation, the Panel stated, is in accordance with the fourth recital of the preamble to the GATS, which recognizes "'the right of Members to regulate, and to introduce new regulations, on the supply of services within their territories in order to meet national policy objectives.'" *Id.* ¶ 7.872 (quoting GATS, *supra* note 11, at the Preamble).

89. *Id.* ¶¶ 7.880 – 7.892.

90. *Id.* ¶ 7.888. "A measure taken 'for' prudential reasons would therefore be a measure with a prudential cause." *Id.*

91. *Id.* ¶ 7.889.

92. *Id.* ¶ 7.891.

each situation and each dispute."[93] In the present dispute, the measures were found to be of a prudential type under Paragraph 2(a) but the Panel held that they had not been taken "for prudential reasons" and were thus inconsistent with the latter requirement.[94]

The Appellate Body did not contradict the Panel, instead reiterating that a Member shall not be prevented from taking measures for prudential reasons,[95] confirming the idea that measures deemed prudential in nature could fall under the scope of an Annex exception, but insisting that no exception could be used to escape existing commitments.[96] In essence, the Appellate Body substantiated the Panel's conclusions as to a right of the Members to regulate and made it clear that the GATS' exception provisions were designed with these considerations in mind.[97]

3. *Temporal Aspects*

Similar to the investment tribunals, the Panel also considered whether measures taken for prudential reasons must be temporary in nature and whether they may be taken as a result of an imminent threat. In so doing, it took a holistic approach and focused on two main points.

First, the Panel emphasised that anticipatory prudence was legitimate because – financial crises being varied, complex and susceptible to emerge suddenly – it is difficult for governments to anticipate their consequences. The Panel admitted that the risks stemming from financial instability evolve as crises unfold[98] and, *in fine*, concluded that paragraph 2(a) of the Annex on Financial Services authorized WTO Members to protect their financial systems from systemic risks in a forward looking, precautionary and anticipatory '*ex ante*' prudential manner.[99] The Panel's finding that the risk, injury or danger that a government is seeking to guard against "does not necessarily have to be imminent",[100] therefore, contrasts with the conclusions of investment tribunals on the matter.

Second, in holding that a measure taken for prudential reasons required a prudential cause, the Panel could easily reject Panama's assertion that "prudential measures should be transitional, provisional or short-term in

93. *Id.*
94. *Id.* ¶¶ 7.946 – 7.949.
95. *Argentina – Financial Services Appellate Body Report*, *supra* note 2, ¶¶ 6.254-6.255.
96. *Id.* ¶¶ 6.244-6.246.
97. *Id.* ¶ 6.260.
98. *Argentina – Financial Services Panel Report*, *supra* note 2, ¶ 7.878 (". . . it is important to understand that 'systemic' problems may be incubating or gestating over the course of time and erupt rapidly; hence the importance of being prepared for them in advance").
99. *Id.* ¶ 7.790. (Financial crises "are typically latent and extremely difficult to identify beforehand, making it practically impossible to deal with those risks by taking corrective measures. This is precisely why paragraph 2(a) of the Annex on Financial Services authorizes WTO Members to take measures for prudential reasons to deal with risks of a systemic nature *ex ante*"). In this regard, the Panel also cited the third-party submissions of the EU, U.S., and Brazil. *See also id.* ¶ 7.873.
100. *Id.* ¶ 7.879.

nature".[101] Instead, the panel found that the time factor was to be read in light of the causes justifying the measures and thus concluded that measures taken for prudential reasons "can remain in place . . . for as long as the factual circumstances that justified their adoption continue to exist."[102] Furthermore, the panel insisted that "nothing in the ordinary meaning of the words 'prudential reasons' conveys the idea of a time-limit" and added that "as a matter of principle" troubles raising prudential concerns "may give rise to long-lasting measures to avoid the recurrence of similar situations in the future."[103] Such a position demonstrates an awareness of the trade regime as part of a larger, integrated world system as opposed to myopically focusing on trade specific obligations.

III. Investment Jurisprudence

While the WTO had not dealt with any right to regulate issues prior to *Argentina – Financial Services*, issues relating to financial stability and financial services have been considered by investment tribunals. Problematically, however, these tribunals have not created a robust and consistent set of case law. On the contrary, some of the tribunals which had an opportunity to explore the issue provided elements of answers on how prudential measures should be handled, but in the main the tribunals failed to reach coherent conclusions. For this reason, it is not possible to clearly assert the position of international investment law. What is possible, however, is to state that the trend coming out of these cases is one of which favours general "prudential freedom". Interestingly, and as will later be discussed in more detail, even some tribunals which dismissed claims on jurisdictional grounds (and therefore did not discuss the issues in detail) made intriguing observations on the relevance of prudential regulations.

A. Leading Cases

In recent years, the issue of measures taken for prudential financial stability reasons has been discussed in six publicly available cases filed against Argentina – *LG&E*, *CMS*, *Enron*, *Sempra*, *Continental Casualty and Urbaser*[104]

101. *Id.* ¶ 7.890.

102. *Id.* ¶ 7.890 (citations omitted). ('an "imminent" danger may give rise to long-lasting measures to avoid the recurrence of similar situations in the future'. . . 'they may be urgent measures to confront an imminent risk, temporary or provisional measures, or even permanent (or long-lasting) measures, which might be taken even in the absence of an imminent risk that would prevent fulfilment of one of the motives or reasons mentioned in that paragraph.' It is therefore, 'the nature of the situation that threatens a particular prudential objective that will dictate the nature of the measure').

