ЦЕНТР МЕЖДУНАРОДНЫХ
И СРАВНИТЕЛЬНО-ПРАВОВЫХ ИССЛЕДОВАНИЙ
INTERNATIONAL AND COMPARATIVE
LAW RESEARCH CENTER

# ЛЕКЦИИ ЛЕТНЕЙ ШКОЛЫ ПО МЕЖДУНАРОДНОМУ ПУБЛИЧНОМУ ПРАВУ

## Право на регулирование в международном инвестиционном праве (доработанное)

Катарина Тити

# COURSES OF THE SUMMER SCHOOL ON PUBLIC INTERNATIONAL LAW

## The Right to Regulate in International Investment Law (Revisited)

Catharine Titi

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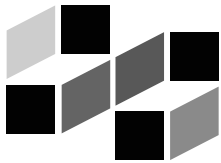

ЦЕНТР МЕЖДУНАРОДНЫХ
И СРАВНИТЕЛЬНО-ПРАВОВЫХ ИССЛЕДОВАНИЙ

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В 2021 году Летняя Школа состоялась в четвёртый раз. Как и в 2020 году, в связи с пандемией COVID-19 она прошла в онлайн-формате на отдельно разработанной платформе. Специальные курсы были посвящены теме «Международное инвестиционное право». Их прочитали Самуэль Вордсворт («Международное инвестиционное право: история, настоящее, перспективы»), Анна Жубан-Брет («Материально-правовые стандарты защиты в международном инвестиционном праве»), Катарина Тити («Право на регулирование в международном инвестиционном праве»), Сергей Усоскин («Иностранные инвестиции и инвесторы»), Макане Моиз Мбенге («Урегулирование споров между инвесторами и государством»). Общий курс международного публичного права прочёл Рюдигер Вольфрум.

Центр международных и сравнительно-правовых исследований выражает благодарность членам Консультативного совета Летней Школы: Р. А. Колодкину, С. М. Пунжину, Л. А. Скотникову, Б. Р. Тузмухамедову, С. В. Усоскину — и всем, кто внёс вклад в реализацию этой идеи, в том числе АО «Газпромбанк» за финансовую поддержку проекта.

## Dear friends,

The International and Comparative Law Research Center continues publication of lectures delivered within the Summer School on Public International Law.

The Summer School is a project of the Center aimed at providing those learning, working, or aspiring to work in the sphere of international law with an opportunity to obtain advanced knowledge of the subject and encouraging participants to engage in independent research. The Summer School's curriculum is comprised of lectures and seminars of the general and special courses under one umbrella theme delivered by leading international law experts, as well as of independent and collective studying.

In 2021, the Summer School was held for the fourth time. As in 2020, due to the COVID-19 pandemic, it was held on a tailor-made online platform. The Special Courses were devoted to the topic "International Investment Law". The courses were delivered by Samuel Wordsworth ("International Investment Law — History, Present, Perspectives"), Anna Joubin-Bret ("Substantive Standards of Protection in International Investment Law"), Catharine Titi ("The Right to Regulate in International Investment Law"), Sergey Usoskin ("Foreign Investments and Investors"), and Makane Moïse Mbengue ("Investor-State Dispute Settlement"). The General Course on Public International Law was delivered by Rüdiger Wolfrum.

The International and Comparative Law Research Center wishes to express its appreciation to the members of the Advisory Board — Roman Kolodkin, Sergey Punzhin, Leonid Skotnikov, Bakhtiyar Tuzmukhamedov, and Sergey Usoskin — as well as others who helped implement the project, including Gazprombank (JSC) for their financial support.

## Катарина Тити

Катарина Тити — штатный научный сотрудник и доцент Национального центра научных исследований (CNRS) — CERSA Университета Парижа II Пантеон-Ассас, Франция. Она также является членом Совета Европейского общества международного права, Учёного совета Института транснационального арбитража Центра американского и международного права и заместителем председателя Академического форума по урегулированию споров между инвесторами и государством, работа которого вносит вклад в дискуссии в Рабочей Группе III ЮНСИТРАЛ. Она является членом Комитета Ассоциации международного права по верховенству права и международному инвестиционному праву и входит в редакционный совет Ежегодника по международному инвестиционному праву и политике (Columbia/OUP). Катарина Тити является членом Королевского института арбитров, она входит в состав коллегии арбитров Арбитражного суда по искусству и включена в список арбитров по Приложению 31-B Соглашения США — Мексика — Канада. Она получила докторскую степень в Зигенском университете в Германии, ранее была консультантом ЮНКТАД. В 2016 году Катарина Тити стала лауреатом престижной премии Смита-Ловенфельда Международного арбитражного клуба Нью-Йорка за лучшую статью в области международного арбитража.

## Catharine Titi

Catharine Titi is a tenured Research Associate Professor at the French National Centre for Scientific Research (CNRS) — CERSA, University Paris II Panthéon-Assas, France. She serves on the Board of the European Society of International Law, on the Academic Council of the Institute for Transnational Arbitration of the Center for American and International Law, and as Deputy Chair of the Academic Forum on ISDS, whose work contributes to the discussions in Working Group III of the UNCITRAL. She is a member of the International Law Association Committee on Rule of Law and International Investment Law and she sits on the Editorial Board of the Yearbook on International Investment Law & Policy (Columbia/OUP). Catharine Titi is a Fellow of the Chartered Institute of Arbitrators, she sits on the panel of arbitrators of the Court of Arbitration for Art, and she is appointed to the roster of the United States-Mexico-Canada Agreement's Annex 31-B panelists. She holds a PhD from the University of Siegen in Germany, and she has previously been a consultant at the UNCTAD. In 2016, Catharine Titi was awarded the prestigious Smit-Lowenfeld Prize of the International Arbitration Club of New York for the best article published in the field of international arbitration.

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# I.

## Introduction

In the last few years, the right to regulate has evolved from a rather inconspicuous, mistrusted concept to a necessary component of international investment agreements. This normative evolution was in many ways inevitable but it certainly met with resistance — at least for a time. For a start, there were those who questioned whether it is appropriate to even ask whether the state has the right to regulate. A state, they argued — and some of them still do –, always has the right to regulate under public international law. This approach has sometimes resulted in willingly misunderstanding the specificity of the concept in international investment law and preventing its development. No one doubts that the state has the right to regulate according to this *lato sensu* understanding. It goes without saying that the sovereign state has the legal capacity to pass legislation and take regulatory measures that may affect the rights of foreign investors. However, the crux of the question, as asked in international investment law, is not whether the state can actually adopt such measures but whether, having adopted them, it incurs international responsibility and needs to compensate adversely affected foreign investors who are protected under an investment treaty. Therefore, the right to regulate in international investment law has a narrower meaning than the broadly understood sovereign right of the state to act as it sees fit within its borders. In this sense, the right to regulate is a technical term that acquires a specific meaning in the international investment law context.

There have also been those who were sceptical about the right to regulate for altogether different reasons. Some regarded it as the ultimate catalyst of investor protections, an element that runs counter to the very object and purpose of investment

treaties. We can probably agree that the primary purpose of investment treaties is to protect foreign investments rather than to safeguard the state's right to regulate. Were the latter the purpose of investment treaties, it might make more sense for states not to sign them in the first place. Yet some argued that safeguarding the state's right to regulate flies in the face of this principle of investment protection; as a result, exceptions protecting policy space should be ignored[1] or, at the very least, they should be narrowly interpreted.[2]

On the other side of the ideological spectrum, the right to regulate has been regarded with suspicion even by some who lobbied against investment protections. M. Sornarajah opposed the right to regulate on the ground that balanced investment treaties incorporating this right to regulate are unworkable and states had better terminate their investment treaties instead.[3] Rather than introduce the right to regulate, a handful of developing states actually did decide to terminate their investment treaties and some denounced the ICSID Convention, in a symbolic gesture against investment arbitration.[4]

However, no matter what the detractors of the right to regulate have declared over the course of the last ten years, they have been fighting a losing battle: the right to regulate was here to stay. Scepticism suddenly gave way and attitudes changed dramatically.

[1] This surprising statement was made to me in a private discussion by a senior and well-respected scholar and arbitrator.

[2] See eg *Enron Creditors Recovery Corporation and Ponderosa Assets, LP v. Argentina*, ICSID Case No. ARB/01/3, Award, 22 May 2007 [331]; *Sempra Energy International v. Argentina*, ICSID Case No. ARB/02/16, Award, 28 September 2007 [373].

[3] M. Sornarajah, *Resistance and Change in the International Law on Foreign Investment* (Cambridge University Press 2015) chs 6-7.

[4] The three countries that denounced the ICSID Convention are Bolivia, Ecuador, and Venezuela. However, in 2021, Ecuador became the first state to rejoin the ICSID Convention after its withdrawal more than ten years ago, see ICSID, "News Release: Ecuador Ratifies the ICSID Convention" (4 August 2021) <https://icsid.worldbank.org/news-and-events/news-releases/ecuador-ratifies-icsid-convention>.

It is now rare for new treaties not to include at least some provisions that safeguard the state's right to regulate.

In this short study, I will offer a complementary account of the right to regulate compared to my treatment of the topic a few years ago. At the time, the main questions asked concerned the very definition and function of the right to regulate. Was the right to regulate an inherent right that states had and that did not need to be safeguarded? Did investment tribunals take it into account *motu proprio*? Was the right to regulate to be equated with general exceptions modelled on Article XX of the General Agreement on Tariffs and Trade (GATT)? Could states protect it by carving types of disputes out of a treaty? While these questions are not new, it is still important to consider some of them, because they are essential to understanding what the right to regulate is. However, new questions are constantly raised. For example, the initial concern with imbalanced treaties that one-sidedly favoured investors at the expense of the state's right to regulate has now become a question of: do new treaties that overly safeguard the right to regulate still have a useful purpose as investment protection instruments? So much has changed in treaty drafting in a short period of time, yet new generation treaties that incorporate the right to regulate through general public welfare exceptions are still very recent — some of them have not yet entered into force and others still mainly "exist" as hopeful negotiating templates. They have seldom as yet been interpreted by arbitral tribunals. When they have been interpreted, their interpretation has often left a lot to be desired, raising — rather than resolving — interpretive conundrums and doubts about the effectiveness of treaty provisions and of the right to regulate, in particular. How much policy space is not enough and how much is too much? While I will still address some basic questions, such as how we are to understand the right to regulate, I will focus on new developments, notably new treaties and recent arbitral case law on the right to regulate and the challenges they raise going forward.

Following this introduction, Chapter II will discuss the definition of the right to regulate. I will explain why the concept has a special meaning in international investment law and is therefore to be distinguished from the *lato sensu* freedom states have to act under public international law. The chapter will also look into some of the regulatory interests that the right to regulate aims to protect. Finally, it will explore complementary elements that, while not belonging in the right to regulate discussion proper, help increase states' regulatory flexibility.

In Chapter III, I will turn to the right to regulate as incorporated in treaty law. This chapter will examine in turn the preamble and treaty provisions on the right to regulate, both express references to it and treaty exceptions allowing states to take measures that would otherwise violate the treaty. The chapter will discuss in particular three types of exceptions: standard-specific exceptions, focusing on clauses that introduce a mitigated form of the police powers doctrine, essential security interests exceptions, and exceptions for the protection of public welfare objectives. The chapter will further consider some issues around the drafting and interpretation of exceptions clauses.

In Chapter IV, I will address the right to regulate and customary international law. In a first step, the chapter will examine the circumstances precluding wrongfulness of the International Law Commission's (ILC) Articles on the Responsibility of States for Internationally Wrongful Acts (hereinafter Articles on State Responsibility), with a focus on the necessity defence, in which interest has revived in light of the COVID-19 pandemic. In a second step, the chapter will consider the police powers doctrine, which some arbitral tribunals have applied as customary international law. The chapter will not examine whether the police powers doctrine actually is customary international law but it will rely on the approach of arbitral tribunals.

Chapter V will turn to the right to regulate in light of the backlash against investment arbitration and the ongoing reform of investor-state dispute settlement (ISDS). The chapter will observe how the right to regulate, a substantive standard, has gained importance in the public discourse on investment dispute settlement and will consider its significance in the negotiations in Working Group III of the United Nations Commission on International Trade Law (UNCITRAL). The chapter will also enquire into Opinion 1/17 of the Court of Justice of the European Union (CJEU), which has raised the protection of the right to regulate into a constitutional obligation for the EU and its 27 member states. Although this is a "domestic" — as opposed to an international — decision,[5] it is likely to impact the multilateral negotiations in UNCITRAL Working Group III and it reiterates the importance of the right to regulate that has come to span not only substantive but also procedural reform of international investment law.

Without aiming to be exhaustive, this brief study will take stock of the right to regulate, focusing in particular on very recent treaty practice and case law. The two interact very closely: tribunals interpret investment treaties and their interpretations impact the drafting of future treaties. I will argue that the right to regulate is here to stay but that its interpretation is uncertain. Part of the uncertainty is due to the fact that there is as yet not one unique understanding of the right to regulate and what actually safeguards it and another part is due to the case law that still leaves a lot to be desired, sometimes taking the right to regulate into account *motu proprio* and sometimes not giving it effect even though it is incorporated in the treaty text.

[5] C. Titi, "Opinion 1/17 and the Future of Investment Dispute Settlement: Implications for the Design of a Multilateral Investment Court", in L. Sachs, L. Johnson and J. Coleman (eds), *Yearbook on International Investment Law & Policy 2019* (Oxford University Press 2021) 514.

# II.

## What Is the Right to Regulate?

### 1. Introduction

The preoccupation with the right to regulate emerged as questions of balance started to be asked about investment treaties. How did investment treaties weigh the rights of investors and the obligations of states? Many saw investment treaties as imbalanced instruments one-sidedly focused on the protection of investors to the detriment of states' public policies.[6] Yet, to attribute the emergence of the right to regulate to mere theoretical questions of balance is to misunderstand the complex confluence of circumstances at its origin and, among them, the impact that investor-state dispute settlement had on states' willingness to incorporate it into their investment treaties. These considerations about the evolution of attitudes towards the right to regulate run through this study. However, in order to appreciate them, it is essential to first comprehend what we mean when we refer to the right to regulate.

[6] For a discussion, see P. Juillard, "The Law of International Investment: Can the Imbalance Be Redressed?" in K.P. Sauvant (ed), *Yearbook on International Investment Law & Policy 2008-2009* (Oxford University Press 2009); P. Muchlinski, "Trends in International Investment Agreements: Balancing Investor Rights and the Right to Regulate — The Issue of National Security", in K.P. Sauvant (ed), *Yearbook on International Investment Law & Policy 2008-2009* (Oxford University Press 2009); K.J. Vandevelde, "A Comparison of the 2004 and 1994 US Model BITs: Rebalancing Investor and Host Country Interests", in K.P. Sauvant (ed), *Yearbook on International Investment Law & Policy 2008-2009* (Oxford University Press 2009); L. Markert, "The Crucial Question of Future Investment Treaties: Balancing Investors' Rights and Regulatory Interests of Host States", in M. Bungenberg, J. Griebel and S. Hindelang (eds), *European Yearbook of International Economic Law 2011, Special Issue: International Investment Law and EU Law* (Springer 2011); C. Titi, "EU Investment Agreements and the Search for a New Balance: A Paradigm Shift from *laissez-faire* Liberalism toward Embedded Liberalism?" Columbia FDI Perspectives (3 January 2013), <https://academiccommons.columbia.edu/doi/10.7916/D85Q54F6>.

This chapter begins by defining the term "right to regulate". Next, it turns to the question of how the right to regulate, as a concept in international investment law, differs from the state's general regulatory capacity. The chapter proceeds by addressing the regulatory interests, notably public welfare objectives, that are principally associated with the right to regulate. Finally, it closes with an examination of some elements complementary to the right to regulate.

## 2. What We Understand by "the Right to Regulate"

The right to regulate is a term that has still not found its place in legal dictionaries. Treaty practice, arbitration practice, the case law, and legal scholarship reveal different understandings of what the right to regulate is. My preferred definition is the following. The right to regulate is the host state's legal right to adopt legislation or other measures in derogation of substantive commitments it has undertaken in its international investment treaties without having to compensate aggrieved investors.[7]

Two elements are particularly important in this definition. First, it is a *legal* right of the host state. In principle, it is safeguarded in conventional law, notably through treaty exceptions. However, it can also derive from other sources of international law, especially customary international law. Since the right to regulate can exist beyond treaty law, it is, strictly speaking, not necessary to incorporate it in treaties. For example, tribunals have sometimes recognised the police powers' doctrine as forming part of customary international law and have consequently found that general non-discriminatory actions taken for the public welfare are regulatory measures that do not amount to indirect expropriation.[8] Yet in practice, to the extent that states wish to safeguard their right to

[7] C. Titi, *The Right to Regulate in International Investment Law* (Nomos and Hart 2014) 33.
[8] See ch IV, section 3 The Police Powers Doctrine.

regulate, their best approach may be to include it in investment treaties. This is what states are actually doing. To continue with the example of the police powers doctrine, it is now increasingly, almost consistently, incorporated in new investment treaties.[9]

The second important, albeit apparently contested,[10] element in the definition is that the right to regulate removes the need for compensation. In this light, the rationale of the right to regulate is not to allow the state to act as it does — the state does not need such an "authorisation" — but to allow it to act without the need to compensate those foreign investors who have been adversely affected by its actions.

### 3. Right to Regulate versus the State's General Regulatory Capacity

The term "right to regulate" can sometimes create confusion and give offence to those who are less familiar with the workings of international economic law. To some it seems inconceivable that the question might even be asked: does the state have the right to regulate? Such censure arises from a misunderstanding of the specificity of the right to regulate in international investment law. It is therefore necessary to distinguish between the state's *lato sensu* right to regulate under public international law and the narrower concept of the right to regulate as understood in international investment law.

The state's capacity to regulate in its domestic legal system is not questioned. Expression of the principles of sovereign equality and permanent sovereignty over natural resources,[11] it signifies the state's freedom to engage in political, economic, legislative, and

[9] Ibid.

[10] See ch III, text to n 152–161, 170.

[11] N. Schrijver, *Sovereignty over Natural Resources: Balancing Rights and Duties* (Cambridge University Press 1997, reprinted 2008) 278ff; also, UN General Assembly

other regulatory activity, as the state sees fit. In effect, it is precisely this *lato sensu* sovereign right of states to regulate that allows them to restrict their freedom by entering into international agreements. By making commitments at the international level, states set limits to this freedom.

States make such commitments all the time. For example, by entering an environmental agreement, states may undertake to reduce greenhouse gas emissions or to prevent and mitigate transboundary environmental harm; by signing a double taxation treaty, states may relinquish the collection of some taxes; by accepting the compulsory jurisdiction of the International Court of Justice (ICJ), states submit to the Court's jurisdiction for the resolution of legal disputes in relation to other states accepting the same obligation.[12] Commitments such as these limit states' *lato sensu* right to regulate.

