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Taming the chaos in investment treaty protection*

by

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In his 2011 Freshfields Lecture, Toby Landau urged the arbitration community to pay more attention to certain core concerns about investor-state dispute settlement (ISDS), particularly after an explosion of cases pushing into ever more sensitive areas of sovereign discretion. According to Landau, there was nothing in the existing legal framework to prevent the community from saving investor-state arbitration from itself.¹ Among the core concerns he highlighted, the extent of the substantive protections provided by international investment agreements (IIAs) remains a crucial one.

Most IIAs concluded until the early 2000s normally grant very broad substantive protections to foreign investors, including, in particular, guarantees vis-à-vis host countries'

- substantial deprivation of a foreign investment's value (through expropriation provisions),
- unreasonable or arbitrary conduct (mainly through the non-impairment and fair-and-equitable-treatment clauses), and
- breach of investment contracts (through umbrella clauses).²

A few treaties even provide for guarantees against regulatory changes introduced by host countries negatively affecting foreign investments (through the little-known stabilization clause).³ Despite arbitral practice gradually bringing some clarity regarding the content of investment-protection guarantees (i.e., umbrella clauses, full protection and security, indirect expropriation), there are still three serious shortcomings, mainly revolving around the content of the fair-and-equitable-treatment clause.

First, while investment tribunals now regularly acknowledge host countries' right to regulate in the public interest, many tribunals still fail to recognize appropriately the legal relevance of the public interest in determining whether a legitimate expectation deserves legal protection. Under EU law, for example, it is undisputed that, "even if the applicant is able to prove a prima facie legitimate expectation, this may be defeated if there is an overriding public interest that trumps the expectation."⁴

Second, several recent decisions, including especially those involving changes to incentives regimes in the photovoltaic industry, fail to exclude categorically an interpretation of fair and equitable

treatment that includes an obligation of regulatory stability in the strict sense. Breaches of a strict stability obligation is premised, crucially, on the existence of radical changes in the applicable regulatory framework rather than on the unreasonable or arbitrary nature of the new framework.⁵

Third, where investment tribunals have focused on reasonableness-based guarantees, there is still no clarity regarding the specific reasonableness test that is employed to review the lawfulness of host countries' conduct under IIAs. While some tribunals have employed a (more deferential) means-ends rationality test, other tribunals have employed a (more intrusive) proportionality-balancing test.⁶

It is thus unsurprising (though disquieting for many) that, following the raft of recent measures undertaken by many governments to face the COVID-19 pandemic, potential IIA claims are being envisaged to remedy any harm caused to foreign investors.

The time for investment arbitration to save itself may be running out. The number of policymakers directly addressing these shortcomings is growing (e.g., India's recent investment policy reforms or the ongoing efforts to "modernize" the Energy Charter Treaty). However, some countries' recent solutions do not appear to enhance legal certainty and ensure that countries' right to regulate is subject to appropriate legal restraints. Among the recent treaty innovations falling short of the mark are:

- General references to the customary minimum standard of treatment (e.g., the Comprehensive and Progressive Agreement for Trans-Pacific Partnership's Article 9.6),
- Broad "rule-of-law" provisions (e.g., the 2019 Dutch model BIT's Article 5), and
- Treaty language expressly or implicitly pointing to strict proportionality balancing (e.g., the EU-Canada Comprehensive Economic and Trade Agreement's expropriation annex or the US-Mexico-Canada Agreement).

Future IIAs should instead clearly identify (a) certain principles of good governance that feature in most public law systems, such as legality, procedural fairness and substantive reasonableness; and (b) the applicable standard of review, including both the nature and intensity of review.⁷ For example, IIAs should guarantee host countries' right to determine their own levels of protection of a public interest, as is true in WTO law and was recognized by the [EU Court of Justice in Opinion 1/17](#).

These reforms should be addressed in a multilateral forum. However, unlike ISDS procedures, reforms of substantive investment protections are taking place at national or regional levels only. Accordingly, these various, parallel reforms may end up being partial in scope, or simply not produce much additional coherence and consistency. Extending UNCITRAL Working Group III's mandate beyond ISDS reform has been suggested, but there appears to be very little appetite for it, yet.

Thus, when it comes to a core aspect of the investment treaty system, investment protection, policymakers find themselves between a rock and a hard place: investment tribunals' shortcomings as described above, on one side, and the politically arduous multilateral mountain to climb, on the other side. Something will have to give.

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¹ Alison Ross, "Freshfields lecture 2011: saving investment arbitration from itself," *GAR*, vol. 6 (2011).

² Federico Ortino, *The Origin and Evolution of Investment Treaty Standards: Stability, Value, and Reasonableness* (Oxford: OUP, 2019).

³ Ortino, pp. 14-20; also [Tarcisio Gazzini, "Beware of freezing clauses in international investment agreements," *Columbia FDI Perspectives*, no. 191 \(Jan. 16, 2017\).](#)

⁴ Paul Craig, *EU Administrative Law* (Oxford: OUP, 2012), p. 584.

⁵ Ortino, pp. 33-43.

⁶ Ortino, pp. 127-152.

⁷ See, Federico Ortino, "The investment treaty system as judicial review," *ARIA*, vol. 24 (2013), pp. 437 et seq.

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