103. *Id.* ¶ 7.890.

104. *See* Urbaser S.A. v. Argentine Republic, ARB/07/26, Award (ICSID 2016) [hereinafter Urbaser Award]; Cont'l Cas. Co. v. Argentine Republic, ARB/03/9, Award (ICSID 2008) [hereinafter Continental Casualty]; Sempra Energy Int'l v. Argentine Republic, ARB/02/16, Award (ICSID 2007) [hereinafter Sempra Award]; Enron Corp. Ponderosa Assets, LP v. Argentine Republic, ARB/01/03, Award (ICSID 2007) [hereinafter Enron Award]; LG&E

– as well as in three annulment proceedings.[105] In the main, arbitral tribunals have identified two different ways of assessing Argentina's legal ability to take adverse measures justified on economic duress in the country. Some tribunals have mainly relied on "non-precluded measures" clauses as a means to identify exceptions to treaty obligations in certain situations. Alternatively, other tribunals have rather allowed the notion of "necessity" under Customary International Law (as provided by Article 25 of the ILC draft articles on Responsibility of States for Internationally Wrongful Acts) to prevail over NPM provisions. Interestingly, however, while the jurisprudence coming from the investment cases lacks coherence, it nonetheless points in the same direction as that of the WTO decision in *Argentina – Financial Services.*

1. *Non Precluded Measures*

In two cases, the *LG&E* and *Continental Casualty*, the tribunals gave weight to the so-called "non-precluded measures" (NPM) treaty clauses which they considered as *lex specialis* exempting the State from its treaty obligations.[106]

NPM clauses commonly ensure that treaty obligations shall not preclude the application by either party of measures necessary for the maintenance of public order or the protection of essential security interests.[107] The relevant provision in both disputes, Article XI of the Argentina – US BIT, reads as follows: "This Treaty shall not preclude the application by either Party of 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."[108]

Energy Corp. v. Argentine Republic, ARB/02/1, Decision on Liability (ICSID 2006) [hereinafter LG&E Award]; CMS Gas Transmission Co. v. Argentine Republic, ARB/01/8, Award (ICSID 2005) [hereinafter CMS Award].

105. Enron Creditors Recovery Corp. v. Argentine Republic, ARB/01/3, Annulment Proceeding (ICSID 2010) [hereinafter Enron Annulment Decision]; Sempra Energy Int'l v. Argentine Republic, ARB/02/16, Annulment Proceeding (ICSID 2010) [hereinafter Sempra Annulment Decision]; CMS Gas Transmission Co. v. Argentine Republic, ARB/01/8, Annulment Proceeding (ICSID 2007) [hereinafter CMS Gas Annulment Decision]. *See also* Antoine Martin, *Investment Disputes after Argentina's Economic Crisis: Interpreting BIT Non-Precluded Measures and the Doctrine of Necessity under Customary International Law* 29 J. INT'L ARB. 1 (2012) (more complete analysis).

106. Continental Casualty, *supra* note 104, para. 163-68; LG&E Award, *supra* note 104, at para. 92-99.

107. Treaty Between United States of America and the Argentine Republic Concerning the Reciprocal Encouragement and Protection of Investment, U.S.-Argentina, art. 10, *entered into force* Oct. 20, 1994, 31 I.L.M. 124 ("This Treaty shall not preclude the application by either Party of 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.").

108. Treaty Between United States of America and the Argentine Republic Concerning the Reciprocal Encouragement and Protection of Investment, U.S.-Argentina, *entered into force* Oct. 20, 1994, 31 I.L.M. 124.

Article 1410 of the NAFTA fulfils the same goals as the abovementioned BIT but provides more space to the host by providing for financial stability and financial market-related exceptions. More specifically, the Article provides that: "nothing [. . .] shall be construed to prevent a Party from adopting or maintaining reasonable measures for prudential reasons, such as:

> (a) the protection of investors, depositors, financial market participants, policyholders, policy claimants, or persons to whom a fiduciary duty is owed by a financial institution or cross-border financial service provider;
> (b) the maintenance of the safety, soundness, integrity or financial responsibility of financial institutions or cross-border financial service providers; and
> (c) ensuring the integrity and stability of a Party's financial system.[109]

In other words, NPM clauses operate as exception clauses capable of precluding the wrongfulness of an action deemed in breach of the applicable treaty. Drafting differences between and among the various treaties, however, make it difficult to authoritatively assert how the clauses operate and/or would be interpreted in a dispute.

Recognizing the possibility of an exception under NPM clauses,[110] nonetheless, the tribunal in *LG&E* held that given the aggregate devastating economic, political and social conditions, the domestic regulations taken by Argentina could qualify as "necessary and legitimate measures" capable of precluding wrongfulness.[111] The tribunal in *Continental Casualty*, similarly, concluded that "a severe economic crisis [could] thus qualify under Art. XI as affecting an essential security interest" of the state despite the absence of a "total collapse" of the system and justify an exception because, overall, "there is no point in having such protection if there is nothing left to protect".[112]

2. *Necessity under Customary International Law*

The tribunals in *CMS*, *Sempra* and *Enron* adopted a different approach. While noticing the existence of NPM clause, they however considered that necessity as provided under Article 25 of the ILC draft articles on Responsibility of States for Internationally Wrongful Acts could justify an exemption to existing commitments under Customary International Law (CIL). As a reminder, Article 25 reads as follows:

Article 25. Necessity

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109. Canada-Mexico-United States: North American Free Trade Agreement, art. 1410, March 1993, 32 I.L.M. 289 [hereinafter NAFTA].