The principle is the same with international investment agreements. It is states' sovereign right to enter into international investment agreements. By doing so, they make a binding legal promise to behave in a certain way (*pacta sunt servanda*). States can still regulate, but if they are found liable for a treaty violation in ISDS proceedings, they assume the obligation to compensate an investor. To ask whether the state has the right to regulate in international investment law is not to question the *lato sensu* right of the state to regulate.

The issue was indirectly addressed in *ADC v. Hungary*, where the tribunal rejected the respondent's argument "that the actions taken by it against the Claimants were merely an exercise of its rights under international law to regulate its domestic economic and legal affairs".[13]

(1962), Resolution 1803 on Permanent Sovereignty over Natural Resources, UN Doc No. A/RES/1803 (XVII) (14 December 1962).

[12] Statute of the ICJ art 36.

[13] *ADC Affiliate Limited and ADC & ADMC Management Limited v. Hungary*, ICSID Case No. ARB/03/16, Award, 2 October 2006 [423].

Instead, the tribunal's "understanding of the basic international law principles" was that

> while a sovereign State possesses the inherent right to regulate its domestic affairs, the exercise of such right is not unlimited and must have its boundaries. … Therefore, when a State enters into a bilateral investment treaty like the one in this case, it becomes bound by it and the investment protection obligations it undertook therein must be honoured rather than be ignored by a later argument of the State's right to regulate.[14]

The fact that states assume obligations by concluding international investment agreements that limit their freedom is not to say that states lose their capacity to regulate. First, states are only bound by investment treaties to the extent that they themselves have agreed to be bound. This depends, for example, on the types of obligations they assume (eg national treatment, fair and equitable treatment, protection in case of indirect expropriation), whether the treaties include exceptions (eg a security exception) or carve-outs (eg for taxation measures). When states include ISDS provisions in their treaties, they offer a means of review, implementation, and enforcement of their treaty obligations, although dispute settlement provisions themselves may contain carve-outs too — for example, an investment treaty may render some types of disputes non-arbitrable.

Second, states retain the freedom to terminate or renegotiate the treaties they have signed. In reality, they regularly do both. New investment treaties are negotiated on the basis of templates, better known as "model bilateral investment treaties", that states update over time. Such updates are a reflection of the fact that law cannot stand still but must evolve[15] and are sometimes the direct result of states' experience with investor-state dispute

[14] Ibid.
[15] R. Pound, *Interpretations of Legal History* (Cambridge University Press 1923) 1.

settlement.[16] For example, in 2004, the United States and Canada made a significant revision to their model investment treaties, in light of their experience with dispute settlement under the North American Free Trade Agreement (NAFTA).[17] It may be possible to trace the earlier interpretive statement of the NAFTA Free Trade Commission explaining that fair and equitable treatment in Article 1105(1) of NAFTA was to be equated with the minimum standard of the treatment of aliens under customary international law[18] to the *Pope & Talbot* tribunal's contrary finding[19] or at least to the arguments that had been advanced to this effect during the dispute. The reaction to the decision on jurisdiction in *Maffezini v. Spain* and the application by that tribunal of the most-favoured-nation clause to the treaty's investor-state arbitration clause[20] is another example. Numerous new treaties specify either expressly or in a so-called "disappearing" footnote[21] that their most-favoured-nation clause does not apply to ISDS provisions.[22] Such treaty "amendments" are an expression of states' sovereign capacity, in other words, of their *lato sensu* right to regulate.

In short, when it comes to discussing the right to regulate in international investment law, the question is not, properly speaking,

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[16] See ch V, section 1 Introduction.

[17] Vandevelde (n 6) 290–292.

[18] NAFTA Free Trade Commission, "Clarifications Related to NAFTA Chapter 11" (31 July 2001) <http://www.worldtradelaw.net/nafta/chap11interp.pdf>.

[19] *Pope & Talbot, Inc v. Canada*, Award on the Merits of Phase 2, 10 April 2001 [113]. See further A. De Luca et al, "Responding to Incorrect Decision-Making in Investor-State Dispute Settlement: Policy Options" (2020) 21(2–3) Journal of World Investment & Trade 374, 388.

[20] *Maffezini v. Spain*, ICSID Case No. ARB/97/7, Decision on Jurisdiction, 25 January 2000.

[21] Reference is made here to the disappearing Maffezini footnote in US investment treaties, see C. Titi, "The Evolution of Substantive Investment Protections in Recent Trade and Investment Treaties", RTA Exchange, International Centre for Trade and Sustainable Development (ICTSD) and Inter-American Development Bank (IDB) (8 November 2018) <https://www.ictsd.org/themes/global-economic-governance/research/the-evolution-of-substantive-investment-protections-in>, VII, 8.

[22] Eg Comprehensive Economic and Trade Agreement between the EU and Canada (CETA) art 8.7(4).

whether the state may or may not regulate, rather it is whether the state by regulating has failed to honour an obligation under an international investment agreement and, if so, whether it needs to compensate the aggrieved investor. This right to regulate is a much narrower concept than the general right of states to legislate and take administrative and other regulatory measures in public international law outside the context of specific commitments they may have undertaken.

### 4. The Right to Regulate and Public Welfare Objectives

The right to regulate has been closely associated with particular public welfare objectives, including, especially, the protection of the public order, essential security interests, public health and safety, the environment, and cultural diversity. The fact that the right to regulate is predominantly linked to such regulatory interests does not mean that it cannot be envisaged in relation to other interests, such as tax policies or preferential treatment offered investors of a third party by virtue of that party's membership of a customs union, free trade zone, economic union, or common market,[23] at least to the extent that an exception in the treaty safeguards such actions. Yet when discussing the right to regulate, the emphasis is often on a narrower set of public welfare interests, such as those mentioned at the beginning of this paragraph.

This has sometimes proved a thorny issue. Some developing countries have considered that these public welfare objectives reflect the interests of the developed world — although I would argue that some such interests, for example measures to tackle climate change, cannot only be in the interest of industrialised countries. In the context of UNCITRAL Working Group III, some delegations

[23] Exceptions for such preferential treatment are invariably to be found in bilateral investment treaties concluded by EU member states. For a discussion, see Titi, *The Right to Regulate in International Investment Law* (n 7) 130–134.

argued that the right to regulate does not sufficiently take into account the interests of developing countries.[24] An example given in that context was regulation in post-apartheid South Africa.[25]

It is understandable that some regulatory interests may be of greater importance to some countries than to others. To safeguard these interests, the best approach for these countries is to include them in their investment treaties. States are the main actors that shape international investment law. It is therefore up to them to draft the investment treaties in a way that takes into account the interests they want to be taken into account.

## 5. Complementary Elements

States' regulatory space can also be reserved through means that do not, properly speaking, form part of the right to regulate. These means do not offer the state a legal right to ignore substantive treaty protections but increase, or may increase, its capacity to regulate without having to compensate foreign investors. Although not belonging in the right to regulate debate, it is useful to consider these means, since states rarely, if ever, draw the distinction. This section will discuss some of the most important elements that are complementary to the right to regulate.

The first example is provisions that carve out of the treaty's protection some industries or policy areas in whole or in part. Rather than introduce exceptions for public interest regulation, such carve-outs exclude the given industries or policy areas from the treaty's scope. For instance, the Comprehensive Economic and Trade Agreement concluded by the EU and Canada (CETA) states that its provisions on establishment of investments and

[24] Such opinions were expressed in UNCITRAL Working Group III, during the Fourth Intersessional Meeting on Investor-State Dispute Settlement Reform, organised by the Republic of Korea on 2–3 September 2021.
[25] Ibid.

non-discrimination do not apply to the "audio-visual services" for the EU and its member states and to the "cultural industries" for Canada.[26] In other words, the contracting parties do not make any investment protection commitments with respect to "audio-visual services" in the EU and "cultural industries" in Canada. The same result is achieved through the use of positive or negative lists at the end of a treaty respectively listing the industries that are, *vel non*, protected by the treaty.[27] Another type of provision that falls within this category are carve-outs for taxation measures or public procurement.[28]

Statements and clarifications offering tribunals interpretive guidance are another element complementary to the right to regulate. An example is an interpretive footnote in the 2019 Australia-Indonesia Comprehensive Economic Partnership Agreement (CEPA) specifying that, while an investment may take the form of "bonds, debentures and other debt instruments and loans", some forms of debt, "such as claims to payment that are immediately due and result from the sale of goods or services", are less likely to have the characteristics of an investment.[29] Depending on how closely the interpretive statement reflects the ordinary meaning of the provisions it aims to clarify, an interpretive statement may be purely that — an interpretive statement — or it may hide a genuine exception. A provision such as CETA's "for greater certainty" statement to the effect that full protection and security refers to "the Party's obligations relating to the physical security of investors and

[26] CETA art 8.2(3).
[27] OECD, *International Investment Law: Understanding Concepts and Tracking Innovations* (OECD 2008) ch 4; T. Broude and S. Moses, "The Behavioral Dynamics of Positive and Negative Listing in Services Trade Liberalization: A Look at the Trade in Services Agreement (TISA) Negotiations", in P. Sauvé and M. Roy (eds), *Research Handbook on Trade in Services* (Edward Elgar 2016); M. Molinuevo and A.K. Pfister, Report: "Look Back to See What's Ahead: A Review of Mega-PTAs on Services and Investment that Will Shape Future Trade Agreements" (World Bank Group 2020) 11–14.
[28] Eg Hong-Kong-New Zealand bilateral investment treaty (BIT) (1995) art 8(2).
[29] Australia-Indonesia CEPA art 14.1, n 3.

covered investments",[30] may be understood either as an exception or as a clarification, depending on whether one, absent the provision, would interpret the full protection and security standard as limited to or extending beyond physical security.

Another type of provision that is complementary to the right to regulate is one carving types of disputes out of the treaty's dispute settlement clause.[31] Not granting investors access to dispute settlement, such as in the case of the Regional Comprehensive Economic Partnership Agreement (RCEP) (2020),[32] is also sometimes seen as enhancing states' regulatory capacity.

Deference afforded to states' regulatory flexibility at the discretion of an arbitral tribunal is also sometimes erroneously assumed to be synonymous with the right to regulate. This category deserves particular attention, since, at some point in time, it was suggested that it was not necessary to take normative action to safeguard the states' right to regulate, since investment tribunals took it into account anyway.[33]

Certainly, a number of tribunals have regard to the state's right to regulate. For example, in the context of an examination of fair and equitable treatment, the tribunal in *Philip Morris v. Uruguay* cited with approval earlier case law recognising that the investor's

[30] CETA art 8.10(5).

[31] Eg CETA art 8.45. See Titi, *The Right to Regulate in International Investment Law* (n 7) 35–40; cf J.E. Viñuales, "Seven Ways of Escaping a Rule: Of Exceptions and Their Avatars in International Law", in L. Bartels and f. Paddeu (eds), *Exceptions in International Law* (Oxford University Press 2020).

[32] However, the agreement does not exclude the possibility of future provisions on ISDS. According to Article 10.8(1), the contracting parties, "without prejudice to their respective positions", will enter into discussions on ISDS, within two years of the agreement's entry into force, but it is made clear that the outcome of these discussions is "subject to agreement by all Parties".

[33] A. Newcombe, "General Exceptions in International Investment Agreements", in M.-C. Cordonier Segger, M.W. Gehring and A. Newcombe (eds), *Sustainable Development in World Investment Law* (Kluwer Law International 2011) 357; cf J.E. Alvarez, *The Public International Law Regime Governing International Investment* (Hague Academy of International Law 2011) 221–222, 322ff.

legitimate expectations and the requirement of legal stability as components of fair and equitable treatment "do not affect the State's rights to exercise its sovereign authority to legislate and to adapt its legal system to changing circumstances".[34] The tribunal reasoned that fair and equitable treatment does not prevent "changes to general legislation", at least if there is no stabilisation clause, so long as "they do not exceed the exercise of the host State's normal regulatory power in the pursuance of a public interest and do not modify the regulatory framework relied upon by the investor at the time of its investment 'outside of the acceptable margin of change'".[35] The tribunal added that, in light of "the State's regulatory powers", an investor who wishes to rely on legitimate expectations must have inquired into the likelihood of changes to the regulatory framework.[36] It concluded that the respondent had not frustrated the investors' legitimate expectations, since they "had no legitimate expectations that such or similar measures would not be adopted".[37]

However, the fact that a tribunal acknowledges the state's right to regulate does not mean that it will necessarily also find in favour of the respondent. In some cases, tribunals accepted that the state had the right to regulate but found that it had violated the investment treaty anyway. So, the *Lemire* tribunal after mentioning the host state's "legitimate right" to adopt legislation in the public interest[38] found a violation of fair and equitable treatment.[39] The *BG* tribunal after invoking the *Saluka* tribunal's "legitimate right

[34] *Philip Morris Brands Sàrl, Philip Morris Products SA and Abal Hermanos SA v. Uruguay*, ICSID Case No. ARB/10/7, Award, 8 July 2016 [422].
[35] Ibid [422]. For a similar reasoning, see *EDF (Services) Limited v. Romania*, ICSID Case No. ARB/05/13, Award, 8 October 2009 [216]–[217], holding that an investment treaty could not function "as a kind of insurance policy against the risk of any changes in the host State's legal and economic framework. Such expectation would be neither legitimate nor reasonable".
[36] *Philip Morris v. Uruguay* (Award) (n 34) [427].
[37] Ibid [434].
[38] *Joseph Charles Lemire v. Ukraine*, ICSID Case No. ARB/06/18, Decision on Jurisdiction and Liability, 14 January 2010 [272]-[273], [285].
[39] Ibid [513].

… to regulate" concluded that the conduct of the host state fell below the international law minimum standard of treatment.[40] In *SD Myers v. Canada*, a NAFTA case, the tribunal acknowledged the "high measure of deference that international law generally extends to the right of domestic authorities to regulate matters within their own borders".[41] It held that:

> When interpreting and applying the "minimum standard", a Chapter 11 tribunal does not have an open-ended mandate to second-guess government decision-making. Governments have to make many potentially controversial choices. In doing so, they may appear to have made mistakes, to have misjudged the facts, proceeded on the basis of a misguided economic or sociological theory, placed too much emphasis on some social values over others and adopted solutions that are ultimately ineffective or counterproductive. The ordinary remedy, if there were one, for errors in modern governments is through internal political and legal processes, including elections.[42]

However, the tribunal ultimately found in favour of the investor.[43]

Certainly, no case can be decided in the abstract. For example, in *Lemire v. Ukraine*, the tribunal observed that it had a duty to "balance" a number of interests, including the host state's "sovereign right to pass legislation and to adopt decisions for the protection of its public interests, especially if they do not provoke a disproportionate impact on foreign investors" but also the investor's legitimate expectations and its behaviour in the host state.[44] In other words, the tribunal never reasoned that the state's right to regulate "takes it all". In short, deference afforded the state at the discretion of the

[40] *BG Group Plc v. Argentina* (UNCITRAL) Final Award, 24 December 2007 [303].
[41] *SD Myers, Inc v. Canada* (UNCITRAL) Partial Award, 13 November 2000 [263].
[42] Ibid [261].
[43] Ibid [268].
[44] *Lemire v. Ukraine* (Decision on Jurisdiction and Liability) (n 38) [285].

tribunal is an approach to interpretation,[45] rather than a legal right on which the state can rely to avoid complying with investment protections in its treaties.

An additional type of provision that has sometimes been discussed in relation to the host state's policy space,[46] but which should not be taken to safeguard the right to regulate, is one on the non-lowering of environmental and other public welfare standards. The 2021 Georgia-Japan bilateral investment treaty (BIT) includes such a provision, entitled "Health, Safety and Environmental Measures and Labour Standards", which establishes:

> Each Contracting Party recognises that it is inappropriate to encourage investment by investors of the other Contracting Party and of a non-Contracting Party by relaxing its health, safety or environmental measures, or by lowering its labour standards. To this effect, each Contracting Party should not waive or otherwise derogate from such measures or standards as an encouragement for the establishment, acquisition or expansion of investments in its Territory by investors of the other Contracting Party and of a non-Contracting Party.[47]

Although this provision does refer to regulatory interests and aims to prevent a regulatory race to the bottom in order to attract foreign investment, a closer look reveals that it does not provide the host state with a "right". On the contrary, it imposes an *obligation* on the host state not to relax its environmental, labour, etc., standards.[48]

Finally, the right to regulate should not be conflated with what has been termed a "'mere declaratory' right to regulate".[49] This is

[45] Markert (n 6) 158.
[46] Eg OECD (n 27) ch 3; M. Bronckers and G. Gruni, "Retooling the Sustainability Standards in EU Free Trade Agreements" (2021) 24(1) Journal of International Economic Law 25.
[47] Georgia-Japan BIT (2021) art 20.
[48] Titi, *The Right to Regulate in International Investment Law* (n 7) 105–107.
[49] Markert (n 6) 149–150.

a type of provision that allows the state to adopt, maintain, and enforce measures in order to ensure that investment activity in its territory is undertaken in a manner sensitive to public policy concerns, so long as such measures are *consistent* with the investment agreement.[50] Although, unhelpfully, such provisions are sometimes entitled "Right to Regulate",[51] they do not offer the state any regulatory flexibility that the state does not already have; the state can anyway take measures *consistent* with the investment agreement without the express permission granted it by this type of clause. In addition, an argument can be made that the scope of this provision is limited, since it only relates to the manner in which investment activity is undertaken in the territory of the host state.[52] So, in *Al Tamini v. Oman*, the tribunal reasoned that a similarly-worded provision on environmental protection[53] "provides a forceful protection of the right of either State Party to adopt, maintain or enforce any measure to ensure that investment is 'undertaken in a manner sensitive to environmental concerns', *provided it is not otherwise inconsistent with the express provisions*" of that treaty's investment chapter.[54]

## 6. Conclusion

This chapter has defined the term "right to regulate" as an international investment law concept and stressed that this *stricto sensu* right must not be conflated with the state's freedom to regulate under public international law. The chapter also considered the public welfare objectives typically associated with the right to regulate. Finally, it sought to distinguish between

[50] Eg USMCA art 14.16; CAFTA-DR art 10.11.
[51] Eg Norwegian Model BIT (2015) art [12].
[52] On the "declaratory right to regulate", see Titi, *The Right to Regulate in International Investment Law* (n 7) 111–115. See also ch III, text to n 166 ff.
[53] Oman-US FTA (2006) art 10.10.
[54] *Adel A Hamadi Al Tamimi v. Oman*, ICSID Case No. ARB/11/33, Award, 3 November 2015 [387] (emphasis added).

the right to regulate proper and elements that, while potentially enhancing states' regulatory flexibility, do not provide them with a legal right to breach substantive treaty obligations without the need to compensate affected investors. After this broad introductory framework, it is now possible to turn to the concrete means by which the right to regulate is safeguarded, starting with the right to regulate in treaty law.

# III.

## The Right to Regulate in Treaty Law

### 1. Introduction

If the right to regulate is a *legal* right, this means that it has to be laid down in international law. It is beyond the scope of this study to examine the right to regulate in light of every source of international law.[55] Instead, the analysis will focus on two sources of international law. Accordingly, this chapter will examine the right to regulate in treaty law, while the following chapter will turn to customary international law.

