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ENVIRONMENTAL CONCERNS IN INTERNATIONAL INVESTMENT TREATY ARBITRATION: IS INTERNATIONAL ARBITRATION AN APPROPRIATE FORUM FOR DISPUTING ENVIRONMENTAL CONCERNS?

Dissertation to obtain a Master's Degree in Law, in the speciality of Litigation and Arbitration

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Anti-Plagiarism Statement

I declare, on my honour, that this Dissertation, entitled “Environmental Concerns In International Investment Treaty Arbitration: Is International Arbitration An Appropriate Forum For Disputing Environmental Concerns?” is the result of research carried out by me, within the scope of the Master in Litigation and Arbitration.

I further declare that all quotes are properly referenced.

Rita de Carvalho

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I declare that the body of this Dissertation, including spaces and footnotes, occupies a total of 153.551 characters, thus being within the limits established in article 33(4) of the 2nd Cycle of Studies Regulation Leading to the Master's Degree in Law: litigation and Arbitration.

Rita de Carvalho

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Abstract

In recent years, more than 3000 + international law instruments adopt investment treaty arbitration as their dispute settlement mechanism. However, these instruments have been criticized for interfering with the right of sovereign states to regulate. For this and other reasons, the international arena has reflected upon the suitability of such disputes related to environmental concerns being settled through investment treaty arbitration. This dissertation pursues the objective of exploring possible outcomes of this discussion, through an analysis of both regimes: international investment treaty arbitration law and environmental law.

Keywords: Arbitration; Investment Treaty Law; International Investment Treaty Arbitration; Environment; Investor-State Dispute Settlement; Dispute Resolution;

LIST OF ABBREVIATIONS

BIT: Bilateral Investment Treaty

CIL: Customary International Law

EIA: Environmental Impact Assessment

FET: Fair and Equitable Treatment

FPS: Full Protection and Security

FTA: Free Trade Agreement

GAT: General Agreement on Trade in Services

GATT: General Agreement on Tariffs and Trade

ICSID: International Centre for the Settlement of Investment Disputes

IP: Intellectual Property

IMF: International Monetary Found

IIA: International Investment Agreement

MEA: Multilateral Investment Agreements

MFN: Most Favoured Nation

MIT: Multilateral Investment Agreement

NAFTA: North American Free Trade Agreement

NT: National Treatment

NIEO: New International Economic Order

OECD: Organisation for Economic Co-operation and Development

PCIJ: Permanent Court of International Justice

PP: Precautionary Principle

PPP: Polluter Pays Principle

PSNR: Permanent Sovereignty over Natural Resources

UN: United Nations

UNEA: United Nations Environment Assembly

UNGA: United Nations General Assembly

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INTRODUCTION

International investment treaty arbitration is one of the most important dispute settlement mechanisms at the international level. Despite its ancient roots, since the turn of the century this litigation tool has been at the centre of a heated debate between scholars.[1] One of the main current discussions regards the suitability of investment treaty arbitration as a mechanisms capable of balancing and enforcing the investor's rights while at the same time allowing states to regulate in a manner pursuant to the public interest without breaching its treaty obligations.

For many years, investment treaties were pre-eminently preoccupied with the protection of investments and less with the protection of the states' sovereign right to regulate for the public interest. This has resulted in a first-generation international investment treaty regime where it is possible to find a certain level 'regulatory chill'[2] considering the fear that the implementation of environmentally beneficial measures could lead adversely affected investors to rise claims against the host states before international arbitration tribunals.

Concerns regarding the effectiveness of international investment treaty arbitration as a 'safe place' for the settlement of environment-related disputes were further motivated by the speculation that arbitral tribunals tended to decide in favour of the investor, condemning States to pay large amounts as compensation. This considered it is possible to find many arguments in favour and against investment treaty arbitration as an ISDS mechanism.

This dissertation seeks to analyse whether international arbitration is an appropriate forum for disputing environmental concerns. For that purpose, our research path is divided into three parts. The choice of this path lies under the idea that to understand the complex relationship there is between environmental concerns which are part of the field

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[1] Eric de Brabandere, *Investment Treaty Arbitration as Public International Law: Procedural Aspects and Implications*, Cambridge Studies in International and Comparative Law, 1st paperback edition (Cambridge, 2015)., 1.

[2] Kyla Tienhaara, 'Regulatory Chill in a Warming World: The Threat to Climate Policy Posed by Investor-State Dispute Settlement', *Transnational Environmental Law*, 7/2 (2017), 229–50., 238.

of environmental law and investment treaty arbitration we must understand the theoretical framework that is behind each.

For this reason, in Part I, we will lay down the core framework of international investment law and environmental law. We will start by defining the underlying concept of FDI and discuss its historical evolution. Next, we will assess the core standards of investment protection and the rationale behind granting investors direct access to arbitration. In order to better understand the *state of art* of the environment law field, we will expose what are the main legal instruments guiding it, as well as its main legal principles.

Separately from this introductory chapter, in Part II, we will sanely explore the existing and possible solutions found in international investment treaty law that aim to integrate environmental concerns through the strengthening of host states' regulatory power, as well as investment treaty arbitration procedures that might have the same objective. For this purpose, we will discuss the role of treaty mechanisms such as preambular provisions, carve-out clauses, general exceptions, and procedural provisions in addressing environmental concerns.

Lastly and more importantly, in Part III we will connect the dots among our findings in Part I and II aiming to answer the following question: is international investment treaty arbitration an appropriate forum to settle environmental disputes?

PART I – THEORETICAL FRAMEWORK

I. A Brief Introduction to Investment Treaty Law

As a field of international public law[3], international investment treaty law arises out of the simple, yet effective, principle that sovereign states conclude legally binding international commitments through international investment agreements (IIAs), which can take the form of Multilateral Investment Treaties (MITs), Bilateral Investment Treaties (BITs) and Free Trade Agreements (FTAs). These instruments were created to protect the investments of foreign investors, so that signatory states reciprocally grant protection to the investments of each other's citizens within their territory[4]. In fact, IIAs are of great relevance for both States and investors, for they are deemed to spur economic development, as well as encourage, promote, and protect investment flows by establishing the legal rules which regulate them[5].

In fact, most new-generation IIAs state these objectives in their preambles, even so that in 2012 the United States, in its Model BIT has expressly dictated that:

> *Desiring* to promote greater economic cooperation between them with respect to investment by nationals and enterprises of one Party in the territory of the other Party;
>
> *Recognizing* that agreement on the treatment to be accorded such investment will stimulate the flow of private capital and the economic development of the Parties;
>
> *Agreeing* that a stable framework for investment will maximize effective utilization of economic resources and improve living standards;
>
> *Recognizing* the importance of providing effective means of asserting claims and enforcing rights with respect to investment under national law as well as through international arbitration;
>
> (…)
>
> *Having* resolved to conclude a Treaty concerning the encouragement and reciprocal protection of investment;[6]

Although the international law of foreign investment is one of the most ancient fields of international public law, investment treaty law has been mostly developed since the

[3] Brabandere, *Investment Treaty Arbitration as Public International Law*., 7-11.
[4] M. Clasmeier, *Arbitral awards as investments: treaty interpretation and the dynamics of international investment law* (Wolters Kluwer, 2017)., 23-27.
[5] Flavia Marisi, *Environmental Interests in Investment Arbitration* (2020)., 8.
[6] 2012 U.S Model Bilateral Investment Treaty's Preamble.

second half of the twentieth century as globalization of communications and businesses expanded.

As of January 2021, more than 3,300 IIAs were concluded globally[7], creating a complex and overlapping network of investment rules. This explains why this field has become one of the most dynamic and broadly studied spheres of international public law.

This chapter aims to provide a short overview through the world of investment treaty law. For that purpose, we will begin by defining *foreign direct investment*. We will then outline the historical context leading to the contemporary *status quo* of international treaty law, further discussing the core standards of investment protection developed through the years. Finally, we will debate the rationale behind the direct access of foreign investors to investment treaty arbitration.

1.1.Defining Foreign Direct Investment

International Investment Law primarily covers the international laws which control Foreign Direct Investment (FDI). FDI aims at capturing the economic activity significantly controlled by foreigners in a given political jurisdiction,.[8] For a foreign investor to bring a claim before an international tribunal, it must prove that (1) they have an investment and (2) are an investor for the purposes of the applicable IIA.

In regard of the first requirement, not every type of commercial venture will qualify as an investment and therefore benefit from the protection of international investment treaty law[9]. According to the OECD, FDI can be defined as a cross-border investment made by a resident in one economy (the direct investor) with a lasting interest in an enterprise (the direct investment enterprise) established in an economy different from that of the direct investor[10].

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[7] Martin A Weiss and Shayerah I Akhtar, 'U.S. International Investment Agreements (IIAs)', 2021 <https://crsreports.congress.gov/product/pdf/IF/IF10052> [accessed 26 December 2021].

[8] Rachel L. Wellhausen, 'Foreign Direct Investment (FDI)', in *The Oxford Handbook of International Political Economy*, by Rachel L. Wellhausen, ed. by Jon C. W. Pevehouse and Leonard Seabrooke (2021) <https://oxfordhandbooks.com/view/10.1093/oxfordhb/9780198793519.001.0001/oxfordhb-9780198793519-e-14> [accessed 18 December 2021]., at 1 et seq.

[9] David Collins, *An Introduction to International Investment Law* (New York, NY, 2017)., 4.

[10] Organisation for Economic Co-operation and Development, International Monetary Fund, Organisation for Economic Co-operation and Development, OECD Group of Financial Statisticians, and SourceOECD (Online service) (eds.), *OECD benchmark definition of foreign direct investment*, 4th. ed (Organisation for Economic Co-operation and Development, 2008)., at 17-18.

The term "direct" is crucial for it is meant to exclude investment activities with negligible extra-territorial component. The foreign firm has to have a significant stake in the enterprise. Hence, the IMF glossary has clarified that, to be considered FDI, the investment has to represent the acquisition of at least ten per cent of the ordinary shares or voting power in a public or private enterprise by non-resident investors[11] - below this threshold, the investment would be qualified as a "portfolio investment", which is an investment that lacks personal management (e.g., when a person invests in stocks and shares in large public corporations)[12].

The fact that the applicability of IIAs comes with great benefits to foreign direct investors is one of the reasons that led several countries to exclude portfolio investments from the definition of investment contained in treaties[13]. This can be done rather indirectly[14], by specifying that only FDI will be covered by the treaty, or, directly, by excluding portfolio investments from the definitions of investment contained in the treaty[15].

Although this might seem straightforward, scholars have faced some difficulty in technically defining what an investment is. Some scholars defend that the absence of a legal definition is due to the term's constant mutation, which happens according to the object and purpose of different investment instruments where the concept is used[16]. As a result, the term investment is purposely undefined under modern IIAs, thus leaving room to arbitration tribunals to interpret it on a case-by-case basis[17].

It has become common for modern investment treaties to refer to this term broadly, including a non-exhausting list of what is deemed to be an investment (e.g., "every kind of asset" or "every kind of asset that has the characteristic of an investment, including

[11] International Monetary Fund, 'Foreign Direct Investment (FDI)', *Glossary Terms and Descriptions* <https://www.imf.org/en/About/Glossary#> [accessed 14 December 2021].

[12] OECD Glossary of Statistical Terms - Portfolio investment Definition, https://stats.oecd.org/glossary/detail.asp?ID=2092 (last visited Dec 18, 2021).

[13] Although it always depends on the applicable IIA.

[14] E.g., Article 901c of the Australia-Thailand FTA.

[15] E.g., article 1 of the Canada-Jordan BIT.

[16] D. Carreau and P. Juillard, *Droit international économique*, 3e éd. (Dalloz, 2007).,. 403.

[17] Keep in mind that some IIAs, such as those of Canada, prefer instead to use a closed definition of investment (e.g., Canada's 2009 BIT with Jordan).

such characteristics as the commitment of capital or other resources, the expectation of gain or profit, or the assumption of a risk").[18]

This level of indeterminacy has raised some litigation on the issue of knowing whether the arbitral tribunal has jurisdiction over the dispute brought before them. Frequently, the parties dispute whether an investment under the applicable IIA was done at all.

Under Article 25(1) of the Washington Convention – a treaty ratified by one hundred and fifty-five Contracting States which, among other matters, establishes ICSID's jurisdiction – determines that *The jurisdiction of the centre shall extend to any legal dispute arising directly out of an investment*. The Convention, however, does not define investment. An ICSID tribunal eventually developed what became known as the *Salini Test*.[19] This has been further adopted and refined by other tribunals.

The aforementioned test requires that an "investment" (1) has to involve a contribution – transfer of funds, money, or assets; (2) said contribution must have the participation of an individual transferring the funds in the management and risks associated with the project; (3) a certain duration is required; (4) it has to result in a contribution to the economic development of the host state[20].

The last element of the *Salini Test* has raised some debate. In the *MHS v. Malaysia*[21] case, an annulment committee overturned an award that decided upon the dismissal of the case based on the argument that the economic contribution was not a mandatory requirement when defining the term 'investment'.

However, while debatable, this has become the leading test employed by arbitral tribunals to define the term investment – even non-ICSID tribunals have used it

[18] Organisation for Economic Co-operation and Development, ed., *International Investment Law: Understanding Concepts and Tracking Innovations* (Paris, 2008)., 9

[19] Salini Costruttori S.p.A. and Italstrade S.p.A. v. Kingdom of Morocco, ICSID Case No. ARB/00/4, Award, July 16, 2001

[20] Salini Costruttori S.p.A. and Italstrade S.p.A. v. Kingdom of Morocco, ICSID Case No. ARB/00/4, paragraphs 50-58., July 16, 2001

[21] Malaysian Historical Salvors, SDN, BHD v. The Government of Malaysia, ICSID Case No. ARB/05/10

(sometimes in a modified version) to determine whether an alleged investment constitutes an "investment" under the applicable IIA.[22]

Some argue that this test should not be applicable even in ICSID arbitrations, as it widens the ICSID's jurisdiction beyond what is granted in its founding documents, introducing some degree of uncertainty in international investment arbitration[23].

Nonetheless, these developments in the definition of investment, aimed at creating a somehow objective definition, have influenced some states' treaty practice, which has followed the examples and narrowed their definitions of investment for the proposes of FDI.

1.2. The beginnings of FDI – Historical Context

The overwhelmingly rapid growth in the number of investment agreements that have been concluded in the past fifteen years may trick us into believing that international investment treaties are a phenomenon exclusive to the nineteenth or even the twentieth century. However, the presence of commercial entities from one state in another is not new to the international arena. For this reason, to better understand the foundations of international investment law as a legal discipline, it is important to know its historical roots.

One of the oldest known examples of this foreign presence from one state in another, in its purest form, takes us back to 1500 BC, when the Phoenicians developed commercial relations with the Greeks by establishing outposts around the eastern Mediterranean, from which they could sell goods from their homeland. Some scholars assert that his type of exchange was not simply international commercial trade, but an actual investment, as these outposts can be correctly described as a lasting commercial presence in a foreign territory[24].

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[22] Peter Tzeng, 'Salini Test', *Jus Mundi*, 2022 <https://jusmundi.com/en/document/wiki/en-salini-test> [accessed 14 June 2022].

