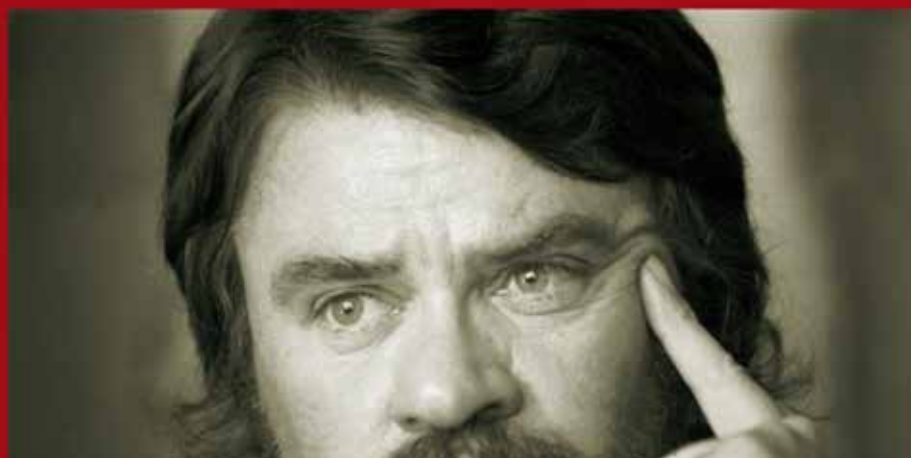


# HOMENAJE A FERNANDO DE TRAZEGNIES GRANDA

TOMO III



## Capítulo 66

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*Homenaje a Fernando de Trazegnies Granda*

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# COMMENTS ON THE DISCIPLINE OF «NATIONAL TREATMENT» IN INTERNATIONAL INVESTMENT LAW: BOOSTING GOOD GOVERNANCE VERSUS INTRUDING INTO DOMESTIC REGULATORY SPACE?

*Thomas Wälde* (†)

## INTRODUCTION<sup>1</sup>

National treatment —that foreign traders and investors should not be treated worse than local businesses— is one of the oldest principles in international economic law, next to only the rule that you can not take foreign property without compensation. It is as old and venerable as it proves difficult to define and apply

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Este artículo reúne una serie de presentaciones del autor en la conferencia internacional de arbitraje organizada por Lord Mustill en St John's College, Cambridge, 2004 y en la conferencia de Derecho de la Organización Mundial de Comercio (WTO), realizada en la universidad de Bar Ilan en Tel Aviv, en diciembre de 2004. También hace referencia de manera particular a un artículo de Jürgen Kurtz que será publicado como parte del seminario de investigación de la Academia del Derecho Internacional de La Haya llevado a cabo en el 2004 (en el cual Thomas Wälde dirigió las sesiones de habla inglesa). También incorpora reflexiones del autor desarrolladas en el contexto del trabajo individual o conjunto con respecto a su rol de árbitro, consultor experto y asesor de varios casos recientes de arbitraje.

El presente trabajo no pretende ser un estudio exhaustivo sobre el principio de tratamiento nacional para litigios de inversión, sino más bien comentar algunos casos recientes, en especial la cuestión de analogía con la legislación de la WTO y la manera en la que la discriminación ha sido y debe ser entendida en un caso de conducta administrativa.

<sup>1</sup> This paper complements a series of related studies of mine on international investment Law: Forthcoming; *International Investment Law: Key Issues; Report of the 2004 Research Seminar on International Investment Law*, Hague Academy of International Law, forthcoming, 2006; *Remedies and Compensation in International Investment Law, report to the ILA Committee on International Law of Foreign Investment; Contract Claims under the Energy Charter Treaty's Umbrella Clause: Original Intentions versus Emerging Jurisprudence*, ICSID-Journal (forthcoming, 2006); already published: 2004a, 2004b, 2004c, 2005a and 2005b.