The principal means by which states can safeguard their right to regulate is by introducing express treaty language to that effect. This is especially achieved through treaty exceptions, which, as of 2021, are being increasingly introduced in new investment treaties. In addition, states have started to draft novel treaty clauses expressly affirming their right to regulate, inviting challenging interpretive questions. Finally, treaty preambles also include language that can help safeguard the host state's right to regulate. This chapter will address this incorporation of the right to regulate in investment treaties in reverse order. First, it will discuss the preamble, second, express mentions of the right to regulate in new generation investment treaties and, third, exceptions. Before closing, the chapter will also offer some reflections on the drafting of treaty exceptions and their interpretation.

[55] Statute of the ICJ art 38.

## 2. The Preamble

The preamble does not create independent legal rights or obligations.[56] However, it contains the treaty's object and purpose and forms part of the context that, according to the Vienna Convention on the Law of Treaties of 1969, must be taken into account when interpreting other treaty provisions.[57] Consequently, the preamble can prove to be an important interpretive tool, as the case law of investment tribunals easily shows.[58]

Old generation treaties tended to include short preambles that focused on the need to strengthen economic relations between the parties, promote and protect investments, stimulate individual business initiative, and encourage the flow of private capital.[59]

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[56] A. Newcombe and L. Paradell, *Law and Practice of Investment Treaties* (2009 Wolters Kluwer) 124; *İçkale İnşaat Limited Şirketi v. Turkmenistan*, ICSID Case No. ARB/10/24, Award, 8 March 2016 [337].

[57] Vienna Convention on the Law of Treaties art 31.

[58] Eg *Siemens AG v. Argentina*, ICSID Case No. ARB/02/8, Decision on Jurisdiction, 3 August 2004; *SGS Société Générale de Surveillance SA v. Philippines*, ICSID Case No. ARB/02/6, Decision on Objections to Jurisdiction, 29 January 2004; *Noble Ventures, Inc v. Romania*, ICSID Case No. ARB/01/11, Award, 12 October 2005; *MTD Equity Sdn Bhd and MTD Chile SA v. Chile*, ICSID Case No. ARB/01/7, Award, 25 May 2004; *Occidental Exploration and Production Company v. Ecuador* (UNCITRAL) LCIA Case No. UN 3467, Final Award, 1 July 2004; *CMS Gas Transmission Co v. Argentina,* ICSID Case No. ARB/01/8, Award, 12 May 2005; *Enron Creditors Recovery Corporation and Ponderosa Assets, LP v. Argentina*, ICSID Case No. ARB/01/3, Award, 22 May 2007; *Saluka Investments BV (The Netherlands) v. Czech Republic*, PCA Case No. 2001-04, Partial Award, 17 March 2006; *National Grid v. Argentina* (UNCITRAL) Award, 3 November 2008; *El Paso Energy International Company v. Argentina*, ICSID Case No. ARB/03/15, Award, 31 October 2011; *Daimler Financial Services AG v. Argentina*, ICSID Case No. ARB/05/1, Award, 22 August 2012 [258].

[59] Eg see the preambles to the Indonesia-Switzerland BIT (1974); Singapore-United Kingdom BIT (1975); France-Sri Lanka BIT (1980); Bangladesh-Germany BIT (1981); France-Nepal BIT (1983); Austria-Yemen BIT (1985); Dominica-United Kingdom BIT (1987); Czech Republic-Finland BIT (1990); Republic of Korea-Romania BIT (1990); Finland-Latvia BIT (1992); Italy-Mongolia BIT (1993); Argentina-Venezuela BIT (1993); Republic of Korea-Sweden BIT (1995); Chile-United Kingdom BIT (1996); India-Oman BIT (1997); Jordan-US BIT (1997); Greece-Moldova BIT (1998); Germany-Nigeria BIT (2000); Angola-United Kingdom BIT (2000); Guatemala-Republic of Korea BIT (2000); Lebanon-Pakistan BIT (2001); Austria-Oman BIT

Some of them added a reference to the need to maintain a stable framework for investments and the desirability of fair and equitable treatment of investments.[60] However, they generally omitted references to public interests, such as the protection of public health and the environment.[61]

This one-sided focus on investment protection encouraged some tribunals to interpret preambles as limiting the state's regulatory power. For instance, in *SGS v. Philippines*, the tribunal took into account the preamble's reference to the parties' intention to "create and maintain favourable conditions for investments" to hold that it was "legitimate to resolve uncertainties in [the treaty's] interpretation so as to favour the protection of covered investments".[62] Reasoning along similar lines, the *Enron* tribunal held that exceptions should be interpreted narrowly, since:

> the object and purpose of the Treaty is, as a general proposition, to apply in situations of economic difficulty and hardship that require the protection of the international guaranteed rights of its beneficiaries. To this extent, any interpretation resulting in an escape route from the obligations defined cannot be easily reconciled with that object and purpose. Accordingly, a restrictive interpretation of any such alternative is mandatory.[63]

(2001); Jamaica-Spain BIT (2002); Bosnia and Herzegovina-Moldova BIT (2003); Albania-Republic of Korea BIT (2003); Greece-Jordan BIT (2005); Colombia-Switzerland BIT (2006).

[60] Eg see the preamble to the Argentina-United States BIT (1991); cf Cuba-Denmark BIT (2001) preamble.

[61] Exceptionally, some older treaty preambles, such as those often found in US BITs, contain the parties' agreement that the objectives announced in the preamble "can be achieved without relaxing health, safety and environmental measures of general application". See Honduras-US BIT (1995); Nicaragua-US BIT (1995); Croatia-US BIT (1996); Jordan-US BIT (1997); Bolivia-US BIT (1998); El Salvador-US BIT (1999).

[62] *SGS Société Générale de Surveillance v. Philippines* (Decision on Objections to Jurisdiction) (n 58) [116]. See also *Siemens v. Argentina* (Decision on Jurisdiction) (n 58) [81]; *National Grid v. Argentina* (Award) (n 58) [170].

[63] *Enron v. Argentina* (Award) (n 58) [331]. See also *Sempra Energy International v. Argentina*, ICSID Case No. ARB/02/16, Award, 28 September 2007 [373].

Not all tribunals followed this approach.[64] In *Saluka v. Czech Republic*, the tribunal reasoned that:

> the protection of foreign investments is not the sole aim of the Treaty, but rather a necessary element alongside the overall aim of encouraging foreign investment and extending and intensifying the parties' economic relations. That in turn calls for a balanced approach to the interpretation of the Treaty's substantive provisions for the protection of investments, since an interpretation which exaggerates the protection to be accorded to foreign investments may serve to dissuade host States from admitting foreign investments and so undermine the overall aim of extending and intensifying the parties' mutual economic relations.[65]

Another example is that of the *Lemire* tribunal.[66] Considering the preamble's rather nondescript mention of the parties' desire "to promote greater economic cooperation between them" and their understanding that the BIT "will stimulate the flow of private capital and the economic development of the Parties", the tribunal established that the BIT's main purpose of stimulating foreign investment and capital flow "is not sought in the abstract" but it is rather inserted in the broader context of the economic development of the contracting parties.[67] Therefore, for the tribunal:

> the object and purpose of the Treaty is not to protect foreign investments per se, but as an aid to the development of the domestic economy. And local development requires that

[64] The above restrictive interpretations must also be constructed with the *SD Myers* Partial Award, deciding in light of environmental language in the NAFTA preamble, see *SD Myers, Inc v. Canada* (UNCITRAL) Partial Award, 13 November 2000 [220].
[65] *Saluka v. Czech Republic* (Partial Award) (n 58) [300].
[66] *Joseph Charles Lemire v. Ukraine*, ICSID Case No. ARB/06/18, Decision on Jurisdiction and Liability, 14 January 2010.
[67] Ibid [272].

> the preferential treatment of foreigners be balanced against the legitimate right of Ukraine to pass legislation and adopt measures for the protection of what as a sovereign it perceives to be its public interest.[68]

More recently, in *Sanum v. Laos* and in *Poštová banka v. Greece*, the tribunals reasoned that the fact that the purpose of investment treaties is to promote international investment does not mean that "every ambiguity found in such treaties should invariably be resolved in favour of the investor"[69] or that "protecting investments is the sole purpose of the treaty".[70]

In contrast with their predecessors, new generation investment treaties are generally mindful of regulatory interests, thus encouraging tribunals to interpret the treaty text in a balanced manner. These treaties tend to incorporate long or longer preambles that sometimes mention the state's "right to regulate". CETA, with its long list of references to regulatory interests and two express mentions of the right of the parties to regulate in the preamble (in italics below), is a good example. The text of that preamble is reproduced here practically *in extenso*. It provides:

> *Reaffirming* their strong attachment to democracy and to fundamental rights as laid down in the Universal Declaration of Human Rights, done at Paris on 10 December 1948, and sharing the view that the proliferation of weapons of mass destruction poses a major threat to international security;
>
> *Recognising* the importance of international security, democracy, human rights and the rule of law for the development of international trade and economic cooperation;

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[68] Ibid [272]–[273].
[69] *Sanum Investments Limited v. Laos*, PCA Case No. 2013-13, Judgment of the High Court of Singapore, 20 January 2015 [124]. See also *Poštová banka and ISTROKAPITAL SE v. Greece*, ICSID Case No. ARB/13/8, Award, 9 April 2015 [310].
[70] *Poštová banka and ISTROKAPITAL v. Greece* (Award) (n 69) [310].

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

*Affirming* their commitments as parties to the UNESCO Convention on the Protection and Promotion of the Diversity of Cultural Expressions, done in Paris on 20 October 2005, and recognising that states have the right to preserve, develop and implement their cultural policies, to support their cultural industries for the purpose of strengthening the diversity of cultural expressions, and to preserve their cultural identity, including through the use of regulatory measures and financial support;

*Recognising* that the provisions of this Agreement protect investments and investors with respect to their investments, and are intended to stimulate mutually-beneficial business activity, without undermining *the right of the Parties to regulate* in the public interest within their territories;

*Reaffirming* their commitment to promote sustainable development and the development of international trade in such a way as to contribute to sustainable development in its economic, social and environmental dimensions;

*Encouraging* enterprises operating within their territory or subject to their jurisdiction to respect internationally recognised guidelines and principles of corporate social responsibility, including the OECD Guidelines for Multinational Enterprises, and to pursue best practices of responsible business conduct;

*Implementing* this Agreement in a manner consistent with the enforcement of their respective labour and environmental laws and that enhances their levels of labour and environmental

> protection, and building upon their international commitments on labour and environmental matters.

Like CETA, albeit often in a more compact manner, other new investment treaties regularly make reference to the right of the state to regulate in their preambles.[71] Exceptionally, a few treaties mention the states' "inherent" right to regulate. So, the preamble to the 2018 Australia-Peru FTA states that the parties to the agreement resolve to:

> RECOGNISE their inherent right to regulate and resolve to preserve the flexibility of the Parties to set legislative and regulatory priorities, safeguard public welfare, and protect legitimate public welfare objectives, such as public health, safety, the environment, the conservation of living or non-living exhaustible natural resources, the integrity and stability of the financial system and public morals.[72]

The reference to an "inherent" right to regulate reveals an understanding of this "right" as inalienable. However, it is difficult to see why, if it is "inherent", it has to be introduced in the treaty — probably *ex abundanti cautela*. In effect, mentions of an "inherent" right to regulate point to states' *lato sensu* right to regulate under public international law and appear to be at odds with the definition of the *stricto sensu* right to regulate in investment law. Inherently, the state can regulate, but inherently it cannot avoid compensating foreign investors if it violates an investment treaty. The better

[71] For some other examples from recent treaties, see the preambles to RCEP (2020); Brazil-India BIT (2020), affirming "the right of Parties to regulate investments in their territory in accordance with their law and policy objectives"; Australia-Hong Kong BIT (2019); Brazil-United Arab Emirates BIT (2019), establishing that the parties affirm "their regulatory autonomy and policy space".

[72] For a similar provision, see the preamble to the Japan-Morocco BIT (2020). See also the preamble to the Intra-MERCOSUR Cooperation and Facilitation Investment Protocol (2017) ("guaranteeing the inherent right of the State Parties to regulate their public policies").

argument is in favour of reading such recitals as evidence of how fundamental states consider this right to regulate to be.

Another example of an "inherent" right to regulate preambular provision that is even trickier to interpret is found in the United States-Mexico-Canada Agreement's (USMCA), which states that the parties:

> RECOGNIZE their inherent right to regulate and resolve to preserve the flexibility of the Parties to set legislative and regulatory priorities, and protect legitimate public welfare objectives, such as health, safety, environmental protection, conservation of living or non-living exhaustible natural resources, integrity and stability of the financial system, and public morals, *in accordance with the rights and obligations provided in this Agreement*.[73]

The latter part of this recital appears to stress that states have the right to regulate to the extent provided for in the USMCA itself.

To conclude, states increasingly include regulatory concerns in their preambles. Express mentions of the term "right to regulate", in particular, are observed in treaties signed in most recent years. Although preambles do not create concrete rights and obligations, in some of these cases, the references to the right to regulate and regulatory interests are in categorical language and could create powerful interpretative arguments in favour of the right to regulate.

### 3. Treaty Provisions Expressly Referring to the Right to Regulate

Another new trend, alongside express mentions of the right to regulate in the preamble, is the drafting of treaty articles containing statements to the effect that the parties safeguard their right to

[73] Emphasis added.

regulate. Such provisions can vary from apparently innocuous hortatory declarations that may even be excluded from the scope of the treaty's dispute settlement clause to rather directive statements that could be capable of application. One such directive provision is Article 8.9 of CETA (*Investment and regulatory measures*). The first two paragraphs of this article establish:

1. For the purpose of this Chapter, the Parties reaffirm their right to regulate within their territories to achieve legitimate policy objectives, such as the protection of public health, safety, the environment or public morals, social or consumer protection, or the promotion and protection of cultural diversity.

2. For greater certainty, the mere fact that a Party regulates, including through a modification to its laws, in a manner which negatively affects an investment or interferes with an investor's expectations, including its expectations of profits, does not amount to a breach of an obligation under this Section.

Provisions of a similar nature have been introduced in a number of new treaties, although they typically rehearse only the first paragraph of CETA's article.[74] The 2021 Canadian model BIT also includes such a provision entitled "Right to Regulate".[75] In addition to the objectives identified in CETA, this article affirms the parties' right to regulate to achieve legitimate policy objectives, including "rights of Indigenous peoples" and gender parity. The article is also notable for specifically referring to the objective of "addressing climate change", although, arguably, this would anyway be covered under the broader objective of environmental protection.

The above provisions must be distinguished from softer language that does not necessarily safeguard policy space. For instance, the

[74] Eg Argentina-United Arab Emirates BIT (2018) art 11 (Right to Regulate); Argentina-Chile FTA (2017) art 8.4 (*Derecho a regular*).
[75] Canadian Model BIT (2021) art 3.

agreement in principle of the EU-China Comprehensive Agreement on Investment (CAI) provides:

> The Parties recognise the right of each Party to determine its sustainable development policies and priorities, to establish its own levels of domestic labour and environmental protection, and to adopt or modify its relevant laws and policies accordingly, consistently with its multilateral commitments in the fields of labour and environment.[76]

This type of provision is silent on the right to regulate. It appears to be making a hortatory statement relating to a *lato sensu* right to regulate. Still, this article must be distinguished from provisions on the non-lowering of environmental, health, and labour standards, discussed in the previous chapter, whereby the state assumes the *obligation* not to lower its environmental, health, and labour standards in order to attract or retain foreign investment.[77] The provision must also be distinguished from the "declaratory" right to regulate, which stresses that measures must be consistent with the investment agreement, thereby expressly disallowing derogations from the treaty.[78]

### 4. Treaty Exceptions

Leaving aside preamble language on the right to regulate and treaty provisions containing an express affirmation of the parties' right to regulate, which are very new and on occasion seem to be introduced *ex abundanti cautela*, the "traditional" and most essential means by which the right to regulate is safeguarded are treaty exceptions. We can divide exceptions into two broad categories:

[76] CAI section IV art 1 of sub-section 2 (Investment and Environment) and art 1 of sub-section 3 (Investment and Labour) <https://trade.ec.europa.eu/doclib/docs/2021/january/tradoc_159346.pdf>.
[77] See ch II, text to n 46–48.
[78] Ibid, text to n 49–54.

standard-specific exceptions, in other words, exceptions that relate to a given protection standard; and general exceptions, which apply to all or a good part of a treaty, typically providing that nothing in the agreement shall prevent the parties from adopting measures that are necessary — or that the parties deem to be necessary — for the protection of specific policy objectives. There are two main types of general exceptions: exceptions for the protection of the state's essential security interests and exceptions for the protection of general public welfare objectives beyond national security, such as public health, safety, and the environment. This section will consider in turn standard-specific exceptions, security exceptions, and general exceptions for the protection of public welfare objectives beyond security.

### i. Standard-specific exceptions

As the name reveals, a standard-specific exception is an exception to a particular standard of treatment only. Article 14.10(3)(c) of the USMCA provides an example of such an exception relating to the prohibition of performance requirements. According to this article, "[p]rovided that such measures are not applied in an arbitrary or unjustifiable manner, or do not constitute a disguised restriction on international trade or investment", the prohibition of specific performance requirements identified in the article will not be interpreted so as to prevent a party from taking measures, *inter alia*, "necessary to protect human, animal or plant life or health" or "related to the conservation of living or non-living exhaustible natural resources".

Another example of a standard-specific exception is the introduction in the treaty text of a mitigated form of the police powers doctrine in relation to the indirect expropriation standard.[79] This kind of provision, often included in an annex, tends to provide some

[79] The police powers doctrine is discussed in ch IV, section 3 The Police Powers Doctrine.

elements to help distinguish between an indirect expropriation and regulatory action that does not constitute indirect expropriation. For example, CETA offers the following guidance: the tribunal must take into account the economic impact of the measure, its duration, whether it interferes with the investor's reasonable expectations, and the object, context, and purpose of the state measure.[80] Then a separate paragraph tends to explain that non-discriminatory measures designed and applied to protect legitimate public welfare objectives, such as public health, safety, and the environment, do not constitute indirect expropriations. For instance, the Australia-Uruguay BIT (2019) establishes that

> 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.[81]

Although phrased as an interpretive statement, this latter part of the provision functions, in effect, as an exception to the indirect expropriation standard.

This type of clause was applied in the recent *Eco Oro v. Colombia* case, a dispute arising out of the respondent's measures in connection with the páramo ecosystem in Santurbán, an environmental conservation area, which affected the investor's mining rights under a concession contract.[82] Annex 811 on indirect expropriation of the Canada-Colombia free trade agreement (FTA) of 2008, applicable *in casu*, includes a mitigated form of the police powers doctrine. According to this provision:

[80] CETA annex 8-A(2).

[81] Australia-Uruguay BIT (2019) annex B(3)(b). Initially, this kind of provision was consistently accompanied by the phrase "except in rare circumstances" (eg CETA annex 8-A(3)) but increasingly new treaties do not incorporate this "exception to the exception". For another example, see Indonesia-Singapore BIT (2018) annex II.