110. It should be noted here that while the LG&E tribunal built its argumentation focusing on a NPM logic, it also confirmed its reasoning by applying the customary international law test to the case, as a mere formality. *See* LG&E Award, *supra* note 104, at para. 245-249.

111. *Id.* at para 240.

112. Continental Casualty, *supra* note 104, at para. 174-80.

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 (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.[113]

In other words, while the previous section considered the possibility of lifting state responsibility for treaty breaches on the basis of a treaty exception and in particular circumstances related to public order and, in certain cases, financial stability, Article 25 ILC provides an additional source of exemption grounded on Customary International Law aimed at preserving the "essential interest" of a state "against a grave and imminent peril."[114]

In practice, this approach led to complex and questionable considerations because it required a review of numerous issues such as whether the situation faced by Argentina (a) threatened its essential interests[115]; (b) represented a grave and imminent peril[116]; (c) was the only way available to settle the issue[117]; (d) had not been created by Argentina itself[118]; and (e) was temporary.[119] The *CMS*, *Enron* and *Sempra* decisions, overall, rejected the argument that an economic crisis could compromise a state's existence as being "not convincing",[120] and in *CMS* the tribunal rejected a finding of

113. Responsibility of States for Internationally Wrongful Acts, U.N. 53rd Sess., art. 25, U.N. Doc. A/56/10 (2001).

114. *Id.*

115. *See* Sempra Award, *supra* note 104, at para. 374; *see* Enron Award, *supra* note 104, at para. 332; *see* LG&E Award, *supra* note 104, at para. 251; *see* CMS Award, *supra* note 104, at para. 359.

116. *See* Sempra Award, *supra* note 104, at para. 329-332; see Enron Award, *supra* note 104, at para. 306; *see* LG&E Award, *supra* note 104, at para. 253-57; *see* CMS Award, *supra* note 104, at para. 322, 354-56.

117. *See* Sempra Award, *supra* note 104, at para. 351; *see* Enron Award, *supra* note 104, at para. 309; *see* LG&E Award, *supra* note 104, at para. 257; *see* CMS Award, *supra* note 104, at para. 323, 355-56.

118. *See* Sempra Award, *supra* note 104, at para. 374; *see* Enron Award, *supra* note 104, at para. 332; *see* LG&E Award, *supra* note 104, at para. 251; *see* CMS Award, *supra* note 104, at para. 359.

119. *See* Sempra Award, *supra* note 104, at para. 255-56; *see* Enron Award, *supra* note 104, at para. 219-224; *see* LG&E Award, *supra* note 104, at para. 251; *see* CMS Award, *supra* note 104, at para. 382.

120. *See* Sempra Award, *supra* note 104, at para. 348-49; *see* Enron Award, *supra* note 104, at para. 306; *see* CMS Award, *supra* note 104, at para. 319-22, 354-58.

Customary International Law-grounded necessity because the "constitutional order was not on the verge of collapse".[121]

In the end, these three decisions were subsequently annulled, with the Annulment proceedings in both *Sempra* and *CMS* concluding that NPM provisions indeed allowed for measures which deviate from treaty obligations without compensation being due,[122] while the *Enron* Annulment Committee questioned the tribunal's reasoning before concluding that it had no jurisdiction to make its own findings on the matter.[123]

What is interesting and worth noting is that all three annulment proceedings provided analogous reasoning in suggesting that, contrarily to the reasoning formulated in the respective awards, NPM treaty provisions and Customary international Law exceptions could *not* be considered as equals or in a similar fashion. In this regard, the *CMS* Annulment Committee emphasised that NPM and CIL exceptions had "different operation and content" and stated that NPM treaty clauses could not be analysed and applied in light of CIL clauses, which must be interpreted separately.[124] Hence, it concluded that the tribunal had failed to analyse the NPM clause:

> 123. "The problem is, however, that the Tribunal stopped there and did not provide any further reasoning at all in respect of its decision under Article XI."[125]
>
> 124. "Along those lines, the Tribunal evidently considered that Article XI was to be interpreted in the light of the customary international law concerning the state of necessity and that, if the conditions fixed under that law were not met, Argentina's defense under Article XI was likewise to be rejected."[126]
>
> 131. "Those two texts having a different operation and content, it was necessary for the Tribunal to take a position on their relationship and to decide whether they were both applicable in the present case. The Tribunal did not enter into such an analysis, simply assuming that Article XI and Article 25 are on the same footing.

121. CMS Award, *supra* note 104, at para. 322. *See also* W. Burke-White & A. von Staden, *Investment Protection in Extraordinary Times: The Interpretation and Application of Non-Precluded Measures Provisions in Bilateral Investment Treaties* 48 VA. J. INTL. L. (2008). *But cf.* Martin, *supra* note 105, at 66.

122. Sempra Annulment Decision, *supra* note 105, at para. 115. *See also* CMS Annulment Decision, *supra* note 105, at para. 133–35.

123. Enron Annulment Decision, *supra* note 105, at para. 408 ("Having annulled these findings of the Tribunal, the Committee cannot go further and make its own findings as to whether or not Argentina is entitled to rely on the principle of necessity under customary international law or on Article XI of the BIT, or as to whether or not Argentina is responsible for breaches of its obligations *vis-à-vis* the Claimants under the fair and equitable treatment clause and umbrella clause of the BIT. These questions could only be determined by a tribunal, in the event that either party were to request resubmission pursuant to Article 52(6) of the ICSID Convention.").

