

LEGAL ISSUES JOURNAL

Volume 4 Issue 2 July 2016

EDITOR-IN-CHIEF

Markus McDowell

GENERAL EDITOR

Aristi Volou

REVIEWERS AND EDITORS

David Felipe Alvarez
M. Sanjeeb Hossain
Marco Bocchi
Riyao Liu
Matthew Channon
Nataly Papadopoulou
Olivia Ford
Daniel Schoeni
Richard Glover
Nazia Shaikh
Janet Furness
Meixian Song

COPY EDITORS

Konstantinos Giorgiadis
Leanne Gray
www.legalissuesjournal.com

Legal Issues is an international journal managed and published by the UK Law Students' Association (UKLSA). The Journal publishes fine research in all fields of law on the basis of its contribution to the society, originality, interdisciplinary interest, and quality. *Legal Issues* also provides important news and interpretation on changes in the legal world and coming trends affecting law, lawyers, and society. The Journal has two primary aims. First, to facilitate a forum for the sharing of knowledge, news, and trends concerning the application of the law throughout

the globe and for further development in all fields of law. Second, to ensure the dissemination of fine accessible work to the public throughout the world.

Every effort has been made to ensure accuracy of the submissions. However, the UKLSA is not responsible for any errors. The views expressed in this journal are those of the authors and do not necessarily reflect those of the Editorial Board or of the UKLSA. We are therefore unable to accept responsibility for the content of the submissions.

ISBN-13: 978-1535124478 (Print)

ISBN-10: 1535124474 (Print)

© 2016 UK Law Students' Association. All rights reserved.

The United Kingdom Law Students' Association

www.uklsa.co.uk

Patrons

Lord Neuberger of Abbotsbury, President of the Supreme Court

Lord Phillips of Worth Matravers, Former President of the Supreme Court

Honorary Board

His Hon Judge Dight, Chancery Specialist Circuit Judge

Professor David Feldman, Rouse Ball Professor of English Law at the University of Cambridge, 39 Essex Street

Andrew Caldecott QC, Barrister, Head of One Brick Court Chambers

Stephen Rubin QC, Barrister, Fountain Court Chambers

Tim Ludbrook, Barrister, 13 Old Square Chambers

Fergus Randolph QC, Barrister at Brick Court Chambers

Board of Governors

Iman Fadaei, Founder of CrowdSkills Ltd., Aha Design; and

The Positive Ideas Company Ltd.

Alex Matheson, Barrister, Manager at Prolegal Solicitors

Fatos Selita, Founder of The UKLSA; Barrister; Attorney and Counselor at Law, New York State, USA; Consultant at Emerging Law Ltd.; AIR Courses Director at Goldsmiths, University of London; Lecturer and

Director of the Department of Intellectual Property Transfers at Tomsk State University; Visiting Lecturer at Higher School of Economics.

Branches

Education and Training

Justice

Advocacy

Careers Division

Access to the Profession

The Dilemma of Indirect Expropriation of Host States and the Right to Regulate in the International Investment Sphere

Bashayer Al-Mukhaizeem¹

This article examines the situation where a State embraces an investment belonging to a foreigner. How a State can regulate its affairs without harming foreign investors and without being accused of implied expropriation of such investment? Some municipal laws restrict the government's power to expropriate investments indirectly, such as Cambodia's Investment Act 1994.² Other domestic laws do not constrain the government from doing so. This article examines specific measures in order to determine whether a State creates new legislation to disengage itself from its obligations towards foreign investment, or whether such a rule is promulgated merely to govern internal matters.

Keywords: International Investment Law, Indirect Expropriation.

1. Introduction

In many countries, foreign investment has expanded to reach between 50-100% of all major sectors, such as railways, mining, and banking.³ Cross-border investment exceeds \$1.5 trillion annually⁴ and is regarded as an engine for economic prosperity, exploiting a State's productive potential⁵ and providing a source of foreign skills, information, technology,

¹ LLM, Sussex University; Legal Researcher, Civil Service Commission of Kuwait.

² Art 9 Cambodia Investment Act 1994. See: Lorenz Cotula, *Foreign Investment, Law and Sustainable Development: A Handbook on Agriculture and Extractive Industries* (London: International Institute for Environment and Development, 2014), 22.

³ Ian Brownlie, *Principles of Public International Law* (Oxford University Press, 2003), 508.

⁴ Gary Born, *International Arbitration: Law and Practice* (Netherlands: Wolters Kluwer, 2012), 411.

⁵ Peter Bossche & Werner Zdouc, *The Law and Policy of the World Trade Or-*

expertise and foreign currency revenue.⁶ In most cases, a State would not sacrifice such advantages, which are seen as outweighing any other consideration. It is undesirable for a country to receive negative publicity and potentially lose its reputation as a foreign investment venue.⁷

There is a three-part test to determine whether the transaction is to be regarded as an investment enterprise.⁸ Firstly, the duration of the project should last for several years.⁹ Secondly, the investment should have a vital role in generating a regular income contributing towards and promoting community affairs, such as consumer services, technology and marketing assistance.¹⁰ Thirdly, investment activity entails a certain degree of risk associated with the difficulty of predicting the transaction's consequences.¹¹

The formation of investment tribunals, such as the International Centre for Settlement of Investment Disputes (ICSID), has created an arbitral forum to resolve disputes between foreign investors and the State where the investment occurred (host State) through the incorporation of ICSID in many bilateral investment treaties (BITs).¹² BITs aim to protect and promote international investments.¹³ Investment tribunals have a substantial role to play in determining whether the acts of the host State amount to indirect expropriation, or reflect the normal exercise of the State's right to regulate, in light of the facts and circumstances of each case.¹⁴ This paper discusses the criteria used by investment tribunals to reach such a distinction.

Indirect expropriation may occur by measures that cause the value or usage of the investment to diminish considerably, even if the possession of the asset remains with the investor.¹⁵ In other words, indirect expropri-

ganization (Cambridge University Press, 2014), 20.

⁶ Surya Subedi, 'International Investment Law' in Malcolm Evans, *International Law* (Oxford University Press, 2014), 741.

⁷ Margaret Moses, *The Principles and Practice of International Commercial Arbitration* (Cambridge University Press, 2012), 231.

⁸ Krista Schefer, *International Investment Law* (Cheltenham: Edward Elgar Publishing, 2013), 59.

⁹ *Ibid.*, 59.

¹⁰ *Ibid.*, 60, 72.

¹¹ *Ibid.*, 73.

¹² Alan Redfern & Martin Hunter, *Redfern and Hunter on International Arbitration* (Oxford University Press, 2009), 467.

¹³ *Ibid.*, 468, Lorenz Cotula, *op. cit.*, 21.

¹⁴ Alan Redfern & Martin Hunter, *op. cit.*, 489.

¹⁵ *Ibid.*, 497, Gary Born, *op. cit.*, 430.

The Dilemma of Indirect Expropriation of Host States and the Right to Regulate in the International Investment Sphere

ation, unlike direct expropriation, does not entail a manifest taking or formal transfer of the title to the host State, but involves covert interference¹⁶ that efficiently incapacitates the use, enjoyment or disposal of property¹⁷ through unduly burdensome regulations.¹⁸ The aggrieved investor should be compensated, even though he retains the formal title.¹⁹ The Convention on the Protection of Foreign Property provides examples of indirect expropriation such as arbitrary taxation, prohibition of dismissal of staff, and refusal of access to raw materials.²⁰

It was argued in the UN Conference on Trade and Development that measures which cause 'effective loss of management, use or control, or a significant depreciation of the value of the assets of a foreign investor' are considered indirect taking.²¹ Some scholars notice that if the alleged measures are at the limit of regulatory activity, the affected investor will not be compensated.²² Others argue that the harmful effect of the State's regulatory actions should be compensated even if they aim to protect the environment, culture or health.²³

¹⁶ *Parkerings Compagniet AS v Republic of Lithuania case* (2007) Case No. ARB/05/8.