[82] *Eco Oro Minerals Corp v. Colombia*, ICSID Case No. ARB/16/41, Decision on Jurisdiction, Liability and Directions on Quantum, 9 September 2021.

> Except in rare circumstances, such as when a measure or series of measures is so severe in the light of its purpose that it cannot be reasonably viewed as having been adopted in good faith, non-discriminatory measures by a Party that are designed and applied to protect legitimate public welfare objectives, for example health, safety and the protection of the environment, do not constitute indirect expropriation.[83]

The tribunal majority held that the challenged measures were non-discriminatory, they were adopted in good faith, and they were designed and applied to protect a legitimate public welfare objective, the environment.[84] The majority concluded that the measures were a legitimate exercise of Colombia's police powers and did not constitute indirect expropriation.[85] However, by majority, the tribunal found that Colombia had violated another investment protection, the treaty's minimum standard of treatment.[86]

### ii. Security exceptions

Exceptions for the protection of the state's essential security interests constitute probably the most important type of exception, since they safeguard an interest crucial to the very existence of the state.[87] The USMCA includes a typical essential security interests exception. According to this treaty:

> Nothing in this Agreement shall be construed to … preclude a Party from applying measures that it considers necessary for 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.[88]

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[83] Canada-Colombia FTA (2008) annex 811(2)(b).
[84] *Eco Oro v. Colombia* (Decision on Jurisdiction) (n 82) [642], [699].
[85] Ibid.
[86] Ibid [920].
[87] The author has discussed these at length in C. Titi, *The Right to Regulate in International Investment Law* (Nomos and Hart 2014) 78–94 and *passim*.
[88] USMCA (2018) art 32.2(1).

Like most security exceptions, especially in new investment treaties, this is a self-judging exception. Self-judging exceptions allow the host economy to be the "judge" of whether an exception applies and are thus regarded as offering states the broadest freedom in relation to the application of an exception.[89] They explain that the state can take "measures *it considers* necessary for" the protection of a regulatory interest, as opposed to "measures necessary for" an identified regulatory interest in non-self-judging exceptions.[90]

The essential security interests exception has been especially considered by arbitral tribunals in the context of the Argentine crisis disputes brought on the basis of the Argentina-US BIT of 1991. The facts that led to the disputes are well known and have been extensively discussed, but I will give a brief overview in order to engage with the case law. Argentina's economic recession of the late 1990s deepened in 2001, precipitating an economic and political crisis[91] that resulted in violent demonstrations, deaths, and a succession of five presidents in less than two weeks.[92] In an effort to "stabilize the economy" and restore confidence in the political system,[93] Argentina adopted a series of measures. Among them were the freezing of bank accounts, aimed to prevent a run on the banks with the *Corralito,*[94] and the abandonment of the currency board system that had pegged the Argentinean peso to the US dollar with

[89] That said, even self-judging exceptions do not remove the jurisdiction of investment tribunals. The latter can still conduct a good faith review. See W.W. Burke-White and A. von Staden, "Investment Protection in Extraordinary Times: The Interpretation and Application of Non-Precluded Measures Provisions in Bilateral Investment Treaties" (2008) 48 Virginia Journal of International Law 307, 376–381.

[90] Burke-White and von Staden (n 89) 376–381; Titi, *The Right to Regulate in International Investment Law* (n 87) 190–205.

[91] *BG Group Plc v. Argentina* (UNCITRAL) Final Award, 24 December 2007 [54]ff; *LG&E Energy Corp, LG&E Capital Corp and LG&E International Inc v. Argentina*, ICSID Case No. ARB/02/1, Decision on Liability, 3 October 2006 [54].

[92] *El Paso v. Argentina* (Award) (n 58) [91]; *BG v. Argentina* (Final Award) (n 91) [60], [72]; *CMS v. Argentina* (Award) (n 58) [64]; *LG&E v. Argentina* (Decision on Liability) (n 91) [63], [235]–[236].

[93] Burke-White and von Staden (n 89) 309.

[94] Decree 1570/2001, OJ 3 December 2001, No. 29787, 1.

the Emergency Law of January 2002.[95] These measures resulted in a spate of disputes, the most formidable in the history of investment arbitration.[96] The Argentina-US BIT of 1991, applicable in some of the disputes, contains a non-self-judging essential security interests exception in Article XI, according to which:

> This Treaty shall not preclude the application by either Party of measures necessary for the maintenance of public order, the fulfillment of its obligations with respect to the maintenance or restoration of international peace or security, *or the Protection of its own essential security interests*.[97]

In *LG&E v. Argentina*, the tribunal found that between December 2001 and April 2003, Argentina was in a severe crisis, which made it necessary to adopt measures to maintain public order and protect its essential security interests, in accordance with Article XI of the Argentina-US BIT.[98] The tribunal explained that Article XI does not only apply "in circumstances amounting to military action and war" but also to an economic crisis, whose severity could "equal that of any military invasion".[99] The tribunal concluded that for the period leading up to April 2003, Argentina was not to be held responsible and the investors should bear the brunt of the state measures.[100]

In contrast with the *LG&E v. Argentina* case, the reasoning of other tribunals in relation to Article XI of the Argentina-US BIT proved highly controversial. While purporting to apply the treaty's essential security interests exception, some of these tribunals conflated the treaty-based exception with the customary

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[95] Act 25.561, *Emergencia Pública y Reforma del Régimen Cambiario*, OJ 7 January 2002.
[96] C. Titi, "Investment Arbitration in Latin America: The Uncertain Veracity of Preconceived Ideas" (2014) 30(2) Arbitration International 357, 382.
[97] Argentina-US BIT (1991) art XI (emphasis added).
[98] *LG&E v. Argentina* (Decision on Liability) (n 91) [226]–[237].
[99] Ibid [238].
[100] Ibid [266].

international law defence of necessity.[101] They relied on the linguistic proximity between the requirement in Article XI that measures be "necessary" for the protection of the state's essential security interests and the plea of "necessity" in customary international law in order to turn to the latter at the expense of the treaty exception. Consequently, these awards were criticised for ignoring the applicable treaty's essential security interests exception and a few of them have now been annulled.[102] The award in *CMS v. Argentina*, although not annulled, was strongly criticised by the annulment committee[103] and this criticism has had an enormous impact on subsequent interpretations, serving as guidance to tribunals deciding other cases involving essential security interests exceptions. Since these tribunals focused on the necessity defence rather than on the treaty exception, this case law is discussed in Chapter IV.[104]

More recently, an essential security interests exception has been interpreted in *Deutsche Telekom v. India*, a dispute arising out of the cancellation of a contract concerning the provision of broadband services.[105] Drawing on the experience of the Argentine crisis disputes, and notably the *CMS* and *Sempra* decisions on annulment,[106] the tribunal stressed that there must be no confusion between the treaty exception and the necessity defence.[107] The

[101] See ch IV, section 2 Circumstances Precluding Wrongfulness, with a Focus on the Necessity Defence.
[102] Eg *Sempra Energy International v. Argentina*, ICSID Case No. ARB/02/16, Decision on Annulment, 29 June 2010; *Enron Creditors Recovery Corporation (formerly Enron Corporation) and Ponderosa Assets, LP v. Argentina*, ICSID Case No. ARB/01/3, Decision on Annulment, 30 July 2010.
[103] *CMS Gas Transmission Company v. Argentina*, ICSID Case No. ARB/01/8, Decision on Annulment, 25 September 2007.
[104] See ch IV, section 2 Circumstances Precluding Wrongfulness, with a Focus on the Necessity Defence.
[105] *Deutsche Telekom v. India*, PCA Case No. 2014-10, Interim Award, 13 December 2017.
[106] *CMS v. Argentina* (Decision on Annulment) (n 103); *Sempra v. Argentina* (Decision on Annulment) (n 102). See also ch IV, text to n 236ff.
[107] *Deutsche Telekom v. India* (Interim Award) (n 107) [229].

treaty exception has to be interpreted independently; it cannot incorporate "requirements from the customary international law state of necessity defense which are not present in the text of the Treaty".[108] Therefore, the respondent does not have to "prove that a measure is the 'only one' available, or that it must not have contributed to the situation of necessity at issue".[109] The tribunal added that a state measure could meet the requirements of the essential security interests clause, even if it does not meet the requirements of the necessity defence.[110]

Interpreting a non-self-judging exception,[111] the tribunal reasoned that, in order to determine whether there was an essential security interest, it owed "a degree of deference" to the state's assessment of the situation, although such deference could not be "unlimited".[112] According to the tribunal, essential security interests cannot be "stretched beyond their natural meaning".[113] Rather, they must concern "security", as opposed to other public welfare interests, and they must be "essential", that is, "go to the core (the 'essence') of state security".[114] In deciding whether a measure is "necessary", the tribunal returned to this need for deference towards the "host state's determination of necessity, given the state's proximity to the situation, expertise and competence".[115] However, the tribunal stressed again that such deference is not unlimited, since "unreasonable invocations" of the essential security interests exception would render the treaty's substantive protections "wholly nugatory".[116] Ultimately, the tribunal rejected the exception, holding

[108] Ibid.
[109] Ibid, see also [238]. On these requirements of the necessity defence, see ch IV, section 2i The necessity defence as a circumstance precluding wrongfulness.
[110] Ibid [229].
[111] Germany-India BIT (1995) art 12. See *Deutsche Telekom v. India* (Interim Award) (n 105) [231].
[112] *Deutsche Telekom v. India* (Interim Award) (n 105) [235].
[113] Ibid [236].
[114] Ibid.
[115] Ibid [238].
[116] Ibid.

that there was "a mix of reasons" for the respondent's measure, of which only some could be said to relate to essential security interests and the respondent had failed to establish that the measure "was necessary to protect those essential security interests".[117]

In the earlier *CC/Devas v. India* case,[118] the applicable exception imposed a "looser" nexus requirement: it provided for measures "directed to" the protection of the state's essential security interests (as opposed to measures "necessary for" it).[119] The dispute arose out of the termination of a contract following a policy decision to reserve part of the electromagnetic spectrum, known as the S-band, "for national needs, including for the needs of defence, para-military forces, railways and other public utility services as well as for societal needs, and having regard to the needs of the country's strategic requirements".[120] Part of this spectrum had previously been leased to the investor.[121]

The tribunal distinguished the exception from Article XI of the Argentina-US BIT, which provides that measures must be "necessary for" the protection of the state's essential security interests.[122] The tribunal held that the respondent did not have to establish the measure's necessity "in the sense that the measure adopted was the only one it could resort to in the circumstances".[123] In fact, the tribunal remarked that, if it had to apply an exception such as Article XI of the Argentina-US BIT, it should determine whether the measure was the only means available to the state.[124] This finding is problematic in that it appears to incorporate one of

[117] Ibid [284]–[285].
[118] *CC/Devas (Mauritius) Ltd, Devas Employees Mauritius Private Limited and Telcom Devas Mauritius Limited v. India*, PCA Case No. 2013-09, Award on Jurisdiction and Merits, 25 July 2016.
[119] India-Mauritius BIT (1998) art 11(3).
[120] *CC/Devas v. India* (Award on Jurisdiction and Merits) (n 118) [5].
[121] Ibid.
[122] Ibid [238].
[123] Ibid [243].
[124] Ibid [252]–[256].

the requirements of the necessity defence, not present in the treaty exception, and it is anyway contradicted by the tribunal's later statement that the necessity defence would not be applicable in such a case.[125]

Interpreting the exception applicable in the case, the tribunal held that the respondent should demonstrate that the measure was related to the state's essential security interests.[126] This tribunal also recognised that it owed a "wide measure of deference" to the respondent,[127] since a tribunal "may not sit in judgment on national security matters".[128] The tribunal added that national security relates to "the existential core of a State" and that an investor challenging a state security measure would face "a heavy burden of proof, such as bad faith".[129] The tribunal concluded that, if a state successfully invokes a national security exception, it cannot be asked to pay compensation of damages,[130] even though this does not remove the effect of wrongful actions that predate the essential security interests situation.[131]

*In casu*, while the tribunal majority had no difficulty deciding that the spectrum relating to "the needs of defence and para-military forces" was directed to the state's essential security interests and therefore fell under the exception, it found that this was not the case in respect of the spectrum relating to "railways and other public utility services as well as for societal needs, and having regard to the needs of the country's strategic requirements".[132] The tribunal majority concluded that although the state's actions were "in part 'directed to the protection of its essential security interests',

[125] See ch IV, section 2i The necessity defence as a circumstance precluding wrongfulness.
[126] *CC/Devas v. India* (Award on Jurisdiction and Merits) (n 118) [243].
[127] Ibid [244].
[128] Ibid [245].
[129] Ibid.
[130] Ibid [293].
[131] Ibid [294].
[132] Ibid [354].

that part remained undefined" and coexisted with "several other objectives" that were unrelated to national security.[133]

In short, essential security interests exceptions, especially self-judging exceptions, are regularly included in new generation treaties. The case law is still limited to a few awards and the exception tends to be dismissed. However, one can probably conclude that, although the early case law, notably some awards rendered under the Argentina-US BIT, was not satisfactory, lessons were learnt from that experience and the interpretation of essential security exceptions has improved. This is certainly true as regards the technical level — the manner in which tribunals approach the exception. This contrasts with the interpretation of general exceptions for the protection of public welfare objectives, which remains very much flawed, as the following section will show.

### iii. General exceptions for the protection of public welfare objectives

Increasingly, new investment treaties incorporate general exceptions for the protection of public welfare objectives beyond security.[134] This type of exception, initially modelled on Article XX of the GATT, was ushered into investment law with Canada's model BIT of the mid-2000s.[135] Article 10 of that model provided:

> Subject to the requirement that such measures are not applied in a manner that would constitute arbitrary or unjustifiable discrimination between investments or between investors, or a disguised restriction on international trade or investment, nothing in this Agreement shall be construed to prevent a Party from adopting or enforcing measures necessary:

[133] Ibid [371].
[134] Eg Australia-Peru FTA (2018) art 8.18; Israel-United Arab Emirates BIT (2020) art 14.
[135] Canadian Model BIT (2004) art 10(1).

(a) to protect human, animal or plant life or health;

(b) to ensure compliance with laws and regulations that are not inconsistent with the provisions of this Agreement; or

(c) for the conservation of living or non-living exhaustible natural resources.

Since then, this type of exception has been gaining currency, even though Canada appears to have removed this particular phrasing from its 2021 model BIT. Some treaties directly incorporate Article XX of the GATT, making it applicable *mutatis mutandis*.[136] Other treaties repeat the wording of Article XX of the GATT,[137] while others still introduce general exceptions styled after Article XX of the GATT but without the chapeau, the introductory paragraph that imposes the condition that the measures in question must not be applied in a manner that constitutes an arbitrary or unjustifiable discrimination or a disguised restriction on international investment.[138]

Unsurprisingly, for Canadian treaties were the ones to introduce general exceptions for the protection of public welfare objectives, the first arbitral interpretations of such clauses come from disputes brought on the basis of investment treaties to which Canada is party. However, as in the case of some of the Argentine crisis disputes, these interpretations sometimes leave a lot to be desired.

In *Copper Mesa v. Ecuador*, a dispute arising out of the termination of the investor's mining concession,[139] the applicable treaty included a general exceptions clause.[140] The tribunal took into account the

[136] Eg Argentina-Japan BIT (2018) art 15.
[137] Argentina-Chile FTA (2017) art 8.19; Israel-United Arab Emirates BIT (2020) art 14; cf Brazil-Ecuador BIT (2019) art 17(1).
[138] An example of a treaty that introduces self-judging general exceptions for the protection, *inter alia*, of human, animal, and plant life or health, the environment, and the state's essential security interests without a chapeau is the 2018 Argentina-United Arab Emirates BIT, see Argentina-United Arab Emirates BIT (2018) art 18.
[139] *Copper Mesa Mining Corporation v. Ecuador*, PCA Case No. 2012-2, Award, 15 March 2016.
[140] Canada-Ecuador BIT (1996) art XVII(3).

chapeau, requiring that state measures be not applied "in an arbitrary or unjustifiable manner".[141] It held that, in light of the circumstances of the case, the resolutions terminating the concession could not be described as "mere regulatory measures", because they "were made in an arbitrary manner and without due process".[142]

In *Eco Oro v. Colombia*, a dispute that arose out of measures prohibiting mining activities in an environmental conservation zone, the applicable treaty contained a general exceptions clause covering environmental measures.[143] In order to interpret this provision, the tribunal invoked Article 31(1) of the Vienna Convention of the Law of Treaties of 1969 but, rather than begin by examining the ordinary meaning of the treaty provision, it started with the preamble.[144] The tribunal observed that, in light of the preamble, the treaty's object and purpose is "to ensure a predictable commercial framework for business planning and investment in a manner that is consistent with environmental protection and conservation".[145] Accordingly, the tribunal reasoned that "neither environmental protection nor investment protection is subservient to the other, they must co-exist in a mutually beneficial manner".[146] In this sense, the tribunal reasoned that the treaty's general exception concerning environmental measures merely ensures that the state is "not prohibited" from taking the measures in question.[147] However, it is unclear what conditions the tribunal envisaged in which, absent the exception, the state may have been "prohibited" from taking such measures. As discussed in Chapter II, the state always retains its *lato sensu* right to regulate. The tribunal continued by noting that there is nothing in the treaty exception "permitting such action to be taken

[141] Ibid.
[142] *Copper Mesa v. Ecuador* (Award) (n 139) [6.66].
[143] Canada-Colombia FTA (2008) art 2201(3).
[144] *Eco Oro v. Colombia* (Decision on Jurisdiction) (n 84) [827]-[828].
[145] Ibid [828].
[146] Ibid.
[147] Ibid [829].

without the payment of compensation".[148] To support this reasoning, the tribunal referred to other treaty provisions, notably the treaty's annex on expropriation laying down the police powers doctrine and explaining that police powers measures "do not constitute indirect expropriation", that is, they do not constitute a breach of the treaty.[149] For the tribunal, if the contracting parties had meant for the general exceptions clause to exclude liability for measures falling within its scope, they would have drafted the clause in a manner similar to the treaty's annex on expropriation.[150] According to this line of reasoning, while "a State may adopt or enforce a measure pursuant to the stated objectives in [the treaty's general exceptions clause] without finding itself in breach of the FTA, this does not prevent an investor claiming under [the investment chapter] that such a measure entitles it to the payment of compensation".[151] In other words, the tribunal stated that the treaty exception made the state measures lawful but did not remove the duty to compensate. It added that, if no measure falling within the scope of the general exception gave rise to state liability, that is, to an obligation to compensate, this would lead to a conflict between the general exception and the treaty's police powers clause in the annex on expropriation, "which expressly acknowledges that in certain circumstances a measure taken for the protection of the environment may constitute indirect expropriation".[152] This interpretation is disappointing. It denies the general exceptions clause any practical usefulness, although it certainly shows the interpretive challenges that treaties with many potentially overlapping exceptions can create.

