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**HOT TOPICS IN INVESTMENT ARBITRATION:  
INVESTMENT PROTECTION AND THE RIGHT TO REGULATE ...**

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**NIELS SCHIERSING, HORTEN**

# GENERATION UKRAINE V. UKRAINE (2003)

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Predictability is one of the most important objectives of any legal system.

It would be useful if it were absolutely clear in advance whether particular events fall within the definition of an "indirect" expropriation.

It would enhance the sentiment of respect for legitimate expectations if it were perfectly obvious why, in the context of a particular decision, an arbitral tribunal found that a governmental action or inaction crossed the line that defines acts amounting to an indirect expropriation.

But there is no checklist, no mechanical test to achieve that purpose. The decisive considerations vary from case to case, depending not only on the specific facts of a grievance but also on the way the evidence is presented, and the legal bases pleaded. The outcome is a judgment, i.e. the product of discernment, and not the printout of a computer programme.

## SALUKA V. CZECH REPUBLIC (2006)

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*It is now established in international law that States are not liable to pay compensation to a foreign investor when, in the normal exercise of their regulatory powers, they adopt in a non-discriminatory manner bona fide regulations that are aimed at the general welfare.*

## AZURIX V. ARGENTINA (2006)

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*For the Tribunal, the issue is not so much whether the measure concerned is legitimate and serves a public purpose, but **whether it is a measure** that, being legitimate and serving a public purpose, **should give rise to a compensation claim**.*

*In the exercise of their public policy function, governments take all sorts of measures that may affect the economic value of investments without such measures giving rise to a need to compensate.*

# EL PASO ENERGY V. ARGENTINA (2011)

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*Some general regulations can amount to indirect expropriation ...*

- 1. As a matter of principle, general regulations do not amount to indirect expropriation ...*
- 2. By exception, **unreasonable general regulations** can amount to indirect expropriation ...*

## POPE & TALBOT V. CANADA (2001)

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*... a blanket exception for regulatory measures would create a gaping loophole in international protections against expropriation.*

# COMPREHENSIVE & ECONOMIC TRADE AGREEM. (CETA)

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## PAPER BY THE EU-COMMISSION:

“How is the right to regulate protected in the investment chapter? **The EU and Canada have agreed to bring very significant clarifications to the key substantive provisions**, which are also the most often invoked by investors when bringing claims under the investor-to-state dispute settlement system. **In concrete terms, this means that arbitrators will now have strict and detailed guidance when these provisions are invoked by an investor.**”

### 1. Reaffirming the right to regulate

The CETA reaffirms the right of the EU and Canada to regulate to pursue legitimate public policy objectives such as the protection of health, safety, or the environment.”

# TRANSATLANT. TRADE & INVESTM. PARTNERSHIP (TTIP)

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## EU COMMISSION: TTIP EXPLAINED 6 MAY 2014:

Investment is an essential element of a developed economy. In order to have a predictable environment investors need to know that they will be treated fairly and not unfairly discriminated against compared to domestic firms.

...

The Commission wants to see the relevant rules and conditions set out more clearly **so as to underline the right to regulate.**



# CETA – “LEAKED” FINAL TEXT (AUGUST 2014)

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## PREAMBLE

**RECOGNIZING** that the **protection of investments**, and investors with respect to their investments, stimulates mutually beneficial business activity;

**RECOGNIZING** the **importance** of international security, democracy, **human rights** and the **rule of law** for the development of international trade and economic cooperation;

...

**RECOGNIZING** that the provisions of this Agreement preserve the right to regulate within their territories and resolving to **preserve their flexibility** to achieve **legitimate policy** objectives, such as public health, safety, environment, public morals and the promotion and protection of cultural diversity; ...

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# CETA: TRADE AND LABOUR

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## CHAPTER X+1: TRADE AND LABOUR

### Article 2: Right to regulate and levels of protection

Recognising the right of each Party to set its **labour priorities**, to establish its levels of **labour protection** and to adopt or modify its relevant laws and policies accordingly in a manner compatible with its international **labour commitments**, including those in this Chapter, each Party shall strive to continue to improve those laws and policies with the goal of providing high levels of labour protection.