¹⁷ *PSEG Global Inc. and Konya Ilgin Elektrik Üretim ve Ticaret Limited Sirketi v Republic of Turkey* (2007) Case No. ARB/02/5. Rudolf Dolzer & Christoph Schreuer, *Principles of International Investment Law* (Oxford University Press, 2012), 103.

¹⁸ Gary Born, *op. cit.*, 430.

¹⁹ Rudolf Dolzer & Christoph Schreuer, *op. cit.*, 102, Bjorn Kunoy, 'Developments in Indirect Expropriation Case Law in ICSID Transnational Arbitration' (2005) 6(3) *The Journal of World Investment & Trade*, 468-469.

²⁰ Anna Luca, 'Indirect Expropriations and Regulatory Takings: What Role for the "Legitimate Expectations" of Foreign Investor?' in Giorgio Sacerdoti, *General Interests in International Investment Law* (Cambridge University Press, 2014), 61.

²¹ Rudolf Dolzer & Christoph Schreuer, *op. cit.*, 103.

²² *Ibid.*, 102.

²³ Gary Born, *op. cit.*, 430.

2. The Difference between Indirect Expropriation and the State's Right To Regulate

The issue is that the host State mostly broadens the concept of non-compensable actions under its sovereignty and regulatory prerogatives,²⁴ whereas the foreign investor will maintain that the measures appertain to indirect taking.²⁵ Making the distinction is not an easy task and needs caustic methods.²⁶ There are some guided approaches, which are discussed below.

Prejudice Doctrine

According to this doctrine, the aim of the State's adoption of harmful measures is purely to damage the investor's reputation or profits, and the interests of public welfare are not pursued.²⁷ Let us assume that the investor produces apple juices which contain 4% sugar and then a health rule is promulgated in the host State to ban any apple juices that contain more than 3% sugar. The question therefore arises whether the law should be regarded as an intentional act of the State to impede the investor's activity. This is a controversial matter. Remarkably, a State may abuse the right to regulate by issuing arbitrary measures which harm the foreign investor, such as, sequestration, oppressive administrative proceedings,²⁸ generating hostility towards the foreign investor through the media,²⁹ and practices associated with dumping, namely importing cheaper products that cause material injury to the foreign investor who produces similar products.³⁰ The Permanent Court of International Justice (PCIJ) resorted to such a doctrine in order to classify host States' acts as indirect expropriation when there is not any legal justification.³¹

Noticeably, a State may appear to show concern for the public, however it is necessary to scrutinise the previous failed attempts of a State to impede investment activity. Examples, such as the postponement of issu-

²⁴ *Ibid.*, 434.

²⁵ Rudolf Dolzer & Christoph Schreuer, *op. cit.*, 102.

²⁶ Bjorn Kunoy, *op. cit.*, 467.

²⁷ Krista Schefer, *op. cit.*, 208-209.

²⁸ Stephen Schwebel, *Justice in International Law* (Cambridge University Press, 1994), 387.

²⁹ Rudolf Dolzer & Christoph Schreuer, *op. cit.*, 99-129.

³⁰ Peter Bossche & Werner Zdouc, *op. cit.*, 39.

³¹ Bjorn Kunoy, *op. cit.*, 470.

ing a license and violating contractual obligations, can appear to be deceptive. Critics assert that attempts may be made by a State to conceal surreptitious measures,³² namely taking a crisis as an excuse to adopt measures that adversely conflict with the rights of the investors.³³

Nevertheless, some scholars affirm that the arbitrator should focus on the effect of the State's actions on foreign investment,³⁴ not tracing the State's intention to expropriate indirectly.³⁵ Article 10(5) of the Harvard Project for Responsibility of States for Injuries to the Economic Interests of Aliens excludes some States' acts from liability when such acts are commonly accepted, even if they have prejudicial effects.³⁶ Furthermore, in *Metalclad*, it was held that the motivation, and the intent, of adopting the 'Ecological Decree' need not be taken into account.³⁷ This leads to focus on the effect of the measures regardless of whether the disputed act was a *bona fide* measure.³⁸

Some scholars argue that the host State cannot arbitrarily, through its domestic legislation, nullify any principle that is universally accepted by international law (such as banning immediate compensation in cases of indirect expropriation).³⁹ On the other hand, others argue that there is no rule that is 'globally-accepted' which forbids a State to regulate otherwise.⁴⁰ In their view, it is legitimate to ban immediate compensation as long as the public interest is pursued, and the legislation has a general and impersonal character.⁴¹ Others advocate the notion of the supremacy

³² Georg Schwarzenberger, *Foreign Investment and International Law* (London: Steven & Sons, 1969), 181.

³³ Charles Brower & Stephan Schill, 'Is Arbitration a Threat or a Boon to the Legitimacy of International Investment Law?' (2009) 9(4), *The Chicago Journal of International Law*, 483.

³⁴ The same conclusion was reached in *Tecnicas Medioambientales Tecmed SA v Mexico* (2003) Case No. ARB (AF)/00/2. The tribunal asserted that the government's intentions were less significant than the impact of the measures on the investors. Peter Leon, 'Creeping Expropriation of Mining Investments: an African Perspective' (2009) 27(4), *Journal of Energy & Natural Resources Law*, 606.

³⁵ Rudolf Dolzer & Christoph Schreuer cited Reisman & Sloane, *op. cit.*, 104.

³⁶ Bjorn Kunoy, *op. cit.*, 470.

³⁷ *Ibid.*, 471.

³⁸ *Ibid.*

³⁹ Surya Subedi cited Hull in Malcolm Evans, *op. cit.*, 732.

⁴⁰ *Ibid.*, 732.

⁴¹ *Ibid.*, 732.

of international law over municipal law.⁴² The PCIJ held that a State cannot rely on its legislation to limit its international obligations.⁴³ Once a State signs an international treaty, the terms of that treaty become enforceable in the signatory State.

The Severity of the Measures

It is argued that in order to allege indirect expropriation, the measures' effects should be equivalent to direct expropriation.⁴⁴ Thus, compensation should be paid if ostensible action dramatically affected the foreign investor.⁴⁵ Deciding how to determine the deprivation of the utility of the investment is controversial. Some scholars argue that, in order to consider a breach as acute, the investor should suffer financial harm.⁴⁶ Others assert that the detriment should extend beyond economic loss⁴⁷ to include intangible interest, such as reputation and inconvenience.⁴⁸ Many tribunals base their decisions on the economic impact on the investor.⁴⁹

In the *Goetz v Burundi* case, the ICSID tribunal held that the revocation of a free-zone status halted all of the investor's activities,⁵⁰ and the impact of this measure was similar to expropriation.⁵¹ Moreover, a North American Free Trade Agreement (NAFTA) tribunal held that the refusal of the local authority to grant a construction permit to the investor was considered as indirect taking.⁵² Additionally, in the *Cement Shipping v*

⁴² Stephen Schwebel. *op. cit.*, 387-388.

⁴³ *Ibid.*, 388.

⁴⁴ Bjorn Kunoy, *op. cit.*, 473.

⁴⁵ Ian Brownlie, *op. cit.*, 518, Georg Schwarzenberger, *op. cit.*, 118.

⁴⁶ Ulrich Schroeter, 'General Provisions: Article 25' in Ingeborg Schwenzer, *Commentary on the UN Convention on the International Sale of Goods* (Oxford University Press, 2014), 409.

⁴⁷ Roy Goode, Herbert Kronke, and Ewan Mckendrick, *Transnational Commercial Law* (Oxford University Press, 2011), 297.

⁴⁸ Michael Bridge, 'Avoidance for Fundamental Breach of Contract under the UN Convention on the International Sale of Goods' (2010) 59(4), *International and Comparative Law Quarterly*, 918.