The tribunal further assumed that its analysis was supported by the ILC Articles on State Responsibility, notably Article 27, which deals with the consequences of invoking a circumstance

[148] Ibid.
[149] Ibid.
[150] Ibid.
[151] Ibid [830].
[152] Ibid [831].

precluding wrongfulness (but not the consequences of invoking a treaty exception!),[153] and Article 36, which concerns compensation as a form of reparation for, an even less related situation, an internationally *wrongful* act.[154] Thus, the tribunal seemed not only to conflate the treaty exception with the circumstances precluding wrongfulness under the ILC Articles on State Responsibility but to also mix up the consequences of upholding a circumstance precluding wrongfulness with reparation in case of a *wrongful* act. Neither of the two scenarios matched the tribunal's analysis, which was an analysis of the *treaty* exception.

The *Eco Oro* tribunal's findings are problematic for an additional reason. While the tribunal claimed to know the intentions of the contracting parties,[155] in reality, it summarily dismissed the express intent of the treaty parties, not only the respondent's but also Canada's. In its non-disputing party submission, Canada had stated that "[i]f the general exception applies, then there is no violation of the Agreement and no State liability. *Payment of compensation would therefore not be required*".[156]

Another unsatisfactory interpretation of a general exceptions clause is the interpretation in the earlier *Bear Creek v. Peru* case, which shared one tribunal member with *Eco Oro v. Colombia*.[157] The dispute arose out of the revocation of a mining licence. In its analysis, the tribunal conflated the treaty's general exceptions clause with the police powers doctrine.[158] According to the tribunal, the general

[153] See ch IV, section 2 Circumstances Precluding Wrongfulness, with a Focus on the Necessity Defence.
[154] *Eco Oro v. Colombia* (Decision on Jurisdiction) (n 82) [835].
[155] Ibid [829], [836], cf [831].
[156] *Eco Oro Minerals Corp v. Colombia*, ICSID Case No. ARB/16/41, Non-disputing Party Submission of Canada, 27 February 2020 [16] (emphasis added).
[157] *Bear Creek Mining Corporation v. Peru*, ICSID Case No. ARB/14/21, Award, 30 November 2017 [471]-[478].
[158] Instead, if the tribunal wanted to discuss the police powers doctrine, it should have done so in relation to the treaty's annex on expropriation, which included a mitigated form of the police powers doctrine (Canada-Peru FTA (2008) annex

exceptions clause in the Canada-Peru FTA[159] with its exhaustive list of regulatory interests "must lead to the conclusion that no other exceptions from general international law or otherwise can be considered applicable in this case".[160] This is a baffling statement. The tribunal appeared to indicate that by including general exceptions for public welfare interests, states render inapplicable all defences under international law. This reasoning is flawed for more than one reason. This is a very generic statement about the relationship between exceptions in treaty law and defences to be found in other sources of international law. In drawing its conclusion, the tribunal did not seem to have considered whether the *lex specialis-lex generalis* conflict rule is respected. Is the treaty's general exceptions clause a *lex specialis* in relation to all defences under international law? For example (let us leave customary international law aside for a moment), why would the treaty's general exceptions clause not allow the respondent to invoke defences based on general principles, such as good faith, estoppel, or the clean hands doctrine? The tribunal majority also seemed to be unaware of the distinction between primary and secondary rules drawn by the International Law Commission in relation to the circumstances preluding wrongfulness, such as the necessity defence, of the Articles on State Responsibility.[161] As will be discussed in the following chapter, such

812.1(c), see *Bear Creek v. Peru* (Award) (n 157) [368]ff). It was this relationship, between the treaty annex and the police powers doctrine, that would determine whether the latter could apply independently of its incorporation in the treaty annex or, as this author suspects, not, rather than the relationship between the treaty's general exceptions and the police powers doctrine.

[159] Canada-Peru FTA (2008) art 2201.

[160] *Bear Creek v. Peru* (Award) (n 157) [473].

[161] On this topic, see ch IV, section 2.ii The relationship between circumstances precluding wrongfulness and treaty exceptions. Philippe Sands in his partial dissent remarked that his agreement with the reasoning of the tribunal with respect to the police powers doctrine was without prejudice to the application of the necessity defence. This observation also raises its own problems. The distinction Sands aims to draw between the function of the police powers doctrine and the function of the necessity defence, one of the circumstances precluding wrongfulness, is difficult to justify, especially if both the necessity defence and the police powers doctrine are considered to be customary international law. It is also unclear in the dissent,

customary law defences are only applicable if the treaty is already found to have been violated.[162]

The tribunal found that the presence in the treaty of the general exceptions clause rendered the police powers doctrine inapplicable.[163] It further concluded summarily that the treaty's general exceptions did not apply either, since the revocation decree did not mention the protection of human life or health, as per the exception, and did not meet the requirements of the chapeau.[164] However, even had the tribunal found that the general exceptions clause was applicable, its usefulness would be limited. The tribunal reasoned that the treaty's general exceptions do "not offer any waiver from the obligation … to compensate" the investor for the treaty breach.[165] As in *Eco Oro v. Colombia*, this interpretation denies the exceptions clause its effectiveness. The tribunal concluded that the revocation decree violated the treaty, "irrespective of a possible applicability of the Exception in Article 2201 of the FTA"(!)

In *Infinito Gold v. Costa Rica*,[166] the applicable treaty contained an unusually-phrased general exceptions clause, which was combined with a "declaratory" right to regulate, that is, with an "otherwise consistent with this Agreement" condition.[167] The tribunal held that

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if he means to distinguish between the necessity defence and other circumstances precluding wrongfulness, eg *force majeure*. Such a distinction would be even more difficult to maintain. See *Bear Creek Mining Corporation v. Peru*, ICSID Case No. ARB/14/21, Partial Dissenting Opinion of Philippe Sands, 30 November 2017 [41].

[162] Ch IV, section 2.ii The relationship between circumstances precluding wrongfulness and treaty exceptions.

[163] *Bear Creek v. Peru* (Award) (n 157) [474].

[164] Ibid [475]-[476].

[165] Ibid [477].

[166] *Infinito Gold Ltd v. Costa Rica*, ICSID Case No. ARB/14/5, Award, 3 June 2021.

[167] Canada-Costa Rica BIT (1998) annex I(III) provides (emphasis added):

1. Nothing in this Agreement shall be construed to prevent a Contracting Party from adopting, maintaining or enforcing *any measure otherwise consistent with this Agreement* that it considers appropriate to ensure that investment activity in its territory is undertaken in a manner sensitive to environmental concerns.
2. Provided that *such* measures are not applied in an arbitrary or unjustifiable manner, or do not constitute a disguised restriction on investment, nothing

this type of clause cannot "be used to override mandatory treaty provisions".[168] According to the tribunal, the exception should be construed as acknowledging that the protection of the environment and of foreign investment "should, if possible, be reconciled… In other words, this provision reaffirms the State's right to regulate".[169] It is unclear, however, how such a provision "reaffirms" the right to regulate, since it does not relieve the state of the obligation to honour its treaty commitments or compensate the foreign investor in case of a breach. This reference to the state's right to regulate must therefore be understood as a reference to the state's *lato sensu* right to regulate under public international law.

In *Gold Reserve v. Venezuela*,[170] *Crystallex v. Venezuela*,[171] *Rusoro v. Venezuela*,[172] three gold mining disputes brought on the basis of the 1996 Canada-Venezuela BIT, the treaty's general exceptions clause was not considered at all. The BIT contains a provision similar to the one in *Infinito Gold v. Costa Rica*, combining general exceptions with a "declaratory" right to regulate.[173] Whether the clause with the particular phrasing could have served as a genuine exceptions clause is unclear. Even so, it is curious that it was not discussed, although Venezuela had invoked environmental grounds in its

in this Agreement shall be construed to prevent a Contracting Party from adopting or maintaining measures:

(a) necessary to ensure compliance with laws and regulations that are not inconsistent with the provisions of this Agreement;

(b) necessary to protect human, animal or plant life or health; or

(c) relating to the conservation of living or non-living exhaustible natural resources if such measures are made effective in conjunction with restrictions on domestic production or consumption.

[168] *Infinito Gold v. Costa Rica* (Award) (n 166) [773], citing Todd Weiler.

[169] Ibid [778].

[170] *Gold Reserve Inc v. Venezuela*, ICSID Case No. ARB(AF)/09/1, Award, 22 September 2014.

[171] *Crystallex International Corporation v. Venezuela*, ICSID Case No. ARB(AF)/11/2, Award, 4 April 2016.

[172] *Rusoro Mining Ltd v. Venezuela*, ICSID Case No. ARB(AF)/12/5, Award, 22 August 2016.

[173] Canada-Venezuela BIT (1996) annex II(10(a)-(b).

defence.[174] In fact, it does not seem that the respondent invoked the clause, yet the tribunal could still have examined it *sua sponte*, in accordance with *iura novit curia*.[175] The *Rusoro* award was partially set aside in 2019 on unrelated grounds.[176]

In conclusion, while general exceptions for public welfare objectives have started to become more mainstream in new generation investment treaties, their interpretation remains a vexed matter. It is true that tribunals have not yet had much occasion to interpret general exceptions clauses. However, if some of the recent case law, such as *Bear Creek v. Peru* and *Eco Oro v. Colombia*, is anything to go by, important limits are placed on the usefulness of this type of clause. Whether this is because these clauses introduce far-reaching exceptions and tribunals have difficulty giving them full effect, or whether this reflects the need for more rigorous arbitrator appointments to ensure a public international law background, or at least competence to interpret international investment agreements, is an open question.

## 5. Some Reflections on the Drafting of Treaty Exceptions and their Interpretation

Over the last few years, states have been progressively incorporating the right to regulate in their international investment

[174] *Gold Reserve v. Venezuela* (Award) (n 170) 2014 [557], [590]; *Crystallex v. Venezuela* (Award) (n 171) [344], [377]-[378]; *Rusoro v. Venezuela*, (Award) (n 172) [381].
[175] For some recent cases upholding *iura novit curia* (or *iura novit arbiter*), see eg *PV Investors v. Spain*, PCA Case No. 2012-14, Final Award, 28 February 2020 [519], [552]; *(DS)2, SA, Peter de Sutter and Kristof De Sutter v. Madagascar*, ICSID Case No. ARB/17/18, Award, 17 April 2020 [132]; *Deutsche Telekom v. India*, PCA Case No. 2014-10, Final Award, 27 May 2020 [68]; *Carlos Ríos and Francisco Ríos v. Chile*, ICSID Case No. ARB/17/16, Award, 11 January 2021 [130]; *Astrida Benita Carrizosa v. Colombia*, ICSID Case No. ARB/18/5, Award, 19 April 2021 [20]; *Infinito Gold v. Costa Rica* (Award) (n 166) [280]. See also A.M. Tanzi, "On Judicial Autonomy and the Autonomy of the Parties in International Adjudication, with Special Regard to Investment Arbitration and ICSID Annulment Proceedings" (2020) 33 Leiden Journal of International Law 57.
[176] Judgment of the Paris Court of Appeal (29 January 2019).

agreements, although this is not always recognised.[177] The yardstick by which to measure the effectiveness of this right to regulate as introduced in treaties is normally the case law. However, relatively few disputes have as yet been brought on the basis of new generation treaties with exceptions. On the rare occasions when such treaties were applicable, as this chapter has shown, they have often received unsatisfactory interpretations that not only fall foul of the Vienna Convention on the Law of Treaties of 1969 but sometimes even defy common sense. Some of these interpretations are problematic in that they interpret treaties with exceptions as if they were treaties without exceptions.

Tribunals have been shown to not always give full effect to general exceptions clauses. One could speculate as to whether this is due to the fact that some such clauses are very broad, practically capable of excusing all but the most egregious arbitrary and discriminatory state conduct or denial of justice — the fear invoked by the *Pope & Talbot* tribunal that "a blanket exception for regulatory measures would create a gaping loophole" in international investment protections.[178] In effect, some treaties include a combination of exceptions and carve-outs so far-reaching that make one wonder what the real reason for signing the investment treaty was in the first place. Introducing the right to regulate in such a sweeping manner that it appears to defeat the very purpose of investment protection can raise challenging interpretive dilemmas and beg the question: have we gone too far in the attempt to safeguard the state's right to regulate?

It is true that there is lingering uncertainty about the exact manner of the application of broad exceptions and, in particular, general exceptions for public welfare objectives. Doubts have been

[177] Eg this became obvious in some developing state submissions in UNCITRAL Working Group III, during the Fourth Intersessional Meeting on Investor-State Dispute Settlement Reform organised by the Republic of Korea on 2–3 September 2021.

[178] *Pope & Talbot Inc v. Canada* (UNCITRAL) Interim Award, 26 June 2000 [99].

expressed, for instance, about how these exceptions relate to direct expropriation and fair and equitable treatment.[179] One author has pertinently argued that it seems surprising that, by introducing general exceptions in their investment treaties, states should have meant "to provide their investors [with] less protection than what is provided by customary international law".[180] New provisions on the right to regulate do not always make the adjudicator's task easier.[181] Yet the fact remains that the right to regulate is sometimes not given effect, even though it is present in the treaty text.

Different questions are raised when treaty provisions on the right to regulate are too narrow. States, for instance, have been drafting exceptions to deal with types of situations that gave rise to disputes in the past. In the wake of *Philip Morris v. Uruguay* and *Philip Morris v. Australia*, a few treaties included specific provisions on tobacco control measures. The Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP), signed in 2018 and incorporating the earlier Trans-Pacific Partnership (TPP), provides an "exception" for tobacco control measures essentially allowing a party to render claims challenging such measures non-arbitrable.[182] The 2021 Canadian model BIT aims to "ensure that all present or future tobacco control measures are automatically excluded from dispute resolution and, therefore, cannot be challenged by investors

[179] Newcombe and Paradell (n 56) 505–506; B. Legum and I. Petculescu, "GATT Article XX and International Investment Law", in R. Echandi and P. Sauvé (eds), *Prospects in International Investment Law and Policy* (Cambridge University Press 2013); Titi, *The Right to Regulate in International Investment Law* (n 87) 179–188.

[180] C. Lévesque, "The Inclusion of GATT Article XX Exceptions in IIAs: A Potentially Risky Policy", in R. Echandi and P. Sauvé (eds), *Prospects in International Investment Law and Policy: World Trade Forum* (Cambridge University Press 2013) 368.

[181] Consider, for example, a clause such as Article 8.9(1) of CETA, which is not phrased as an exception and whereby the parties "reaffirm their right to regulate" to achieve a broad range of legitimate policy objectives, including the protection of public health, safety, the environment, social or consumer protection and the promotion and protection of cultural diversity.

[182] CPTPP (TPP) art 29.5.

under ISDS or State-to-State dispute settlement".[183] Following the COVID-19 pandemic and in response to disputes potentially arising out of measures adopted during the pandemic, we may see new provisions in treaties taking into account states' recent experience, if — and it is still a big "if" — COVID-19-related claims arise in big numbers.[184] In the short term, such provisions targeting narrowly-identified situations (tobacco control measures, measures to tackle a pandemic or to rebound after a pandemic) may appear to be useful. However, in the long term, they could unnecessarily complicate the interpretation of investment treaties.

For a start, incorporating too narrowly-defined exceptions in the treaty may create the impression that other concerns, not expressly included, are not covered. The treaty becomes complex and difficult to interpret — too long, sometimes contradictory. States react to the past but cannot predict the future. Inevitably, new situations will arise that are not covered by the narrow exception. What constitutes better treaty drafting is to include broader exceptions — with some interpretive clarifications, when necessary, in order to guide interpretation.

Ultimately, the question of how to interpret and apply the right to regulate as incorporated in an investment treaty must depend on the particular wording of the treaty and its exceptions and on the individual case. This exercise must certainly take into account the widely-accepted techniques of interpretation and conflict resolution in international law, including the general interpretation rule in the Vienna Convention on the Law of Treaties (art 31), effective treaty interpretation (art 32 of the Vienna Convention on the Law of Treaties), and the *lex specialis* conflict rule. These

[183] See "2021 FIPA model — Summary of main changes" <https://www.international.gc.ca/trade-commerce/trade-agreements-accords-commerciaux/agr-acc/fipa-apie/2021_model_fipa_summary-2021_modele_apie_resume.aspx?lang=eng>. The provision will probably be included in Annex III: Exclusions from Dispute Settlement, whose text is not available at the time of writing.

[184] Cf Indonesia-Republic of Korea CEPA (2020) art 7.19(3)(b).

interpretation techniques revolve around the specific configuration of legal norms that an international court or tribunal is called to apply. It is therefore very difficult, if not impossible, to state in the abstract how one is to interpret the right to regulate. This is obvious when the treaty itself provides contradictory information, when the treaty is silent on the right to regulate (eg then one might ask, is for example the police powers doctrine customary international law?) and even when the treaty expressly includes the right to regulate.

Let us take an example. Annex 8-A of CETA lists factors that must be taken into account in order to decide whether the challenged state measure was an indirect expropriation or a non-compensatory regulatory measure. These factors include the "object, content and intent" of the measure in question, its economic impact, and the extent to which it interferes with "distinct, reasonable investment-backed expectations".[185] The annex further incorporates the police powers doctrine combined with a proportionality test: except in rare circumstances "when the impact of a measure or series of measures is *so severe in light of its purpose* that it appears manifestly excessive", non-discriminatory measures taken for the protection of public welfare objectives do not constitute an indirect expropriation.[186] The application of Annex 8-A of CETA cannot be automatic but requires us to look carefully into the particular case and match the factual matrix to the applicable law.

Tribunals' most difficult task then is to decide whether an exception applies. Yet, as and when a tribunal finds that the exception applies, the interpretation rule is — or ought to be — simple. It was stated by the *CMS* annulment committee in 2007 in relation to the essential security interests exception in the Argentina-US BIT: "Article XI is a threshold requirement: if it applies, the substantive obligations under the Treaty do not apply".[187] If the exception applies

[185] CETA annex 8-A(2).
[186] CETA annex 8-A(3) (emphasis added).
[187] *CMS v. Argentina* (Decision on Annulment) (n 103) [129].

and the substantive investment protections do not apply, the state bears no international responsibility and, contrary to what some of the above tribunals decided, there is no need to compensate.

## 6. Conclusion

Over the last few years, states have been increasingly incorporating the right to regulate in their international investment agreements. They have done so by including references to regulatory interests and the "right to regulate" in the preamble, by referring to the right to regulate in the main body of the treaty, and especially by drafting exceptions, including essential security interests exceptions and general exceptions for the protection of other public welfare objectives, such as the environment, safety, and public health. This chapter has argued that, while not always acknowledged by states, the right of the state to regulate is already safeguarded by new generation treaties. Some of them possibly even go too far by incorporating too many or too far-reaching exceptions. However, challenges remain. In particular, the case law yet leaves a lot to be desired. This is especially the case when investment tribunals interpret treaties with exceptions as if they were treaties without exceptions. It is very early to tell how the interpretation of new generation treaties that incorporate the right to regulate will evolve.