[23] On this subject, the Pantechniki v Albania case (ICSID case No. ARB/07/21 (30 July 2007)), lucidly referred to this controversy by stating that "[The Salini test] may introduce elements of subjective judgment on the part of the arbitral tribunal (…) which a) transforms arbitrators into policymakers and above all b) increases the unpredictability of ICSID to settle disputes.".

[24] Collins, *An Introduction to International Investment Law*., 6.

If we travel a few centuries forward, we will find the silk road land-based routes established under the control of the Roman Empire. With more than six thousand kilometres across the Middle East and the Pacific Ocean, they allowed the exchange not only of goods but also of culture and language – this type of trade was often conducted through agents that spend long periods in foreign states and could be seen as one of the early forms of FDI. Later on, during the colonial period, Western European states began to establish permanent colonies in the regions where they had previously travelled to explore trade opportunities and built ports. This practice was implemented with the economic objective of exploring the natural resources these regions had to offer and access to cheap labour in less developed countries with the threat of military and administrative presence. Territorial expansion of sovereignty and land acquisition became common practices[25].

Much like today's FDI, these early investments were conducted by applying technology and infrastructure from the industrialized world to the natural resource-rich developing regions, such as Africa and Asia. Naturally, these early forms of investment did not need protection once it was understood that local law could not be applied to these new people since they were already subjected to a more civilized and more evolved jurisdiction as seen by the international community. In this sense, colonies were successfully integrated into the jurisdiction of the home state, therefore the risks associated with these commercial transactions were no greater than the ones of domestic investment[26].

As a result, from the eighteenth century until WWII, the protection of FDI was not often addressed in international agreements. Most agreements that existed often concerned trade-related issues and the protection of the property of nationals of one state in the territory of another. During this period of history, we can find the bilateral treaties of "friendship, commerce and Navigation"[27], celebrated mostly by the United States[28]. These early treaties addressed a wide range of provisions related to trade, investment, immigration, taxation, and other issues today understood as human rights. Also, these

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[25] Collins, *An Introduction to International Investment Law*., 9

[26] Collins, *An Introduction to International Investment Law*., 10.

[27] Keep in mind that this is a generic name, as not all treaties were titled FNC.

[28] About this subject, see John F Coyle, 'The Treaty of Friendship, Commerce and Navigation in the Modern Era', *Columbia Journal of Transnational Law*, 51/302 (2013), 58.

treaties often foresaw payment of compensation in case of expropriation and granted the most favoured nation treatment[29], even though the aim was to protect property and not investments[30].

Be as it may, the main source of norms for the protection of international investments in the colonial era was customary international law. The idea that early investors carried their laws wherever they went, which resulted them getting a more favoured treatment by the local community than a native person would. Later, this treatment came to be defined by reference to an international minimum standard by which aliens should be treated.[31] However, this was not uncontested. The Latin American Calvo Doctrine[32], for example, sustained that foreign investors were only entitled to the treatment afforded by the host state to its nationals.

As Colonialism began to crumble in the late nineteenth century in Latin America, this minimum standard was also heavily contested by the newly independent states eager to assert their autonomy. In the beginning of the twentieth century, a mixture of diplomacy and force was implemented by what was later designated as the Gunboat Diplomacy, designed to ensure that these new states did not encroach adversely on the investor's rightful use of their property. If the interference did happen, from a change in the fees, taxation, or any other form, instead of relying on international or even domestic law, the capital-exporting state would retaliate by seeding a fleet of warships to lurk around the coast of the host state and prompt the colonial era[33]. The idea of state intervention to protect their citizen's rights, rather than expecting them to act for themselves is the one behind what we today understand as diplomatic protection.[34]

Nowadays, contemporary investment law gives the investors the direct right of action against foreign governments through investor-state arbitration[35]. Before the era of BITs,

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[29] About the Most Favoured Nation Treatment, *see infra*, chapter 1.3.3.

[30] Kenneth J. Vandevelde, 'A Brief History of International Investment Agreements', *U.C. Davis Journal of International Law & Policy*, Thomas Jefferson School of Law Research Paper No. 1478757, 12/1 (2005), 157–94.

[31] Collins, *An Introduction to International Investment Law*., 9

[32] This doctrine arose, in 1868, in consequence to the ideas expressed by Carlos Calvo in his book *Derecho Internacional teórico y práctico de Europa y América*.

[33] Borzu Sabahi, Noah Rubins and Don Wallace, 'II. History and Limitations of the Traditional System for Resolving Investment Disputes', in *Investor-State Arbitration*, Second edition (Oxford, 2019)., 28-30.

[34] Collins, *An Introduction to International Investment Law*., 11.

[35] As explored in chapter 1.4. of this work.

negotiation backed by the threat to use force was the only effective method of investment protection. This "policy" was only believed to be over in 1957, after the Suez Canal Crises[36].

Just as importantly, the post-colonial era was the time when the newly independent states were seeking to stimulate their economies through access to foreign capital, to reach full autonomy[37]. This goal was largely supported by the UN, even so, that in 1962 the Declaration of Permanent Sovereignty over Natural Resources granted both jurisdictional rights and rights of ownership over the natural resources found in nation-states.[38]

Some scholars defend that this can be considered the backbone of international investment arbitration because it covers the basic principle of a state's right to regulate, which can be sometimes surrounded by the obligations contained in the treaties – a problem that will be highly explored during this dissertation.

In the late twentieth century, more precisely during the mid-70s, an energy crisis hit the west, when members of the States of the Overseas Private Investment Corporation cartel proclaimed an oil embargo. This jeopardised economies and proved how vulnerable capital-exporting states were to the whims of the resource-rich developing countries' governments, which can be seen as a radical change in the international arena's powerplay.[39]

As consequence, reinforced by the UN'S support of PSNR and NIEO, less developed countries proceeded to expropriate oil projects, especially in Arab countries and Latin America, which naturally had concerning consequences not only for the energy sector but for all of the developed world. These expropriations consequently affected the way FDI was perceived by investors, who feared for the security of their investments placed in former colonies and triggered additional BIT programs during this decade. As it is known, the first BITs appeared in the 1960s[40], however, with the constant demand to achieve a neutral dispute resolution method to obtain full compensation for these expropriations,

[36] Regarding the Israeli, British and French invasions of Egypt in 1957, after the nationalization of the Suez Canal.

[37] Collins, *An Introduction to International Investment Law*., 13.

[38] UN General Assembly resolution 1803 (XVII) of 14 December 1962, "Permanent sovereignty over natural resources".

[39] Collins, *An Introduction to International Investment Law*., 13.

[40] The world's first BIT was signed on November 25, 1959, between Pakistan and Germany.

IIAs did not fulfil their promises, as treaty-based investor's rights did not reach their full prominence until the beginning of the twenty-first century.

During the 1980s, the rise of the free market accompanied by the change of ideologies, contributed to the increase in the number of FDI, at the same time the UN encouraged developing states to be more receptive to FDI, especially under the new PSNR and NIEO doctrines. As a result, the explosion in FDI in the latter part of the twentieth century reinforced the idea that investors and investments needed protection to thrive, which increased, significantly, the number of IIAs signed between states, lifting barriers of entry to foreign investment, through capital injection into stagnant economies.[41]

From the beginning of the twentieth-first century, we have witnessed what has been described as an "astronomical growth"[42] in the rates of the emerging markets associated with the mid-2000s.

1.3.The Standards of Protection of Investments

Considering the historical background narrated in the previous chapter of this work, we are now able to discuss the standards of investment protection found in modern IIAs. As previously highlighted, the protection given to investors and their investments has not been the same throughout time, something which can be explained by the political and economic context of each period.

These standards of protection are commonly used in BITs and MITs to establish the treatment a foreign investor is entitled to by a host state. Modern IIAs normally revolve around the following issues: (1) Conditions for market access or admission of foreign investors in the host state; (2) methods of dispute resolution; (3) standards of treatment of foreign investors and (4) compensation for expropriation[43].

In this chapter, we will focus on the last two, more precisely on the key substantive protections for foreign investors, including protection against expropriation without

[41] Collins, *An Introduction to International Investment Law*., 15
[42] Collins, *An Introduction to International Investment Law*., 16.
[43] B. Sabahi, I. A. Laird, and G. E. Gismondi, 'International Investment Law and Arbitration: History, Modern Practice, and Future Prospects' (2018), in *Brill Research Perspectives in International Investment Law and Arbitration*, 1 et seq..

compensation, Fair and Equitable Treatment (FET), Most Favoured Nation (MFN), National Treatment (NT) and Full Protection and Security (FPS).

a) Guarantees Against Expropriation

Expropriation can be defined as the taking of privately owned property by a State, being considered the outmost serious interference a state can impose on investments.[44] Because of that, one of the main goals of IIAs policy is to protect FDI against it, by ensuring the investor's right to make productive use of their assets.

According to the principle of sovereignty, States have an inherent right under international law to expropriate the property of foreign nationals[45]. Nevertheless, some criteria must be fulfilled: (1) the expropriation must pursue a public purpose; (2) it must be carried out in a non-discriminatory manner and, (3) it must abide by the principle of due process; (4) compensation must be paid to the owner of the investment[46].

In fact, generally, all modern BITs have an 'expropriation provision' recognizing these rights and requirements. These norms do not consider expropriation illegal, but rather recognize it as a State right subjected to certain conditions. Therefore, IIAs do not protect investors against expropriation itself, but rather expropriation without due compensation.[47]

States also retain the power to tax and manage their natural resources according to their own environment and development policies. Similarly, they have power over internal affairs to regulate the health and safety of their people. On this note, the UNCTAD series on issues in international investment agreements regarding taking of property states that:

> Certain governmental measures may not involve an actual physical taking of property but may still result in the effective loss of management, use or control, or a significant depreciation

[44] At this point, it is important to recall that, as we have previously pointed out in other chapters, the concept of 'investment' for this purpose includes non-tangible assets, such as IP, and not only real property – this is reflected, as we have seen, in the definition that some IIAs make of investment.

[45] Although it is arguably an aspect of customary international law, most IIAs acknowledge the States' right to expropriate.

[46] Sabahi, Laird, and Gismondi, 'International Investment Law and Arbitration.

[47] E.g., article 9(1) of the 2021 Canadian Model BIT, which states that *No Party shall expropriate a covered investment either directly or indirectly, except (a) for a public purpose; (b) in accordance with due process of law; 3 (c) in a non-discriminatory manner; and (d) on payment of compensation in accordance with paragraph 5.*

> of the value, of the assets of a foreign investor. Such measures pose the problem of distinguishing between measures that trigger the takings clause and its requirement of payment of compensation, and those that involve interference with the property rights of foreign investors but would nevertheless be considered as not falling within the ambit of the takings clause. Typically, a measure that is a consequence of the violation of a regulation has been regarded as non-compensatory in many legal systems. A penal measure following the violation of a criminal statute cannot give rise to a compensatory taking. There is authority that a tax measure, if not excessive, also cannot amount to a taking. The same is true of violations of antitrust laws. In some jurisdictions, even interference with property rights in order to further environmental or planning decisions could be considered non-compensatory.

Another interest point about this matter concerns the difference between direct expropriation and indirect expropriation: in the first case, we find a mandatory transfer of the title of the property or its physical seizure by the State, with an unequivocal intent; in the second case there is a near-total deprivation of the investment but without the before-mentioned transfer of title or physical seizure[48] – this happens when there is excessive regulation of foreign investment, through taxation or even intrusive supervision by the government.

All in all, direct expropriations of foreign investments by host states were essentially a temporary phenomenon of the 1960s and 1970s given the historical context. Therefore, they are not a particular concern in modern IIAs, since some other provisions, such as FET or even indirect expropriation have assumed more practical importance, as claims of indirect expropriation have increased [49].

b) Fair and Equitable Treatment

The FET standard is the most difficult substantive standard to define. It has been described both by scholars and tribunals as ambiguous, "frustratingly vague", and

[48] A classical definition can be found in the Starrett Housing Corporation, Starrett Systems, Inc., and others v. The Government of the Islamic Republic of Iran, Bank Markazi Iran and others, IUSCT Case No. 24, Interlocutory Award, where it was stated that *it is recognized under international law that measures taken by a State can interfere with property rights to such an extent that these rights are rendered so useless that they must be deemed to have been expropriated, even though the State does not purport to have expropriated them and the legal title of the property formally remains with the original owner*.

[49] Collins, *An Introduction to International Investment Law*., 162

imprecise[50]. Nonetheless, as a result of the growth in the number of investment arbitration jurisprudence, scholars have become more interested in asserting its meaning[51].

Notwithstanding this standard being more recent than some of the non-discriminatory standards, such as MFN and National Treatment[52], almost all modern IIAs contain FET clauses. In fact, it is the most frequently claimed standard in investment disputes[53]. Also, if an IIA does not contain this type of clause but stipulates MFN treatment, it is generally accepted that investors may rely on FET through the MFN clause, as long as the host state has celebrated an IIA with a third party in which FET is stipulated.[54]

On another note, the essential purpose of the FET clause in investment treaties is to fill in the gaps left the more specific standards.

As it has already been explained, IIAs are considered to serve the purpose of protecting foreign investors against the intervention of host states in their investment. FET works as an additional means of creating investor confidence and, consequently, a favourable environment for FDI. All in all, FET can be described as related to the "due process" principle found in some jurisdictions. Instead of dictating the content of the host state's laws, it provides a guide to how these should be applied, essentially in a transparent and open manner[55].

An example of a FET clause can be found in article 6, chapter 11 of the Agreement Establishing the ASEAN-Australia-New Zealand Free Trade Area (2009):

> 1. Each party shall accord to covered investments fair and equitable treatment and full protection and security.
>
> 2. For greater certainty:
>
> (a) fair and equitable treatment requires each party not to deny justice in any legal or administrative proceedings.
>
> (…)

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[50] About this topic and possible definitions of the FET standard, see August Reinisch and Christoph Schreuer, *International Protection of Investments: The Substantive Standards* (Cambridge, GB New York, 2020)., 272-279.

[51] On this subject, see Conférence des Nations Unies sur le commerce et le développement, ed., *Fair and Equitable Treatment*, UNCTAD Series on Issues in International Agreements, 11 3 (New York Geneva, 1999).

[52] Reinisch and Schreuer, *International Protection of Investments*., 255.

[53] Collins, *An Introduction to International Investment Law*., 125.

[54] Reinisch and Schreuer, *International Protection of Investments*., 270.

[55] Collins, *An Introduction to International Investment Law*., 125.

> (c) the concepts of 'fair and equitable treatment and 'full protection and security' do not require treatment in addition to or beyond that which is required under international law, and do not create additional substantive rights.
>
> (…)

This being said, the proper interpretation and application of FET remains a fired debate in investment treaty arbitration, even considering the growing number of arbitral awards on this issue that has helped make this standard more precise by indicating some of its potential breaches, which include matters of procedural fairness, action in good faith and the protection of investor's legitimate expectations[56].

c) Most Favoured Nation

Although considered one of the oldest and most important standards of protection in international law and having appeared in several IIAs since the middle age[57], the MFN treatment, alongside National Treatment, is not a feature of CIL, which makes its beneficiaries entirely dependent on treaties to base related claims[58].