⁴⁹ Rudolf Dolzer & Christoph Schreuer, *op. cit.*, 99-129.

⁵⁰ August Reinisch, 'Introductory Note to International Centre for Settlement of Investment Disputes (ICSID): *LG&E Energy Crop., LG&E Capital Crop., LG&E International INC. v the Argentine Republic* (2007) 46(1) *International Legal Materials*, 38.

⁵¹ Rudolf Dolzer & Christoph Schreuer, *op. cit.*, 107.

⁵² Art 1110 NAFTA, *Metalclad v Mexico case*, Case No. ARB(AF)/97/1, Ru-

Egypt case, the ICSID tribunal decided that the prohibition of importing cement in the territory of Egypt, which was essential to the investor's cement distribution business,⁵³ constituted indirect taking, on the ground that such a measure paralysed the investor's activities.⁵⁴ In *Tecmed v Mexico*, the tribunal also found that the refusal to renew a permit allowing the use of landfill caused substantial deprivation of the value of the investment.⁵⁵ However, in *LG&E*, the tribunal found that the mere diminution of profits could not be equivalent to indirect expropriation.⁵⁶

Furthermore, some tribunals held that the most significant part of the measure is the effect,⁵⁷ namely it is immaterial to take into account the motive of the host State's measures which amount to indirect expropriation, such as environmental reasons⁵⁸ or political reorientation,⁵⁹ as long as the effect deprives the investor of the expected benefit of the asset.⁶⁰ Environmentalists argue that it is unrealistic to depend on the 'sole effect doctrine' and neglect the regulatory situation of a State.⁶¹ According to this doctrine, there is no room for regulating environmental matters without compensating every effected investor.⁶²

In the case of *Pope & Talbot*, the investor was obliged to pay export fees on manufactured wooden boards which exceeded 14.7 billion board feet, whereas smaller quantities were free. The investor claimed depriva-

dolf Dolzer & Christoph Schreuer, *op. cit.*, 107-108.

⁵³ Peter Leon, *op. cit.*, 605.

⁵⁴ *Middle East Cement Shipping and Handling Co. S.A. v Arab Republic of Egypt* (2002), Case No. ARB/99/6.

⁵⁵ *Tecmed v Mexico case*, Case No. ARB (AF)/00/2. Anna Luca in Giorgio Sacerdoti, *op. cit.*, 64, Bjorn Kunoy, *op. cit.*, 472.

⁵⁶ Charles Brower & Stephan Schill, *op. cit.*, 486, Zeyad Alqurashi, 'Indirect Expropriation in the Field of Petroleum' (2004) 5(6) *The Journal of World Investment & Trade*, 911.

⁵⁷ *Compania de Aguas del Aconquija SA and Vivendi Universal SA v Argentine Republic case*, Case No. ARB/97/3, Alan Redfern & Martin Hunter, *op. cit.*, 500.

⁵⁸ *Compania del Desarrollo de Santa Elena SA v Republic of Costa Rica case*, Case No. ARB/96/1.

⁵⁹ *Phillips Petroleum Co. Iran v The Islamic Republic of Iran case*. 21 IRAN-U.S. C.T.R.

⁶⁰ Alan Redfern & Martin Hunter, *op. cit.*, 500.

⁶¹ Rudolf Dolzer, 'Indirect Expropriation: New Developments?' (2003) 11 *New York University Environmental Law Journal*, 92.

⁶² *Ibid.*, 92.

tion of economic interests. The claim was based on the reduction in quantity of exports in order to pass the boundaries without fees. The tribunal held that the deprivation was not substantial enough to amount to indirect expropriation.⁶³ In this respect, in *Siemens AG v Argentine Republic*, the tribunal noted that each State's isolated measure might not amount to indirect expropriation, but the cumulative effect of several 'creeping' measures might deprive the investor of the use, value and enjoyment of the investment.⁶⁴

Regulatory Power

A State has the power to regulate in certain circumstances. This power is regarded as an exception for not compensating the affected investor even if the action taken could be interpreted as an indirect expropriation. There are a number of conditions governing this exemption.⁶⁵

First, the State should not breach any contractual obligations that it has towards a foreign investor. Second, the State can create regulatory statutes merely when such statutes are non-discriminatory, i.e. they apply both to domestic and foreign investors. Finally, the measure should appeal to the general welfare.⁶⁶ This was held in *Methanex Corporation v United States of America* when the State banned a harmful gasoline additive containing methanol while the investor was a producer of this substance.⁶⁷ The US Model BITs articulate that legitimate public objectives do not constitute indirect taking.⁶⁸

Many investment treaties, such as the North American Free Trade Agreement⁶⁹ (NAFTA),⁷⁰ provide significant protection to the foreign in-

⁶³ Rachel Edsall, 'Indirect Expropriation under NAFTA and DRCAFTA: Potential Inconsistencies in the Treatment of State Public Welfare Regulations' (2006) 86, *Boston University Law Review*, 942-943.

⁶⁴ *Siemens AG v Argentine Republic*, Case No. ARB/02/8. Alan Redfern & Martin Hunter *op. cit.*, 501, *Enron Creditors Recovery Corporation and Ponderosa Assets, L.P. v Argentine Republic*, [2007] Case No. ARB/01/3.

⁶⁵ Charles Brower & Stephan Schill, *op. cit.*, 484.

⁶⁶ Alan Redfern & Martin Hunter, *op. cit.*, 501.

⁶⁷ *Methanex Corporation v United States of America*. Case No. 44 ILM 1345 [2005], *Ibid.*, 501, Gary Born, *op. cit.*, 434.

⁶⁸ Rudolf Dolzer & Christoph Schreuer, *op. cit.*, 102-103.

⁶⁹ Between Canada, Mexico and the United States.

⁷⁰ Also US-Argentina BIT Article 3(1), Energy Charter Treaty & Jordan – USA BIT. Surya Subedi in Malcolm Evans, *op. cit.*, 744, Gary Born, *op. cit.*, 412-430, Alan Redfern & Martin Hunter, *op. cit.*, 496.

vestor. In particular, NAFTA prohibits direct and indirect expropriation except for a public purpose.⁷¹ Regulations for public purpose should be implemented in a non-discriminatory manner and in accordance with due process of law. Moreover, the State should compensate the foreign investor adequately, promptly and effectively.⁷² For example, a new legislation outlaws all gambling halls, which mostly belong to foreign investors, to preserve public morals,⁷³ or a new decree bans billboard advertising on highways to reduce accidents. This dramatically affects the investor.⁷⁴ In these cases, if the State respects the international minimum standard of fair and equitable treatment, it will not generally be accused of indirect expropriation.⁷⁵ However, in *Compania del Desarrollo de Santa Elena SA v Republic of Costa Rica*, the ICSID tribunal affirmed that the State should compensate the investor for deprivation of the interest, although the purpose of the indirect expropriation was legitimate and classified as a public purpose.⁷⁶ Moreover, some commentators suggest that even if the State duly uses the right to regulate, the investor should be compensated for the results of the action when such results significantly impair the investor's property.⁷⁷ Nevertheless, changing economic, political or social circumstances compel the State to change its legal status.⁷⁸ The use of regulatory power is likely to be significantly limited if a large volume of adversely affected investors seek compensation.⁷⁹ Fur-

⁷¹ Surya Subedi in Malcolm Evans, *op. cit.*, 740.

⁷² Bronwyn Pavey & Tim Williams, 'The North American Free Trade Agreement: Chapter 11' (26 February 2003) <<http://publications.gc.ca/Collection-R/LoPBdP/inbrief/prb0254-e.htm>> accessed 13 May 2015, Joy Cheria, *Investment Contracts and Arbitration: The World Bank Convention on the Settlement of Investment Disputes*, (Leyden: A. W. Sijthoff, 1975), 88-89.