in the modern practice of international economic law. This essay focuses on the legal scope of the national treatment principle in international investment law, mainly as it is formulated in international (bilateral and multilateral) investment treaties and in particular as it is slowly emerging in recent, law-applying and law-making, jurisprudence of arbitral tribunals set up for direct investor-state arbitration under modern investment treaties. The issue is the scope of the national treatment obligation in the context of protection of existing investments. There have been a number of awards over the last 5 years which have started to grapple with the contours of this key principle and «discipline» —claim or cause of action— in such treaties. While these awards do not as yet constitute an established jurisprudence, certain issues, arguments and directions are already emerging. This essay is intended to provide a conceptual and theoretical underpinning for analyzing this emerging jurisprudence, an analysis of these recent cases and an effort to define the current state of play, together with some suggestions as to how the principle of national treatment will, and should, evolve in the near future. This essay will in particular pay attention to efforts to specify the quite open-ended formulations on national treatment with respect to analogies with other areas of international economic law, in particular the extensive jurisprudence from within the WTO dispute resolution process. Some of the conclusions can only be tentative as we are rather in an initial phase than at the end of mature case law. Investment law now evolves both on its own on the basis of an increasing number of cases, but also in close interaction with other areas of international law, primarily international trade, but also human rights and economic integration law<sup>2</sup>. While academic reflection has its place, it can not be equal to the in-depth testing of facts and law that takes place in the charged litigation dynamics of an actual high-value complex investment arbitration<sup>3</sup>.

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<sup>2</sup> Pauwelyn (2003).

<sup>3</sup> Cases are referred by the name of parties; if available from an internet site, no further citation will be done. The sites for investment claims are at present: [www.naftaclaims.com](http://www.naftaclaims.com); [www.investmentclaims.com](http://www.investmentclaims.com); [www.transnational-dispute-management.com](http://www.transnational-dispute-management.com); [www.worldbank.org/icsid](http://www.worldbank.org/icsid); <http://ita.law.uvic.ca/>; for back-up on other references see the extensive bibliography prepared by the international law library of the Peace Palace in The Hague for the seminar, available at: <http://www.ppl.nl/bibliographies/all/?bibliography=investment>

TDM means [www.transnational-dispute-management.com](http://www.transnational-dispute-management.com); OGEL means: [www.gasandoil.com/ogel/](http://www.gasandoil.com/ogel/); *JWIT* means *Journal of World Investment and Trade*; *ICSID-Journal* means: *ICSID Journal/Foreign Investment Law Review*. The main books so far are: WEILER (editor), 2004 and 2005; BROWER & J. BRUESCHKE, 1998; PAULSSON 2004; GAILLARD, 2004; SORNARAJAH, 2004; see also the representative surveys by UNCTAD on specific areas of investment law, e.g. 2003, 2004; HORN & KROLL (ed.), 2004; MANCIAUX, 2004; SCHREUER, 2001; BISHOP, CRAWFORD & REISMAN, 2005. Investment dispute issues are continuously discussed, with posting of commentary and information on OGEMID, my internet discussion forum linked to TDM.

## 1. A HISTORICAL PRIMER

National treatment —equality between foreign and domestic businesses— is recorded in treaties of the Hanseatic league with the kings of England<sup>4</sup> in the high middle ages, but one would suspect that the principle can be identified in the first treaties between the first formal states thousands of years earlier in the Middle East. Such treaties were, in today's sense, both investment and trade treaties as such distinction is relatively recent<sup>5</sup>. The principle can be identified in formal trade treaties of the past centuries. It is disputed if non-discrimination is an established principle of customary international law<sup>6</sup>. Advocates of trade liberalization have always argued in favour; opponents of trade liberalization and followers of statist, nationalist and Communist thinking have always been in favour of «sovereignty» rather than international law rules reducing unfettered discretion of the rulers of states. Defensive attitudes —and that includes developing countries in fear of being exposed to strong outside economic influences, but also forces in all countries threatened by developments in the international economy and in particular in times of economic crisis— will always insist on prerogatives to favour domestic interests, «infant» industry arguments for some, industries in decline arguments for others. Those who rule states —in particular poor, badly governed and declining economies— will be compelled by political and self-interested financial logic to set themselves up as a necessary channel through which foreign commerce has to pass and for which foreign commerce has to pay a «political rent». An international law discipline of non-discrimination is by its nature an impediment to the interest of national rulers to seek political and direct financial «rent» out of the control over barriers between the domestic and global economy and to seek gain out of bargaining with foreign traders and investors for access to and operation in a national economy.

National treatment is the corner stone of all international regimes setting up external, legally, politically and economically enforceable disciplines over national economic policies in order to mobilize the wealth-creating forces of economic integration by trade and investment. It is therefore the key pillar of the WTO regimes —though here at least traditionally focused on tariff equality, an issue

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<sup>4</sup> ERLER (1956: 46-47).