# IV.

## The Right to Regulate and Customary International Law

### 1. Introduction

Customary international law too can be a source of the state's right to regulate. Although the question of a hierarchy of norms in international law is contested (at least beyond *ius cogens* and the Charter of the United Nations),[188] in principle, treaty law will prevail over customary international law "*as between the parties to the treaty*".[189] In practice, customary international law may apply to an investment dispute, so long as there is no contrary *lex specialis* in the applicable investment treaty or while respecting the primary-secondary rules distinction of the International Law Commission, both of which are considered in this chapter. The analysis that follows will enquire into the right to regulate outside treaty law. It will focus in turn on the circumstances precluding wrongfulness of the International Law Commission's Articles on State Responsibility, an instrument that is meant to codify the customary international law on state responsibility,[190] and the police powers doctrine,

[188] M. Prost, "Sources and the Hierarchy of International Law", in S. Besson and J. d'Aspremont (eds), *The Oxford Handbook of the Sources of International Law* (Oxford University Press 2017); E. de Wet, "Sources and the Hierarchy of International Law", in Besson and d'Aspremont (eds), *The Oxford Handbook of the Sources of International Law* (Oxford University Press 2017); C. Greenwood, *Sources of International Law* (2008) <http://legal.un.org/avl/pdf/ls/greenwood_outline.pdf>; D. Shelton, "Normative Hierarchy in International Law" (2006) 100(2) American Journal of International Law 291; M. Prost, "Hierarchy and the Sources of International Law" (2017) 39(2) Houston Journal of International Law 285.

[189] Greenwood (n 188) (emphasis in original).

[190] J. Crawford, *State Responsibility: The General Part* (Cambridge University Press 2013) 45–49; International Law Commission, Draft Articles on Responsibility of States for Internationally Wrongful Acts, with Commentaries, Report adopted at the

which some tribunals have interpreted as reflecting customary international law.

### 2. Circumstances Precluding Wrongfulness, with a Focus on the Necessity Defence

The ILC Articles on State Responsibility establish six circumstances precluding the wrongfulness of a state's conduct. These circumstances are consent (art 20), self-defence (art 21), countermeasures (art 22), *force majeure* (art 23), distress (art 24), and necessity (art 25). In principle, *force majeure* and necessity are the two most relevant circumstances that may preclude the wrongfulness of state conduct in international investment law. Not all circumstances precluding wrongfulness are relevant to international investment law. One of the reasons is that the ILC Articles on State Responsibility were drafted to govern interstate relations, rather than *investor*-state relations. This can raise the question of whether the ILC Articles as a whole are applicable to investment disputes. However, a convincing argument can be made in favour of applying them to investor-state relations by analogy.[191]

This section addresses, first, the plea of necessity, since this is the defence that has mostly been discussed in the context of investment disputes, before turning to the relationship between circumstances precluding wrongfulness and treaty exceptions, and, finally, the question of compensation when upholding a circumstance precluding wrongfulness.

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ILC's fifty-third session (2001) *Yearbook of the International Law Commission II*, Part Two, General Commentary, para 1.

[191] C. Titi, *The Right to Regulate in International Investment Law* (Nomos and Hart 2014) 268–269.

### i. The necessity defence as a circumstance precluding wrongfulness

The necessity defence is reflected in Article 25 of the ILC Articles on State Responsibility. According to this provision, necessity may not be invoked as a ground for precluding wrongfulness unless two positive (para 1) and two negative (para 2) conditions are met. Article 25 provides:

> 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.

It is beyond the purpose of this study to explore at any length the necessity defence.[192] Instead, I would like to focus on two conditions for its invocation and the way they have been interpreted in arbitral case law: the requirement that the act be "the only way" for the state to protect an essential interest and the condition that the state must not have contributed to the situation of necessity.

[192] For an in-depth analysis of the necessity defence in investment disputes, see Titi, *The Right to Regulate in International Investment Law* (n 191) 236–270.

According to the ILC commentary, the "only way" requirement precludes application of the necessity defence if other means are available, even if these are costlier or "less convenient".[193] Necessity is inherent in the defence; conduct that goes "beyond what is strictly necessary" will not allow the plea to be upheld.[194] In the Argentine crisis disputes, tribunals that examined the necessity defence also considered the "only way" requirement. In *CMS v. Argentina*, the tribunal relied on the various views presented by the parties and economists, some of which discussed alternatives to the measures adopted, including "dollarization of the economy, granting of direct subsidies to the affected population or industries and many others", to conclude that the "only way" requirement was not met.[195] In *Enron v. Argentina*, the tribunal also noted that the parties and their experts were divided regarding whether Argentina's measures were "the only way" to deal with the crisis.[196] Somewhat ironically, the tribunal added that "[a] rather sad world comparative experience in the handling of economic crises, shows that there are always many approaches to address and correct such critical events, and it is difficult to justify that none of them were available in the Argentine case".[197] In *Sempra v. Argentina*, the tribunal adopted similar reasoning.[198] These tribunals' interpretation of the only way requirement raises a very high threshold for the successful invocation of the necessity defence. Let us consider for instance the interpretation of the *Enron* tribunal. That tribunal had found that an economic crisis may qualify as an essential security interest.[199]

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[193] International Law Commission, Articles on Responsibility of States for Internationally Wrongful Acts, with Commentaries (n 190) Part Two, art 25, para 15.
[194] Ibid.
[195] *CMS Gas Transmission Company v. Argentina*, ICSID Case No. ARB/01/8, Award, 12 May 2005 [323]-[324].
[196] *Enron Creditors Recovery Corporation (formerly Enron Corporation) and Ponderosa Assets, LP v. Argentina*, ICSID Case No. ARB/01/3, Award, 22 May 2007 [308].
[197] Ibid.
[198] *Sempra Energy International v. Argentina*, ICSID Case No. ARB/02/16, Award, 28 September 2007 [350]-[351].
[199] *Enron v. Argentina* (Award) (n 196) [332].

However, when considering the "only way" requirement, it decided that there are "always" many alternatives, essentially ruling out application of the necessity defence to economic crises altogether. If there are "always" alternatives, the "only way" requirement can *never* be satisfied nor can the defence ever apply to an economic crisis. This seems to be a narrow interpretation indeed.

In contrast with the above decisions, in *LG&E v. Argentina*, the tribunal, which examined the necessity defence in a complementary manner, since it had already found that the treaty's essential security interests exception was applicable,[200] also considered the "only way" requirement. The tribunal reasoned that "an economic recovery package was the only means to respond to the crisis. Although there may have been a number of ways to draft the economic recovery plan, the evidence" demonstrated that "an across-the-board response was necessary".[201] The tribunal reasoned that its analysis of Article 25 supported its interpretation of the treaty's essential security interests exception[202] and that the "only way" requirement was met.[203] While this interpretation too can surprise and more careful wording may have been preferable, this reasoning has the advantage of rendering the "only way" requirement effective. The *LG&E* tribunal's finding is exceptional; investment tribunals since then have generally held that the "only way" requirement was not satisfied.[204]

An example of a different kind of dispute where a tribunal dismissed the argument that the "only way" requirement was met

[200] *LG&E Energy Corp, LG&E Capital Corp and LG&E International Inc v. Argentina*, ICSID Case No. ARB/02/1, Decision on Liability, 3 October 2006 [245].
[201] Ibid [257].
[202] Ibid [258].
[203] Ibid [259].
[204] See eg *Suez, Sociedad General de Aguas de Barcelona SA and Interagua Servicios Integrales de Agua SA v. Argentina*, ICSID Case No. ARB/03/17, Decision on Liability, 30 July 2010 [238]; *Unión Fenosa Gas, SA v. Egypt*, ICSID Case No. ARB/14/4, Award, 31 August 2018 [8.46], [8.48]; *Guris Construction and Engineering Inc and others v. Syria*, ICC Case No. 21845/ZF/AYZ, Final Award, 31 August 2020 [320].

was *Suez and Interagua v. Argentina*.[205] The dispute, which related to a concession for water distribution and waste water treatment in the Province of Santa Fe, arose out of a series of alleged acts and omissions, including Argentina's alleged failure to apply previously agreed adjustments to the tariff regime.[206] Considering the "only way" requirement, the tribunal reasoned that the provision of water and sewage services was "vital to the health and well-being of a large population and was therefore an essential interest" of both the state and the province.[207] However, the tribunal remained unconvinced that the only way to safeguard this essential interest was "by adopting measures that would subsequently violate the treaty rights of the Claimants' investments to fair and equitable treatment".[208] The tribunal suggested that the province could have resorted to "more flexible means to assure the continuation of the water and sewage services to the people of Santa Fe and at the same time respected its obligations of fair and equitable treatment. The two were by no means mutually exclusive".[209]

The second condition in Article 25 that has been much discussed in investment disputes is the requirement that the state must not have contributed to the situation of necessity. According to the ILC commentary, for the necessity defence to be precluded under this condition, "the contribution to the situation of necessity must be sufficiently substantial and not merely incidental or peripheral".[210] Here too, it is important to consider the case law in order to understand how this condition has been interpreted. In *CMS v. Argentina*, the tribunal found that Argentina's contribution to the crisis had been "sufficiently substantial".[211] The tribunal

[205] *Suez and Interagua v. Argentina* (n 204).
[206] Ibid.
[207] *Suez and Interagua v. Argentina* (Decision on Liability) (n 204) [238].
[208] Ibid.
[209] Ibid.
[210] International Law Commission, Articles on Responsibility of States for Internationally Wrongful Acts, with Commentaries (n 190) Part Two, art 25, para 20.
[211] *CMS v. Argentina* (Award) (n 195) [329].

considered that, although the crisis was not attributable to one particular government, the policies that had been adopted over a period of time contributed significantly to the crisis and exogenous factors, while complicating the situation, did not exempt Argentina from its responsibility.[212]

In *Enron v. Argentina* and *Sempra v. Argentina*, the tribunals acknowledged that both endogenous and exogenous factors intervened, but they did not pronounce on their respective contribution to the crisis.[213] Both concluded, without further elaboration, that the respondent state had substantially contributed to the situation of necessity and that it could not "be claimed that the burden falls entirely on exogenous factors".[214] Argentina was therefore found to be responsible.

Other tribunals too held that Argentina had contributed to the crisis.[215] In *El Paso v. Argentina*, another dispute arising out of Argentina's economic and financial crisis, the tribunal, after considering at length the respondent's potential contribution to the crisis,[216] held that both internal and external factors were at the root of the crisis.[217] It reasoned that the respondent's "failure to control several internal factors, in particular the fiscal deficit debt accumulation and labour market rigidity, substantially contributed to the crisis".[218] However, the *El Paso* tribunal examined the respondent's contribution to the crisis, not while considering Article 25 of the ILC Articles on State Responsibility, but as a direct

[212] Ibid.
[213] *Enron v. Argentina* (Award) (n 196) [311]; *Sempra v. Argentina* (Award) (n 198) [353].
[214] *Enron v. Argentina* (Award) (n 196) [312]; *Sempra v. Argentina* (Award) (n 198) [354].
[215] *National Grid PLC v. Argentina* (UNCITRAL) Award, 3 November 2008 [260]; *Suez and Interagua v. Argentina* (Decision on Liability) (n 204) [264]; *Impregilo SpA v. Argentina*, ICSID Case No. ARB/07/17, Award, 21 June 2011 [356]-[359].
[216] *El Paso Energy International Company v. Argentina*, ICSID Case No. ARB/03/15, Award, 31 October 2011 [649]-[670].
[217] Ibid [656].
[218] Ibid [656], [665].

condition for the application of the treaty's essential security interests exception.[219]

In *LG&E v. Argentina* and in *Continental Casualty v. Argentina*, the tribunals came to a different conclusion regarding the respondent's contribution to the situation of necessity. According to the *LG&E* tribunal, "the attitude adopted by the Argentine Government has shown a desire to slow down by all the means available the severity of the crisis"[220] and there was no evidence that the respondent had contributed to it.[221] In *Continental Casualty v. Argentina*, the tribunal delved into an in-depth analysis of the state's potential contribution to the crisis. It held that, while a state is responsible for its economic decisions,[222] the policies that ultimately led to the crisis had been deemed to be "sound economic policies which had been beneficial for years to Argentina's economy" and had been "praised by the international financial community and by many qualified observers", such as the International Monetary Fund (IMF) and the United States.[223] It had been argued that the respondent could have dismissed "the advice it was receiving" or that it could have pursued the policies recommended to it in a more determined manner.[224] However, in both cases, the tribunal noted, "conflicting qualified views ha[d] been expressed retrospectively on the soundness and feasibility of those policies or of the alternatives".[225] The tribunal concluded that, in order to avoid the crisis, Argentina ought to have adopted "different policies years before, against the advice

[219] Ibid [665], stating that, "having found that Article XI is not 'self-judging', the Tribunal has the power and duty to make sure that *all conditions for its application* are satisfied, including the absence of a substantial contribution by Argentina to the crisis of 2001", emphasis added).
[220] *LG&E v. Argentina* (Decision on Liability) (n 200) [256].
[221] Ibid [257].
[222] *Continental Casualty Company v. Argentina*, ICSID Case No. ARB/03/9, Award, 5 September 2008 [234]-[236].
[223] Ibid [235].
[224] Ibid [236].
[225] Ibid.

and support that [it] was receiving from the outside".[226] In this light, the tribunal found that Argentina was not prevented from invoking the treaty's essential security interests exception.[227] As in *El Paso v. Argentina*, the *Continental Casualty* tribunal appeared to conflate the investment treaty's essential security interests exception with the conditions for a successful invocation of Article 25 of the ILC Articles on State Responsibility.[228]

The necessity defence was also invoked in *Pezold v. Zimbabwe*, a dispute arising out of the expropriation of land and other property as part of the respondent's land reform programme.[229] The tribunal rejected the respondent's plea of necessity, because the state was found to not only have "have contributed to its economic decline", but to also be "one of the primary instigators of the situation that gave rise to the imminent peril".[230]

In conclusion, the necessity defence as a circumstance precluding wrongfulness can be relevant to investment disputes. The case law provides mixed results and the reasoning often comes from the interpretation of treaty exceptions. Yet what does become clear is that invocation of the defence is subject to a particularly high threshold.

### ii. The relationship between circumstances precluding wrongfulness and treaty exceptions

In order to better understand the relationship between the circumstances precluding wrongfulness of the ILC Articles on State Responsibility and treaty exceptions, it is important to consider the distinction between primary and secondary rules, as well as

[226] Ibid.
[227] Ibid.
[228] Ibid.
[229] *Bernhard von Pezold and others v. Zimbabwe*, ICSID Case No. ARB/10/15, Award, 28 July 2015.
[230] Ibid [667].

the distinct function of a treaty exception as a *lex specialis* when compared to the customary law defences. The International Law Commission has explained that "the rules that place obligations on States, the violation of which may generate responsibility" (essentially treaty law) are *primary* rules,[231] while the rules on state responsibility are *secondary* rules. Accordingly, the emphasis in the Articles on State Responsibility is on the secondary rules, that is, "the general conditions under international law for the State to be considered responsible for wrongful actions or omissions, and the legal consequences which flow therefrom".[232] The Articles on State responsibility do not attempt to identify the international obligations whose breach "gives rise to responsibility".[233] Rather, this is "the function of the primary rules".[234] The ILC Articles on State Responsibility apply to the whole field of state responsibility; in this sense, they are general in nature and apply to states' international obligations, independently of what underlying primary obligations may have been breached.[235]

In *CMS v. Argentina*, the annulment committee explained that the necessity defence was "only relevant once it has been decided that there has otherwise been a breach of those substantive obligations".[236] In other words, the customary international law defence "could only be subsidiary to the exclusion based on Article XI".[237] The tribunal should have examined "first whether there had

[231] International Law Commission (1970) *Yearbook of the International Law Commission II*, Part Two, 306, para 66.
[232] International Law Commission, Articles on Responsibility of States for Internationally Wrongful Acts, with Commentaries (n 190) Part Two, General Commentary, para 1.
[233] Ibid.
[234] Ibid. See also International Law Commission (1970) *Yearbook of the International Law Commission II* (n 231) Part Two, 306, para 66.
[235] International Law Commission, Articles on Responsibility of States for Internationally Wrongful Acts, with Commentaries (n 190) Part Two, General Commentary, para 5.
[236] *CMS Gas Transmission Company v. Argentina*, ICSID Case No. ARB/01/8, Decision on Annulment, 25 September 2007 [129].
[237] Ibid [132].

been any breach of the BIT and whether such a breach was excluded by Article X I. 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".[238]

The *CMS* annulment committee continued to also paint a different picture. Moving beyond the distinction between primary and secondary rules, the committee concluded that the treaty exception and the necessity defence have a relationship of *lex specialis* to *lex generalis*.[239] Accordingly, it is the exception (*in casu*, Article XI of the Argentina-US BIT) that is applicable as a *lex specialis*.[240] The *lex specialis* principle emphasises that, in addition to being general and "secondary", the ILC Articles on State Responsibility are also residual.[241] The principle is generally understood to involve rules that belong to the same hierarchical order, rather than become relevant in a primary-secondary rules relationship.[242] This *lex specialis* interpretation has also been adopted in more recent awards that tend to avoid the distinction between primary and secondary rules,[243] sometimes closely echoing the reasoning of the *CMS* Committee in this respect.[244]

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[238] Ibid [134].
[239] Ibid [133].
[240] Ibid.
[241] International Law Commission, Articles on Responsibility of States for Internationally Wrongful Acts, with Commentaries (n 190) Part Two, General Commentary, para 5; Crawford (n 190) 65. See also ILC Articles on State Responsibility art 55.
[242] C. Binder, "Changed Circumstances in Investment Law: Interfaces between the Law of Treaties and the Law of State Responsibility with a Special Focus on the Argentine Crisis", in C. Binder et al. (eds), *International Investment Law for the 21st Century — Essays in Honour of Cristoph Schreuer* (Oxford University Press 2009) 620.
[243] Eg *Sempra Energy International v. Argentina*, ICSID Case No. ARB/02/16, Decision on Annulment, 29 June 2010; *Enron Creditors Recovery Corporation (formerly Enron Corporation) and Ponderosa Assets, LP v. Argentina*, ICSID Case No. ARB/01/3, Decision on Annulment, 30 July 2010; *El Paso Energy International Company v. Argentina*, ICSID Case No. ARB/03/15, Award, 31 October 2011.
[244] *Sempra v. Argentina* (Decision on Annulment) (n 243) [200].