⁷³ Andrew Newcombe, 'The Boundaries of Regulatory Expropriation in International Law' (2005) 20(1), *Foreign Investment Law Journal*, 3-4.

⁷⁴ *Ibid.*, 3-4.

⁷⁵ *Ibid.*, 40. This conclusion was reached in: *Parkerings-Compagniet v Republic of Lithuania*. The tribunal noted that a State is prohibited to act unfairly or inequitably towards foreign investors in the exercise of its legitimate power. Alan Redfern & Martin Hunter, *op. cit.*, 492.

⁷⁶ *Compania del Desarrollo de Santa Elena SA v Republic of Costa Rica*. Case No. ARB/96/1.

⁷⁷ Zeyad Alqurashi, *op. cit.*, 915.

⁷⁸ *Ibid.*, 910.

⁷⁹ Rudolf Dolzer & Christoph Schreuer, *op. cit.*, 120, Charles Brower & Stephan Schill, *op. cit.*, 483.

thermore, some scholars assert that the legal stability requirement does not require a State's legal system to remain frozen in the time of the investment⁸⁰ and not all States' measures affecting foreign property can be termed as an indirect expropriation,⁸¹ such as subjecting the foreign assets to taxation⁸² or trade restrictions regarding licenses or quotas.⁸³ Others argue that, under the principles of justice and equity, no State is allowed, whatever the purpose is, to enact legislation or issue measures that are equivalent to indirect expropriations without an appropriate compensation.⁸⁴ In the *Iran-US* case, the tribunal affirmed that even if the regulations are lawful, the aggrieved investor should be compensated.⁸⁵ The UN Declaration on Permanent Sovereignty over Natural Resources⁸⁶ emphasises that a State should exercise its sovereignty over its natural resources.⁸⁷ This concept reinforces the legitimacy of regulating measures for a public purpose.

Measures' Duration

In the case of *LG&E International Inc v Argentina*, the tribunal considered the duration of the State's measures to decide whether they amount to indirect expropriation.⁸⁸ In *S.D Myers v Canada*, the investor was a firm engaged in producing PCBs (Polychlorinated Biphenyls) in Canada and exporting them to the US. However, Canada imposed an export ban. The tribunal refused to regard such a measure as indirect expropriation due to the temporary nature of the measure.⁸⁹ Furthermore, in the case of *Suez v Argentina*, the tribunal refused to consider the refusal to adjust the tariffs as an indirect taking on the ground that the effect should amount to 'a substantial, permanent deprivation' of the investment.⁹⁰ Moreover, in

⁸⁰ Alan Redfern & Martin Hunter, *op. cit.*, 491.

⁸¹ Ian Brownlie, *op. cit.*, 509.

⁸² Krista Schefer, *op. cit.*, 207.

⁸³ Ian Brownlie. *op. cit.*, 509.

⁸⁴ Surya Subedi cited Hull in Malcolm Evans, *op. cit.*, 732.

⁸⁵ Veijo Heiskanen, 'The Doctrine of Indirect Expropriation in Light of the Practice of the Iran-United States Claims Tribunal' (2007) 8(2) *The Journal of World Investment & Trade*, 218-227.

⁸⁶ **Permanent Sovereignty over Natural Resources, General Assembly Resolution, 1803 (XVII)**, New York (14 December 1962).

⁸⁷ Ian Brownlie, *op. cit.*, 516-517.

⁸⁸ Alan Redfern & Martin Hunter, *op. cit.*, 498.

⁸⁹ Zeyad Alqurashi, *op. cit.*, 909-910.

⁹⁰ Rudolf Dolzer & Christoph Schreuer, *op. cit.*, 110-111.

the *Telenor v Hungary* case, the tribunal found that the effects of imposing a levy were not indirect expropriation on the ground that it was not a permanent action.⁹¹ However, if the investor's main activity is producing seasonal goods, and the State has adopted impermanent measures, this will hinder the production process, as producing such goods at the end of their season will impair their value.⁹² Remarkably, it is argued that financial subsidiaries given by host States to bodies which practice the same activity as the foreign investor may have adverse effects on the foreign investor and may be considered as indirect taking.⁹³ On the contrary, the PCIJ considered such subsidiaries as transient circumstances, which are subject to change.⁹⁴

Investor's Control

By this criterion, the affected investor loses the ability to control the project and make decisions due to the State's restrictive measures. Therefore, deprivation of the economic benefit of an investment does not necessarily mean that expropriation has occurred as long as the investor maintains control over his investment.⁹⁵ However, the sole control over the entity of the investment, following the destruction of the economic purpose of the investment through a new legislation, may be worth nothing.⁹⁶

An ICSID tribunal held that although Argentina violated the contract by its measures, which caused less profit, there was no indirect expropriation as long as the investor remained in control of the investment.⁹⁷ Further, in *Tippetts*, the tribunal rejected the allegation by the claimant, who owned 50% in a joint venture with an Iranian company, that the appointment of a new manager by the Iranian government constituted an indirect expropriation.⁹⁸ This measure did not affect the claimant's ability to par-

⁹¹ *Ibid.*, 113.

⁹² Ulrich Schroeter in Ingeborg Schwenzer, *op. cit.*, 179.

⁹³ Peter Bossche & Werner Zdouc, *op. cit.*, 38-39.

⁹⁴ *The Oscar Chinn, United Kingdom v Belgium, Judgment*, PCIJ Series A/B No 63. Rudolf Dolzer & Christoph Schreuer, *op. cit.*, 104-105.

⁹⁵ Rudolf Dolzer & Christoph Schreuer, *op. cit.*, 117.

⁹⁶ *Ibid.*, 118.

⁹⁷ *LG&E Energy Crop and others v Argentina Republic case*, Case No. ARB/02.

⁹⁸ Zeyad Alqurashi, *op. cit.*, 907.

ticipate in the management and to control the enterprise.⁹⁹ Conversely, in *Payne*, the tribunal held that such measures effectively reduced the investor's control.¹⁰⁰

Proportionality Test

In order to determine the lawfulness of a measure, some tribunals compare the impact of such regulations on the investor with the advantages of public policy.¹⁰¹ In *S.D. Myers v Canada*,¹⁰² the tribunal balanced the purpose and effects of the measure and investigated whether there was a capacity to adopt an alternative measure¹⁰³ with lesser effect on the investment. This test was adopted in order to determine whether the measure fell within the State's regulatory power.¹⁰⁴

In *Tecmed v Mexico*¹⁰⁵ the government was under pressure from the local community to oppose the investor's operation and location, which caused hazardous waste disposal in an urban area of Mexico. The national authority responded to such opposition and refused to renew the investor's permit to use the facility in order to protect the environment and public health. The tribunal made a comparison between the significance of achieving the State's goals and the significance of preventing the harmful effects on the investor. It found that responding to the community's concerns was not regarded as a legitimate purpose and such a pressure on the government did not cause an urgent situation. According to the suitability and reasonability test, the government could design measures that did not excessively affect the investor's interests. The tribunal found that the harmful effects outweighed the State's targets. Consequently, it amounted to indirect expropriation.¹⁰⁶ The European Court of Human Rights, for example, held that 'the State's responsibility in envi-

⁹⁹ *Ibid.*, 907.

¹⁰⁰ Hassan Sedigh, 'What Level of Host State Interference Amounts to a Taking under Contemporary International Law?' (2001) 2(4) *The Journal of World Investment & Trade*, 649-650.

¹⁰¹ Krista Schefer, *op. cit.*, 210 & Caroline Henckels, 'Indirect Expropriation and the Right to Regulate: Revising Proportionality Analysis and the Standard of Review in Investor-State Arbitration' (2012) 15(1) *Journal of International Economic Law*, 228.

¹⁰² *Feldman V Mexico case*, Case No. ARB(AF)/99/1.

¹⁰³ Anna Luca in Giorgio Sacerdoti, *op. cit.*, 58-74.