124. CMS Annulment Decision, *supra* note 105.

125. *Id.* at para. 123

126. *Id.* at para. 124.

> 132. In doing so the Tribunal made another error of law. One could wonder whether state of necessity in customary international law goes to the issue of wrongfulness or that of responsibility. But in any case, the excuse based on customary international law could only be subsidiary to the exclusion based on Article XI."[127]
>
> 133. "Article XI and Article 25 thus construed would cover the same field and the Tribunal should have applied Article XI as the *lex specialis* governing the matter and not Article 25."
>
> 134. "Only if it concluded that there was conduct not in conformity with the Treaty would it have had to consider whether Argentina's responsibility could be precluded in whole or in part under customary international law."[128]

The *Enron* and *Sempra* Annulment Committees formulated similar reasoning to reach the same conclusion. The *Enron* Committee, however, did apply a largely procedural methodology while the *Sempra* Committee was more forceful in stating that CIL cannot equate treaty exceptions. More specifically, the Committee in the *Enron* Annulment proceedings[129] focused on whether the tribunal provided reasons for its decision before finding the reasoning problematic due to the tribunal giving primacy to CIL over the explicit treaty exception under Article XI of the BIT without considering to what extent Article 25 ILC could apply in the relevant situation. Hence, with the CIL reasoning failing, the treaty exception could likewise not be applied:

> 394. "The final issue considered by the Tribunal was whether the BIT itself "*excludes the possibility of invoking necessity*", thereby precluding reliance on that principle in terms of Article 25(2)(a) of the ILC Articles. At paragraph 310 of the Award, the Tribunal said that it would discuss this issue subsequently. The Committee finds that the Tribunal did not subsequently make any determination of this question."[130]
>
> 403. "[. . .] The apparent meaning of these paragraphs is that the Tribunal found that the effect of Article XI of the BIT is the same or similar to the effect of Article 25 of the ILC Articles, or at least, that the expression "*measures necessary for . . . the Protection of its own essential security interests*" in Article XI of the BIT has the same or similar meaning as the expression "*[an act that is] the only way for the State to safeguard an essential interest against a grave and imminent peril*" in Article 25 of the ILC Articles. The Committee finds that the reasons for the Tribunal in reaching the conclusion are sufficiently clear, that it is not for the Committee to determine whether or not that interpretation was

127. *Id.* at para. 131-32.

128. *Id.* at para. 134.

129. Enron Annulment Decision, *supra* note 105.

130. *Id.* at para. 394.

> correct, and the Committee accordingly finds no annullable error in these paragraphs of the Award."[131]
>
> 405. "The Committee has concluded above that the Tribunal's finding that the requirements of Article 25 of the ILC Articles are not satisfied in this case must be annulled.[132] Because that finding formed the basis of the Tribunal's finding that Article XI of the BIT was inapplicable in this case, the Committee concludes that the latter finding of the Tribunal must also be annulled."

Overall, while the Committee refused to take a position on whether Article XI of the treaty could equate to CIL exceptions, it nonetheless suggested that in practice both preclusion sources had to be considered and analyzed separately.

By contrast, the Annulment Committee in the *Sempra* Proceedings[133] insisted that a treaty's *lex specialis* (the NPM clause) would have to be applied first, before even considering the possibility of a CIL exception, and explicitly rejected the idea that CIL exceptions could prevail over treaty exceptions. In fact, the Committee went as far as to explain that while a CIL exception was meant to make a wrongful act non-compensable, a treaty exception was rather intended to make the same type of act lawful from the beginning:

> 196. "In the opinion of the Committee, the reasoning of these passages compels the conclusion that the Tribunal did not deem itself to be required – or even entitled – to consider the applicability of Article XI, both because this provision did not deal with the legal elements necessary for the legitimate invocation of a state of necessity and because the Tribunal found that the Argentine economic crisis did not meet the customary international law requirements as set out in Article 25 of the ILC Articles."[134]
>
> 197. "[. . .] It does not follow, however, that customary law (*in casu*, Article 25 of the ILC Articles) establishes a peremptory "definition of necessity and the conditions for its operation". While some norms of customary law are peremptory (*jus cogens*), others are not, and States may contract otherwise [. . .]"[135]
>
> 198. "[. . .] Article XI differs in material respects from Article 25 [. . .]"[136]
>
> 199. "It is apparent from this comparison that Article 25 does not offer a guide to *interpretation* of the terms used in Article XI. The most that

131. *Id.* at para. 403.

132. *Id.* at para. 405.

133. Sempra Annulment Decision, *supra* note 105.

134. *Id.* at para. 196.

135. *Id.* at para. 197.

136. *Id.* at para. 198.