<sup>5</sup> The distinction may also be on the wane again as there might be a tendency towards wider and more integrated economic cooperation agreements. See UNCTAD, press release of 30 August 2005, on TDM 2005. It is noteworthy that the main multilateral treaties —Energy Charter Treaty and NAFTA— are both trade and investment treaties (with elements of competition, transit and environmental law as well).

<sup>6</sup> SORNARAJAH (2004: 318 ff); UNCTAD (1999: 14-15).

that is more quantitative and thus easier to handle; with the focus shifting from tariffs to NTBs (non-tariff barriers), i.e. regulation, the WTO national treatment principle is, though, coming closer to its parallel in investment treaties. It is the concept underlying any economic integration— be it in the forms of intensive integration such as the US, the EU, middle-intensive forms such as various other regional integration agreements (MERCOSUR, ASEAN, NAFTA, etc)<sup>7</sup> or very early low-intensive forms such as initiated by bilateral economic (trade and/or investment) agreements. «Equality» is a fundamental principle of comparative constitutional and administrative law, though here applicable primarily only to nationals. Non-discrimination is a core principle of human rights law<sup>8</sup>, though it tends to focus on rights of individuals and is often directed at discrimination for racial, national, religious and political reasons<sup>9</sup>. In modern comparative discrimination law, discrimination —the mirror concept for equality— is also aimed at detrimental differentiation for reasons of gender and sexual preference<sup>10</sup>, and the ways of enforcing them come in a variety of ways, some much more pro-active and intrusive and some with only a very «light touch», both in the way a non-discrimination situation is defined and in the scope and impact of the consecutive obligation to remedy such breach.

At one end of the spectrum are situations defined only by clearly and visibly intended and explicitly formulated legislative discrimination against foreign traders and investors because they are foreign; at the other end are situations where there are no visible or even intended discriminatory rules, but where the domestic regulatory, administrative and in the extreme case institutional, commercial and social practices and culture constitute a certain handicap for entry and operation to foreign business. There can not be a society where being foreign —i.e. not a born and acculturated member of the relevant domestic communities— does not create a handicap. At one end of the «remedy spectrum» are obligations to gradually, with only a prospective impact, remove clearly visible, explicit and intentional legal impediments for greater equality; at the extreme other end where any handicap is captured, states are under an obligation to remove not only state-owned regulatory, administrative and institutional practices that handicap a

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<sup>7</sup> UNCTAD (2004).

<sup>8</sup> MCKEAN (1983).

<sup>9</sup> But one should note that different to the emphasis of SORNARAJAH (2004: 450 ff) the most legally and factually effective human rights instruments include property protection and cover legal persons (for the ECHR) - e.g. art. 1, Additional Protocol, for the most recent collection of excerpts from significant cases on the ECHR and Latin American Convention on Human Rights: BISHOP (2005: 478-485); MARROQUIN-MERINO (1991); ANDERSON (1999).

<sup>10</sup> DINE and WATT, editors (1996).

foreign business, but even to intervene into a society's commercial culture, possibly even with «affirmative action» to equalize the conditions of competition. The closer the integration intended—usually a sign of greater homogeneity—shared history and a will to develop an already pre-existing sense of community, the more will states be under an obligation, with joint enforcement institutions, to go very far into creating, pro-actively, effective equality. The lesser the intensity of integration intended and realistically achievable, the more will non-discrimination measures be of a «light touch», prospective, triggered only by glaring breaches and with soft remedies.

National treatment—expressed usually in an obligation to provide at least the same treatment, or the most favourable treatment accorded to nationals to foreign investors—is in modern treaties aimed at providing an advantage to foreign investors. This takes the form of a «discipline» (in WTO language) on states that can be enforced by investor-initiated arbitration of a «claim» that the «national treatment» obligation was breached, thus providing a distinct «cause of action» entitling, usually, to monetary compensation<sup>11</sup>. Its role is to «lift» the quality of treatment of foreign investors to the quality available to domestic businesses. Foreign investors may get sometimes better treatment (including in particular access to professional justice independent of the host state), but one of the «floors» is that at a minimum they should be treated as well as domestic investors. It has thus an «offensive» character. It has not always been so.