¹⁰⁴ Caroline Henckels, *op. cit.*, 230.

¹⁰⁵ *Ibid.*, 230-233.

¹⁰⁶ *Ibid.*

ronmental cases may form a failure to regulate private industry.¹⁰⁷ On the other hand, some commentators argue that pressure on the government from community may arise from the people affected by an investor's acts. However, this may merely constitute an urgent situation.¹⁰⁸ Thus, there is no requirement for permanent measures against the investor.

Investor's Expectations

Legitimate expectations do not only include the State's contractual obligations being fulfilled, but also the status of the State's legal framework not dramatically changing at the time of the investment.¹⁰⁹ The definition of 'substantial deprivation of reaching prospective aims'¹¹⁰ is not found in investment contracts, leaving the arbitrator without a benchmark.¹¹¹ In the case of *Occidental Exploration & Production Company v Ecuador*, the tribunal concluded that the stability of a legal framework is a fundamental element of fair and equitable treatment, especially if the BIT requires such stability.¹¹² In the case of *LG&E International Inc v Argentina*, the tribunal¹¹³ noted that the investor's expectations should be based on the conditions offered by the State and when such expectations are violated, the investor should be compensated for damages.¹¹⁴

Some legal changes that happen within the boundaries of a normal reform of a State should ideally be predicted by any prudent investor. Thus, such transformations do not violate the investor's expectations.¹¹⁵ Changing circumstances, as well as the adoption of new legislation, which may reduce the profitability of the investment project, reflect the risk which is

¹⁰⁷ Antenor Wolf, 'Human Rights and the Regulation of Privatized Essential Services' (2013) 60(2) *Netherlands International Law Review*, 174-175.

¹⁰⁸ *Ibid.*, 178.

¹⁰⁹ Rudolf Dolzer & Christoph Schreuer, *op. cit.*, 115.

¹¹⁰ Roy Goode, *et al.*, *op. cit.*, 297.

¹¹¹ Eduardo Grebler, 'Fundamental Breach of Contract under the CISG: A Controversial Rule' (2007) 101 *American Society of International Law*, 413.

¹¹² Michele Potesta, 'Legitimate Expectations in Investment Treaty Law: Understanding the Roots and the Limits of a Controversial Concept' (2013) 28(1) *ICSID Review*, 111.

¹¹³ Alan Redfern & Martin Hunter, *op. cit.*, 290.

¹¹⁴ *Ibid.*, 491.

¹¹⁵ Rudolf Dolzer & Christoph Schreuer, *op. cit.*, 115.

entailed in an investment.¹¹⁶ In the case *Saluka Investment v Czech*, the tribunal held that the State's right to regulate cannot be frozen and that the investor should not expect that the circumstances at the time of investment remain unchanged.¹¹⁷

The concept of investor's expectations received much criticism for its bias towards investment.¹¹⁸ Reliance on the affected investor's expectations could be an easy way to demonstrate that the measures constitute indirect taking.¹¹⁹ The unconditional protection of legitimate expectation could fetter the State's right to regulate.¹²⁰ An objective criterion should be added to investment treaties to specify the investors' expectation, namely, what a reasonable investor of the same kind in the same circumstances is entitled to expect.¹²¹ Some scholars relate the expectations of the aggrieved investor to the original purpose of his investment,¹²² which can be determined by recognising the nature of the investor's activities—whether he is an undertaker, producer or supplier.¹²³

The Situation of the State

According to this yardstick, the State's actions are carried out pursuant to goals associated with necessity, security, and minimising investments' disadvantages in the society.

The Defence of Necessity

A State might confront extraordinary circumstances that make the implementation of the contractual commitments difficult to fulfill (such as economic crises or wars).¹²⁴ Some scholars assert that exercising police power in wartime is lawful even if the associated measures are regarded as indirect expropriation.¹²⁵ The US Restatement of Foreign Relations Law recognises that a State is not liable for any economic disadvantages

¹¹⁶ Michele Potesta, *op. cit.*, 90.

¹¹⁷ *Ibid.*, 112.

¹¹⁸ Anna Luca in Giorgio Sacerdoti, *op. cit.*, 64.

¹¹⁹ Michael Bridge, *op. cit.*, 912.

¹²⁰ Michele Potesta, *op. cit.*, 88.

¹²¹ Ulrich Schroeter in Ingeborg Schwenzer, *op. cit.*, 179, Alan Redfern & Martin Hunter, *op. cit.*, 290.

¹²² Roy Goode, *et al.*, citing Mullis, *op. cit.*, 300.

¹²³ *Packaging machine case* [2009] Case No. 4A_68/2009.

¹²⁴ Giorgio Sacerdoti, *op. cit.*, 8-9.

¹²⁵ Ian Brownlie, *op. cit.*, 514.

The Dilemma of Indirect Expropriation of Host States and the Right to Regulate in the International Investment Sphere

resulting from non-discriminatory, *bona fide* regulations for a public purpose under the police power of a State (such as forfeiture for crime).¹²⁶ Under such circumstances a State is not responsible for compensating affected foreign investors.¹²⁷

The US Model BITs permit the adoption of 'non-precluded measures' in the case of emergency.¹²⁸ The International Law Commission (ILC) issued strict conditions under which this measure could be used. Firstly, the country faces 'grave and imminent peril'. Secondly, the State's adopted measures are the only route to safeguard public interests. Thirdly, the State has not contributed to the necessity situation,¹²⁹ for example by declaring a war with other countries. Such conditions prevent, to a large extent, any prejudicial application of measures which may amount to indirect expropriation. In the case of *CMS v Argentina*, the tribunal held that indirect expropriation had not occurred when Argentina adopted measures freezing agreed tariffs, de-dollarising the economy and restricting public debt¹³⁰ during a financial crisis, even though such measures had a great impact on the investor.¹³¹

The State's National Security

National security may be threatened if strategic assets, such as aerospace, nuclear sector, weapon production, transportation and communication, are under the control of a foreign investor.¹³² The investor may misuse the access to secret information or influence companies to adopt strategies that benefit the investor's home State.¹³³ In such a case, the State may adopt measures to safeguard its national security, such as withdrawal or denial of certain authorisations that may adversely affect the investor. Such measures are unlikely to be regarded as an indirect expropriation. This is especially the case if the investor violates the 'Santiago

¹²⁶ Susan Karamanian, 'The Place of Human Rights in Investor-State Arbitration' (2013) 17(2) *Lewis & Clark Law Review*, 434.

¹²⁷ *Ibid.*, 434.

¹²⁸ Giorgio Sacerdoti, *op. cit.*, 11.

¹²⁹ *Ibid.*, 11.

¹³⁰ *Ibid.*, 4, 11.

¹³¹ Rudolf Dolzer & Christoph Schreuer, *op. cit.*, 113.

¹³² Michele Barbieri, 'Sovereign Wealth Funds as Protected Investors under BITs and the Safeguard of the National Security of Host States' in Giorgio Sacerdoti, *op. cit.*, 131-133.

¹³³ *Ibid.*, 131-133.

Principles'.¹³⁴ These Principles¹³⁵ impose obligations on the investor, such as the prohibition of misusing investor's influence, in order to protect local security.¹³⁶ Measures in significant industries, such as inland shipping, are often excluded from the protection of the BIT.¹³⁷ Consequently, the State can freely regulate the affairs of this sector.

Impact of Investment

An investment may severely affect the local life of a State contrary to what was foreseen. For example, investments may cause severe impact on environmental degradation, the livelihood of the nationals, cultural identity, political stability and public morals.¹³⁸ Such consequences increase the likelihood of governmental regulations, which may distinctly disadvantage the investor. Thus, a State may regulate against some investment activities, such as depriving a community of its holy properties.¹³⁹ These activities would not be protected, even if such regulations amount to indirect expropriation.¹⁴⁰ If, for example, an investor uses cheap colours to manufacture clothes, and these clothes cause skin cancer, consumer protection associations may object to such action and invoke the interference of the government to preserve consumer safety.