> can be said is that certain words or expressions are the same or similar."[137]
>
> 200. "More importantly, Article 25 is concerned with the invocation by a State Party of necessity "as a ground for precluding the wrongfulness of an act not in conformity with an international obligation of that State". Article 25 presupposes that an act has been committed that is incompatible with the State's international obligations and is therefore "wrongful". Article XI, on the other hand, provides that "This Treaty shall not preclude" certain measures so that, where Article XI applies, the taking of such measures is not incompatible with the State's international obligations and is not therefore "wrongful". Article 25 and Article XI therefore deal with quite different situations. Article 25 cannot therefore be assumed to "define necessity and the conditions for its operation" for the purpose of interpreting Article XI, still less to do so as a mandatory norm of international law."[138]

As a result, while the *CMS*, *Enron* and *Sempra* tribunals considered that no necessity could excuse Argentina's financial crisis-related measures *and* suggested that there was possibly little difference between treaty and CIL exceptions, the respective Annulment Committees both came to very different conclusions. More or less implicitly (depending on the case), the Committees also accepted the notion that states ought to have leeway in their decision-making powers. The Committee in the *Enron* Annulment, stated clearly that while tribunals ought to consider whether the authorities *could* have relied on alternative measures, it is not for a tribunal to decide whether the authorities *should* have opted of one reason over another. In so doing, explicitly and repeatedly questioned who would be capable to decide what course of action is suitable for the State.[139] It is worth stressing again that another point of agreement among the Committees is that treaty and CIL exceptions are different and cannot be set on equal footing. That being the case, the Committees have not applied common and consistent reasoning or formulated clear guidelines in this regard. While the Committee in Sempra rather clearly confirmed the CMS conclusion that treaty and CIL are different, the Enron Committee refused to take a position on this point and annulled the award due to the tribunal's failure to adequately discuss the relevant issues.

The above points are important as they suggest that despite several cases (and their respective annulments) there is so far no clear rule as to how to rely on and apply treaty and CIL exceptions. Interestingly, the recent tribunal in *Urbaser v. Argentina* confirms this particular conclusion, although as will be explained below, does so by only considering one of the two sources of exception.

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137. *Id.* at para. 199.

138. *Id.* at para. 200.

139. *See* Enron Annulment Decision, *supra* note 105, at para. 309, 360-78, 392-93.

In December 2016, the tribunal in *Urbaser v. Argentina* also dealt with the issue of necessity,[140] but the award made no mention of "Non-Precluded Measures" clauses and essentially focused on the Customary Law-based and necessity-based argument. Thus, without providing any legal analysis, the award rather matter-of-factly acknowledged that a state of necessity can have priority over investment considerations before concluding that Argentina did not have a choice in taking its measures.[141]

More specifically, the tribunal first focused on section 2 of Article 25 ILC and commented on the idea that necessity exceptions cannot be invoked where the state is responsible for the duress situation at stake. In this regard, the tribunal found no proof that Argentina could be held responsible for the alleged state of emergency. Perhaps more interesting, the tribunal insisted that a finding of responsibility would require the demonstration "that the Government must have known that such crisis and emergency must have been the outcome of its economic and financial policy."[142]

The tribunal next considered section 1 of Article 25 ILC and discussed whether Argentina had alternative means of acting. To the tribunal, the issue of regulatory alternatives depended on two perspectives, "the wide one, taking into account the needs of Argentina and its population nation-wide, and the narrower one of the situation of investors engaged in performing contracts protected by the international obligations arising out of one of the many BITs."[143] Hence, the tribunal considered that the claimant ought to have offered "at least a serious indication as to the nature of other measures that had been available to the Government at that time"[144] and concluded that its argument was "too short" in that it failed to "resolve the [hosts'] conflict between the obligation to guarantee the Concessionaire's right under the Concession and the access of the poor and vulnerable population to water when this cannot be ensured otherwise than by failing to comply with the host State's obligations toward the Concessionaire."[145] As a result, the tribunal concluded that Argentina had indeed faced "a situation of state of necessity as sufficient support for the emergency measures when promulgated in January 2002"[146] and emphasized that, overall, contract renegotiation would have been the only alternative method.[147]

3. *Preliminary Conclusions*

The few cases that had an opportunity to clarify the state of the law on prudential measures in times of financial instability thus provided interesting

140. Urbaser Award, *supra* note 104.
141. *Id.* at para. 683-730.
142. *Id.* at para. 711.
143. *Id.* at para. 716.
144. *Id.* at para. 717.
145. *Id.* at para. 720.
146. Urbaser Award, *supra* note, at para. 718.
147. *Id.* at para. 730-32.

ways to deal with the circumstances but did not do so in a consistent manner and thus did not definitively resolve the issue.

More specifically, while the tribunals identified two methods of allowing a certain degree of regulatory freedom to the host states in times of financial duress, their analysis has failed in two main regards. First, and most obviously, the tribunals have failed to determine which of the interpretive methods ought to prevail over the other, or more precisely when and to what extent one should prevail over the alternative approach. Second, the tribunals failed to provide robust guidelines capable of equipping states (and future tribunals) with a reliable methodological precedent.

Thus, while the tribunals provided a direction towards prudential regulatory freedom, the precise legal mechanisms for framing and processing such freedom remains unclear. On the one hand, the earliest cases did not make equal use of or give similar weight to the Customary International Law based notion of exceptions precluding wrongfulness and have rather used and relied on treaty-based NPM clauses in order to allow for exceptions to treaty obligations. In fact, and as explained before, Annulment proceedings have largely insisted on whether the two sources of exceptions ought to be treated similarly. On the other hand, the recent *Urbaser* case relied exclusively on a CIL-based reasoning in order to allow for exceptions to treaty obligations. Of course, the approach of the *Urbaser* tribunal was in itself taken by necessity as the applicable BIT between Argentina and Spain does not contain any NPM clause.[148] Nonetheless, while this explains why the award does not contain the word "non-precluded measure," the tribunal's logic and decision to apply a CIL-based exception is at odds with the findings of previous Annulment Committees in implying that exceptions can be found with or without explicitly drafted treaty provisions for this purpose. Given this, one would have expected to find a discussion in the award as to what the presence or absence of such a clause could have meant for the investor and the host. If other tribunals follow the reasoning of the *Urbaser* tribunal, the decision of the parties to include (or not include) an NPM clause could be rendered entirely moot.