In the 19<sup>th</sup> century foreign investors were typically accorded—for similar reasons as today (attract capital to higher-risk environments)—special privileges; these were enforced not only legally, but by political and direct military pressure («gunboat diplomacy»). In reaction, then already independent, but still (as now) «developing» or «emerging» countries mainly in Latin America protested. Argentine foreign minister Carlos Calvo developed in reaction the doctrine of national treatment as the maximum—the absolute «ceiling»—available to foreigners. Quite different from today's concept that national treatment is a minimum (together with the fair and equitable treatment sometimes seen as identical or related to the customary international law «minimum» standard), national treatment was here advocated as a maximum. In particular it meant that access to justice outside the control of the host state and host state law was cut off—while the modern concept is that national treatment provides primarily substantive treatment standards, but enforceability is before an international

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<sup>11</sup> A separate section on remedies and compensation, related to my report to the IIA Foreign Investment Law Committee on Remedies & Compensation, has been omitted from this paper for reasons of length and will form the nucleus of a separate study.

system of justice. One needs to be therefore careful over confusion between the modern investment treaty concept with the Calvo doctrine's understanding of «national treatment»<sup>12</sup>. With Calvo, national treatment meant «pulling down» even if national treatment was awful; with the modern concept, national treatment means being pulled up, together with access to international justice and with another floor securing the downside: That if national treatment is awful, then the fair and equitable and/or international minimum standard is meant to provide protection against domestic standards which may be applied equally to all, but which are from an international perspective un-acceptable.

National treatment has re-emerged forcefully in many if not most of the over 2500<sup>13</sup> bilateral investment treaties currently reportedly in existence<sup>14</sup>; the cumulative effect of the few multilateral treaties (Energy Charter Treaty —with over 50 members; NAFTA— with Canada, Mexico and the US and others)<sup>15</sup> would add the equivalent of probably more than another 1000 state-to-state treaty relationships. Next to the traditional expropriation discipline (modernized with the reference to action «tantamount to expropriation» and to the «fair and equitable treatment obligation», national treatment has become the third most significant pillar of the investment protection regime of such treaties<sup>16</sup>. Claimant investors will in most cases raise discrimination as one of the several causes of actions; tribunals have based several recent awards solely or in conjunction with

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<sup>12</sup> SHEA (1955); PAULSSON (2005); LIPSTEIN (1945).

<sup>13</sup> The figures are changing; the most recent reports seem to indicate about 2500 bilateral investment treaties but we should add the equivalent of a bilateral, legally binding treaty relationship created by the 50-odd countries' Energy Charter Treaty, the NAFTA and the Asean investment instruments. The current number of bilateral investment protection treaty relationships is therefore at something like 3600+ by the end of 2005. About 500 are in the stage between signature and ratification. The main new development (see UNCTAD, August 30, 2005 press release, on TDM 2005, is the developed of broader bilateral or multilateral economic cooperation treaties, some of them include investor-enforceable investment disciplines, others leave this rather for government-government (or EU-host state) discussions, sometimes (as for example the EU — ACP countries Cotonou agreements) with at least the theoretical availability of quite sharp sanctions. For up to date information: [www.unctad.org](http://www.unctad.org). For an intelligent discussion of the «number of investment treaties and obligation-creating investment treaty relationships» and the ratification issue: M. Kantor. OGE MID archive, September 2005, on TDM.

<sup>14</sup> For a generalized discussion of the national treatment provisions in investment treaties: UNCTAD (1999); OECD (2004); for an up to date and lucid statement on BITs: SALACUSE and SULLIVAN (2005).

<sup>15</sup> E.g. ASEAN and Mercosur investment agreements (partly not ratified): UNCTAD, <[www.unctad.org](http://www.unctad.org)>.

<sup>16</sup> For an up to date treatment of these disciplines see the contributions in WEILER, editor (2005 and 2004).



other causes of action on a breach of the national treatment provision<sup>17</sup>. The main investment treaty disciplines are not completely separated, though it is recognized that the breach of one does not automatically allow to infer the breach of another one<sup>18</sup>; but a breach of one discipline may also have some weight in the examination of another one; elements relevant for one discipline that may not as yet amount to a full breach (e.g. «discriminatory elements», elements of lack of due process or unfair conduct) may be taken into account for assessing the breach of another discipline (obligation). For example, elements of discrimination or even full breach of the national treatment discipline will make it easier to find a breach of the fair and equitable discipline or of the «regulatory expropriation» discipline.