Some claim that suitable governmental legislation cannot be achieved if every single negatively affected investor seeks recompense.¹⁴¹ An IC-SID tribunal observed that privatising essential services, such as electricity, gas and water utilities, to foreign investment companies may affect millions of people.¹⁴² Thus, it is vital to endorse regulatory reforms to guarantee that foreign investment privatisation works properly and to ensure that it is sufficient and reasonably priced. Furthermore, States should adopt the necessary measures to protect affected people from the negative outcomes of investments.¹⁴³

¹³⁴ Ibid., 136-149.

¹³⁵ These Principles are not binding, but when adopted by investment treaties, their nature converts to binding principles. Sovereign Wealth Funds: Generally Accepted Principles and Practices 2008 ('Santiago Principles').

¹³⁶ Michele Barbieri in Giorgio Sacerdoti, *op. cit.*, 149-151.

¹³⁷ Gary Born, *op. cit.*, 434.

¹³⁸ Peter Bossche & Werner Zdouc, *op. cit.*, 14, 17.

¹³⁹ Susan Karamanian, *op. cit.*, 435.

¹⁴⁰ Ibid., 435.

¹⁴¹ Peter Leon, *op. cit.*, 610.

¹⁴² Antenor Wolf, *op. cit.*, 170.

¹⁴³ Ibid., 171-174.

Contractual Obligations and the Host State's Promises

The violation of contractual obligations is a valid criterion to assess the extent of the illegality of indirect expropriation.¹⁴⁴ If the arbitrator belongs to a country governed by civil law, which glorifies the contract as a source of obligation, it is likely that priority will be given to contractual obligations even if the measures are adopted for a public purpose.¹⁴⁵ In the case of *Biwater Gauff v Tanzania*, the investor claimed that the annulment of the contract without cause violated the contractual obligations and amounted to indirect expropriation.¹⁴⁶ The tribunal rejected the claim and regarded the formal termination of the contract as an ordinary contractual characteristic, which could not amount to indirect expropriation.¹⁴⁷

In *Siemens AG v Argentina*, the ICISD tribunal held that the measure was indirectly expropriative as the State used its regulatory power over the investor instead of acting as a contracting party. The contract was invalidated by a unilateral decision through precedential decree.¹⁴⁸ In order to be safe, an 'umbrella clause' needs to be included in the contract. This means that all contractual obligations between the State and home State of the investor will be protected under the BIT. This puts pressure on the host State to respect the protection terms of the contract.¹⁴⁹

Furthermore, a new regulation which breaches a State's promises¹⁵⁰ constitutes indirect expropriation in most circumstances.¹⁵¹ In many cases, the State offers assurances against any legal changes which would be unfavourable to the investor's interests in order to reinforce the investment. These assurances create acquired rights for investors. A failure by the State to respect such assurances may amount to indirect expropriation

¹⁴⁴ This was held in the case *Continental Casualty v Argentina*. Michele Potesta, *op. cit.*, 101, Surya Subedi in Malcolm Evans, *op. cit.*, 749.

¹⁴⁵ Eduardo Grebler, *op. cit.*, 411, Rudolf Dolzer & Christoph Schreuer, *op. cit.*, 122.

¹⁴⁶ Bjorn Kunoy, *op. cit.*, 483.

¹⁴⁷ Rudolf Dolzer & Christoph Schreuer, *op. cit.*, 110.

¹⁴⁸ *Siemens AG v Argentina case*, Case No. ARB/02/8. Peter Leon, *op. cit.*, 607-608.

¹⁴⁹ Margaret Moses *op. cit.*, 245.

¹⁵⁰ This was held in *Parkerings-Compagniet AS v Republic of Lithuania* (2007) Case No. ARB/05/8.

¹⁵¹ Michele Potesta, *op. cit.*, 89.

because it deprives the investor of the investment's benefits.¹⁵² This conclusion was reached in the case of *CME v Czech Republic*.¹⁵³ Some scholars assert that the claim of indirect expropriation does not immunise investors from regulatory alteration unless the State promised to refrain from such modification.¹⁵⁴

In the case of *Revere Copper v OPIC*, the parties concluded an agreement which did not impose any further taxes on the investor.¹⁵⁵ However, the newly elected government announced that an increase in the revenues had to be paid by the investor. The tribunal found that such a measure impeded the investor from effectively controlling the enterprise. As a result, the government decision was repudiated.¹⁵⁶ Furthermore, in the case of *Metalclad v US Investor*,¹⁵⁷ the investor had received guarantees from the federal authorities that he would be granted all the required licenses in the investment's life. Despite this, the local authority refused to give a building authorisation for an investment plant. The tribunal regarded this measure as an indirect expropriation.¹⁵⁸ Moreover, a United Nations Commission on International Trade Law (UNCITRAL) tribunal decided in favour of one investor, who claimed against the policy adopted by the Indian government, which caused excessive delay (nine years) in order to enforce an international arbitration award. The government had breached its promise to provide 'effective means' in the investment dispute resolution process.¹⁵⁹

Obligations under International Conventions

A problem arises when a State is committed to an international obligation that contradicts the BIT's obligations of protecting foreign investors. For example, Indonesia is bound by such international obligations. It is a party to the Convention on Biological Diversity and Statement of Forest Principles¹⁶⁰ that commits States to ban any procedures that are likely to

¹⁵² Alan Redfern & Martin Hunter, *op. cit.*, 498-500.

¹⁵³ *Ibid.*, 499.

¹⁵⁴ Charles Brower & Stephan Schill, *op. cit.*, 488.

¹⁵⁵ *Revere Copper and Brass Incorporated v Overseas Private Investment Corporation* (1980) Case No. 628 F.2d 81.

¹⁵⁶ Rudolf Dolzer & Christoph Schreuer, *op. cit.*, 105-106.

¹⁵⁷ Bjorn Kunoy, *op. cit.*, 472.

¹⁵⁸ *Ibid.*, 472.

¹⁵⁹ Vyoma Jha, 'International Investment Treaty Implications for the Indian Position on Nuclear Liability' (2014) 17(1) *Journal of Risk Research*, 82-83.

¹⁶⁰ Kyla Tienhaara, 'What You Don't Know Can Hurt You: Investor-State Dis-

have considerable impact on the environment.¹⁶¹ Indonesian Forestry Law was promulgated to protect forests. It helps regulate erosion, hydrology, and the preservation of plant and animal diversity.¹⁶² Mining investment was affected by such law which prohibits open-cast mining in protected forests. It was difficult to claim that such a law amounted to indirect taking because the law prohibits only surface mining in specific areas, whereas underground mining is still permitted. Consequently, the effects were not serious.¹⁶³

Additionally, the World Health Organization (WHO) Framework Convention on Tobacco Control (FCTC) obliges the parties to adopt regulatory measures in production and taxation of tobacco products.¹⁶⁴ The FCTC also encourages parties to adopt stricter measures in order to protect public health.¹⁶⁵ A tobacco company began arbitration proceedings to challenge an Australian legislation which imposed requirements for cigarette packs on the grounds that such measures constituted indirect expropriation.¹⁶⁶ The Australian legislation provided that plain cigarette packs had to contain graphic health warning. The New Zealand government is waiting for the decision before issuing similar anti-smoking legislation.¹⁶⁷ Philip Morris also brought a claim against Uruguay for new 'cigarette-labeling measures' which required manufacturers to increase the size of illustrative health warnings from 50% to 80% on the front and back of cigarette packs. Philip Morris described the requirement as 'excessive' and that it would destroy its trademark, adding that 50% sufficed to warn consumers about the harmful effects of smoking.¹⁶⁸ The host State should demonstrate the stimuli to adopt such measures, such as the prevalence of tobacco in its territory, the public health crisis and the ab-

putes and the Protecting of the Environment in Developing Countries' (2014) 6(4) *Global Environmental Politics*, 87-92.