Such clauses require contracting parties to give investors and investments of the other contracting party a treatment that is no less favourable than the one accorded to investors and investments from third parties. For that reason, it is a so-called comparative or relative investment standard[59]. One example of an MFN clause can be found in Articles 3(1) and 3(2) of the 1980 Sri Lanka – United Kingdom BIT, which states as follows:

> (1) Neither Contracting Party shall in its territory subject investments admitted in accordance with the provisions of Article 2 or returns of nationals or companies of the other Contracting Party to treatment less favourable than that which it accords to investments or returns of its own nationals or companies or to investments or returns of nationals or companies of any third State.
>
> (2) Neither Contracting Party shall in its territory subject nationals or companies of the other Contracting Party, as regards their management, the enjoyment or disposal of their

[56] Reinisch and Schreuer, *International Protection of Investments*., 535.

[57] Reinisch and Schreuer, *International Protection of Investments*., 687

[58] About this topic, see Reinisch and Schreuer, *International Protection of Investments*., 687: *Like the national treatment standard, examples of MFN provisions in the field of commercial and economic relations date back to the middle ages.*

[59] About this subject, UNCTAD, *Most-Favoured-Nation Treatment*, UNCTAD Series on Issues in International Investment Agreements / United Nations Conference on Trade and Development, Mos (New York, 2010)., 23-24, *The MNF provision is a relative standard, which means that it implies a comparative teste. Conversely, absolute standards require treatment no matter how other investors are treated by the host state.*

> investments, to treatment less favourable than that which it accords to its own nationals or companies or to nationals or companies of any third State

It is possible to find the first MFN clauses in the previously mentioned FCN treaties[60], these being the precursors to modern IIAs. Nevertheless, the 1967 OECD Draft Convention did not contain an MFN clause, instead, it included a non-discriminatory clause, prohibiting *unreasonable and discriminatory measures*, as follows:

> Each Party shall at all times ensure fair and equitable treatment to the property of the nationals of the other Parties. <u>It shall accord within its territory the most constant protection and security to such property and shall not in any way impair the management, maintenance, use, enjoyment or disposal thereof by unreasonable or discriminatory measures</u>. The fact that certain nationals of any State are accorded treatment more favourable than that provided for in this Convention shall not be regarded as discriminatory against nationals of a Party by reason only of the fact that such treatment is not accorded to the latter.[61]

While it is safe to say that the purpose of MFN clauses is to ensure that contracting parties treat each other at least as favourably as they treat third parties[62], considering the potential this standard has in controlling how the host state applies its laws to foreign investors from different home states, this clause is often subjected to a range of exceptions. For that reason, as it happens with National Treatment, MFN tends to only be extended after the establishment of the investment, which means that host states might be allowed to discriminate against investors before agreeing to let them set up their business in their territory.[63]

These exceptions often regard special rights based on customs unions, Free Trade Agreements, and other topics like tax treatment. More rarely, it is also possible to find exemptions of foreign aid programmes or even the treatment grated in the procurement field[64]. Nonetheless, under the rules of treaty interpretation, in the absence of express limitation in the text of the treaty, the applicability of the MFN treatment is unconditional.

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[60] *See* chapter 1.2.

[61] OECD Draft Convention on the Protection of Foreign Property, Article 1(a), underlined by us.

[62] As stated, for example, in Article 3(1) of the 1991 Czechoslovakia–Netherlands BIT, which states that *More particularly, each Contracting Party shall accord to such investments full security and protection which <u>in any case shall not be less than that accorded either to investments of its own investors or to investments of investors of any third State</u>, whichever is more favourable to the investor concerned.*, underlined by us.

[63] Collins, *An Introduction to International Investment Law*., 111.

[64] This Procurement exception was addressed in the *Mesa Power v. Canada* case.

Regarding its scope of application, MFN clauses have mostly served to claim a better substantive treatment or even to import more beneficial procedural advantages from third parties' agreements. They have also been used to achieve other purposes, like, for example, import definitions established in other treaties[65].

Although it is widely accepted that MFN provisions grant the right to the same substantive treatment, it is more controversial whether these clauses also grant the right to benefit from more favourable dispute settlement provisions found in IIAs concluded between a host state and a third state.[66] In fact, in the *Sanum v. Laos* Award on Jurisdiction the tribunal stated that:

> The MFN clause in Article 3(2) refers to the treatment and protection in Article 3(1). Article 3(1) provides for fair and equitable treatment and protection of investments and activities associated with investments of investors. The Claimant has argued in favor of a broad meaning of the term “protection” under Article 3(1). On the other hand, the Claimant seems to realize that the term “protection” as used in Article 3(1) of the Treaty has a limited meaning. Indeed, the Claimant argues that, under the BITs of Laos with Germany, Korea and the United Kingdom, Laos has agreed to accord “full protection and security” and this obligation offers investors broader protection than that afforded under Article 3(1) of the Treaty. The Claimant does not discuss the implications of this statement for its reading of Article 3(1). In the view of the Tribunal, this argument shows that the Claimant considers it necessary to have recourse to the MFN clause to reach the level of protection afforded by the addition of the terms “full” and “security”. In other words, the Claimant’s argument on the application of the MFN clause contradicts the Claimant’s broad reading of the term “protection” in Article 3(1) as including all protections under the Treaty. If this were the case, there would be no need to have recourse to the MFN clause to enjoy wider protection.[67].

Today, the interpretation of MFN clauses remains one of the most controversial issues of international investment arbitration, often referred to as one of the prime examples of a lack of consistency and predictability, regarding the extent to which these clauses can

[65] Reinisch and Schreuer, *International Protection of Investments*. at. 741, “For instance, in *Societé Générale v. Dominican Republic*, an LCIA tribunal rejected the investor’s attempt to ‘import’ a broader investment definition via the applicable MFN Clause.”

[66] Reinisch and Schreuer, *International Protection of Investments*., 697.

[67] Sanum Investments Limited v. Lao People's Democratic Republic, UNCITRAL, PCA Case No. 2013-13, Award on Jurisdiction, para. 357.

be relied upon to obtain more favourable jurisdictional or even procedural rules imported from third party's IIAs.[68]

d) National Treatment

In the same line as MFN, NT is one of the basic non-discrimination disciplines in international investment law and can be found in the majority of IIAs. It consists of provisions that grant the investor the right to treatment no less favourable than the one given to the host state's investors. The idea is to prevent protectionist measures that would benefit national investors over foreign ones, and for that reason, it is safe to say that, together with MFN provisions, it is one of the cornerstones of non-discriminatory measures usually found in international investment treaties[69].

Like MFN provisions, NT provisions, although normally included in IIAs, are not part of customary international law and therefore states are free to discriminate between foreign and domestic investors in the absence of a specific treaty obligation stating otherwise.[70] This can be explained by the fact that regardless of the prevalence of NT clauses in IIAs suggesting a consistent and general state practice sufficient to the formation of customary law, there is nothing that points to a sense of legal obligation, one of the requirements for the creation of an obligation under international customary law.[71]

Regarding its practical application, although NT case law in international investment arbitration remains limited compared to other standards, tribunals have developed certain criteria that they apply consistently which are known as the 'three-step test'[72] to assert whether there is a discriminatory measure at hand.

This test consists of (1) identifying a domestic comparator 'in like circumstances' against which it is possible to measure the alleged discriminatory behaviour by the host state; (2) investigating if the treatment accorded to the investor is, in fact, less favourable

[68] Reinisch and Schreuer, *International Protection of Investments*., 812.
[69] Reinisch and Schreuer, *International Protection of Investments*., 591.
[70] Andrew Newcombe and Lluís Paradell, *Law and Practice of Investment Treaties: Standards of Treatment* (Austin (Tex.), 2009)., 149.
[71] Newcombe and Paradell, *Law and Practice of Investment Treaties*., 149.
[72] This test has been used in various arbitration proceedings where a breach of NT has been claimed by the investor, e.g., *Bayindir v. Pakistan*, Award, 27 August 2007: an ICSID tribunal stated that *the tribunal will first determine whether Bayindir's investment was in a "similar situation'. If so, it will then assess whether Bayindir's investment was accorded less favourable treatment than PMC-JV and whether the difference in treatment was justified*.

than the one given to the domestic investor; (3) examining if there is a legitimate justification to this different treatment. Regarding the burden of proof of the breach of an NT clause, there is a broad consensus that claimants have to be the ones proving that they were discriminated against, while respondent states bear the burden of proofing that the specific discrimination was justified.[73]

Another interesting fact about this substantive standard of treatment is that, since state measures often discriminate against foreign investors to the benefit of national investors, reservations and exceptions are widely adopted, being more common in specific sectors of the economy with particular strategic, economic, political, or even social or economic significance to the state, like petroleum[74].

Nonetheless, the most crucial limitation on NT possibly found in IIAs regards its application only to investments that have already been admitted under the laws of the host state – this means that all NT provisions only apply on a post-entry investment, which translates into the promise of non-discrimination based on the foreign nature of the investment only applying once a business is established in the host state.[75]

Arbitral tribunal's jurisprudence on National Treatment is still evolving, since many aspects are yet to be clarified[76] (e.g., the burden of proof). Nevertheless, as previously mentioned, tribunals have developed some criteria in a rather consistent manner (e.g., the three-step test). However, references to "no less favourable treatment" in IIAs also do not clarify whether the investor is entitled to the best treatment afforded to any other investor, national or foreign, or the average treatment afforded.[77]

Nonetheless, it is relatively safe to say that relative standard provisions apply to any form of less favourable treatment between different nationals, once preferences cannot be given to one category investors, in disregard to another[78].

e) Full Protection and Security

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[73] Reinisch and Schreuer, *International Protection of Investments*., 623-679.
[74] Newcombe and Paradell, *Law and Practice of Investment Treaties*., 190.
[75] Collins, *An Introduction to International Investment Law*., 100.
[76] Reinisch and Schreuer, *International Protection of Investments*., 679.
[77] Newcombe and Paradell, *Law and Practice of Investment Treaties*., 186-187.
[78] Newcombe and Paradell, *Law and Practice of Investment Treaties*., 188.

IIAs also regularly contain FPS provisions, which typically appear close to FET clauses, often in the same sentence. Differently from MNF and NT, FPS is an absolute standard because its content does not depend upon the level of treatment given to other investors, nevertheless, it has been debated that, in some respects, the legal protection conceded under domestic law relates FPS to an NT standard, which is, as we have seen, a relative one.[79] Regarding its historic origin, FPS takes us back to the previously mentioned international minimum standard for the protection of foreigners (or aliens), as FCN treaties celebrated in the nineteenth century referred to this level of protection and security.[80]

Much like FET, the FPS standard is a form of protection that has developed in a somewhat general focus, in this case on physical harm, requiring the host state to grant physical protection and security to the foreign investor's property set in its territory, which means that there is an obligation, under these provisions, for the host state to deploy its police or military personnel to guard the investor's assets that are a damage risk.[81] This damage can occur in different manners, (e.g., a political uprising that may result in civil disturbances).[82] Most modern IIAs have FPS provisions[83]. This protection is granted against violence from both private and state entities. In the latter, under international law, the state's responsibility extends to actions perpetrated by any of its organs as unjustified coercive measures taken by organs of the host state against the investor and its property constitute violations of the FPS standard if they jeopardise the investment to a material degree[84].

Interestingly enough, most treaties do not state explicitly whether the FPS standard extends to legal security. However, it is generally accepted that the FPS standard reaches beyond the safeguard of physical violence and requires legal protection for the investor through the host state's regulatory power.[85] Backing this theory, we can find several

[79] Reinisch and Schreuer, *International Protection of Investments*., 540.

[80] About this topic, see chapter 1.2.

[81] Collins, *An Introduction to International Investment Law*., 137-138.

[82] Collins, *An Introduction to International Investment Law*., 137.

[83] Other ways in which this standard has been referred to include "most constant protection and security", "protection and security", "full protection", or merely "protection".

[84] This has been addressed in some investment arbitration cases, such as *Eureko v. Poland*, Partial Award, 19 August 2005, in which the claimant alleged harassment by Polish authorities of the investment's senior representatives.

[85] Collins, *An Introduction to International Investment Law*., 143-145.

arbitral cases in which this standard was applied in regards of legal protection, one of them being *Saluka v. the Czech Republic*[86].

In fact, there is substantial authority to support the proposition that the FPS standard includes protection through a functioning legal system. Thomas Wälde, for one, states that:

> This obligation would not only be breached by the active and abusive exercise of State powers, but also by the omission of the state to intervene where it had the power and duty to do so to protect the normal ability of the investor's business to function (…) a duty, enforceable by investment arbitration, to use the powers of government to ensure the foreign investment can function properly on a level playing field, unhindered and not harassed by the political and economic domestic powers that be.[87]

Nevertheless, it is important to remind that there has been an exclusion of legal security in some cases and tribunals have denied that the FPS standard relates to anything but physical or police protection. Among these cases, we can find the *PSEG v. Turkey*[88], where the claimant alleged that the FPS standard included in the Turkey-US BIT protected the investment and the investor against adverse effects made by an amendment of the law or even administrative actions.[89] The tribunal found that in this specific case it was not possible to find that there had been an exceptional situation that could qualify under the FPS standard as a separate heading for state liability, once it considered that only in some cases is it possible to admit a broader interpretation that could be justifiable under a breach of FET or even some form of expropriation.[90]

This being said, the FPS standard has led to conflicting interpretations, especially about the question of physical versus legal protection. Regarding its relationship with customary international law, there is also some debate. The question is whether the FPS

[86] *Saluka v. the Czech* Republic, Partial Award, 17 March 2006, paras. 483-484.
[87] Thomas W. Wälde, 'Investment Arbitration under the Energy Charter Treaty: An Overview of Selected Key Issues Based on Recent Litigation Experience', in *Arbitrating Foreign Investment Disputes: Procedural and Substantive Legal Aspects*, by Norbert Horn and Stefan M. Kröll, Studies in Transnational Economic Law, Kluwer Law International, 2004, 193–235., 213.
[88] PSEG Global, Inc., The North American Coal Corporation, and Konya Ingin Electrik Üretim ve Ticaret Limited Sirketi v. the Republic of Turkey, ICSID Case No. ARB/02/5
[89] PSEG Global, Inc., The North American Coal Corporation, and Konya Ingin Electrik Üretim ve Ticaret Limited Sirketi v. the Republic of Turkey, ICSID Case No. ARB/02/5, Award para. 222-237.
[90] PSEG Global, Inc., The North American Coal Corporation, and Konya Ingin Electrik Üretim ve Ticaret Limited Sirketi v. the Republic of Turkey, ICSID Case No. ARB/02/5, Award, para. 257-259.

standard and FET create a new independent treaty standard or are merely references to the international minimum standard under international customary law.[91]

The theory that defends that FPS, as well as FET, are autonomous treaty standards that are independent of the international minimum standard is, for some scholars, preferable, nevertheless, even without an FPS treaty provision, an investor may find some protection and comfort under international law once the international minimum standard includes certain duties to protect foreign investors against adverse action[92], from both private and public entities.