One needs to distinguish the application of the national treatment principle to admission/entry of investors («pre-investment») from application in the context of protection of existing investments («post-investment»). National treatment with respect to admission is in the main a policy to liberalize entry of investors to countries; it exists in the main only, and with mainly sectoral reservations, in US bilateral treaties and in a soft-law version in Art. 10 (2) of the Energy Charter Treaty<sup>19</sup>. These provisions have so far not been tested in investment arbitration; their legal value is unclear and the provision is not taken very serious<sup>20</sup>. The national treatment for access condition is the one that is most comparable to the national treatment provision in the GATT (Art. III<sup>21</sup>) and related instruments and in Art. 28, 29 and other provisions of the EU treaty relating to freedom of

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<sup>17</sup> Mainly: *Nykomb v. Latvia*, an Energy Charter Treaty award (published in [www.transnational-dispute-management.com](http://www.transnational-dispute-management.com) and [www.gasandoil.com/ogel](http://www.gasandoil.com/ogel); commented by WÄLDE & HOBER (2005); *Myers v. Canada*, *Feldman Karpa v. Mexico* (based on art. 1102 NAFTA) at [www.naftaclaims.com](http://www.naftaclaims.com); *Occidental v. Ecuador* (BIT-based), published in TDM ([www.transnational-dispute-management.com](http://www.transnational-dispute-management.com)) with a case comment by J Kurtz; discrimination has been discussed in quite some detail (though ultimately not relied upon for an award) in *Pope-Talbot v. Canada*. The *Lauder v. Czech Republic* tribunal determined a breach of the relevant BIT's national treatment provision, but it did not find that breach was a sufficiently proximate cause for the damage suffered by claimant. For a review of current jurisprudence WEILER (2004 and 2005); CREPET (2004); WANG (2001); national treatment has been the subject of official international agency reports by UNCTAD (mainly 1999) and (more or less identical): Chapter 5- *National Treatment*, in: UNCTAD (199 and 2004). The official agency papers tend to be more descriptive than interpretative of treaty practice. Professors Sornarajah and Muchlinski have served as legal consultants in —very useful— the UNCTAD investment treaty series of publications.

<sup>18</sup> NAFTA Chapter XI: Interpretative Decision, available from <[www.naftaclaims.com](http://www.naftaclaims.com)>.

<sup>19</sup> WANG (1995).

<sup>20</sup> See on NT as a pre-investment rule: UNCTAD (1999 and 2004); extensively and repeatedly (and always highly critically) SORNARAJAH (2004: 120, 319 and *passim*).

<sup>21</sup> The Reference Paper for the Telecommunications Protocol contains a pre-investment/ access to foreign investors set of rules within the WTO, but not enforceable directly by investors.

movement. This essay focuses on national treatment as a «post-entry» obligation on host states.

While non-discrimination was included in older investment protection instruments<sup>22</sup>, it acted largely as an ancillary reference to disciplines on expropriation reflecting the role of the non-discrimination principle in classical international law<sup>23</sup>. It now engages the emerging «regulatory state» and the large shadow of the WTO. In the contemporary «regulatory state», direct public ownership has been largely replaced by post-privatization private ownership of functions and assets hitherto assumed directly by the state as owner and operator. Foreign investment flowed, throughout the 1990s, massively into the privatization of state enterprises and agencies in public infrastructure (energy, transport, utilities in particular)<sup>24</sup>. The public interest function moved from direct ownership and operation to «regulation», i.e. supervision (setting of standards, tariffs, and access conditions) by often semi-independent public regulatory bodies<sup>25</sup>. This has created a large potential for discriminatory treatment of foreign as compared to domestic (public and private) operators. The national treatment obligation has won, in this new context, a new and much more poignant role for protecting foreign investors post-privatization and often in competition with domestic operators in a highly politicized climate of industries that interact very directly with large numbers of local people. With the transition to the regulatory state, investment protection had to move and did move as well: Direct expropriation has become very rare. Modern complaints about improper state conduct regularly focus on regulatory conduct and administrative practice<sup>26</sup>: the disciplines invoked are typically

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<sup>22</sup> Art. 2 of the Abs-Shawcross convention —no impairment of property by «unreasonable or discriminatory measures»; art. 12 Havana Charter has a very soft law provision: «undertaken»... «to give due regard to the desirability of avoiding discrimination as between foreign investments». The first BIT —1959 Germany-Pakistan— provides in art. 2: «neither party shall subject to discriminatory treatment any activities carried on in connection with investments [...] unless specific stipulations are made in the documents of admission of an investment».