¹⁶¹ Art 14 Convention on Biological Diversity Foreign. Lorenz Cotula, *op. cit.*, 73.

¹⁶² Kyla Tienhaara, *op. cit.*, 87-92.

¹⁶³ *Ibid.*, 87-92.

¹⁶⁴ WHO Framework Convention on Tobacco Control 2005.

¹⁶⁵ Tsai Lin, 'The Status of FCTC in the Interpretation of Compensable Indirect Expropriation and the Right to Adopt 'Stricter' Tobacco Control Measures under Bits' (2014) 9(1) *Asian Journal of WTO & International Health Law and Policy*, 125-127.

¹⁶⁶ Lorenz Cotula, *op. cit.*, 25.

¹⁶⁷ *Ibid.*, 25.

¹⁶⁸ Tsai Lin, *op. cit.*, 127-129.

sence of alternative methods with a lesser effect on the investors, in order for such measures to not be regarded as indirect expropriation.¹⁶⁹

Human Rights

One of the core principles of the UN Human Rights Council is the duty of a State to protect human rights. Foreign investors should also bear such a basic responsibility.¹⁷⁰ Moreover, refraining from indirect expropriation measures reflects the duty to respect human rights.¹⁷¹ Many municipal laws, such as Cambodia's Investment Act 1994, restrict the government's power to expropriate investments indirectly.¹⁷²

In 2013, a factory building collapsed and 1000 workers were killed in Bangladesh whilst working for a foreign investment.¹⁷³ A State should not neglect individuals who work under inadequate conditions. On the contrary, a State should promote and conform to the rules on minimum working conditions of the International Labour Organisation (ILO).¹⁷⁴ Such measures should not be interpreted as indirect expropriation.¹⁷⁵ Suppose, for example, that a petroleum company concluded a contract with a State to manufacture petrochemical products. The company could subsequently be charged under a new legislation on air quality. According to the new legislation, the company is required to install antipollution devices. It could claim that it is impossible to conform to such regulations due to time and financial constraints.¹⁷⁶ In such a case, a tribunal is likely to favour international legal obligations in the field of ecosystems, regardless of the investor's interests. Moreover, some found that if an investment is in an uncompetitive field, the State could issue a regulation permitting national enterprises to enter such field, which may adversely harm the investor. This State action could be interpreted as promoting the rights of the State's citizens.¹⁷⁷

¹⁶⁹ Ibid., 139.

¹⁷⁰ Surya Subedi in Malcolm Evans, *op. cit.*, 739-740.

¹⁷¹ Susan Karamanian, *op. cit.*, 433.

¹⁷² Art 9 Cambodia's Investment Act 1994. Lorenz Cotula, *op. cit.*, 22.

¹⁷³ BBC News, 'Bangladesh Factory Collapse Toll Passes 1,000' (10 May 2013) <<http://www.bbc.co.uk/news/world-asia-22476774>> accessed 20 May 2015.

¹⁷⁴ Lorenz Cotula, *op. cit.*, 84.

¹⁷⁵ Ibid., 23.

¹⁷⁶ Joy Cherian, *Investment Contracts and Arbitration*, (Leyden, A.W. Sijthoff, 1975), 96-99.

¹⁷⁷ Susan Karamanian, *op. cit.*, 428-437.

Some forcefully argue that a State has a duty to adopt measures in order to safeguard citizens' life, health, property and safety. The States cannot justify a failure to fulfil these duties by arguing that such responsibilities can be waived on the pretext of not harming foreign investors.¹⁷⁸ Thus, such measures would not attract a State's liability even if they are inconsistent with BITs.¹⁷⁹ However, in *S.A. v Argentina*, the tribunal held that the State must respect human rights and BIT's obligations equally. Thus, the tribunal refused to outweigh the necessity of the State's measures to preserve the right to water over the investor's rights.¹⁸⁰ States may rely on human rights, such as the rights to health, labour and a clean environment, as a defence to their acts which contradict the investor's interests.¹⁸¹

3. Conclusion

The abstract language of most international investment treaties and contracts makes the distinction between indirect expropriation and the State's right to regulate imprecise and unpredictable.¹⁸² It is advisable to include a clause in the investment contract that requires the investor to comply with social and environmental matters. This can assist States in adopting measures for sustainable development goals.¹⁸³

Adding a legality requirement term into the contract will force investors to comply with the applicable law in order to be protected. This will enable governments to regulate against investments which violate their rules without being accused of indirect expropriation.¹⁸⁴ Treaties may not penalise States when they regulate in order to protect public welfare.¹⁸⁵ For instance, the US Model BITs expel from indirect expro-

¹⁷⁸ Kojo Yelapaala, 'Fundamentalism in Public Health and Safety in Bilateral Investment Treaties' (2008) 3(1) *Asian Journal of WTO & International Health Law and Policy*, 493-492.

¹⁷⁹ *Ibid.*, 493-492.

¹⁸⁰ *Suez, Sociedad General de Arguvas de Barcelona, S.A. v Argentina* case. IC-SID Case No. ARB/03/19.

¹⁸¹ Susan Karamanian, *op. cit.*, 432.

¹⁸² Eduardo Grebler, *op. cit.*, 413.

¹⁸³ Lorenz Cotula, *op. cit.*, 29.

¹⁸⁴ *Ibid.*, 29.

¹⁸⁵ Susan Karamanian, *op. cit.*, 434.

priation 'non-discriminatory regulatory actions ... that are designed and applied to protect legitimate public welfare objectives.'¹⁸⁶ Worrying phenomena occur when there is an urgent need to regulate but the government is reluctant to do so on the ground that the arbitral tribunal may consider such a conduct as an indirect expropriation,¹⁸⁷ especially if the applicable BIT does not contain a clause permitting legislation according to the public purpose. Article 31(1) of the Vienna Convention on the Law of the Treaties provides that the treaty is to be interpreted in the light of the treaty's purpose.¹⁸⁸ The main purpose of the BITs is to protect foreign investments. Interpreting the BITs in the light of their purpose would result in an outcome which would favour the foreign investor.¹⁸⁹ Bolivia, Ecuador and Venezuela withdrew from the ICSID, arguing that investment tribunals erode State's sovereignty and incline towards foreign investors.¹⁹⁰ Some countries, such as the US and Canada, revised their BITs to restrict the scope of investor protection.¹⁹¹

On the other hand, it is expedient to specify in the investment contract that a foreign investor's property should not be disturbed by any action, except from those which pursue a public purpose.¹⁹² Peru avoided affecting the investment sector by promulgating new legislation which included a provision indicating that all contracts which were concluded before the promulgation remained valid until the expiry date of such contracts.¹⁹³ So the investments' activities continued by virtue of the non-retroactive effect of the legislation.¹⁹⁴ The analysis should be underpinned by using case law. Otherwise, it is difficult to ensure predictability in advance and this may negatively affect the investor or the host State.

¹⁸⁶ *Ibid.*, 434.

¹⁸⁷ Zeyad Alqurashi, *op. cit.*, 912.

¹⁸⁸ Vienna Convention on the Law of Treaties 1969.

¹⁸⁹ Bjorn Kunoy, *op. cit.*, 471.

¹⁹⁰ Gary Born, *op. cit.*, 419.

¹⁹¹ *Ibid.*, 420.

¹⁹² Georg Schwarzenberger, *op. cit.*, 118.

¹⁹³ Kyla Tienhaara, *op. cit.*, 92-93.

¹⁹⁴ *Ibid.*, 92-93.