1.4. The Rationale for the Direct Access of Foreign Investors to Investment Treaty Arbitration

Another relevant topic in international investment treaty arbitration that cannot be left behind in this introduction is the reasoning behind the direct access to investment arbitration granted to investors in IIAs' provisions.

Being one of the most important innovations made in contemporary international arbitration, the protections granted to investors[93] and their investments, would be immaterial if there was no mechanism available to investors through which to enforce them and to receive monetary compensation.[94] For this reason, in addition to substantial provisions, IIAs contain several procedural guarantees for access to dispute resolution – but why is this access given directly to non-state entities?

To understand this issue, it is important to highlight that, without an alternative ISDS mechanism, disputes between individuals and states in the exercise of their sovereign authority could only be taken before the domestic courts of said state, considering that state immunity would prevent the submission of such claims before domestic courts of the individual's home state.[95] In other words, given the specific context of international investment treaty law, this would mean that to protect their investment from a breach of substantial or other treaty provisions, the investor's only possibility would be resorting to

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[91] Reinisch and Schreuer, *International Protection of Investments*., 586.

[92] C. Schreuer, 'Full Protection and Security', *Journal of International Dispute Settlement*, 1/2 (2010), 353–69 <https://academic.oup.com/jids/article-lookup/doi/10.1093/jnlids/idq002> [accessed 9 February 2022].

[93] *See* Chapter 1.3.

[94] Brabandere, *Investment Treaty Arbitration as Public International Law*., 17-19.

[95] Brabandere, *Investment Treaty Arbitration as Public International Law*., 19-21.

the domestic courts of the host state, coupled with the possibility of diplomatic protection from their home state, which, in itself, can sometimes be a somewhat difficult, lengthy, and uncertain process.

If this was the case, only in exceptional situations would the investor have the possibility of having their claims settled on the international level, namely with the resort to diplomatic protection. Even in such cases, under the mentioned circumstances, it would be required that they first exhaust all local remedies, which, again, would be a very time-consuming and unreliable process,.[96] This would mean that only after having exhausted all local remedies, as required under international law, would the investor be able to resort to diplomatic protection, under which their home state would invoke state immunity in order to expose the claim of its national.

It is important to note that, in this particular situation, the state would not be enforcing the rights of the individual, but rather its own rights: the right to have its citizens treated legally. This issue was well placed by the Permanent Court of International Justice in the *Mavromattes Palestine Concessions v. Britain* case, as follows:

> It is an elementary principle of law that a State is entitled to protect its subjects, when injured by acts contrary to international law committed by another State, from whom they have been unable to obtain satisfaction through ordinary channels. By taking up the case of one of its subjects and by resorting to diplomatic action or international judicial proceedings on his behalf, a State is, in reality, asserting its own rights – its right to ensure, in the person of its subjects, respect for the rules of international law[97].

Avoiding this uncertain and somewhat cumbersome procedure is one of the reasons behind granting the foreign investor a right to bring a claim against the host state by the tribunal – the rationale is mainly motivated by the ineffectiveness of the traditional system of diplomatic protection.[98] This direct access to arbitration, therefore, provides a guarantee to the investor that, in case of dispute, there is an adequate, effective, and impartial international remedy that, at the same time, creates an investor-friendly environment for the host state[99].

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[96] Brabandere, *Investment Treaty Arbitration as Public International Law*., 21.
[97] Mavromattes Palestine Concessions v. Britain, PCIJ Judgment No. 2, 30 August 1924., para. 21.
[98] Brabandere, *Investment Treaty Arbitration as Public International Law*., 19
[99] Brabandere, *Investment Treaty Arbitration as Public International Law*., 21.

Also, it is important not to forget that, as De Brabandere highlights[100], regardless of the undeniable link between the direct access to investment arbitration and the protection of investments, the grant of certain individual rights does not automatically mean that this procedure applies to any kind of claim for a violation of rights under international law. On the contrary, the express consent of the host state is required, which means that for this direct access to international investment arbitration to be granted, an international treaty has to be concluded or that national legislation has to be adopted by the host state. States, when expressing consent to direct investment arbitration may condition it by, for example, inserting "fork-in-the-road" clauses that compel the investors to choose between international arbitration or domestic courts.

In conclusion, the underlying idea behind this direct access to international investment arbitration given to investors is to provide a standing offer or unilateral consent of the host state, for arbitration, which can be accepted by a qualified investor, thereby creating a binding arbitration agreement. On the other hand, it is understandable, from the investor's point of view, that this mechanism is more attractive and secure for investments once it ensures that there will be a place to enforce their rights in case of the rise of a dispute.

2. An Introduction to International Environmental Law

In the last three decades, considering the increasing levels of pollution, environmental protection an urgent necessity. Having that in mind, the international community has increasingly recognized the value of the natural environment and created guidelines to be followed to safeguard its deterioration and states have celebrated several treaties and created instruments aimed to protect the environment, the so-called MEAs. [101]

As it happens, more often than not, environmental law and investment arbitration meet, not only in theory but also in disputes[102]. To better understand the connection between these two fields of law, in this part of this dissertation, we will explore which are the most

[100] Brabandere, *Investment Treaty Arbitration as Public International Law*., 22-24.

[101] Marisi, *Environmental Interests in Investment Arbitration*., 34.

[102] As it was proved in *S.D. Myers, Inc. v. Government of Canada,* partial award, 13 November 2000, a leading case in which the partial award finds that each party of the NAFTA had the right of establishing high levels of environmental protection as they were not obliged to loosen their standards of environmental protection merely to satisfy the economic and political interests of other states.

important environmental soft law instruments, its principles and the role of those principles in the war against climate change.

2.1.Core International Environmental Law Principles

Defining the concept of principles can revel to be quite hard, which is why scholars use different approaches, mainly stressing the structural differences between principles and rules.

In the field of environmental studies, scholars have embraced the difference identified by Dworkin[103] as he stated that what divides them is a logical distinction: rules are, for this author, applicable in an "all-or-nothing" fashion and principles, on the other hand, merely give a reason that argues on one direction but does not need a particular decision – all in all, various roles and functions are fulfilled by principles in international law, all of them related to the regulation of the state's behaviour[104]. On this note, it is safe to say that international environmental principles are designed to induce specific results in certain contexts. In other words, they result from the states' rational desire of maximizing their interests and the distribution of states' powers.

According to Marisi[105], several benefits can occur along with the adoption of certain international environmental principles as they are useful for the negotiation process and facilitate the development of consensus while establishing a harmonization between the different interests at stake, which in itself diminishes the transaction costs and unpredictability that accompanies negotiations undertaken by states in the international arena (they function as guidelines on how the states should act when negotiating in the international arena).

Considering the specific context of climate change litigation, principles can sometimes directly affect and even define the resolution of cases once they are of extreme importance for interpretation before courts – they supply basic ideas for different regulations which can make their interpretation and implementation process less challanging. This being said, we will explore the Core principles of international Environmental Law: the Polluter

[103] Marisi, *Environmental Interests in Investment Arbitration*., 31.
[104] Ronald Dworkin, *Taking Rights Seriously*, Bloomsbury Revelations Series, Paperback ed (London, 2013)., 39.
[105] Marisi, *Environmental Interests in Investment Arbitration*., 32 et seq.

Pays Principle, the Principle of Prevention, and the Precautionary Principle will be analysed.

a) The Polluter Pays Principle in Environmental International Law

According to the PPP, as we can understand from its formulation, the costs of pollution should be borne by the person causing the pollution. However, the extent and nature of the costs included, as well as the circumstances in which this principle is not applicable, are still open to interpretation. Nevertheless, this principle has received broad support as it is closely related to the rules governing civil and state liability for environmental damage[106].

Although the PPP can be traced back to the first instruments that predicted liability for damage resulting from high-risk activities, such as the 1960 Paris Convention and the 1963 Vienna Convention, it was only expressly adopted for the first time in the 1972 OECD Council Recommendation on Guiding Principles Concerning International Aspects of Environmental Policies, where it was stated that:

> The principle to be used for the allocating of pollution prevention and control measures to encourage rational use of scarce environmental resources and to avoid distortion in international trade and investment is the so-called "Polluter-Pays Principle". This principle means that the polluter should bear the expenses of carrying out the above-mentioned measure decided by public authorities to ensure that the environment is in an acceptable state. In other words, the cost of these measures should be reflected in the cost of goods and services which cause pollution in production and/or consumption. (…)
>
> (…) This principle should be an objective of Member countries; however, there may be exceptions or special arrangements. (…)[107]

Nevertheless, as we can understand from the above-made citation, the 1972 Recommendation does not apply to the costs of environmental damage. Other recommendations about the application of the Polluter Pays Principle were adopted in the following years. In 1989, the OECD Council recommendation extended the principle to imply that the operator of a hazardous installation should bear the costs of reasonable

[106] Philippe Sands and others, *Principles of International Environmental Law*, Fourth edition (Cambridge New York, NY Port Melbourne, VIC New Delhi Singapore, 2018)., 240 et seq.

[107] OECD, 'Recommendation of the Council on Guiding Principles Concerning International Economic Aspects of Environmental Policies', (1972).

measures introduced by public authorities to prevent and control accidental pollution that might result from that same installation, in conformity with the domestic law before the occurrence of said accident.

Regarding the definition of "reasonable measures", the recommendation stated that they depend on the circumstances under which *they are implemented, the nature and extent of the measures, the threats and hazard existing when the de decision is taken, the laws and regulations in force, and the interests which must be protected*.[108]

We find that more and more international treaties incorporate this principle, which has also been codified in EU law, although in a non-binding form.[109] Some examples of international declarations and regimes that have incorporated this principle are the 1972 Stockholm Declaration, the 1990 International Convention on Oil Pollution Preparedness, Response and Cooperation, the 1992 Rio Declaration, the 1992 Helsinki Convention on Protection of the Marine Environment of the Baltic Sea Area, and other agreements such as the NAFTA agenda 21.

The increasing attention paid to this principle results from the undeniable link between environmental protection and economic development. For that reason, some questions related to the extent of pollution control costs that should be paid by the polluter as well as the exceptions to this principle, particularly regarding its relation to the rules governing the grant of subsidies, must be defined, and further clarified, in the future.

On this note, and to conclude, it is important to state that, as observed by De Sadeleer, the Polluter Pays Principle represents a certain level of ambiguity because while contributing the behaviour of those subject to the carried-out policy, it might lead to the understanding that paying for the environmental damage caused grants a somewhat "right to pollute"[110].

b) The Principle of Prevention

[108] OECD, 'Recommendation of the Council OECD Legal Instruments Concerning the Application of the Polluter-Pays Principle to Accidental Pollution' (1989).

[109] Marisi, *Environmental Interests in Investment Arbitration*., 51.

[110] Nicolas De Sadeleer, *Environmental Principles: From Political Slogans to Legal Rules*, 2nd ed (Oxford, 2020)., 83.

As Marisi States, *According to the Principle of Prevention, states, corporations, and individuals are, in certain circumstances, under the general obligation to avoid causing damages to the environment, including the environment beyond their territory*[111] or property. This principle has been adopted by some conventions, including Article 194(1) and (2) of the UN Convention on the Law of the sea, as follows:

> 1.states shall take, individually or jointly as appropriate, all measures consistent with this Convention that are necessary to prevent, reduce and control pollution of the marine environment from any source, using for this purpose the best practicable means at their disposal and in accordance with their capabilities, and they shall endeavour to harmonize their policies in this connection.
>
> 2.states shall take all measures necessary to ensure that activities under their jurisdiction or control are so conducted as not to cause damage by pollution to other states and their environment, and that pollution arising from incidents or activities under their jurisdiction or control does not spread beyond the areas where they exercise sovereign rights in accordance with this Convention.[112]

The rationale behind this principle seems clear: although throughout the years the curative approach has been deeply practised in environmental law, the relatively recent understanding that these measures may remediate but not avert environmental damage modified the field drastically, signalling a fundamental change of approach. In fact, Preventive measures can anticipate the damage rather than repair it. In reality, by demanding the adoption of preventive measures to protect the environment, this principle complements the PPP, once the latter does not necessarily compel polluters to reduce their polluting acts but rather only requires them to internalize their costs.[113]

The most heated debate regarding this principle is as to whether the concept of prevention can be deemed as a principle in itself. Duvic-Paoli and Viñuales[114] defended that for a principle to be qualified as a principle, a statement has to perform three functions, (1) an architectural function, by directing the contents or section of a treaty; (2) an interpretive function, by ensuring that a stipulation is understandable or by

[111] Marisi, *Environmental Interests in Investment Arbitration*., 61.

[112] Article 194(1) and (2) (Measures to Prevent, reduce and control pollution of the marine environment) of the United Nations Convention on the Law of the Sea.

[113] De Sadeleer, *Environmental Principles*., 85.

[114] Leslie-Anne Duvic-Paoli and Jorge E. Viñuales, 'Principle 2: Prevention', in *The Rio Declaration on Environment and Development: A Commentary*, Oxford Commentaries on International Law, First edition (Oxford, United Kingdom, 2015).

integrating the requirements of two opposite norms; and (3) a decision-making function, by ensuring that a particular act complies with legal requirements, interdictions, or permissions, which should be reflected in how the statement is formulated.

It is possible to conclude that, by these requirements, the Prevention principle can be considered a principle once it can be illustrated by reference to numerous environmental treaties, it performs an important interpretive function relating to other matters, such as the clarification or even the conciliation of different considerations and, finally, it is precise enough to perform a decision-making function.[115]

According to these authors[116], it is possible to establish three components of the Prevention Principle: (1) sovereignty over natural resources (2) preventing harm to the environment of other states and (3) preventing harm to the environment beyond national jurisdiction.

Looking more deeply into the first concept, it is possible to conclude that it is not an environmental one but rather assigns legal powers over natural resources.[117] Its adaptation to the environmental sphere shaped this principle, creating a dynamic balance between sovereignty and environmental protection, which is the centre and heart of this principle. Sovereignty and environmental protection do not necessarily need to be seen as competing considerations and for that reason, in recent years, there has been some effort at reconceptualizing sovereignty as *powers held in the trust to the benefit of the present and future generations*.[118]

Nevertheless, as environmental elements are increasingly included in investment awards, this principle is considered a factor that can legitimise differential treatment of two projects and as a vital interest that requires protection and concern[119] that investors must consider in the formulation of their legitimate expectations[120]. It is also understood

[115] Marisi, *Environmental Interests in Investment Arbitration*., 67.
[116] Duvic-Paoli and Viñuales, 'Principle 2: Prevention'., para 2.1.2.1.
[117] Duvic-Paoli and Viñuales, 'Principle 2: Prevention'., para. 2.1.2.2
[118] Duvic-Paoli and Viñuales, 'Principle 2: Prevention'., para. 2.1.2.2.
[119] *Suez, Sociedad General de Águas de Barcelona S.A. and InterAgua Servicios Integrales del Água S.A. v. The Argentine Republic*, ICSID Case No. ARB/03/17
[120] *Plama Consortium Ltd v. Republic of Bulgaria*, ICSID Case No. ARB/03/24, Award, 27 Aug. 2008, paras 219–221.

that arbitrators must take it into account in the decision-making process regarding the compensation for environmental damages[121].