## Chapter XX: Trade and Environment

### Article X.4: Right to regulate and levels of protection

Recognizing the right of each Party to set its own **environmental priorities**, to establish its own domestic **levels of environmental protection**, and to adopt or modify its relevant laws and policies accordingly in a manner consistent with the multilateral environmental agreements to which they are a party and with this Agreement, each Party shall seek to ensure that those laws and policies **provide for and encourage high levels of environmental protection** and shall strive to continue to improve those laws and policies and their underlying levels of protection.

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## **CETA ARTICLE X.11: EXPROPRIATION**

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1. **Neither** Party may nationalize or **expropriate** a covered investment either **directly, or indirectly** through measures having an effect equivalent to nationalization or expropriation (hereinafter referred to as “expropriation”), **except:**

- (a) for a public purpose;
- (b) under due process of law;
- (c) in a non-discriminatory manner; and
- (d) against payment of prompt, adequate and effective compensation.

**For greater certainty, this paragraph shall be interpreted in accordance with Annex X.11 on the clarification of expropriation.**

...

## CETA ANNEX X.11: EXPROPRIATION (1)

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The Parties confirm their shared understanding that:

1. Expropriation may be either direct or indirect:

(a) **direct expropriation** occurs when an investment is nationalised or otherwise directly expropriated through formal transfer of title or outright seizure; and

(b) **indirect expropriation** occurs where a **measure** or series of measures of a Party has an effect equivalent to direct expropriation, in that it **substantially deprives** the investor of the **fundamental attributes** of property in its investment, including the **right to use, enjoy and dispose** of its investment, without formal transfer of title or outright seizure.

## CETA ANNEX X.11: EXPROPRIATION (2)

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2. The determination of whether a measure or series of measures of a Party, in a specific fact situation, constitutes an indirect expropriation **requires a case-by-case, fact-based inquiry** that considers, among other factors:

(a) the economic **impact** of the measure or series of measures, although the **sole fact** that a measure or series of measures of a Party has an **adverse effect** on the economic value of an investment does **not establish** that an indirect **expropriation** has occurred;

(b) the **duration** of the measure or series of measures by a Party;

(c) the extent to which the measure or series of measures interferes with **distinct, reasonable investment-backed expectations**; and

(d) the **character** of the measure or series of measures, notably their **object, context** and **intent**.

## CETA ANNEX X.11: EXPROPRIATION (3)

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

# NAFTA

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## **Art 1110 – Expropriation and Compensation**

1. No Party may directly or indirectly nationalize or expropriate an investment of an investor of another Party in its territory or take a measure tantamount to nationalization or expropriation of such an investment ("expropriation"), except:

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



## US MODEL BIT ANNEX B

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

# EXPROPRIATION V REGULATION

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**A lawful expropriation is (e.g. CETA, NAFTA etc.):**

1. done for a public purpose;
2. done in a non-discriminatory manner;
3. done in accordance with due process of law
4. **Against payment of compensation**

**And a non-compensable regulation is (e.g. Chemtura v Canada and Methanex v USA ):**

1. Non-arbitrary
2. Non-discriminatory
3. **Non-excessive**
4. In good faith serving legitimate public welfare interests

# SOME FUTURE FAULT LINES OR BATTLEFIELDS ?

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WHEN IS A MEASURE "EXCESSIVE"?

"MANIFESTLY EXCESSIVE" v "EXCESSIVE"?

"INTENT" v "EFFECT"?

# ”MANIFESTLY EXCESSIVE”

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CETA ANNEX.11

(1)

(2)

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

## METHANEX V USA (2005)

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- I. It was **not** made in an **arbitrary manner** since it respected due process and was based on valid science – based on facts and fixed standards (scientific) – i.e. based on facts and fixed standards (scientific) and allowing the affected parties to be heard – in the case it was common ground that the tribunal should not "not second guess the correctness of the science based decision making of highly specialized national regulatory agencies ...
- II. It was **non-discriminatory** – translates into not the result of an unjust distinction ... an unjust distinction would of course an action that is targeted at the property rights of persons of a particular nationality or certain market participants or protectionism
- III. It was **not excessive** – i.e. it was **proportional to the goals pursued**
- IV. It was made in **good faith** to combat the serious occupational exposure risks posed by Lindane – **aimed at the general welfare** within the mandate of the relevant government branch ...