Works Cited

Primary Sources

Legislation

Cambodia's Investment Act 1994

Draft Convention on International Responsibility of States for Injuries to Aliens 1961

Permanent Sovereignty over Natural Resources, General Assembly Resolution, 1803 (XVII), New York (14 December 1962)

Sovereign Wealth Funds: Generally Accepted Principles and Practices ('Santiago Principles') 2008

Vienna Convention on the Law of Treaties 1969

WHO Framework Convention on Tobacco Control 2005

Case Law

Compania de Aguas del Aconquija SA and Vivendi Universal SA v Argentine Republic. Case No. ARB/97/3

Compania del Desarrollo de Santa Elena SA v Republic of Costa Rica. Case No. ARB/96/1

Enron Creditors Recovery Corporation (formerly Enron Corporation) and Ponderosa Assets, L.P. v Argentine Republic, [2007] Case No. ARB/01/3

Feldman V Mexico. Case No. ARB(AF)/99/1

LG&E Energy Crop and others v Argentina Republic. Case No. ARB/02

Metalclad v Mexico. Case No. ARB(AF)/97/1

Methanex Corporation v United States of America, UNCITRAL

Middle East Cement Shipping and Handling Co. S.A. v Arab Republic of Egypt [2002] Case No. ARB/99/6

Oscar Chinn, United Kingdom v Belgium, Judgment, PCIJ Series A/B No 63

Packaging machine [2009] Case No. 4A_68/2009

Parkerings-Compagniet AS v Republic of Lithuania [2007] Case No. ARB/05/8

Phillips Petroleum Co. Iran v The Islamic Republic of Iran. 21 IRAN-U.S. C.T.R.

PSEG Global Inc. and Konya Ilgin Elektrik Üretim ve Ticaret Limited Sirketi v Republic of Turkey [2007] Case No. ARB/02/5

Siemens AG v Argentine Republic. Case No. ARB/02/8
Suez, Sociedad General de Aguas de Barcelona, S.A. v Argentina. IC-
SID Case No. ARB/03/19
Tecmed v Mexico. Case No. ARB (AF)/00/2

Secondary Sources

Books

Born G, *International Arbitration: Law and Practice*, Netherlands: Wolters Kluwer, 2012
Bossche P & Zdouc W, *The Law and Policy of the World Trade Organization*, Cambridge University Press, 2014
Brownlie I, *Principles of Public International Law*, Oxford University Press, 2003
Cherian J, *Investment Contracts and Arbitration: The World Bank Convention on the Settlement of Investment Disputes*, Leyden: A. W. Sijthoff, 1975
Cotula L, *Foreign Investment, Law and Sustainable Development: A Handbook on Agriculture and Extractive Industries*, London International Institute for Environment and Development, 2014
Dolzer R, & Schreuer, C. *Principles of International Investment Law*, Oxford University Press, 2012
Evans M, *International Law*, Oxford University Press, 2014
Goode R, Kronke H & Mckendrick E, *Transnational Commercial Law*, Oxford University Press, 2011
Moses M, *The Principles and Practice of International Commercial Arbitration*, Cambridge University Press, 2012
Redfern A, & Hunter, M. *Redfern and Hunter on International Arbitration*, Oxford University Press, 2009
Sacerdoti G, *General Interests in International Investment Law*, Cambridge University Press, 2014
Schefer K, *International Investment Law*. Cheltenham, Edward Elgar Publishing, 2013
Schwarzenberger G, *Foreign Investment and International Law*, London: Steven & Sons, 1969
Schwebel S, *Justice in International Law*, Cambridge University Press, 1994
Schwenzer I, *Commentary on the UN Convention on the International Sale of Goods*, Oxford University Press, 2014

Articles and Essays

Alqurashi Z, 'Indirect Expropriation in the Field of Petroleum', *The Journal of World Investment & Trade* 5(6), 897-926

Bridge M, 'Avoidance for Fundamental Breach of Contract under the UN Convention on the International Sale of Goods', *International and Comparative Law Quarterly* 59(4), 911-940

Brower C & Schill S, 'Is Arbitration a Threat or a Boon to the Legitimacy of International Investment Law?', *The Chicago Journal of International Law* 9(4), 471-498

Dolzer R, 'Indirect Expropriation: New Developments?', *New York University Environmental Law Journal* 11, 64 -93

Edsall R, 'Indirect Expropriation under NAFTA and DRCAFTA: Potential Inconsistencies in the Treatment of State Public Welfare Regulations', *Boston University Law Review* 86, 931-962

Grebler E, 'Fundamental Breach of Contract under the CISG: A Controversial Rule', *American Society of International Law* 101, 407-413

Heiskanen V, 'The Doctrine of Indirect Expropriation in light of the Practice of the Iran-United States Claims Tribunal', *The Journal of World Investment & Trade* 8(2), 215-231

Henckels C, 'Indirect Expropriation and the Right to Regulate: Revising Proportionality Analysis and the Standard of Review in Investor-State Arbitration,' *Journal of International Economic Law* 15(1), 223-255

Jha V, 'International Investment Treaty Implications for the Indian Position on Nuclear Liability', *Journal of Risk Research* 17(1), 81-95

Karamanian S, 'The Place of Human Rights in Investor-State Arbitration', *Lewis & Clark Law Review* 17(2), 423-447

Kunoy B, 'Developments in Indirect Expropriation Case Law in ICSID Transnational Arbitration', *The Journal of World Investment & Trade* 6(3), 467- 491

Leon P, 'Creeping Expropriation of Mining Investments: An African Perspective', *Journal of Energy & Natural Resources Law* 27(4), 597-644

Lin T, 'The Status of FCTC in the Interpretation of Compensable Indirect Expropriation and the Right to Adopt "Stricter" Tobacco Control Measures under Bits', *Asian Journal of WTO & International Health Law and Policy* 9(1), 123-160

Newcombe A, 'The Boundaries of Regulatory Expropriation in International Law', *Foreign Investment Law Journal* 20(1), 1-50

Potesta M, 'Legitimate Expectations in Investment Treaty Law: Understanding the Roots and the Limits of a Controversial Concept', *ICSID Review* 28(1), 88-122

Reinisch A, 'Introductory Note to International Centre for Settlement of Investment Disputes (ICSID): *LG&E Energy Crop., LG&E Capital Crop., LG&E International INC. v the Argentine Republic*', *International Legal Materials* 46(1), 36-39

Sedigh H, 'What Level of Host State Interference Amounts to a Taking under Contemporary International Law?', *The Journal of World Investment & Trade* 2(4), 631-684

Tienhaara K, 'What You Don't Know Can Hurt You: Investor-State Disputes and the Protecting of the Environment in Developing Countries', *Global Environmental Politics* 6(4), 87-92

Wolf A, 'Human Rights and the Regulation of Privatized Essential Services', *Netherlands International Law Review* 60(2), 165-204

Yelpaala K, 'Fundamentalism in Public Health and Safety in Bilateral Investment Treaties', *Asian Journal of WTO & International Health Law and Policy* 3(1), 465-500

Internet Sources

BBC News. 'Bangladesh Factory Collapse Toll Passes 1,000', (10 May 2013) <<http://www.bbc.co.uk/news/world-asia-22476774>> accessed 20 May 2015

Pavey B & Williams T, 'The North American Free Trade Agreement: Chapter11' (26 February 2003) <<http://publications.gc.ca/Collection-R/LoPBdP/inbrief/prb0254-e.htm>> accessed 13 May 2015.

The UKLSA

Legal Issues is operated by volunteers and relies on donations.

To support the Journal or UKLSA in general, email president@uklsa.co.uk.

Website: <http://www.uklsa.co.uk>

Facebook: <http://www.facebook.com/UKLSA>

Twitter: twitter.com/UKLSA

The *Legal Issues Journal*

If you are interested in joining the editorial board as an editor, reviewer, copy-editor, or formatting editor, email editor@uklsa.co.uk

Website: [http:// www.legalissuesjournal.com/](http://www.legalissuesjournal.com/)

Facebook: <http://www.facebook.com/legalissuesjournal/>