Regardless, the point to be made here is that there is a trend in the investment tribunal case law pointing towards a general ability of host states to take on measures for prudential reasons, but that the trend is not anchored to a robust and predictable legal framework.

B. Additional Case Law

Several other investment awards deserve mention even though the insights they provide are far more limited than the cases highlighted in the previous subsection. In the main, these awards did not proceed due to jurisdictional issues and thus failed to fully discuss and interpret the prudential measure. Moreover, while these cases have been described as

148. Agreement between the Argentine Republic and the Kingdom of Spain on the Reciprocal Promotion and Protection of Investments, *adopted* Oct. 3, 1991, 1699 U.N.T.S. 202.

relating to prudential measures,[149] most only briefly mention or do not even contain the term "prudential measure." For instance, the word "prudential" appears only once in *KT Asia Investment Group*, in a factual manner as part of a descriptive section of the award and without any analysis of the concept.[150] Likewise, in *Renée Rose Levy*, the phrase "prudential regulator" is again mentioned once and without any analysis of prudential measures being taken.[151] Another example is *Ping An Life Insurance*, which directly relates to financial matters, but the tribunal does not make mention of financial crisis or prudential measures.[152]

Having said this, some other cases provide further evidence of the trend towards regulatory freedom in regards to prudential measures. For instance, while the word "prudential" does not appear in *Poštová Banka*, the decision nonetheless emphasized that, economic crisis or not, a "sovereign debt is an instrument of government monetary and economic policy and its impact at the local and international levels makes it an important tool for the handling of social and economic policies of a State."[153] In other words, while the tribunal did not elaborate on the ability of host states to take prudential measures in order to safeguard financial stability, it nonetheless noted the importance of preserving room for financial, economic, and monetary policy.

While making no mention of prudential measures, the previously mentioned *Renée Rose Levy* tribunal did make two important statements concerning a host states actions in time of financial crisis. First, the tribunal emphasised that "it [is] logical to assume that State authorities would take measures to maintain the stability of the financial system, as mandated by Peruvian law and, to that end, promulgate Emergency Decrees."[154] Second, the tribunal recognized the important role to be played by financial authorities in times of financial crises and stated that the relevant governmental authority "should contribute to the stability of the financial system, for which purpose it has discretionary powers, and that no bank has the power to require [it] to act in a certain way in order to disprove rumors."[155]

Another example in this regard is the *Saluka* Award, where the tribunal had to deal with an investor claiming that its legitimate expectations had been frustrated by the introduction of more stringent prudential rules on banks.[156] On the one hand, the tribunal emphasized "that the increased

149. *See* Mitchell, Hawkins and Mishra, *supra* note 4.

150. *See* KT Asia Investment Group B.V. v. Kazakhstan, ARB/09/8, Award (ICSID 2013).

151. *See* Renée Rose Levy de Levi v. Peru, ARB/10/17, Award (ICSID 2014) [hereinafter Renee Award].

152. *See* Ping An Life Ins. Co. v. Belgium, ARB/12/29, Award (ICSID 2015).

153. Poštová banka, a.s v. Hellenic Republic, ARB/13/8 para. 324, Award (ICSID 2015).

154. Renee Award, *supra* note 151, at para. 323.

155. *Id.* at para. 335.

156. Saluka Investments B.V. v. The Czech Republic, Partial Award (UNCITRAL 2006), at para. 354.

stringency of the CNB's prudential rules contributed to the distress suffered by the Czech banking system by forcing the banks to increase provisioning. Consequently, it became even more difficult for the banks to meet the regulatory capital requirements than it had been before due to the bad loan problem".[157] On the other hand, it nonetheless insisted that the "tightening the regulatory regime" had to be seen as part of a larger European Accession process[158] and concluded that the host's financial policy was not a breach of the treaty standards.[159]

Another relevant case is *Fireman's Fund Insurance*, which had the potential to provide important interpretive guidance but did not engage in any legal reasoning on the issue. The case was the first brought under Chapter Fourteen (cross-border investment in Financial Services) of the North American Free Trade Agreement (NAFTA) following a financial crisis in Mexico (and a 96% reduction in the value of the Mexican peso) in the mid-1990s.[160] In defending the claim brought by an investor concerning the loss of investment in financial products, Mexico emphasised that the "sophisticated investor . . . made a risky investment in a bank at a time that there was a very serious financial crisis in Mexico"[161] and argued "that the measures in question are 'reasonable measures for prudential reasons' within the meaning of Article 1410 (Exceptions) of the NAFTA."[162] Article 1410, as a reminder, provides that "nothing [. . .] shall be construed to prevent a Party from adopting or maintaining reasonable measures for prudential reasons, such as:

(a) the protection of investors, depositors, financial market participants, policyholders, policy claimants, or persons to whom a fiduciary duty is owed by a financial institution or cross-border financial service provider;
(b) the maintenance of the safety, soundness, integrity or financial responsibility of financial institutions or cross-border financial service providers; and