To conclude, it is important to acknowledge that there are two major challenges confronting this Prevention Principle, which have been brilliant pointed out by Marisi: its lack of specificity and differentiation[122].

c) The Precautionary Principle

As De Sadeleer points out, environmental damage policy measures have been modified over time: during the first phase, public authorities' intervention came in a stage where environmental damage had already happened, and the only possible course of action was remedial action.[123] This approach evolved and started to include a preventive dimension when public authorities began to intervene before any damage occurred which explains why this second stage is marked by the understanding that threats to the environment are tangible and that situations might rapidly become critical. Lastly, a third variation became marked by anticipation, which differs from the other two since authorities are prepared for potential, uncertain, or hypothetical threats.[124]

It is safe to say that what we find now is a change of paradigm once precaution distinguishes itself based on a concept different from certain risk, but rather intrusion or uncertainty. It is sufficient that risk is suspected, conjectured, or feared to justify public authorities action. Hence, the idea is to anticipate risks even when they are not assessable, calculable, or even certain, which explains the increasing invocation of the PP. On this line, the decision-making process must take all risks into account, despite their degree of certainty[125]. Nevertheless, although widely adopted in positive law, this principle's outlines are still far from consensual once it can be interpreted in a variety of ways.

[121] *Southern Pacific Properties (Middle East) Limited (SPP) v. Arab Republic of Egypt*, ICSID Case No. ARB/84/3, Award, 20 May 1992, paras 191, 250.

[122] About this issue, see Marisi, *Environmental Interests in Investment Arbitration*., 75.
[123] De Sadeleer, *Environmental Principles*., 135.
[124] *Id*.
[125] *Id*.

Some authors[126] stress that there is still yet to be a consensus about the features of this PP in international law: there is some debate around the wording of the principle since it has been classified both as a principle and an approach, which has serious implications on the normative nature of the concept and its possible contribution to international law, as it has been previously mentioned when analysing the role of principles under international environmental law[127].

Regarding its inclusion in International Conventions, the development of the PP has begun in the 1960s in the former Federal Republic of Germany, alongside the popularity of social democratic planning.[128] In fact, there was consensus in the idea that prudent planning had to be prioritized by public authorities as a way to prevent environmental damage. In the following years, the PP became a requirement that industrial processes had to endure to reduce polluting emissions, as much as possible, at the source, by using the most advanced abatement technology.[129]

Later, this principle was legitimized in several MEAs, including decisions adopted in the 1990s by the States within the North Sea Ministerial Conferences that marked the first use of PP in international law. Consequently, this principle expanded its domination in the field of marine pollution, transboundary Watercourses, and fisheries, as well as atmospheric pollution. Nonetheless, the PP rapidly moved beyond these spheres into other areas of international environmental law.[130] As a result, since the 1992 Rio Conference, the PP has been included in the majority of MEAs and is today found in more than sixty of them, covering a wide range of environmental issues that vary from air pollution to waste management. Hence, PP has occupied an uncontested position in international environmental law, to the point that it is safe to say that it has overshadowed the Principle of Prevention, not regardless of the remaining controversy[131].

[126] Jorge E. Viñuales and Jacqueline Peel, 'Precautionary Principle', in *The Rio Declaration on Environment and Development: A Commentary*, Oxford Commentaries on International Law (Oxford, United Kingdom, 2015)., 250.
[127] See, chapter 2.1., 24.
[128] Marisi, *Environmental Interests in Investment Arbitration*., 78.
[129] *Id*.
[130] *Id*.
[131] For further analyses of this controversy, *see* De Sadeleer, *Environmental Principles*., 152 et seq.

2.2.Soft Environmental Law

It is easy to understand that damages caused to the environment concern every and each nation for they indiscriminately cross borders. For that reason, it was soon realized that domestic legislation and regulation were insufficient to prevent them. This realization has led states to conclude Multilateral, Regional and Bilateral Environmental Treaties regarding its protection, where it was essential to choose whether it is preferable to integrate them into the body of soft or hard law. The main difference between them is that, for international law, hard law agreements and principles that are directly enforceable and soft law instruments are non-binding and give rise to non-treaty obligations that are, therefore, not enforceable.[132]

Be as it may, international soft law is intended to determine states to comply with particular norms by integrating them into their national law and giving substance to the standards that are commonly applied or aimed for. Also, like principles, soft law facilitates the process of states finding an agreement when negotiating the terms of binding written law, in fact, as Boyle states, one of the reasons why soft law instruments may represent an attractive alternative to law-making by treaty is that it is considered to be easier to reach agreement when the form is non-binding. This use of soft law instruments enables states to agree to more detailed and precise provisions because their legal commitment, and the consequences of any non-compliance, are more limited.[133]

Two examples of Environmental Soft Law are the 1972 Stockholm Declaration, in which twenty-six principles on humans and the surrounding environment were issued and the 1982 World Charter for Nature, developed by the International Union for the Conservation of Nature and Natural Resources, where it was stated that *activities which might have an impact on the nature shall be controlled, and the best available technologies that might minimize significant risks to the nature or other adverse effects shall be used*.[134]

Nonetheless, it is safe to say that the most important soft law instruments in International Environmental Law are the 1972 Stockholm Declaration and Action Plan,

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[132] Marisi, *Environmental Interests in Investment Arbitration*., 34.

[133] Alan E. Boyle, 'Some Reflections on the Relationship of Treaties and Soft Law', *The International and Comparative Law Quarterly*, 48/4 (1999), 901–13., 902-903.

[134] UN World Charter for Nature, para. 11(b).

the 1992 Rio Declaration and the 2017 Global Pact for the Environment, which will be analysed in the subsequent chapters. Beforehand, it is also important to note that experts, scholars, and practitioners have been claiming the need for a hard law instrument that could render the body of international environmental law more coherent and systematised[135], however, to this day, it still has not happened. This pledge is understandable under the idea that the above-mentioned principles[136] are part of soft environmental law and that leads to divergences in their practical application and creates limitations to their effectiveness.

a) The 1972 Stockholm Conference

The 1972 Stockholm Conference was the first world conference on the environment. The participants adopted a series of resolutions, including the Stockholm Declaration and Action Plan for the Human Environment[137]. The major result of this conference was, however, the creation of the United Nations Environment Programme (UNEP), which has, since then, been the global authority that sets the environmental agenda, promotes the coherent implementation of the environmental dimension of sustainable development within the UN's system and serves as an authoritative advocate for the global environment.[138]

For the first time, the Stockholm Declaration placed environmental issues at the centre of international discussion and opened the dialogue between industrialized and developing countries on topics related to economic growth, the polluting of the air, water, and oceans as well as the well-being of all people and their link. This declaration contained 26 principles. Out of those principle 21 is of great importance once it states that *States, in accordance with the Charter of the UN and the principles of international law, the sovereign right to exploit their own resources pursuant to their own environmental policies, have the responsibility to ensure that activities within their jurisdiction or*

[135] See, UNGA Resolution 72/277, titled *Towards a Global Pact for the Environment*, 14th May ,2018.
[136] *See* Chapter 2.1.
[137] United Nations, *Report of the United Nations Conference on the Human Environment,* 1972 <https://undocs.org/en/A/CONF.48/14/Rev.1>.
[138] Philippe Sands, 'International Law in the Field of Sustainable Development', *British Yearbook of International Law*, 65/1 (1995), 303–81 <https://academic.oup.com/bybil/article-lookup/doi/10.1093/bybil/65.1.303> [accessed 20 February 2022].,309-310.

control do not cause damage to the environment of other states or of whereas beyond the limits of national jurisdiction.[139]

The UN Report of the UN Conference on the Human Environment also contained an Action Plan incorporating three main categories: (1) Global Environmental Assessment Programme; (2) Environmental Management Activities and (3) international measures to support assessment and management activities carried out at the national and international levels. These categories ended up being broken into one hundred and nine recommendations.

As a diplomatic conference declaration, this instrument is formally not binding, nevertheless, it includes provisions that, at the time of their adoption were either understood to already reflect CIL or expected to shape the future normative expectation. As we will see, the Rio Declaration expressly reaffirms and builds upon this first declaration, which reinforces the normative significance of the common concepts of both instruments.

b) The 1992 Rio Declaration

> *Environmental protection shall constitute an integral part of the development process and cannot be considered In isolation from it.*[140]

In June 1992, on the 20th anniversary of UNEP, the representatives of one hundred and seventy-two states gathered in Brazil in what was then famously known as "The Earth Submit". This Conference resulted in the Rio Declaration on Environment and Development – a pledge to save the planet. This Declaration represents a series of delicate compromises adopted to achieve a harmonious equilibrium between environmental protection objectives and economic development. It also reaffirmed the 1972 Stockholm Declaration on the Human Environment in its preamble, although the text of Principle 21 was altered in Principle 2 with the addition of the wording "and developmental" to the affirmation of national environmental policies for the exploitation of resources.

The Declaration was adopted by the Earth Submit and perhaps made the transition from international environmental law to the international law of sustainable development,

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[139] Principle 21 of the Stockholm Declaration
[140] Principle 4 of the Rio Declaration.

as said by Sands *The emergence of "international law in the field of sustainable development should herald the disappearance of the self-contained and compartmentalized worlds of environmental and economic* law. [141] However, the Declaration is, in part, a restatement of existing customary international law and enforcement of twenty-seven new or developing principles of law concerned with the protection of the environment, such as the PPP (principle 16), the Principle of Prevention (principle 2), the Precautionary Principle (principle 15) and EIA (principle 17)[142].

Although this document was initially baptized as the "Earth Charter" it was changed to the current name when developing states pointed out that the title prioritized earth and nature more than people and development. In fact, there were several occasions where developing countries have had an opposite position to the of developed countries, which mainly included a change in the formulation of the Convention in itself.

As it happens, the first refuted not so much the reference to pollution and waste but rather wanted to include the idea that the excessive consumption in affluent countries was the reason for the poverty of developing countries. On this note, the latter demanded the right to development, poverty alleviation, and the recognition of "common but differentiated responsibilities" to integrate the core of principles recognized in the convention.The sequence of events that followed together with its signature by almost every country, has made the Rio Declaration "the most significant universally endorsed statement of general rights and obligations of the states affecting the environment".[143]

All in all, as pointed out by Marisi[144], *the success of soft law in guiding the evolution of International Environmental Law has led the phrasing of certain provisions to be accepted by numerous states and, therefore, has allowed it to become customary law*.

c) The Global Pact for the Environment – The New International Environmental Constitution to be?

The Global Pact for the Environment was first launched in France in 2017. Later, in May 2018, UNGA adopted a resolution paving the way to start negotiations aimed at

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[141] Sands, 'International Law in the Field of Sustainable Development', 303–81., 381.
[142] About these principles *see* Chapter 2.1.
[143] Alan E. Boyle and David A. C. Freestone, eds., *International Law and Sustainable Development: Past Achievements and Future Challenges*, 1. publ. new in paperback (Oxford, 2001)., 68.
[144] Marisi, *Environmental Interests in Investment Arbitration*., 46.

creating an international legally binding agreement to be adopted under the UN's umbrella, which would be considered a "New International Environmental Constitution".[145] For this purpose, it was requested for the Secretary-General to submit a report on gaps in International Environmental Law and environment-related instruments and establish a working group to consider the report and discuss possible solutions to address such gaps. [146]

The obvious precursors of the Global Pact are the 1972 Stockholm declaration and the 1992 Rio Declaration on Environment and Development, whose principles the draft pact repeats in a similar or even identical language.[147] It is safe to say that it comprises well-established norms, broadening their scope and clarifying some interpretational doubts. Nevertheless, new principles have been included, once the group seems to want to make a compromise between innovation and consolidation.

Under the latter falls the above-mentioned PPP, Prevention Principle, Precautionary Principle and EIA as well as the access to information, the principle of intergenerational equity, the participation in environmental decision-making and access to justice.

It is then possible to conclude that the aim is to create an instrument that globally reinforces the environmental rule of law, provides clear guidance to judges, and integrates the currently fragmented Environmental International Law, facilitating its implementation.

On this note, the Draft Project was formulated by a group of more than one hundred renowned environmental law specialists – also known as the "Group of Experts on the Pact" – and coordinated by the Environmental Commission of the *Club des Juristes*, with the French Constitutional Council. ~

On the 30th of August 2019, the UNGA adopted resolution 73/333[148] known as the "Follow up Report of the ad-hoc open-ended working group established pursuant to

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[145] Marisi, *Environmental Interests in Investment Arbitration*., 43.

[146] UNGA, *Gaps in international environmental law and environment-related instruments: towards a global pact for the environment*, Report of the Secretary General., 33-39.

[147]

[148] United Nations General Assembly, *Resolution 73/333,* 2019 <https://undocs.org/en/A/RES/73/333>.

General Assembly resolution 72/277”, in which the work of the group was welcomed along with its report.

All recommendations as set out in the annexe to resolution 72/277 were endorsed. On May 8, 2020, the President of UNEA and the Chair of the Committee of Permanent Representatives nominated two co-facilitators to lead the negotiation process. Their mandate is to supervise three consultative meetings, the first of which occurred in June 2020. The other two ended up being rescheduled due to the COVID-19 Pandemic. The second consultation took place in November 2021, in Nairobi, and the Last took place in February 2022 also in Nairobi.

This sets the stage for a special session of the UNEA, which will take place in Nairobi on the 3rd and 4th of March 2022. It will be a high-level event named UNEP@50, celebrating the 50 years of the 1972 Stockholm Declaration, and will be devoted to “strengthening UNEP for the implementation of the environmental dimension of the 2030 Agenda for Sustainable Development”. If adopted, the Pact will be the first international treaty on the environment as a whole.

PART II – BALANCING ENVIRONMENTAL CONCERNS AND INVESTMENT PROTECTION IN INVESTMENT TREATY ARBITRATION

3. Environmental Concerns in International Investment Treaty Arbitration

Now that we have had the opportunity to clear the theoretical framework that will follow us during this dissertation, this chapter will solely focus on how to balance environmental concerns and the protection and promotion of investment through investment treaties.

The most relevant issue that comes with the existing tension between environmental concerns and the protection of investments is the balancing of the state's right to regulate and the compliance to other treaty obligations, which, as we know, does not come easy. In fact, most literature sympathises with the notion that investment treaty arbitration has the potential to frustrate the legitimate authority of host countries to regulate sensitive subjects such has environmental protection, and thus curtail the policy space of host sates, due to the level of protection that is granted to foreign investment and investors.[149]

This being said, this chapter focuses on the potential that these responses offer to create a sustainable investment treaty arbitration regime that is, at the same time, able to reconcile competing public and private interests and assure regulatory power to host states policies that promote sustainable development. For that purpose, we will firstly discuss the tension that there is between the persecution of public welfare by host states and the protection of investments and investors' rights.

3.1.The State's Right to Regulate

As it already been stated in this dissertation, reconciling investment and environmental protection can come as a challenge in the context of investment treaty arbitration.[150] This can be recalled to the general idea that, as we have had the opportunity to explore in chapter 1.3 of this dissertation, one of the pillars of international investment treaty arbitration is the general understanding that a foreign investor should be treated in a fair and equitable manner by the host state.[151] This notion is therefore supported by the

[149] Taejoon Ahn, 'The Utility of Carve-out Clauses in Addressing Regulatory Concerns in Investment Treaty Arbitration', *Asian International Arbitration Journal*, 12/1, 2016, 65–76., 66.