### iii. The question of compensation

Finally, it is worth considering whether upholding a circumstance precluding wrongfulness has the same effect as upholding a treaty exception with respect to compensation. As previously discussed, if an exception applies, there is no duty to compensate.[245] Under the ILC Articles on State Responsibility, the issue of compensation when upholding a circumstance precluding wrongfulness remains an open question. According to Article 27:

> The invocation of a circumstance precluding wrongfulness in accordance with this chapter is without prejudice to … [t]he question of compensation for any material loss caused by the act in question.[246]

Article 27 is described as a without prejudice clause.[247] The article is silent on the question of whether compensation is payable, in other words, it is "a reservation as to questions of possible compensation".[248] Rather, the provision "contemplates that sometimes a state relying on a circumstance to preclude the wrongfulness of an act may nonetheless be expected to make good any material loss suffered by a state affected by that act".[249] The history of the adoption of this clause reveals that whether or not there is a need to make good material loss may depend on the actual circumstance invoked in order to preclude wrongfulness.[250] According to the ILC commentary, it is "for the State invoking a circumstance precluding wrongfulness to agree with any affected

[245] See ch III, section 5 Some Reflections on the Drafting of Treaty Exceptions and their Interpretation.
[246] ILC Articles on State Responsibility art 27(b).
[247] International Law Commission, Articles on Responsibility of States for Internationally Wrongful Acts, with Commentaries (n 190) Part Two, art 27, Commentary, para 1.
[248] Ibid para 4, see also para 6.
[249] Crawford (n 190) 318.
[250] Ibid 318–319.

States on the possibility and extent of compensation payable in a given case".[251]

In *CMS v. Argentina*, the tribunal reasoned that the necessity defence "may preclude the wrongfulness of an act, but it does not exclude the duty to compensate the owner of the right which had to be sacrificed".[252] This finding was criticised by the annulment committee.[253] For a start, the tribunal had relied on the ILC Articles on State Responsibility. The annulment committee pointed out that the tribunal should have examined compensation under the investment treaty, if the adopted measures fell within the scope of the treaty's essential security interests exception.[254] To the extent that that exception applied, it "excluded the operation of the substantive provisions of the BIT".[255] The second criticism was that the tribunal had anyway rejected Argentina's necessity defence.[256] Therefore, "Article 27 was not applicable and the paragraphs relating to that Article were obiter dicta which could not have any bearing on the operative part of the Award".[257] Article 27 is applicable when one of the circumstances precluding wrongfulness is upheld, not when these circumstances are dismissed. In that case, one needs to turn to Article 34 of the ILC Articles on State Responsibility, which provides for reparation.[258] The annulment committee further stressed, what seemed to be unclear in the award, that "Article 27 itself is a 'without prejudice' clause, not a stipulation. It refers to

[251] International Law Commission, Articles on Responsibility of States for Internationally Wrongful Acts, with Commentaries (n 190) Part Two, art 27, Commentary, para 6.
[252] *CMS v. Argentina* (Award) (n 195) [388].
[253] *CMS v. Argentina* (Decision on Annulment) (n 236) [144]-[150].
[254] Ibid [146].
[255] Ibid.
[256] Ibid [331].
[257] Ibid [145].
[258] International Law Commission, Articles on Responsibility of States for Internationally Wrongful Acts, with Commentaries (n 190) Part Two, art 34; Crawford (n 190) ch 15.

'the question of compensation' and does not attempt to specify in which circumstances compensation could be due".[259]

More recently, in *South American Silver v. Bolivia*, the tribunal, discussing what it found to be a direct expropriation, stated that the respondent's plea of necessity "was not designed to excuse the non-payment of compensation for the expropriation, nor could it, since the invocation of this defense does not preclude the payment of compensation by the State for the damages effectively resulting from acts attributable to it".[260]

In short, Article 27 of the ILC Articles on State Responsibility leaves open the question of compensation, when a circumstance precluding wrongfulness is upheld. According to the definition of the right to regulate in this study, where the right to regulate exists, there is no need to compensate. If a circumstance precluding wrongfulness is upheld but a duty to compensate investors is imposed on the respondent, does the state have the right to regulate?

### 3. The Police Powers Doctrine

According to the police powers doctrine, a measure resulting in loss of property that falls within the state's police powers does not constitute an indirect expropriation and, as a consequence, it does not give rise to a duty to compensate.[261] The *Restatement of the Law (Third)* is often relied upon when discussing the police powers doctrine: "A state is not responsible for loss of property or for other economic disadvantage resulting from bona fide general taxation, regulation, forfeiture for crime, or other action of the kind

[259] *CMS v. Argentina* (Decision on Annulment) (n 236) [147].
[260] *South American Silver Limited v. Bolivia*, PCA Case No. 2013-15, Award, 30 August 2018 [620].
[261] For a discussion, see C. Titi, "Police Powers Doctrine and International Investment Law", in F. Fontanelli, A. Gattini, and Attila Tanzi (eds), *General Principles of Law and International Investment Arbitration* (Brill 2018).

that is commonly accepted as within the police power of states, if it is not discriminatory".[262] Some tribunals have recognised the police powers doctrine as forming part of customary international law, and it is for this reason that the topic is addressed in this chapter. A few tribunals have even incorporated the doctrine in their definition of indirect expropriation.[263] As already discussed in the previous chapter, some form of the police powers doctrine is regularly incorporated in new generation investment treaties, often in an annex on expropriation.[264] This section focuses on arbitral interpretations that have taken into account the state's police powers outside specific treaty provisions, *as customary international law*.[265]

Probably the most commonly cited reference to the police powers doctrine as customary international law comes from *Saluka v. Czech Republic*, a case arising out of the restructuring of the Czech banking sector and the forced administration by the Czech National Bank of a bank in which the investor held shares.[266] According to the *Saluka* tribunal, "[i]t is now established in international law that States are not liable to pay compensation to a foreign investor when,

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[262] *Restatement of the Law (Third)* — Foreign Relations Law of the United States (American Law Institute 1987) § 712, Comment g; see also § 712, Reporter's Note 6. Eg see *Pope & Talbot Inc v. Canada* (UNCITRAL) Interim Award, 26 June 2000 [99]; *Marvin Feldman v. Mexico*, ICSID Case No. ARB(AF)/99/1, Award, 16 December 2002 [105]-[106]; *Saluka Investments BV (The Netherlands) v. Czech Republic*, PCA Case No. 2001-04, Partial Award, 17 March 2006 [260]; *Glamis Gold, Ltd v. United States* (UNCITRAL) Final Award, 8 June 2009 [354]; *AWG Group Ltd v. Argentina* (UNCITRAL) Decision on Liability, 30 July 2010 [139]; *Tza Yap Shum v. Peru*, ICSID Case No. ARB/07/6, Award, 7 July 2011 [146]; *Quiborax SA and Non Metallic Minerals SA v. Bolivia*, ICSID Case No. ARB/06/2, Award, 16 September 2015 [202]; *Philip Morris Brands Sàrl, Philip Morris Products SA and Abal Hermanos SA v. Uruguay*, ICSID Case No. ARB/10/7, Award, 8 July 2016 [293].

[263] Eg *Burlington Resources Inc v. Ecuador*, ICSID Case No. ARB/08/5, Decision on Liability, 14 December 2012 [471]; *Mohamed Abdel Raouf Bahgat v. Egypt*, PCA Case No. 2012-07, Final Award, 23 December 2019 [221].

[264] Ch III, section 5 Standard-specific exceptions.

[265] It is beyond the scope of this study to examine whether there is state practice and *opinio iuris* with respect to the police powers doctrine.

[266] *Saluka v. Czech Republic* (Partial Award) (n 262).

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".[267] The tribunal reasoned that this "principle that a State does not commit an expropriation and is thus not liable to pay compensation to a dispossessed alien investor when it adopts general regulations that are 'commonly accepted as within the police power of States' forms part of customary international law today".[268]

In another case, *AWG Group v. Argentina*, in which some of the challenged measures related to the respondent's financial crisis of 2001, the tribunal stated that "in evaluating a claim of expropriation it is important to recognize a State's legitimate right to regulate and to exercise its police power in the interests of public welfare and not to confuse measures of that nature with expropriation".[269] The tribunal found that, in light of the severity of the crisis, the measures Argentina adopted to face it were within its police powers.[270] Therefore, these measures did not constitute an indirect expropriation,[271] although the tribunal did later find that they breached fair and equitable treatment.[272]

In *Chemtura v. Canada*, the tribunal held that measures taken by Canada's Pest Management Regulatory Agency, in light of "the increasing awareness of the dangers presented by lindane for human health and the environment", were "a valid exercise of the State's police powers and, as a result, [did] not constitute an

[267] Ibid [255].
[268] Ibid [262]. See also *Tecmed SA v. Mexico*, ICSID Case No. ARB (AF)/00/2, Award, 29 May 2003 [119]; *Methanex Corporation v. United States* (UNCITRAL) Final Award on Jurisdiction and Merits, 3 August 2005 pt IV, ch D [7].
[269] *AWG v. Argentina* (Decision on Liability) (n 262) [139].
[270] Ibid [140]. Contrast *SAUR International v. Argentina*, ICSID Case No. ARB/04/4, Decision on Jurisdiction and Liability, 6 June 2012 [396]-[405].
[271] *AWG v. Argentina* (Decision on Liability) (n 269) [140].
[272] Ibid [276].

expropriation".[273] In *Philip Morris v. Uruguay*, the tribunal found that Uruguay's tobacco control measures adopted for the protection of public health "were a valid exercise by Uruguay of its police powers for the protection of public health" and that, as such, they could not constitute an indirect expropriation.[274]

The fact that a tribunal recognises the police powers doctrine does not mean that the state is automatically excused from fulfilling its obligations under the treaty. In *Tza Yap Shum v. Peru*, the tribunal reasoned that a state does not bear international responsibility when it exercises its police powers in a manner "reasonable" and "necessary for" the protection of public health, security and, more generally, public welfare.[275] The tribunal acknowledged that deference thus accorded the host state is not unlimited; for example, arbitrary or discriminatory measures would not merit such defence.[276] In the circumstances of the case, the tribunal found that an indirect expropriation had taken place.[277]

In *Quiborax v. Bolivia*, a dispute arising out of the revocation of mining concessions, the tribunal reasoned that "[i]nternational law has generally understood that regulatory activity exercised under the so-called 'police powers' of the State is not compensable".[278] *In casu*, the tribunal found that Bolivia's actions were not "a legitimate exercise" of its police powers.[279] In *Copper Mesa v. Ecuador*, the tribunal found that, since the resolutions terminating the investor's mining concession were arbitrary and

[273] *Chemtura Corporation v. Government of Canada*, PCA Case No. 2008-01, Award, 2 August 2010 [266].
[274] *Philip Morris v. Uruguay* (Award) (n 262) [307].
[275] *Tza Yap Shum v. Peru* (Award) (n 262) [145].
[276] Ibid [148].
[277] Ibid [170].
[278] *Quiborax v. Bolivia* (Award) (n 262) [202].
[279] Ibid [227].

did not respect due process,[280] the state could not successfully invoke the police powers doctrine.[281]

In *Magyar v. Hungary*, a claim arising out of the alleged expropriation of the investors' leasehold rights to agricultural land,[282] the tribunal followed a qualified approach. Ruling out "an unqualified exception from the duty of compensation for all regulatory measures",[283] the tribunal reasoned that investment awards tend to uphold the police powers doctrine in only two sets of circumstances: a) "generally accepted measures of police powers that aim at enforcing existing regulations against the investor's own wrongdoings, such as criminal, tax and administrative sanctions, or revocation of licenses and concessions"; and, b) "regulatory measures aimed at abating threats that the investor's activities may pose to public health, environment or public order".[284] The measures adopted by the host state in the case did not fall into either category and the tribunal concluded that expropriation had taken place.[285]

*Hydro v. Albania* was a dispute that arose out of a series of actions that according to the investors targeted their energy and media industries.[286] The tribunal agreed with the claimants and found that the host state's conduct was "the culmination of a political campaign against the Claimants" and could therefore not be described as "a legitimate exercise of its police powers".[287] The tribunal concluded that there had been an expropriation in breach of the investment treaty.[288]

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[280] *Copper Mesa Mining Corporation v. Ecuador*, PCA Case No. 2012-2, Award, 15 March 2016 [6.66].
[281] Ibid [6.67].
[282] *Magyar Farming Company Ltd, Kintyre Kft and Inicia Zrt v. Hungary*, ICSID Case No. ARB/17/27, Award, 13 November 2019 [5].
[283] Ibid [364].
[284] Ibid [366].
[285] Ibid [367].
[286] *Hydro Srl and others v. Albania*, ICSID Case No. ARB/15/28, Award, 24 April 2019.
[287] Ibid [724]-[725].
[288] Ibid [725].

In another case, *Bahgat v. Egypt*, a dispute arising out of criminal charges and a seizure of the investor's assets, the tribunal described expropriation as a measure that "deprives the investor of its investment", where the deprivation is permanent and "finds no justification under the police powers doctrine, that is, ordinary measures of a State and its agencies in the proper execution of the law".[289] The tribunal explained that this police powers doctrine is not *carte blanche* to allow the state to act as it pleases.[290] State conduct must still "be justified, meet the international standards of due process, and *inter alia* be proportional to the threat to public order to which it purports to respond".[291] This led the tribunal to conclude that, in the case, although the state measures pursued legitimate policy goals, they were not proportional to the goal pursued and for this reason they failed the "police powers test".[292]

Proportionality was also invoked in *Olympic Entertainment v. Ukraine*, a dispute arising out of a gambling ban, where the tribunal established that, although the applicable investment treaty did not expressly refer to the state's police powers, the disputing parties agreed that it was applicable, although they disagreed as to whether the challenged state measure fell within the state's police powers.[293] The tribunal held that:

> the condition of proportionality must be included in the test for a valid exercise of the police powers doctrine. Proportionality has become an important factor in international investment law and the substantive protections that it provides for investors. It is bound up in the concepts of fairness and equity which are

[289] *Bahgat v. Egypt* (Final Award) (n 263) [221].
[290] Ibid [230].
[291] Ibid.
[292] Ibid [232].
[293] *Olympic Entertainment Group AS v. Ukraine*, PCA Case No. 2019-18, Award, 15 April 2021 [86].

commonly reflected in the substantive standards included in investment treaties.[294]

The tribunal found that the respondent's measures could not be held to be proportionate and therefore they were not "a valid exercise of the police powers doctrine".[295]

### 4. Conclusion

This chapter has enquired into the extent to which customary international law can safeguard the state's right to regulate. The chapter considered in turn necessity as a circumstance precluding wrongfulness under the ILC Articles on State Responsibility and the police powers doctrine, which tribunals increasingly cite as forming part of customary international law. The analysis of the necessity defence shows that tribunals have set a particularly high threshold for its successful invocation. This, combined with the fact that a circumstance precluding wrongfulness does not guarantee that the respondent will not need to compensate affected investors, raises some doubts as to the extent to which such circumstances precluding wrongfulness protect the state's right to regulate. Arbitral interpretations of the police powers doctrine seem somewhat more promising for the right to regulate, although gradually the police powers doctrine becomes more and more embedded in treaty law. That said, acknowledging the doctrine of the state's police powers must not be taken to mean that there has been no indirect expropriation. Finally, an interesting aspect of the analysis of the police powers doctrine by some tribunals is the introduction of proportionality as a balancing element to be taken into account in the application of the doctrine.

[294] Ibid [90].
[295] Ibid [101].

# V.

## The Right to Regulate and Reform of ISDS

### 1. Introduction

Although the right to regulate has an impact on the application of substantive investment protections, it has become part and parcel of states' efforts to reform procedural standards, that is, ISDS. In effect, one of the criticisms of investment dispute settlement is that it limits states' regulatory capacity and it creates regulatory chill.[296] This perception is somewhat curious, since, in principle, any such limitation is the result of substantive international commitments that host states undertake in their investment agreements. States' reform efforts have targeted investment treaties' substantive *and* procedural standards, but the ire of civil society and of some states ultimately settled on ISDS, the mechanism that ensures the respect of substantive investment protections.

That states should view the ISDS mechanism as a limitation on their regulatory flexibility is, to some extent, understandable. In addition to the fact that investment treaty arbitrations showed states that their investment treaties have "teeth", part of the dissatisfaction with ISDS relates to (real or perceived) broad or erroneous arbitral interpretations of substantive investment protections that do not take into account the state's right to regulate.[297]

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[296] UNCITRAL, "Report of Working Group III (Investor-State Dispute Settlement Reform) on the work of its thirty-seventh session (New York, 1–5 April 2019)", UN Doc No. A/CN.9/970 (9 April 2019) para 36.

[297] UNCITRAL, "Report of Working Group III (Investor-State Dispute Settlement Reform) on the work of its thirty-fifth session (New York, 23–27 April 2018)" (14 May 2018) <https://documents-dds-ny.un.org/doc/UNDOC/GEN/V18/029/59/PDF/V1802959.pdf?OpenElement>, paras 23, 39-42. See further Submission from the European Union and its Member States, "Possible reform of investor-State dispute settlement (ISDS)" (24 January 2019) <https://documents-dds-ny.un.org/doc/

This chapter considers the right to regulate against the background of the reform of ISDS. First, it addresses the right to regulate in the reform negotiations in UNCITRAL Working Group III. Second, it turns to Opinion 1/17 of the Court of Justice of the European Union, which stressed the importance of the right to regulate, arguably raising it to a constitutional requirement for EU investment agreements. The chapter argues that the right to regulate is likely to be further embedded in the multilateral ISDS reform negotiations and to become part of a prospective multilateral instrument on ISDS.

## 2. The Right to Regulate in the UNCITRAL Reform Negotiations

The right to regulate has fed into the negotiations on reform of ISDS that were launched in 2017 in UNCITRAL Working Group III. The Working Group was entrusted with "a broad mandate" to explore the possible reform of ISDS.[298] The negotiations then focus on reform of *procedural* rather than substantive standards. However, if one expected the right to regulate to be irrelevant to the reform negotiations for that reason, one would be wrong.

In order to understand how the right to regulate fits into the UNCITRAL reform negotiations, let us first consider the overall structure and workplan of the negotiations. The work in Working Group III has been divided into three phases. Phase 1 and Phase 2 of the negotiations focused on identifying concerns with ISDS and

UNDOC/LTD/V19/004/19/PDF/V1900419.pdf?OpenElement>, para 6; A. De Luca et al, "Responding to Incorrect Decision-Making in Investor-State Dispute Settlement: Policy Options" (2020) 21(2-3) Journal of World Investment & Trade 374. It is in fact very difficult to obtain agreement on whether a particular interpretation is broad or erroneous, except, arguably, in cases, such as *CMS v. Argentina*, where the annulment committee stated that the award contained errors of law.