157. *Id.* at para. 356.
158. A particularity of the *Saluka* case lies in the fact that the Czech Government justified its financial regulatory measures by the fact that the country had signed a pre-accession agreement with the European Commission committing it to bring its regulatory regime into line with the norms in the European Union. In 1999 a "Twinning Programme" for banking supervision had been launched to adjust the Czech regulatory methodology and the practical implementation of banking supervision to European Union standards. *See id.* at para. 357.
159. *Id.* at para. 500 ("The Tribunal does not find, however, that the Respondent has violated its 'fair and equitable treatment' obligation by a failure to ensure a predictable and transparent framework for Saluka's investment. Neither was the increase of the provisioning burden for nonperforming loans unpredictable for Saluka/Nomura, nor could Saluka/Nomura legitimately expect that the Czech Republic would fix the legal shortcomings regarding the protection of creditor's rights and the enforcement of loan security within a timescale of help to Nomura.").
160. *See* Fireman's Fund Ins. Co. v. The United Mexican States, ARB(AF)/02/1, Award (ICSID 2006) [hereinafter Fireman Award].
161. *Id.* at para. 116.
162. *Id.* at para. 156.

(c) ensuring the integrity and stability of a Party's financial system.[163]

The tribunal did not engage in, discuss, or contribute to the NPM vs Customary International Law exceptions debate. Instead, the tribunal simply held that before considering an exception a measure must be found to be inconsistent with a provision of the NAFTA[164] and concluded that in the case at stake "the condition precedent for invocation of the Prudential Measures Exception, a finding of expropriation, ha[d] not been fulfilled."[165] Hence, it found that it had no ground for proceeding with a further analysis of the prudential exception and left the issue untouched.

C. Convergence with WTO Law?

While the above analysis demonstrates the lack of uniformity in the investment jurisprudence on prudential measures, the various investment tribunals have nonetheless paved the way towards recognizing a right to regulate for the preservation of financial stability. In this regard, three important aspects are worth emphasising.

First, and from a very practical point of view, the investment case law – and in particular the Annulment Proceedings – have provided host states with a certain amount of latitude when regulating for the preservation of economic and financial stability, despite the existence of clear obligations contained in the treaty. At the same time, the awards have failed to clarify whether the overall state of an economy could constitute an acceptable essential interest susceptible of justifying necessity or even whether an economic crisis would constitute a sufficient peril justifying the taking of special measures. The Annulment Committees have, however, for the most part agreed that two distinct exceptions exist which are capable of precluding wrongfulness in specific situations, unlike the initial awards which barely considered the issues.

Notable in this regard is the *Continental Casualty* award, which stated that a tribunal's "objective assessment" on regulatory matters "must contain a significant margin of appreciation for the State applying the particular measure: a time of grave crisis is not the time for nice judgments, particularly when examined by others with the disadvantage of hindsight".[166] Similarly, while the *Urbaser* award lacked legal analysis, it rather significantly highlighted the importance of differentiating between a wide perspective "taking into account the needs of Argentina and its population nation-wide" and a "narrower . . . situation of investors engaged in performing contracts protected by the international obligations arising out of one of the many BITs".[167] Thus, while commentators have asserted that "to date, [the

163. NAFTA, *supra* note 109.

164. Fireman Award, *supra* note 160, at para. 160.

165. *Id.* at para. 165.

166. Continental Casualty, *supra* note 104, at para. 181.

167. Urbaser Award, *supra* note 104, para 716. ('. . . the question whether "other means" were available has to be captured in both perspectives: the wide one, taking into account the needs of

relevant case law] provide[s] little direct guidance on the interpretation prudential exceptions",[168] it is our contention that despite the absence of direct discussion and decisions on prudential matters per se, this case law nevertheless points very clearly towards regulatory freedom in times of financial duress and thus contains important indicative value.

The second point worth emphasizing is that the findings of investment tribunals are converging with those of the WTO Appellate Body in *Argentina – Financial Services*. Although the arbitral findings are complex and not entirely consistent, the investment tribunals have found consensus and therefore agree with the WTO Appellate Body that governments have the right to retain the ability to regulate in times of economic turmoil and instability.

The third observation is that while *Argentina – Financial Services* provided extensive analysis of treaty-based exceptions, the investment tribunals have failed to reach consensus on the proper interpretation. If some have emphasized the relevance of NPM clauses towards wrongfulness preclusion and would therefore seem to be in line with the WTO jurisprudence, other tribunals discussed the opportunity of CIL-grounded exceptions, particularly in the absence of NPM provisions in the applicable treaties. Hence, the investment jurisprudence to date leaves us uncertain whether CIL exceptions might make the treaty-based NPM exception moot and without legal effect. Simply put, the ease with which the *Urbaser* tribunal ignored the NPM argument (and the lack of a NPM clause in the relevant treaty) and entirely focused on CIL suggests that – if future tribunals followed the path – prudential measures could be dealt with under investment law as a matter of CIL and without the need for a more specific treaty provision.[169]

Argentina and its population nation-wide, and the narrower one of the situation of investors engaged in performing contracts protected by the international obligations arising out of one of the many BITs').

168. *See* Mitchell, Hawkins and Mishra, *supra* note 4, at 15.