[150] Marisi, *Environmental Interests in Investment Arbitration*., 255.

[151] About this issue see chapter 1.3. of this dissertation, pp. 16-24.

inclusion of FET standard in almost all IIAs currently in force, as well as its invocation in the vast majority of investment disputes.[152]

As it happens, sometimes this protection granted to investors collides with the state's right to regulate within their territory without risking international liability for breaching treaty provisions related to the protection of investments[153] (such as National Treatment, MFN, FET and FPS)[154]. For this reason, calls for a reform of the investment protection regime have increased, mostly in favour of the asserting and strengthen the state's right to regulate.[155] On this note, many critics and authorities have been releasing a range of arguments regarding the reform of the current investment treaty arbitration system, regulatory concerns being, by large, the most raised ones.[156]

These concerns are understandable under the assumption that early investment treaties concluded between 1960 and 2000 usually did not explicitly mention the state's right to regulate.[157] One example of this trend is the 1991 German Model BIT in which the right to regulate could only be implied indirectly from the expropriation provision. In reality, the old IIAs had provisions on the protection of investment did not have any language on the state's right to regulate, as follows:

> Investments by nationals or companies of either Contracting Party shall not be expropriated, nationalized or subjected to any other measure the effects of which would be tantamount to expropriation or nationalization in the territory of the other Contracting Party except for the public benefit and against compensation. Such compensation shall be equivalent to the value of the expropriated investment immediately before the date on which the actual or threatened expropriation, nationalization or comparable measure has become publicly known. The compensation shall be paid without delay and shall carry the usual bank interest until the time of payment; it shall be effectively realizable and freely transferable. <u>Provision shall have been made in an appropriate manner at or prior to the time of expropriation, nationalization or comparable measure for the determination and payment of such compensation</u>. The legality of

[152] Yulia Levashova, *The Right of States to Regulate in International Investment Law: The Search for Balance between Public Interest and Fair and Equitable Treatment*, International Arbitration Law Library, volume 50 (Alphen aan den Rijn, 2019)., 1.

[153] Catharine Titi, *The Right to Regulate in International Investment Law*, Studies in International Investment Law, 10, 1. ed (Baden-Baden, 2014)., 125-14.

[154] About these standards of protection, please see chapter 1.3. of this dissertation.

[155] Marisi, *Environmental Interests in Investment Arbitration*., 254-255.

[156] *Id*.

[157] Inga Martinkute, 'Right to Regulate in the Public Interest: Treaty Practice', *Jus Mundi*, 2021 <https://jusmundi.com/en/document/wiki/en-right-to-regulate-in-the-public-interest> [accessed 4 June 2022].

> any such expropriation, nationalization or comparable measure and the amount of compensation shall be subject to review by due process of law.[158]

According to Martinkute, the hope was that arbitral tribunals would be more successful than negotiating states in drawing the line between investors' rights and public interests protected by regulations. However, the effect might have been the opposite. In fact:

> (…) the sole focus of the early BITs on the investment protections and their silence on how these protections interacted with various areas of public interest might have created an impression of the absolute rights and protections accorded to the investors that were not limited by other considerations. The arbitral tribunals hearing investment disputes frequently found that they lack jurisdiction or facts to address other complaints related to the public interest regulation (…). [159]

This being said, it is possible to conclude that first-generation BITs could be considered imbalanced instruments, for they were born from a need to protect investors from host state abuses, which could have led to their design only having this sole aim in mind[160]. However, with the turn of the century, a number of Model BITs have expressly included regulatory space for host states to pursue the public interest which, for some scholars, did not seem enough[161]. For this and other reasons, almost 12 years ago, in August 2010, a group of 35 academics published the *Public Statement on the International Investment Regime*[162], which stated that:

> We have a shared concern for the harm done to the public welfare by the international investment regime, as currently structured, especially its hampering of the ability of governments to act for their people in response to the concerns of human development and environmental sustainability.

This political statement intended to expose that investment treaties have allegedly provided arbitrators with unduly pro-investor interpretations of IIAs and for that reason considered that investment treaty arbitration is was a fair, independent, and balanced method for the resolution of investment disputes. The statement also recommended for governments to review their treaties with a *view to withdrawing from or renegotiating*

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[158] Article 4(2) of the 1991 German Model BIT, our underlining.
[159] Martinkute, 'Right to Regulate in the Public Interest: Treaty Practice'., para. 4.
[160] Titi, *The Right to Regulate in International Investment Law*., 72.
[161] The 2004 USA Model BIT is one example, which was later followed by the 2012 Model BIT.
[162] Various, *The Public Statement on the International Investment Regime*, 31 August 2010 <https://www.osgoode.yorku.ca/public-statement-international-investment-regime-31-august-2010/>.

them in light of the concerns expressed above [as well as] *take steps to replace or curtail the use of investment treaty arbitration* in order to *strengthen their domestic justice system for the benefit of all citizens and communities, including investors.*[163]

Although relatively old, these concerns and mistrust still hover around investment treaty arbitration, even though treaty practice with respect to foreign investor's substantive and procedural rights has continued to evolve, particularly in respect of these concerns.[164] In fact, various International instruments propose a variety of approaches to achieve a better balance between the right to regulate for a public interest and investment protection. The approaches range from including a reference to the right to regulate in the preamble, to explicitly carving out regulatory space in the context of various investment guarantees.[165] In fact, there is a growing number of Investment Treaties including which include provisions such mechanisms. One example of this trend is the 2021 Italian Model BIT which, in its preamble states that:

> (…)
>
> RECOGNIZING the importance to promote equal opportunities and participation for women and men in the economy;
>
> WILLING to duly protect the intellectual property rights of their investors and
>
> RECOGNISING that the provisions of this Agreement preserve the right of the Parties to regulate within their territories in order to achieve legitimate public policy objectives, such as public health, safety, environment, public morals, financial stability, social or consumer protection, and the promotion and protection of cultural diversity;
>
> (…)[166]

On this note, different types of clauses aimed at enabling the state to protect its environment while not breaching its investment treaty obligations have been identified and include (1) Preambular provisions which reference environmental protection; (2) exceptions limiting the application of treaty obligations to environmental measures. In the next chapters we will analyse each one of them.

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[163] Various, *The Public Statement on the International Investment Regime*.

[164] In fact, as we have stated before, this generation of IIAs already includes provisions in favor of t a more strengthened right to regulate.

[165] Marisi, *Environmental Interests in Investment Arbitration*., 103-104.

[166] 2021 MODEL BIT Italy preamble.

3.2.The Role of Preambular Provisions

This first method, that probably is the most abstract way to introduce the right to regulate into the equation, is to mention it in the preambles or elsewhere in the text of international investment agreements. Repository to a treaty's object and purpose, the preamble does not create independent legal rights or obligations. Accordingly, regulatory interests in the preamble do not establish a veritable right to regulate. Nonetheless they are of particular interest for the host state policy space[167]. For one, preambular provisions help identify the object and purpose of a treaty. Under Article 31 of the Vienna Convention on the Law of Treaties, they can be considered a key element of interpretation, even though they are not legally binding.[168]

Sentences referring to the protection of the environment do exist in several IIAs' preambles and may constitute an important interpretative tool at the arbitrators' disposal, so much as encapsulating the treaty's object and purpose as by forming part of its context.[169] However, As we have seen, more often than not, substantive provisions such as the ones including the substantive protection of investment and investors might raise interpretation issues[170]For this and other reasons, IIAs' preambles are commonly necessary for the context of investor-state arbitration, once they provide the arbitrators guidelines they can follow when interpreting disputed substantive principles that might have an unclear meaning and/or content. Neverttheless is important to keep in mind that preambles are not placed on a hierarchically superior level to other aims the treaty addresses, which provides arbitrators with a certain level of discretion when balancing these goals with environmental aims.

This being said, when interpreting an IIA, if preambular provisions state that investment promotion and protection are the exclusive aims of said instrument, it is highly likely that the tribunal will decide in favour of the investor and host states will see themselves prevented from following their legitimate environmental interests and policies. On the other hand, if environmental concerns are mentioned in the preambular provisions, aside from the extrinsic values of investment protection, the interpretation of

[167] Titi, *The Right to Regulate in International Investment Law*., 115.
[168] Marisi, *Environmental Interests in Investment Arbitration*., 108.
[169] Titi, *The Right to Regulate in International Investment Law*., 115.
[170] See chapter 1.3. of this dissertation.

IIAs will not solely focus on property value protection, but rather integrate the body of international and domestic environmental law instruments and principles, which will become better integrated into investment treaty arbitration.

According to Marisi, there are three solutions to address this issue[171]. The first solution would be to make preambles more precise and stringent, however, we must consider that this could lead to a reduced scope of environmental protection, once it would restrict the possibility of applying environmental safeguards, instead of expanding it. The second solution pointed out by this author is to continue with generic phrasing which, on the other hand, would allow tribunals to make an evolutionary interpretation, while fostering environment protection as well as the shift in treaties interpretation and, therefore the evolution of legal reasoning. Lastly, a third option would be the swirl of environmental language and a language that would address more explicitly specific environmental concerns, such as climate change or biodiversity. Hence, the third solution pointed out by Marisi seems to be the most likely to succeed, considering that *optimal environmental protection may be accomplished by merging environmental preambular language and substantive obligations of environmental safeguarding*[172]. This way, investment and environmental protection can both live as harmonious goals in the preambles of IIAs.

One of the first investment instruments that included environmental language in its preamble is the 1992 NAFTA, which reads:

> The Government of Canada, the Government of the United Mexican States, and the Government of the United States of America resolved to:
>
> (…) UNDERTAKE each of the preceding in a manner consistent with the environmental protection and conservation;
>
> PRESERVE their flexibility to safeguard the public welfare;
>
> PROMOTE sustainable development;
>
> STRENGTHEN the development and enforcement of environmental laws and regulations (…)

[171] Marisi, *Environmental Interests in Investment Arbitration*., 109.
[172] Marisi, *Environmental Interests in Investment Arbitration*., 110.

These preambular provisions were considered in a claim of a NAFTA arbitration under the UNCITRAL arbitration rules, the S*.D. Myers vs Canada*[173] case. In this case, the North American company S.D. Myers whose activity relies on the transportation, processing, and disposal of polychlorinated biphenyl waste, a hazardous chemical substance used for the production of electronics, claimed that Canada's measure to close the border for companies exporting PCB waste was a breach of NAFTA treaty obligations, such as NT and minimum standards of treatment, including FET and protection against expropriation[174]. On its defence, Canada argued that its ban had been issued for environmental reasons stating that "the obligations in NAFTA Chapter Eleven should be interpreted so that they are consistent with international environmental obligations"[175]. When analysing the case, the arbitral panel stated that:

> The Preamble to the NAFTA, the North American Agreement on Environmental Cooperation (NAAEC) and the international agreements affirmed in the NAAEC suggest that specific provisions of the NAFTA should be interpreted in light of the following general principles:
>
> –Parties have the right to establish high levels of environmental protection. They are not obliged to compromise their standards merely to satisfy the political or economic interests of other states;
>
> –Parties should avoid creating distortions to trade;
>
> –Environmental protection and economic development can and should be mutually supportive[176].

This was one of the first ISDS cases where preambular provisions which integrate environmental concerns where considered by the arbitral tribunal when interpreting the content of the IIA at question, which is an important step to a more environmental-aware investment treaty arbitration.

Nevertheless, NAFTA is not the only IIA which contains environmental concerns in its preambular provisions. It is possible to find several different refences to environmental protection in IIAs. Some examples of other IIAs that integrate such clauses are: (1) The

[173] S.D. Myers, Inc. v. Government of Canada, UNCITRAL.
[174] *Id.*, Claimant's Statement of Claim, 30th October 1998, para. 34 et seq,
[175]*Id.*, Respondent's Statement of Defence, 18th June 1999, para. 35.
[176] *Id.*, Partial award, 13th November 2000, para. 220.

United States-Rwanda BIT, where it reads "(…) Recognizing that agreement of the treatment to be accorded in such investment will stimulate the flow of private capital and the economic development of the parties (…) Desiring to achieve these objectives in a manner consistent with the protection (…) of the environment (…)"; (2) the China-Canada BIT, where it states that "(…) recognizing the need to promote investment based on the principles of sustainable development; and, (4) the Brazil-Mozambique BIT, that recognizes "(…) the essential role of investment in the promotion of sustainable development (…)".

Another preamble that embodies a large number of regulatory interests is the Austrian Model BIT, once it expands through references to international instruments, as follows:

> Reaffirming the commitments under the 2006 Ministerial declaration of the UN Economic and Social Council of Full Employment and Decent Work, […]
>
> C. The right to regulate and the preamble 117 Expressing their belief that responsible corporate behaviour, as incorporated in the OECD Guidelines for Multinational Enterprises, can contribute to mutual confidence between enterprises and host countries;
>
> Emphasising the necessity for all governments and civil actors alike to adhere to UN and OECD anti-corruption efforts, most notably the UN Convention against Corruption (2003);
>
> Taking note of the principles of the UN Global Compact;
>
> Acknowledging that investment agreements and multilateral agreements on the protection of environment, human rights or labour rights are meant to foster global sustainable development and that any possible inconsistencies there should be resolved without relaxation of standards of protection'[177].

Nonetheless, two issues are raised about this preamble[178]: (1) it is bent towards regulatory interests and international instruments to the extent that it does not expressly incorporate investment protection on its objectives and; (2) the ultimate quoted recital determine that investment agreements are meant to foster global sustainable development, as it appears to be saying that inconsistencies between investment agreements and multilateral agreements on the protection of the environment (among others), should be resolved in favour of the latter, without relaxation of the standards of protection.

[177] Austrian Model BIT (2008).
[178] Titi, *The Right to Regulate in International Investment Law*., 121.

This trend seems to be followed in more recent Trade agreements. One example is the 2022 FTA signed between New Zealand and the United Kingdom states which, in its chapter related to investment, states that:

> The objective of this Chapter is to encourage and promote the flow of investment between each Party on a mutually advantageous basis, under conditions of transparency within a stable framework of rules to ensure the protection and security of investments by investors of the other Party within each Party's territory, while recognising the right of each Party to regulate in order to achieve legitimate public policy objectives, such as the protection of public health, safety, and the environment.[179]

This being said, it is possible to state that, considering all the problems that have been pointed out during this dissertation, it is expected that future IIAs include preambles that expressly mention the host state's right to regulate in order to achieve, among other, the protection of the environment without compromising other treaty obligations.

One of the advantages of using this mechanism is that it allows to still follow the usual structure of traditional IIAs while granting wider protection to the state's right to regulate as an interpretative scope that extends to the entire treaty. One of the possible downsides is that including regulatory interests exclusively in the preamble creates no concrete or legally enforceable right to regulate, but a mere interpretative device. All in all, incorporating regulatory interests in the preamble may contribute to a more balanced interpretation of International Investment Treaties, one that considers the state's regulatory interests while also protecting investors' interests.