[298] UNCITRAL, "Report of Working Group III (Investor-State Dispute Settlement Reform) on the work of its thirty-fourth session (Vienna, 27 November–1 December 2017)" (19 December 2017) para 6.

deciding on the desirability of reform, while Phase 3, ongoing at the time of writing, delves into the content of the desired reform.[299]

The concerns identified by the Working Group in Phase 1 (2017–2018) can be split into three broad categories: a) concerns pertaining to the lack of consistency, coherence, predictability and correctness of investment decisions; b) concerns relating to adjudicators, such as issues pertaining to insufficient guarantees of independence and impartiality, and lack of diversity, and c) concerns surrounding the cost and duration of investor-state dispute settlement proceedings.[300] Some further more specific concerns were identified, such as the lack of regulation of third-party funding.[301] In Phase 2 (2018), the Working Group considered whether reform was desirable in light of the identified concerns and there was agreement that such reform was desirable. This allowed the negotiations to proceed to Phase 3. In Phase 3 (2019-), the Working Group looks into the substance of reform and works to "develop any relevant solutions to be recommended to the Commission".[302] According to the current provisional workplan, negotiations could conclude in 2026.[303]

If the right to regulate has not so far formed the basis of a standalone discussion within Working Group III, still it has often underlain the negotiations.[304] Although it was not identified as

[299] All the relevant documentation is available on the webpage of UNCITRAL Working Group III <https://uncitral.un.org/en/working_groups/3/investor-state>.
[300] UNCITRAL, "Report of Working Group III (Investor-State Dispute Settlement Reform) on the work of its thirty-fifth session" (n 297); Submission from the European Union and its Member States (n 297) para 6.
[301] Ibid.
[302] UNCITRAL, "Report of Working Group III (Investor-State Dispute Settlement Reform) on the work of its thirty-fourth session" (n 298) para 6.
[303] UNCITRAL, "Report of Working Group III (Investor-State Dispute Settlement Reform) on the work of its resumed fortieth session (Vienna, 4 and 5 May 2021)" UN Doc No. A/CN.9/1054 (27 May 2021) <https://uncitral.un.org/sites/uncitral.un.org/files/wg_iii_resumed_40th_session_final_003.pdf> (information correct as of June 2021).
[304] Eg UNCITRAL, "Report of Working Group III (Investor-State Dispute Settlement Reform) on the work of its thirty-sixth session (Vienna, 29 October–2 November

an issue that states ought to consider — unsurprisingly, for the right to regulate is not a procedural standard — concerns about the "correctness" of arbitral decisions related, among others, to an understanding that investment tribunals did not adequately take it into account.[305] More recently, in the Commission session in July 2021, the right to regulate was recognised as a "cross-cutting issue" that is "of particular interest to developing countries" and the suggestion was made that the workplan of Working Group III should put more emphasis on it.[306] The right to regulate was also discussed in the virtual Fourth Intersessional Meeting on Investor-State Dispute Settlement Reform organised by the Republic of Korea on 2–3 September 2021.[307] The reason for including the right to regulate in this discussion was to provide the UNCITRAL Secretariat with guidance for working papers that it may prepare with a view to addressing it as a standalone topic in a regular session of Working Group III.[308] During the intersessional meeting, developing states, in particular, took the floor and expressed their concern about the perceived lack of the right to regulate and the regulatory chill attendant on it.

The meeting also revealed that there is incomprehension as to what the right to regulate is. Some delegations seemed to believe that the right to regulate is not part of new treaties. This study has

2018)", UN Doc No. A/CN.9/964 (6 November 2018) para 16; UNCITRAL, "Report of Working Group III (Investor-State Dispute Settlement Reform) on the work of its thirty-seventh session (New York, 1–5 April 2019)" (n 296) para 36; UNCITRAL, "Report of Working Group III (Investor-State Dispute Settlement Reform) on the work of its thirty-eighth session (Vienna, 14–18 October 2019)", UN Doc No. A/CN.9/1004 (23 October 2019) para 80; UNCITRAL, "Report of Working Group III (Investor-State Dispute Settlement Reform) on the work of its thirty-ninth session (Vienna, 5–9 October 2020)", UN Doc No. A/CN.9/1044 (10 November 2020) para 23.

[305] Eg see De Luca et al (n 297) 396.

[306] UNCITRAL, "Report of the United Nations Commission on International Trade Law, Fifty-fourth session (28 June–16 July 2021)" UN Doc No. A/76/17 (2021) para 256.

[307] See <https://uncitral.un.org/sites/uncitral.un.org/files/media-documents/uncitral/en/rok_intersessional_meeting_programme_final68.pdf>.

[308] Ibid.

shown the opposite. While developed states have often been faster at incorporating the right to regulate in their investment treaties, this "complaint" of a minority of developing states that the right to regulate is not included in new generation treaties does not reflect reality. The discussion also made clear that not everyone understands the right to regulate in the same manner. While the debate continues, there is an expectation that the right to regulate will be considered further in the course of the negotiations.

In conclusion, the right to regulate will probably further inform the UNCITRAL negotiations on ISDS reform. In reality, not only developing countries but also developed economies, including the European Union, an important player in the negotiations, are likely to push for a right to regulate provision to be part of the statute of a prospective multilateral investment court or another multilateral instrument on ISDS reform. It is to this topic that the following section will now turn.

### 3. The Case of Opinion 1/17 of the Court of Justice of the European Union

The right to regulate was discussed in the context of Opinion 1/17 of the Court of Justice of the European Union in relation to the compatibility of CETA's ISDS mechanism, an investment court, with EU law. Although Opinion 1/17 is not an international decision, it is worth examining, because it impacts the position of the European Union and its 27 member states in international investment negotiations and in UNCITRAL Working Group III in particular. What is strange about the discussion of the right to regulate in Opinion 1/17 is that this decision did not concern substantive investment protections, rather it appraised CETA's ISDS mechanism in light of EU law. Considering the autonomy of the EU legal order, Opinion 1/17 found that CETA's investment court does not prevent the EU institutions from operating in accordance

with the EU's constitutional framework, since it does not affect the "level of protection of a public interest",[309] in other words, it does not interfere with the right to regulate. Let us consider the Opinion and the Court's reasoning more closely.

The CJEU examined whether CETA's investment court may have jurisdiction to find a violation of CETA following an assessment of "the level of protection of a public interest" established by the EU.[310] If that "level of protection of a public interest" had to be abandoned, that is, if the EU or a member state had to abandon legislation concerning the protection of a public interest in order to avoid repeated findings of a treaty violation that would incur financial liability, this would undermine the autonomy of the EU legal order.[311] To decide whether CETA's investment court might have this effect on the level of protection of a public interest, the Court examined CETA's substantive provisions, including especially those that guarantee the right to regulate.[312] The fact that CETA includes numerous provisions aimed to guarantee the right to regulate[313] led the Court to conclude that CETA's investment court "has no jurisdiction to declare incompatible with the CETA the level of protection of a public interest established by EU measures ... and, on that basis, to order the Union to pay damages".[314] Since, according to the Court's reasoning, CETA's investment court cannot

[309] Opinion 1/17 *Comprehensive Economic and Trade Agreement between Canada and the European Union* [2019] EU:C:2019:341 [148]-[150].
[310] Ibid [149].
[311] Ibid [149]-[150].
[312] C. Titi, "Opinion 1/17 and the Future of Investment Dispute Settlement: Implications for the Design of a Multilateral Investment Court", in L. Sachs, L. Johnson and J. Coleman (eds), *Yearbook on International Investment Law & Policy 2019* (Oxford University Press 2021) 531.
[313] Eg see CETA arts 8.9, 28.3(2), annex 8- A. On the right to regulate in CETA, see C. Titi, "Right to Regulate", in M.M. Mbengue and S. Schacherer (eds), *Foreign Investment under the Comprehensive Economic and Trade Agreement (CETA)* (Springer 2019) 159–183.
[314] Opinion 1/17 (n 309) [153]. See also [156], [159], and [160].

call into question the right to regulate, CETA "does not adversely affect the autonomy of the EU legal order".[315]

This analysis of the CJEU is surprising on many counts. For a start, the assumption that CETA's investment court would not uphold jurisdiction over measures adopted in order to protect the public interest is curious.[316] Nothing in CETA suggests that the investment court would lack jurisdiction over such measures. On the contrary, the investment court could be called upon to decide whether the very exceptions that protect the public interest apply in a given case.[317] CETA's court may have to pronounce on whether, in the circumstances of a given case, the level of protection of a public interest established by the EU, or by a member state in the course of implementing EU law, is covered by an exception or not and, by the same token, whether it breaches a substantive investment standard. The CJEU could not have been unaware of this and so its line of reasoning must have been intentional.[318] However, what the Court's exact intention was is open to debate.

One possible explanation is that the CJEU understood CETA to require the investment court to decline jurisdiction over measures taken in order to safeguard public welfare objectives. However, it is also possible that this reasoning was used to ensure that CETA's investment court respects the host economy's right to regulate and that when measures are adopted in pursuance of the public interest, as this is laid down in the agreement, these measures cannot lead to a finding of a violation of CETA. An alternative interpretation is that the CJEU was simply underlining the importance of the right to regulate and its role as a principle of the EU legal order.[319]

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[315] Ibid [161].
[316] Titi, "Opinion 1/17 and the Future of Investment Dispute Settlement" (n 312) 532.
[317] Ibid.
[318] Ibid 533.
[319] Ibid.

Judge Koen Lenaerts, President of the CJEU, has supplied a different explanation. According to President Lenaerts, the Court here does not attempt to protect "EU measures of general application as such".[320] While acknowledging that these measures are not "immune" from review by CETA's investment court,[321] he has argued that what the Court aims to safeguard is "the *essence of the democratic process* leading to the adoption of EU norms protecting public interests".[322] This contributes to the EU's "functional constitution", which means "a Union founded upon democracy, justice and rights".[323] However, it is unclear how the nuance he tries to draw, notably with respect to the investment court's jurisdiction, relates to the text of Opinion 1/17.

Be that as it may, the mystery remains whole, as does the question of what happens if CETA's investment court not only upholds jurisdiction in a case involving "the level of protection of a public interest" but it also finds that a measure taken to further a public interest established under EU law falls foul of the agreement. For the sake of argument, let us imagine that such a measure has the potential to affect adversely a number of investors across the EU and therefore it can generate many claims. In such a scenario, would an award of damages be inconsistent with EU constitutional law and so be denied effect in the internal legal order? If the EU did not comply with an order to pay monetary damages, the other party may initiate enforcement proceedings. CETA provides for enforcement of decisions under the ICSID Convention and under the New York Convention[324] but, in reality, enforcement outside

[320] K. Lenaerts, "Modernising Trade whilst Safeguarding the EU Constitutional Framework: An Insight into the Balanced Approach of Opinion 1/ 17" (Speech at the Belgian Ministry of Foreign Affairs, Brussels, 6 September 2019) <https://diplomatie.belgium.be/sites/default/files/downloads/presentation_lenaerts_opinion_1_17.pdf> 16.
[321] Ibid.
[322] Ibid (emphasis in original).
[323] Ibid.
[324] CETA art 8.41.

the territory of the contracting parties could face legal obstacles. Enforcement under the ICSID Convention does not appear to be a realistic option and the New York Convention may be the only possibility.[325] By this token, in theory, enforcement sought in an EU member state might be refused, if the local court were to hold that CETA's investment court has upheld jurisdiction it did not have or that it has exceeded its jurisdiction; or that its decision violates public policy. Enforcement may also be refused if the enforcement court submits a request for a preliminary ruling to the CJEU.[326] Were EU courts to follow such an approach, Canadian courts could conceivably reciprocate,[327] with the effect — absurd in light of the text of the agreement — that findings of a violation of the treaty owing to measures taken in order to protect "the level of protection of a public interest" would not lead to an enforceable decision.

A different interpretation is that "the level of protection of a public interest" may have to be protected at the cost of compensation.

[325] A. Reinisch, "Will the EU's Proposal Concerning an Investment Court System for CETA and TTIP Lead to Enforceable Awards? — The Limits of Modifying the ICSID Convention and the Nature of Investment Arbitration" (2016) 19(4) Journal of International Economic Law 761; C. Titi, "The European Union's Proposal for an International Investment Court: Significance, Innovations and Challenges Ahead" (2017, advance publication May 2016) 1 Transnational Dispute Management 1, 25–27. On enforcement of decisions of an international investment court, see further M. Bungenberg and A. Holzer, "Potential Enforcement Mechanisms for Decisions of a Multilateral Investment Court", in G. Ünüvar, J. Lam, and S. Dothan (eds), *Permanent Investment Courts — The European Experiment* (Special Issue of the European Yearbook of International Economic Law, Springer 2020); Marc Bungenberg and August Reinisch, *From Bilateral Arbitral Tribunals and Investment Courts to a Multilateral Investment Court* (Special Issue of the European Yearbook of International Economic Law, 2nd edn, Springer 2018, 2020) ch 7; G. Kaufmann-Kohler and M. Potestà, "Can the Mauritius Convention Serve as a Model for the Reform of Investor-State Arbitration in Connection with the Introduction of a Permanent Investment Tribunal or an Appeal Mechanism?" (2006) CIDS Research Paper on ISDS Reform 1, 52–68.

[326] Titi, "Opinion 1/17 and the Future of Investment Dispute Settlement" (n 312) 533–534.

[327] R. Howse, "The European Court of Justice Advisory Opinion on CETA and the Future of Investor-State Dispute Settlement" (2019) (unpublished, on file with the author).

As previously mentioned,[328] the concern of the CJEU was that decisions of CETA's ISDS mechanism should not "create a situation where, in order to avoid being *repeatedly* compelled by the CETA Tribunal to pay damages to the claimant investor, the achievement of that level of protection needs to be abandoned by the Union".[329] It could be argued that, if this level of protection of public interest does not lead to repeated findings of a violation of CETA with the effect described above, then this may be "acceptable" to the Court.[330]

However, the Court's reasoning in Opinion 1/17 is also surprising for another reason. To decide whether CETA's investment court does not interfere with the autonomy of the EU legal order, the CJEU turned to CETA's *substantive* standards: the right to regulate, and provisions on fair and equitable treatment, expropriation, and non-relaxation of social welfare standards. While forming part of the context of CETA's dispute settlement provisions, these are substantive standards. This shows the interconnectedness of substantive and procedural standards and, at the same time, creates challenges for the position of the EU and its member states in the UNCITRAL negotiations on the reform of ISDS. While the EU has the capacity to negotiate substantive protections in its bilateral investment agreements, the scope of the negotiations in Working Group III is limited to ISDS. In that context, the EU may pursue the inclusion of a provision in the statute of a prospective multilateral investment court to the effect that adjudicators must take into account the "level of protection of a public interest" or, simply, some kind of provision on the right to regulate. Were such a provision not to be included, the EU would have to offer assurances to the CJEU that the *substantive* provisions in its investment agreements, those that will refer disputes to the prospective court, will safeguard the right to regulate. However, in light of the earlier discussion of the right to regulate as a consideration in UNCITRAL Working Group

[328] See text to n 311.
[329] Opinion 1/17 (n 309) [149] (emphasis added).
[330] Titi, "Opinion 1/17 and the Future of Investment Dispute Settlement" (n 312) 534.

III[331] and in light of the overall evolution of new investment treaties, it is highly probable that a multilateral instrument on reform of ISDS will include some kind of provision on the right to regulate.[332]

## 4. Conclusion

This chapter has considered the right to regulate in relation to investor-state dispute settlement provisions. It has observed that, although not a procedural standard, the right to regulate has become closely linked to the debate about ISDS. In the multilateral reform negotiations in UNCITRAL Working Group III, the right to regulate has informed part of the debate and it could be considered as a standalone topic in a future session of the Working Group. Within the European Union, Opinion 1/17 of the Court of Justice of the European Union relied, *inter alia*, on the right to regulate to conclude that CETA's investment court is compatible with EU law, thus raising the right to regulate to a constitutional requirement of the EU legal order. Against this backdrop, it does not seem unreasonable to expect that the future statute of a prospective multilateral investment court or other instrument on multilateral reform of ISDS could include some type of provision on the right to regulate.

[331] This chapter, section 2 The Right to Regulate in the UNCITRAL Reform Negotiations.
[332] The same suggestion was made in Bungenberg and Reinisch (n 325) 6.

# VI.

## Conclusion

This study took stock of the right to regulate, in light of the dramatic change of attitude towards it in the last few years, and gave a complementary account of the right to regulate compared to my treatment of the topic a few years ago. While also offering a general presentation of the concept, it focused on what is new about the right to regulate in treaty practice and in arbitral case law.

After an introductory chapter, Chapter II discussed what we understand by the term "right to regulate" and explained how the concept must be distinguished from the state's general regulatory capacity. The chapter considered the public welfare objectives that the right to regulate is generally understood to safeguard and it examined some elements complementary to the right to regulate that may increase policy space but that do not, strictly speaking, form part of the right to regulate proper.

Having defined the right to regulate as a "legal" right, Chapter III considered how we can identify this right in treaty law. In a first step, it inquired into the role of preambular language and other novel treaty provisions expressly reaffirming the parties' right to regulate. In a second step, the chapter turned to treaty exceptions and their interpretation. In particular, the chapter examined standard-specific exceptions, focusing on the incorporation of a mitigated form of the police powers doctrine in new generation investment treaties, essential security interests exceptions and general exceptions for the protection of other public welfare objectives. The chapter argued that tribunals do not always give effect to treaty exceptions and that overall arbitral interpretations have thus far proved unsatisfactory. Ultimately, it is not enough that a treaty should preserve the state's right to regulate but tribunals must recognise it too.

Chapter IV turned to the right to regulate and customary international law. First, it examined the ILC Articles on State Responsibility, focusing on the necessity defence. In this context, it discussed necessity as a circumstance precluding wrongfulness; it assessed the relationship between circumstances precluding wrongfulness and treaty exceptions; and, it considered the question of compensation when the wrongfulness of state conduct is precluded under the ILC Articles on State Responsibility. Second, the chapter canvassed the police powers doctrine, which some tribunals have held forms part of customary international law. The chapter concluded that, while customary international law defences can safeguard the state's right to regulate, their successful invocation is subject to a high threshold, which means that customary international law will safeguard the right to regulate in a few factual situations.

Finally, Chapter V turned to the right to regulate and the reform of ISDS. It observed that although the right to regulate relates to the treaty's substantive standards, it has become important in the efforts to reform ISDS. The chapter considered in turn the efforts made within UNCITRAL Working Group III to address the right to regulate and Opinion 1/17 of the Court of Justice of the European Union, which elevated the right to regulate in EU investment agreements to a constitutional requirement of EU law.

Overall, this study showed that the right to regulate is increasingly present in new generation investment treaties, of which some may even go too far in their attempt to protect regulatory space. That said, the study also commented on the unsatisfactory arbitral interpretations of some treaty exceptions, including general exceptions for the protection of public welfare objectives, which reveal that even when states introduce the right to regulate in their treaties, arbitral tribunals are not certain to give it effect. This in itself could point to a need for better drafting of treaty exceptions and interpretive guidance, or, as this author

believes, a more rigorous screening of adjudicators to ensure they are competent to interpret and apply an international treaty.

Questions remain open that have as yet no answer, since the right to regulate is still evolving. Arbitral interpretations, including interpretations of new provisions expressly referring to the right to regulate and general exceptions clauses, will certainly impact the drafting of future investment treaties. As yet, we can only speculate on the possible direction of such interpretations. New approaches may develop too. For example, in light of some recent trends, proportionality may be introduced such as in order to help determine whether a measure is covered by an exception or in relation to compensation so as to avoid an all-or-nothing approach that may sometimes fail to reflect the reality of the dispute. Ultimately, what is important, in contrast to what M. Sornarajah would argue, is to ensure that states offer a modern, robust system of investment protections backed up by dispute settlement provisions, a system that achieves some kind of balance, both ensuring that a state can protect its investors abroad and that some measures in exceptional circumstances will not automatically entail a treaty violation.

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