## CHEMTURA V CANADA (2010)

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Even if the Tribunal concluded that there was a substantial deprivation of the Claimant's investment, (as mentioned before, this is a necessary prerequisite for an expropriation) there was still no expropriation because the (Government Agency's) decision to phase out all agricultural applications of lindane was a valid exercise of Canada's police powers to protect public health and the environment.

...

## CHEMTURA V CANADA (2010)

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*The decision of the (Government Agency) to de-register Lindane meets the test of this doctrine because*

- I. It was not made in an arbitrary manner since it respected due process and was based on valid science*
- II. It was non-discriminatory*
- III. It was not excessive*
- IV. It was made in good faith to combat the serious occupational exposure risks posed by Lindane*

## CHEMTURA V CANADA (2010)

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*Irrespective of the existence of a deprivation, the Tribunal considers in any event that the measure challenged by the Claimant constituted a valid exercise of the Respondent's police powers. ... The government agency took measures within its mandate, in a non-discriminatory manner, motivated by the increasing awareness of the dangers presented by lindane for human health and the environment. A measure adopted under such circumstances is a valid exercise of the State's police powers and, as a result, does not constitute an expropriation.*



## **ACHMEA V SLOVAK REPUBLIC (2012)**

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Nothing in these findings of the Tribunal should be taken to suggest that the Treaty is hostile towards particular policies on the provision of healthcare facilities.

The Contracting Parties are free to adopt the policies that they choose. The Treaty focuses on the manner in which policies may be changed and implemented, not on the policies themselves.

The decision in a case such as the present could be very different if, for example, reforms had been introduced in a phased manner together with provision for the compensation of any private health insurance providers who were caused loss by the reforms. Indeed, the Contracting Parties could go further, and exclude health care altogether from the coverage of the BIT if they so wish.

But as long as the provisions of the Treaty remain in force and applicable, they must be respected. That is what the Governments of the Contracting Party intended when they chose to conclude the Treaty, for what they judged to be the benefit of their States and their nationals.

## JAMES AND OTHERS V. UNITED KINGDOM (ECHR 1986)

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*"a measure depriving a person of his property [must] pursue, on the fact as well as in principle, a legitimate aim 'in the public interest'", and bear "a reasonable relationship of proportionality between the means employed and the aim sought to be realized". **This proportionality will not be found if the person concerned bears "an individual and excessive burden"**.*

*The Court considered that such **"a measure must be both appropriate for achieving its aim and not disproportionate thereto"***

*The Court found relevant that non-nationals "will generally have played no part in the election or designation of its [of the measure] authors nor have been consulted on its adoption", and observed that **"there may well be legitimate reason for requiring nationals to bear a greater burden in the public interest than non-nationals."***

# ”INTENT”

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CETA ANNEX.11

(1)

...

(2)

...

(d) the **character** of the measure or series of measures, notably their object, context and **intent**

## DEUTSCHE BANK V. SRI LANKA (2012)

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**Many tribunals** in other cases have tested governmental conduct in the context of indirect expropriation claims by reference to **the effect** of relevant acts, **rather than the intention behind them**.

In general terms, a substantial deprivation of rights, for at least a meaningful period of time, is required.

The required level of interference with rights has been variously described as *“unreasonable”*; *“an interference that renders rights so useless that they must be deemed to have been expropriated”*; *“an interference that deprives the investor of fundamental rights of ownership”*; *“an interference that makes rights practically useless”*;

# **SOME PENDING CASES ON THE RIGHT TO REG.**

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**VATTENFALL V GERMANY**

**PHILIP MORRIS V AUSTRALIA**

## **MORE THAN 50 YEARS AGO....**

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### **G. C. Christie in WHAT CONSTITUTES A TAKING OF PROPERTY UNDER INTERNATIONAL LAW**

It is evident that the question of what kind of interference short of outright expropriation constitutes a "taking" under international law presents a situation where the common law method of **case by case development is pre-eminently the best method, in fact the only method, of legal development**

*38 Brit. Y.B. Int'l L. 307-338 (1962)*

**Potter Stewart in *Jacobellis v. Ohio* 378 U.S. 184 (1964):**

**“I KNOW IT WHEN I SEE IT”!**