3.3.Carve-Out Clauses

Carve-out clauses can be defined as treaty provisions by which the parties exclude certain claims or remedies from their arbitration clause. By making use of this mechanism, host states can effectively restrict substantive treaty obligations' applicability. [180]The rationale of the use of this treaty device lies on the premise that investment treaties and investment treaty arbitration therein originate the consent of states to the international agreement as to the exercise of their sovereignty. As a result of this sovereign act as a "legal representative" of its citizens, each party is subject to disciplines

[179] Free Trade Agreement between the United Kingdom of Great Britain and Northern Ireland and New Zealand (2022 – signed but not yet in force).
[180] Marisi, *Environmental Interests in Investment Arbitration*., 112.

in the treaty, as international commitments even when exercising its sovereign right to regulate business and their activities. In this sense, the consent of a state to investment treaties as a sovereign act[181] involves some surrender of domestic sovereignty to international obligations.

Therefore, to avoid regulatory concerns in certain areas, such as environmental law, states may have to carve-out these areas involving their vital regulatory concerns from the scope of international obligations in advance of the exercise of their sovereign choice. Based on this rationale, these clauses can attain the legal certainty that international investment treaties were lacking, for predictability is a crucial attribute to the substantive reform of investment treaty policy, on the part of both host states and foreign investors. In this way, carve-out clauses have the power to explicitly cut out environmental measures form their commitment to investment disciplines when negotiating, and therefore, as Ahn points out, results in host states not needing to cringe for fear of investors' claims when they take regulatory action which are considered to fall within the scope of said carve-out.[182] This being said, if the carve-out is phrased in a clear way, the likelihood of confusion as to the scope of the investment treaty would be low, therefore both investors and host states will have certainty on their mutual rights and obligations[183].

If states desire to avoid regulatory concerns in certain areas while also protecting investors from abuse of powers and securing the possibility to legislate *bona fide*, it is imperial to draw the line between the two different behaviours, which is attainable through the use of carve-out clauses.[184] This way states can select a certain subject, in this case environmental regulation, without incurring in a duty to compensate the investor.

On the other hand, these clauses can also provide foreign investors with a cost-effective and simple guideline as to the scope of investor protection to which they are

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[181] About this issue see chapter 1.4. of this dissertation, where the rationale behind the direct access to investment treaty arbitration that is granted to foreign investors in investment treaties.

[182] Ahn, 'The Utility of Carve-out Clauses in Addressing Regulatory Concerns in Investment Treaty Arbitration', 65–76., 70.

[183] Ahn, 'The Utility of Carve-out Clauses in Addressing Regulatory Concerns in Investment Treaty Arbitration', 65–76., 74.

[184] Ahn, 'The Utility of Carve-out Clauses in Addressing Regulatory Concerns in Investment Treaty Arbitration', 65–76., 71.

entitled. In other words, foreign investors would not anticipate asserting their right to protection if they decided to invest in an area carved out after an investment treaty.

Taejoon Ahn adds that the carve-out system conforms also to political acceptability because it can become a political inducement to a state party which resists the conclusion of an investment treaty due to the concern over a specific regulatory area as well as the other party which is willing to concede the carve-out of the specific area in exchange for subjecting the resisting party to other investment disciplines.

One classic example of a carve-out clause is the one included in Article 3(2) of the 2005 China-Madagascar BIT. It expressly excludes measures dealing with issues of security, public order, public health and ethics and environmental protection from the scope of the BIT, as follows:

> Legal or de facto obstacles to the fair and equitable treatment mainly mean, but not limited to: non-equitable treatment of all kinds of restrictions on the means of production and management, non-equitable treatment of all kinds of restrictions on sale of products at home and abroad, as well as other measures with similar effect. But measures for reasons of security, public order, health, ethical and environmental protection and other reasons, these measures shall not be regarded as obstacles[185].

A more recent example is the Hong Kong-ASEAN FTA, which includes a carve-out in its Expropriation and Compensation Section, which states:

> Non-discriminatory regulatory actions by a Party that are designed and applied to achieve legitimate public welfare objectives, such as the protection of public health, safety, and the environment, do not constitute expropriation of the type referred to in subparagraph 2 (b)[186].

With the inclusion of this clause, it becomes unlikely that non-discriminatory state's measures aimed at protecting the environment are considered compensable expropriation. However, as Marisi[187] notes, although this is a very advanced example of treaty drafting, it is possible to argue that it constitutes a specific carve-out to the expropriation provisions, and not a carve-out from the scope of the treaty in its whole.

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[185] Agreement Between the Government of the People's Republic of China and the Government of the Republic of Madagascar for the Reciprocal Promotion and Protection of Investments (2005).

[186] Agreement on Investment among the Governments of the Hong Kong Special Administrative Region of the People's Republic of China and the Member States of the ASEAN (2017).

[187] Marisi, *Environmental Interests in Investment Arbitration*., 116.

To sum up, it is possible to say that even considering the arguments against the inclusion of carve-out clauses in investment treaties, they are expected to be adopted by the new version of investment treaties as an effective instrument for alleviating regulatory concerns in terms of legal certainty, predictability, and political acceptability.

3.4. The Role of General Exceptions in International Investment Treaties

According to Andrew Newcombe[188], a growing number of IIAs include general exceptions, which is understandable once they provide a general exemption for regulatory measures that might be found to breach IIAs' obligations. For this author, the inclusion of general exceptions in future IIAs is one potential response to the general concern that lies on the fact that IIA's obligations are too broad. In fact, the power of general exceptions is that they create a protected environment in which states are given regulatory space for the state to implement a broad range of measures to address unknown future harms to the public welfare while also justifying existing regulatory measures.

This being said, according to Sabanogullari[189] the rationales for including general exception clauses in IIAs are twofold. On one hand, these clauses are meant to enhance regulatory flexibility, which allows host states to regulate foreign investment without incurring in international liability for their actions. Nevertheless, the degree of this flexibility would always depend on how the investment tribunals interpret the clause. On the other hand, general exceptions are intended to increase legal certainty in investment adjudication, which would solve the above-mentioned problem related to the lack of predictability and certainty in the investment regime, by offering express points of reference to which public interest considerations may be attached.

Nonetheless, although general exceptions may appear to offer an innovative solution to legitimacy and sustainability concerns regarding the scope of foreign investors' rights under investment treaties, there is significant uncertainty about how these clauses will be applied in the context of international investment law, considering that they are drawn from international trade treaties. In light of that interpretative uncertainty, the inclusion

[188] Andrew Newcombe, 'The Use of General Exceptions in IIAs: Increasing Legitimacy or Uncertainty?', in *Improving International Investment Agreements*, ed. by Armand De Mestral and Céline Lévesque, Routledge Research in International Economic Law (London, 2013), 267–83., at 268 et seq.

[189] Levent Sabanogullari, 'The Merits and Limitations of General Exception Clauses in Contemporary Investment Treaty Practice', *Investment Treaty News*, 2015 <https://www.iisd.org/itn/en/2015/05/21/the-merits-and-limitations-of-general-exception-clauses-in-contemporary-investment-treaty-practice/>.

of general exceptions in investment instruments does not provide a particular helpful guidance to treaty interpreters and arbitrators in determining how to balance the public right to regulate and the protection of investors' rights[190].

Until now, for these and other reasons, general exceptions are not popular as a treaty mechanism in international investment law, in fact, a 2011 study has highlighted that only 8% or around 82 of a sample of 1623 IIAs had such clause with reference to environmental values, and 30 out of them were built on Article XX GATT or GATS, Article XIV[191], which respectively state that:

> Article XX General Exceptions
>
> Subject to the requirement that such measures are not applied in a manner which would constitute a means of arbitrary or unjustifiable discrimination between countries where the same conditions prevail, or a disguised restriction on international trade, nothing in this Agreement shall be construed to prevent the adoption or enforcement by any contracting party of measures:
>
> …
>
> (b) necessary to protect human, animal or plant life or health;
>
> …
>
> (g) relating to the conservation of exhaustible natural resources if such measures are made effective in conjunction with restrictions on domestic production or consumption.
>
> GATS, Article XIV General Exceptions
>
> Subject to the requirement that such measures are not applied in a manner which would constitute a means of arbitrary or unjustifiable discrimination between countries where like conditions prevail, or a disguised restriction on trade in services, nothing in this Agreement shall be construed to prevent the adoption or enforcement by any Member of measures:
>
> …
>
> (b) necessary to protect human, animal or plant life or health;

[190] Newcombe, 'The Use of General Exceptions in IIAs: Increasing Legitimacy or Uncertainty?', 267–83., 268.

[191] Kathryn Gordon and Joachim Pohl, 'Environmental Concerns in International Investment Agreements: A Survey', *OECD Working Papers on International Investment*, OECD Investment Division, 2011/1, 2011.

Analysing these articles, it is possible to conclude that it appears that unlike GATT Article XX, no exception regarding the conservation of natural resources is included in GATS Article XIV.

This approach conditions the exception by the satisfaction of previous determined criteria intended to avoid any kind of abusive exploration. Nevertheless, this wording coerces the host state to ensure that the application of otherwise non-conforming measures does not engender arbitrary or unjustifiable discrimination while also preventing its use as a dissimulated investment limitation[192].

For one, Canada signed a variety of BITs including general exceptions, the first of them being the Canada-Ukraine 1994 BIT, which established under its Article XVII:

> Application and General Exceptions
>
> (1) This Agreement shall apply to any investment made by an investor of one Contracting Party in the territory of the other Contracting Party before or after the entry into force of this Agreement.
>
> (2) 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.
>
> (3) Provided that such measures are not applied in an arbitrary or unjustifiable manner, or do not constitute a disguised restriction on international trade or investment, nothing in this Agreement shall be construed to prevent a Contracting Party from adopting or maintaining measures, including environmental 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.[193]

Although general exceptions in BITs other than Canadian Foreign Investment Protection Agreements are extremely rare, they have begun to appear more frequently in

[192] Marisi, *Environmental Interests in Investment Arbitration*., 121
[193] Article XVII of the 1994 Canada-Ukraine BIT

comprehensive bilateral FTAs, particularly those celebrated between Asian States[194].Not regardless, as Newcombe[195] states, although the inclusion of general exceptions remains some-what limited, three points can be made regarding treaty practice: (1) Although there are differences between the drafting of the various exceptions, the basic structure of general exception clauses is based on Article XX GATT; (2)A number of states that have included general exceptions in their IIAs have inconsistent IIA treaty practice. Some of their IIAs contain general exceptions and others do not, which can lead to significant interpretative uncertainty and; (3) Some general exception clauses incorporate GATS Article XVI's exact formulation.

One risk with the use of general exceptions is that, since they provide a closed list of legitimate policy objectives, their inclusions might have the consequence of limiting the range of objectives available to the state. Additionally, further interpretative questions arise with respect to the interaction between general exceptions and specific investment obligations, especially with consideration to the NT, minimum standard of treatment and expropriation obligations in IIAs. In fact, the problem of applying exceptions to minimum standards of treatment is symptomatic of the difficulty of transplanting a clause from a trade treaty into an investment protection treaty with a different purpose and legal structure. This is understandable once the trade-in-goods regimes seeks to discipline protectionist measures and ensure that states do not cheat on their tariff bargains. It uses state-to-state dispute settlement, the aim of which is for the state to bring its measures into compliance with its trade obligations and also does not provide compensation to the trader who has lost sales as a result of inconsistent trade measures[196].

On the other hand, it is known as a consensual general rule that the role of IIAs is to promote and protect investment which means that allowed justifications of the host state regulatory measures breaching other investment treaty obligations are only exceptional. Keeping this in mind, we conclude that even though general exceptions can be used as a tool for states to clarify their willingness to maintain their right to regulate certain matters,

[194] Some examples are the Japan-Singapore FTA and the Comprehensive Economic Cooperation Agreement between the Republic of India and the Republic of Singapore.

[195] Newcombe, 'The Use of General Exceptions in IIAs: Increasing Legitimacy or Uncertainty?', 267–83., 275-276.

[196] Newcombe, 'The Use of General Exceptions in IIAs: Increasing Legitimacy or Uncertainty?', 267–83., 277.

such as environmental concerns, it is yet to be proven that this can be accomplished by articles on general exceptions in international investment treaties.

3.5. Procedural provisions

Traditionally, IIAs, including Investment Treaties, do not include comprehensive and detailed procedural provisions.[197] Normally procedural issues are left to be decided in accordance with the applicable arbitration laws and rules, or even pursuant to the arbitrator's discretionary decisions, when stipulated by the parties. However, as Chi points out, some procedural provisions can be closely connected to sustainable development.

This author points out the following typical provisions, which we will analyse in a non-exhausting manner (full books are written about this topic, which, although important to our dissertation, is not the main subject of study):

a) Restrictive Compromissory Clauses

As we have mentioned in chapter 1.4. a typical feature of modern investment treaties is that foreign investors and almost always granted direct access to arbitration against host states when a treaty obligation is breached. In the particular case of investment treaty arbitration, the compromissory clause plays a critical role in preserving the state's right to regulate once the arbitral jurisdiction is based on and limited to the compromissory provisions of the applicable IIA.

This being said, it is possible to point out two opposing modes of comprmissory clauses[198]: (1) restrictive compromissorys expressly limit the types of disputes that can be submitted to arbitration - One fair example of such clauses is Article 24(1) of the already mentioned 2012 United States Modle BIT, which reads that an investor may submit *An investment dispute" against the respondent state under Articles 3 through 10. These Articles only relate to investment protection and treatment, but do not include sustain able development, such as the provisions of "investment and labor" (Article 13), "investment and environment" (Article 12) and "transparency" (Article 11)*.Considering

[197] Manjiao Chi, *Integrating Sustainable Development in International Investment Law: Normative Incompatibility, System Integration and Governance Implications*, Routledge Global Cooperation Series (London New York, NY, 2018)., 115.

[198] Chi, *Integrating Sustainable Development in International Investment Law: Normative Incompatibility, System Integration and Governance Implications*.,116.

this clause and keeping in mind that this Model BIT has explicitly incorporated a number of sustainable development provisions, it is possible to conclude that a restrictive compromissory clause can, in fact, help the contracting parties in preserving regulatory power, especially in the field of environmental law.

Secondly, we have open compromissory clauses employ general and broad term with regard to the admissibility of disputes to arbitration.

These clauses can be found the Chinese IIAs[199] and normally are articulated with plain language that does not impose any restriction on the character of the dispute. Nevertheless, they are generally accompanied by certain requirements which, if not restricted b other applicable provisions of the IIA, would allow foreign investors to submit any kind of dispute to arbitration.

This being said, and as Chi[200] concludes, although compromissory clauses alone do not serve environmental concerns in a rather direct way, they may play a very helpful part in the preservation of the state's regulatory power by limiting the access of foreign investors to arbitration.

b) Transparency Provisions

It is known that arbitration is considered a confidential dispute settlement mechanisms between private parties. When this concept is applied to ISDS it is understandable that some concerns are raised once the pursuance of the public interest should be the state's main concern and its action should be publicly analysed.

Taking this issue at heart, the 2006 amendment to the ICSID Arbitration Rules incorporated several procedural innovations in three different aspects: (1) the opening of hearings (2) the publications of awards and; (3) the admission of *amicus* briefings.