169. To this extent, it is also worth noting that while investment tribunals have so far considered the possibility of justifying measures taken for prudential reasons by making reference to necessity, some commentators have also highlighted the idea of relying on 'Force majeure' as a relevant tool for use by States. Gourgourinis, in particular, notes that in various cases falling under the jurisdiction of the Court of Justice of the European Free Trade Association (EFTA) and of the Permanent Court of International Justice, financial crisis – particularly the recent Greek crisis – could be considered as force majeure and preclude wrongfulness. Thus, the margin of appreciation doctrine might in the future be considered by investment tribunals either through necessity or force majeure, with the latter perhaps providing a more flexible exception in that the role played by the host state in creating the crisis would not be given the same weight. For more details on the force majeure discussion, *See* Anastasios Gourgourinis, *Financial crisis as force majeure under international law and EU law: Defending emergency measures, à l'européenne in investment arbitration under intra-EU BITs*, INT'L INVESTMENT L. AND THE GLOBAL FINANCIAL ARCHITECTURE, 281-315, 311-313 (2017).

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IV. Concluding Remarks

The main observation of this analysis is that there is a growing consensus both in trade and investment jurisprudence towards a right to regulate for prudential reasons and in order to preserve financial stability.

Investment tribunals and the WTO panel/Appellate Body demonstrate an awareness and appreciation of broader, societal interests and in the main avoided interpreting the relevant treaties in a narrow and constricting manner. Both fora agree that the prudential carve-out clause is meant to be functional and to provide States with regulatory room in the face of financial crisis. The recent jurisprudence in both fora also provides several valuable and instructive lessons as to the effectiveness of prudential provisions.

Among those lessons is the distinction the Panel in *Argentina – Financial Services* made between the commonly used term "prudential measure" and the preferred understanding that the subject matter must refer to measures that are being taken "for prudential reasons." The distinction between a "prudential measure" and a measure taken "for prudential reasons" may at first appear illusory, but the Panel spent some time explaining the divergence in meaning and effect of the difference in meaning and this distinction will likely survive and be used in future disputes.

Another related lesson is the focus of both the investment and trade disputes on the circumstances in which the measures have been designed – i.e. whether the measures operate in line with the exceptional goal they serve or whether the mechanisms put into place generate a certain degree of unfairness detrimental to the legitimately pursued goal. In this regard, the tribunals have shown a high degree of deference to the host government while at the same time applying the prudential provisions as a good faith or anti-abuse mechanism in a manner similar to the general exception clauses of GATT and the GATS (less the need for a necessity test).

The third lesson is that the tribunals have gone some way in clarifying the context in which exceptions may legitimately occur. While the investment tribunals have not been hesitant to engage in second guessing policy decisions of host governments, it is noteworthy that those decisions that rejected the notion of preserving economic stability were annulled. Meanwhile, the *LG&E* tribunal held that exceptions could be justified by aggregate devastating economic, political and social conditions. Similarly, the Panel in *Argentina – Financial Services* concluded that measures could be taken for "preventive or precautionary reasons" so as to prevent a risk, injury, or danger that does not necessarily have to be imminent and that Members should be granted a certain dose of freedom when assessing the necessity to act. Although the jurisprudence between the investment and trade spheres is not in complete harmony – for instance, the time limitation criteria listed by investment tribunals has not been confirmed by the WTO Panel – the decisions do pave the way for the emergence of a definitive standard, regardless of whether the standard in trade and investment law differs.

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The fourth lesson is that carve-out provisions are not uniformly drafted in most investment and trade agreements, and thus the interpretation of each provision will not necessarily correspond to the interpretation of another provision with even slightly different wording. This is critical to some issues, including when determining whether the provision contains a temporal limitation. In essence, a rather large question regarding the prudential carve-out is whether such measures have to be temporary in nature. In contrast with the findings of investment arbitral tribunals, *Argentina – Financial Services* suggests that governments facing the threat of financial instability could take long-term regulatory measures and remain in compliance with Paragraph 2(a) of the Annex, provided that the measures are indeed taken for prudential reasons and without intent to escape existing trade obligations.

The fifth lesson is that while there is an emerging jurisprudence relating to prudential measures, it is important to remember that the tribunals have relied upon different assessment methods in reaching their determinations. The investment tribunals considered whether states could regulate on the grounds of both customary law exceptions and *lex specialis* provisions (NPM) specifically drafted to offer carve-out opportunities in times of duress. In contrast, the WTO tribunal assessed whether a prudential measure could qualify as a general exception to GATS commitments (under Article XIV) and whether the carve-out clause contained in its *lex specialis* Annex on Financial Services could qualify a measure as a valid exception to existing commitments. In the end – and most importantly – the conclusions of both the investment and trade tribunals largely converge in terms of direction but perhaps tend to diverge in terms of logic. The tribunals share a common reliance on a two-step procedure involving the identification of a special objective and establishment of a cause and effect relationship (to ensure that regulatory measures avoid arbitrariness, unjustifiable discrimination and do not constitute disguised restrictions on existing obligations). A divergence, however, occurs as the depth of the logic provided by the WTO Appellate Body is much more significant than that of investment tribunals which have tended to focus on and make factual assessments without spending much time on the legal analysis. The classic example here is the recent *Urbaser* case, which while relying on a CIL approach to justify the use of a prudential measure (due to the lack of NPM clause in the applicable treaty) provided no analysis for the decision or on the legal consequences (or lack thereof) of the absence of a NPM clause in the treaty.

A final lesson is that both the trade and investment tribunals have recognized a right of States/Members to take measures deemed necessary to preserve their essential interests against a threat of instability – that is, before the emergence of a crisis renders action too late and moot – notwithstanding existing commitments, and as long as certain requirements are observed. This is in an important point because, although the idea has long been defended in the doctrinal debates, until now it lacked the

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jurisprudence to substantiate the position and counter critics offering a different viewpoint.

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