[199] E.g., the China-Japan-Korea Trilateral Investment Treaty
[200] Chi, *Integrating Sustainable Development in International Investment Law: Normative Incompatibility, System Integration and Governance Implications*., 17.

In general, it is possible to state that this amendments represent a right step in the path of responding to these transparency issues raised by some critics. In fact, an increasing number of IIAs incorporate transparency provisions of various types[201].

c) Non-Disputing party (*amicus curiae*) participation in investment arbitration

The participation of non-disputing parties in arbitration has been welcomed since the 1990s and rises to continue to be used as non-state actors gain more influence in the international arena.[202]

The *amicus curiae* participation comes with both advantages and disadvantages: On one hand their participation might help protect public interests that, sometimes, are overlooked in investment arbitration, such as environmental concerns. This is due to the fact that their participation (1) protects the public interest; (2) enhances the arbitration's transparency; (3) improves the quality of the award and (3) engages public scrutiny of the adjudication. On the other hand, their participation is known to cause (1) delays in the process; (2) an increase of costs. Other critics against this mechanism it that some consider it to disregard the parties consent and interfere with their strategies.[203]

Regardless these critics, the use of participating amicus curiae in investment arbitration is becoming a fixture in cases involving important public policy considerations. In fact, arbitrators are authorized by various IIAs and arbitration rules to determine whether and how this mechanism can be allowed.[204]

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[201] Chi, *Integrating Sustainable Development in International Investment Law: Normative Incompatibility, System Integration and Governance Implications*., 124.

[202] Chi, *Integrating Sustainable Development in International Investment Law: Normative Incompatibility, System Integration and Governance Implications*.,127.

[203] Eugenia Levine, 'Amicus Curiae in International Investment Arbitration: The Implications of an Increase in Third-Party Participation', *Berkeley Journal of International Law*, 29 (2011), 200–224.

[204] Chi, *Integrating Sustainable Development in International Investment Law: Normative Incompatibility, System Integration and Governance Implications*., 125.

III. CONNECTING THE DOTS: CHALLENGES, REFLECTIONS AND DIRECTIONS

4. Connecting the Dots

International Investment law and the current investor-state dispute settlement system are going through a legitimacy crisis. As we have had the opportunity to expose during this dissertation a wide range of critics have been formulated towards both the international investment treaties' legal framework and the adopted ISDS.[205]

This can be explained by the fact that integrating the protection of the environment, a non-commercial objective, into investment treaties can be proven to be a challenge given the risky balance there is between the public and private interests. In fact, as Chi states, even though investors and host states are both involved in the same investment transaction, they do not necessarily share the same objectives. These different is more evident in disputes that touch upon non-commercial objectives such as environmental issues.[206]

The previous Chapters paved an overview of the complex interaction between the protection of the environment and the protection of foreign investment. This chapter seeks to connect the dots between the attempts to reconcile the two balancing interests. At the same time, some reflections on the challenges that lie ahead and the directions to be followed will be explored. All in all, at the beginning of this dissertation we raised the question: is international investment treaty arbitration appropriate for resolving environmental disputes? Now, all things considered, we will try to answer it.

As we have had the opportunity to explore, a reform of the investment protection regime has been called for quite some time now. The existing proposals for ISDS reform primarily take a normative perspective, focusing on the design of treaty provisions that can either preserve state regulatory power or limit the foreign investor's access to ISDS in certain matters.[207] Despite the merit of these suggestions, considering the challenge that comes with the adoption of standard environmental principles by all international

[205] About this issue, see chapter 3

[206] Chi, *Integrating Sustainable Development in International Investment Law: Normative Incompatibility, System Integration and Governance Implications*., 156.

[207] Chi, *Integrating Sustainable Development in International Investment Law: Normative Incompatibility, System Integration and Governance Implications*., 161.

players, others could be pointed out. Among these are the application of environmental norms and the use of treaty mechanisms to enhance the regulatory space given to states.

4.1. The adoption of Environmental Norms in International Investment Treaties

Environmental law is one of the fields that, as we have had the opportunity to explore in chapter 2, is giving rise to several principles, such as the polluter pays principle, the principle of prevention and the precautionary principle.

These principles were agreed on by the parties to the 1992 Rio Conference and have been invoked by parties in arbitral cases or at least mentioned by the competent arbitral tribunals. However, as we have highlighted in chapter 2, although well intentioned, these principles are of abstract nature and therefore do not have a binding nature.

In fact, if we reflect upon their applicability in case law, it is possible to recognize that this indeterminate nature of environmental principles can leave space to the absence of enforcing mechanisms which is the reason that leads us to believe that their inclusion in substantive provisions might be one of the solutions to maintain their normative effect.[208]

Nevertheless, if practice favouring the integration of environmental principles and norms spread, it would be possible to create an investment dispute regime where environmental domestic measures would not need to succumb in front of conflicting provisions included in investment treaties, such as the standards of protection of foreign investors and their investments. On this note, Chi stated that:

> IIAs are the primary source of norms for the regime of global investment governance. IIAs' norms not only stand for a series of commitments by the host states to foreign investors, but also form the primary source of law to be applied in settling investment disputes. Without a sufficient norm supply from IIAs, an effective global investment governance regime can hardly be imagined.[209]

This being said, similar to what happens to the standards of protection of investment[210], if investment treaties stipulated minimum environmental standards to be followed by

[208] Marisi, *Environmental Interests in Investment Arbitration*., 101.
[209] Chi, *Integrating Sustainable Development in International Investment Law: Normative Incompatibility, System Integration and Governance Implications*..161-162.
[210] About this topic see chapter 1.3.

investors upon the installation of their investment, maybe international investment arbitration could become a mechanism able to enforce environmental norms.

To conclude, it is possible to state that one of the directions to be followed in order to get to an international investment arbitration regime capable to dispute environmental concerns is through a comprehensive international investment norm-making reform.[211]

4.2. Balancing public and private interests

As we have explored in chapter 3 of this dissertation, treaty mechanisms can have a great impact on the regulatory power that is given to states in the context of international investment treaty arbitration.

This is important considering that with more regulatory space comes less fear of investors' claims for compensation when environmental measures that affect their investment are implemented by the host state.
Doubtlessly, investment treaties' design has significantly changed with the turn of the century and the right to regulate has been included in some of them. In fact, an increasing number of investment treaties now include sustainable development provisions, aimed at leaving more regulatory space to host states to pursue their environmental protection objectives.

While acknowledging that investment treaties should primarily aim at protecting foreign investment, it is advisable that they are also compatible with balancing provisions. Thus, we can conclude that the first step to enhance this compatibility between environmental concerns and investment treaty arbitration would be to adopt environmentally aware clauses in investment treaties. The right and duty of the state to protect the environment without exposing itself to liability towards investors can, in fact, be based in treaty mechanisms such as (1) preambular provisions including reference to environmental protection; (2) carve-out clauses excluding states' measures in determinate sectors from the scope of the treaty aims at achieving sustainable development; (3) general expectations and; (4) procedural provisions providing investment arbitral tribunals with procedural guidelines and rules connected with

[211] Chi, *Integrating Sustainable Development in International Investment Law: Normative Incompatibility, System Integration and Governance Implications*., 182.

Starting with preambular provisions, as we have seen[212], although not being a part of the treaty provisions, explain its objectives and purposes which allows more on the balancing of the different values of environmental and investment protection. Carve-out clauses, on the other hand, provide states with the possibility to select certain matters, such as environmental and sustainable development issues, and carve them out from being subject to investment arbitration, in this way reducing the scope of their own international commitments.

A third way for states to reflect their intent to expand their regulatory flexibility pursuant to public interest goals would be to negotiate the inclusion of general exceptions. However, from our point of view this last solution is the least likely to be effective because: (1) of the degree of the regulatory flexibility granted to the host state would always depend on the arbitral tribunal's interpretation; (2) There is still a significant level of uncertainty about how these clauses would be applied in the context of international investment disputes once they are drawn from international trade treaties. In fact, this becomes a wider problem once they do not provide a particular helpful guidance to arbitrators in determining how to balance the public right to regulate and the minimum investment protection standards. (3) by providing a closed list of legitimate policy objectives it can result in the limiting of the range of objectives available to the state.

Lastly, procedural provisions can also have a great impact in this tricky balance once they can influence the dispute settlement proceedings while also influencing the realization of sustainable development goals. Theses clauses can take form of (1) restrictive compromissory clauses (2) transparency provisions and (3) non-disputing party. Restrictive compromissory, despite not serving environmental concerns directly, preserve the state's regulatory power and are helpful to the extent that they expressly limit the types of disputes that can be submitted to arbitration[213].

Transparency clauses that implement measures such as the opening of hearings, the publication of awards and the admission of amicus briefings also come in handy in responding to concerns that are raised regarding the pursuance of the public interest in investment arbitration. Also, regarding the pursuance of the public interest the

[212] See Chapter 3.2.
[213] See chapter 3.5

participation of non-disputing parties in environmental disputes in investment arbitration is also one useful mechanism. In fact, transparency promises a more accountable, more democratic, and more legitimate ISDS.

This being said, it is our opinion that, as far as environmental concerned treaty mechanisms go, the inclusion of environmental aware preambular provisions, carve-out clauses and clean-cut procedural clauses are more likely to be a direction to be followed in order to reach a more balanced ISDS.

4.3. Is international investment treaty arbitration an appropriate forum for resolving environmental disputes?

At the beginning of this dissertation, we proposed to answer the following question: is international investment treaty arbitration an appropriate for resolving environmental disputes?

FDI has proven to allow the transfer of technology, particularly in the form of new varieties of capital inputs that cannot be achieved through financial investments or trade in goods and services which is why it is important to create a system that promotes it. As we have seen in chapter 1.4 the rationale of the direct access that is granted to foreign investors to investment treaty arbitration lies under the idea that this mechanism is more attractive and secure to investors once it ensures that there will be a place to enforce their rights in case a dispute rises.

Many of the 3000 + international investment treaties up to date allow investors to take host state's to international arbitral tribunals, where the decisions are binding and enforceable within and beyond state boundaries[214]. This being said, we can conclude that, in fact, arbitration is the most effective ISDS system.[215] However, despite the success of investment arbitration on said protection of investors and their investment against host states arbitrary actions and policies, as we have had the opportunity to see throughout this dissertation, some scholars have argued that not enough attention has been dedicated to environmental interests.

[214] Lorenzo Cotula, 'Investment Treaties and Sustainable Development: An Overview', *International Institute for Environment and Development*, 2014 <http://www.jstor.org/stable/resrep01583.> [accessed 10 June 2022].

[215] See chapter 1.4.

In fact, the first-generation international investment treaties solely focused on the protection of investment and did not leave much room to specially dedicated policy space, showing, as Marisi points out, *that the attainment of regulatory interests in certain areas such as environmental protection had been limited in order to encourage outflow and inflow of FDI.*[216]On this note, some scholars have pointed out that investment treaties might give rise to a certain degree of regulatory chill once host states are likely to fear that new environmental measures might trigger an arbitration claim by the foreign investor.

Maybe for that reason some states such as Bolivia, Ecuador and Venezuela denounced the ICSID Convention, and a number of other states have terminated a number of first-generation BITs. Nevertheless, what we see in this new generation of international investment treaties is a more environmentally aware policy by which certain treaty mechanisms, such as preambular provisions, carve-outs, general exceptions, and procedural clauses reinforce the states' sovereign right to regulate in certain areas, such as sustainable development.

In fact, according to the 2017 World Investment Report, under the title "Investment and the digital economy"[217], modern IIAs include sustainable development-oriented reform elements that simultaneously preserve the right to regulate and maintain investment protection, foster responsible investment, and improve dispute settlement. More recently, the 2021 Report concludes that all IIAs concluded in 2020 contain reform-oriented provisions aimed at preserving regulatory space and promoting sustainable investment[218].

This being said, it is our opinion that investment arbitration is an appropriate forum to solve disputes in which environmental concerns are raised, although it needs some tailoring. Firstly, as suggested in chapter 4.1., one of the directions passes by a comprehensive international investment norm-making reform where environmental principles start to be stipulated in investment treaties. A second suggestion would be to

[216] Marisi, *Environmental Interests in Investment Arbitration*., 284.

[217] UNCTAD, ed., *Investment and the Digital Economy*, World Investment Report, 2017 (New York Geneva, 2017).

[218] UNCTAD, 'Recent Developments in the IIA Regime: Accelerating IIA Reform', *IIA Issues Note*, 3, 2021.

include more balancing provisions like the ones included the chapters 3.2, 3.3, and 3.5 of this dissertation. This would mean that when there was a conflict between investors' rights and the protection of the environment, the latter would not have to succumb

All in all, the results of our research conclude that new-generation investment treaties are taking the right step into an international investment treaty arbitration regime that is able to effectively dispute environmental concerns.

CONCLUDING REMARKS

This research aimed at exploring the relationship between international investment treaty arbitration and environmental protection, once we consider that FDI and environmental law are the two components of states' sustainable growth, development, and prosperity. For that reason, at the begging of this dissertation, we raised the question: is international investment treaty arbitration an appropriate forum to settle environmental disputes?

We have concluded that the main problem at stake is the risky and tricky balance between the state's sovereign right to regulate and the protection and promotion of investment. However, we find that environmental policies enacted by host states and the protection of investments can live peacefully in the international arena. As follows:

In part I of this dissertation we opened the debate with the explanation of the theoretical framework regarding international investment treaty law and international environmental law. We have concluded that, throughout the years, investment protection has been in the centre of investment policies, as minimum standards of protection of investments have been included in first-generation investment treaties and have become a part of CIL.

On the other hand, regarding environmental law, we have reached the conclusion that its instruments only take part in soft international law and therefore principles and regulations made in an attempt to redeem environmental concerns do not possess a binding nature to the international players.

Additionally, we note that international investment treaties (at least the first-generation ones) often do not contain environmentally sensitive clauses binding investors to act in a more environmentally friendly manner.

For this reason, in part II we analysed the possible solutions to the 'regulatory chill' experienced regarding environmental concerns. We have concluded that there are some treaty mechanisms, such as preambular provisions, carve-out clauses, general exceptions, and procedural provisions that might come in handy when the state desires to regulate environment-related matters.

In part III, taking this into consideration, and answering the question we proposed at the beginning of this dissertation, we have concluded that international investment treaty arbitration can be an appropriate forum to dispute environmental concerns, although we recognize that it is time for reform. Our suggestions for this reform are twofold:

(1) On the one hand, we believe that one of the directions to be followed in order to get to an international investment arbitration regime capable to dispute environmental concerns is through a comprehensive international investment norm-making reform where environmental principles and norms would become a part of international investment treaties' provisions.

(2) On the other hand, we advocate that next-generation investment treaties urgently need to include mechanisms which comply with the states' right to regulate their own environmental measures. As we have seen, these can come in different shapes and sizes, with preambular provisions, carve-out clauses and procedural provisions being more likely to succeed than others such as general exceptions.

We conclude that, although investment treaty arbitration is not a perfect system, taking into consideration the above-mentioned suggestions, it is the best system, to date, to effectively respond to the needs of both investors and host states in balancing their interests.

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