<sup>23</sup> MANIRUZZAMAN (1998).

<sup>24</sup> WÄLDE (2000).

<sup>25</sup> One has to be careful here not to confuse the legal and formal independence of such regulators from the de-facto independence. Even in the UK —case of railway regulator— direct pressure on theoretically independent regulators is not uncommon, e.g. the pressure to resign reported by the UK regulator from the UK prime minister, *Daily Telegraph*, 23/9/2005.

<sup>26</sup> It would be helpful to analyse that issue in terms of recent awards/cases: NAFTA cases: *Myers v. Canada* is about discriminatory regulation; *Pope-Talbot v. Canada* about administrative practice; *Feldman Karpa v. Mexico* about discriminatory audit practice; *Thunderbird v. Mexico* about administrative practice; *Gami v. Mexico* — about regulatory practice (?); *Fireman Insurance v. Mexico*: financial regulation; *Tecmed v. Mexico*: municipal licensing; *Waste Management*: municipal licensing (?); *Metalclad v. Mexico*: municipal licensing practice; *Loewen v. US*: miscarriage of justice; *Methanex v. US*: environmental regulation; *ADF v. US*: procurement practice and regulation;

«regulatory taking» —i.e. regulation with the impact and scope of expropriation, but without formal taking<sup>27</sup>—, the breach of the «fair and equitable treatment standard» (with subcategories such as due process, arbitrary and discriminatory decision-making, breach of legitimate expectation) and national treatment. Expropriation has therefore been largely replaced, both in terms of conduct and protective investment treaty discipline, by regulatory conduct that does not measure up to authoritative good-governance standards.

National treatment has also, whatever the justification of legal analogies, gained significantly in visibility and status from its association with the WTO and other trade and economic integration (mainly EU) agreements. While already contained in the Havana Charter and the first BIT in 1959, it is hard to find any investment award which rests on a breach of national treatment —until the first NAFTA and the first ECT case. The negotiators and drafters of multilateral treaties (such as the Energy Charter Treaty) and BITs were often the same as those who negotiated the 1994 WTO agreements<sup>28</sup>. Both the WTO agreements, the NAFTA, the Energy Charter Treaty and the modern BIT model were negotiated in the same period (say 1985-1995) and represent the same economic philosophy: liberalization, privatization and «regulatory state», investment promotion and creation of open competitive economies). The language in investment treaties is often literally transposed (without much thinking) from the new trade treaties to the simultaneously or consecutively negotiated investment treaties. Clearly, the drafters considered investment treaty a corollary to the global liberalization policy embodied in the world trade treaties of the 1990s<sup>29</sup>. While investment protection has traditionally rested exclusively on expropriation disciplines, the GATT jurisprudence has largely focused on the national treatment principle. It is therefore hard to avoid the conclusion that the greater prominence of national treatment in modern investment treaties is very much due to the intellectual—but also simply drafting— influences from international trade law. I will examine the implications of such influences —the issue of analogy with WTO law— more closely in this study. But this increasing proximity and partial convergence can also be explained as both regimes now focus primarily on economic regulation affecting international economic integration (with trade and investment closely intertwined): The WTO on non-tariff barrier regulation, investment treaties on

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Mondev v. US: planning practice (?); MTD v. Chile: planning and investment promotion practice; Occidental v. Peru: tax regulation and tax practice.

<sup>27</sup> WÄELDE and KOLO (2001).

<sup>28</sup> BAMBERGER, in WÄLDE (Ed), 1996.

<sup>29</sup> On this, critically and with a general, pervasive and repetitive anti-imperialist, de-colonialist and pro-NIEO perspective, SORNARAJAH (2004: 51, 211, 288, 297 and *passim*).

economic regulation affecting operations by foreign businesses established in the host state. The object and the purpose of regulation relevant under the WTO and relevant under the investment treaties have become much less distinct than in the past, when there was little if any linkage between tariff policies and formal expropriation.

There is however a major difference between the national treatment principle under the WTO and its role in investment treaties. Invocation of the national treatment discipline remains under the control of governments. Dispute settlement in the WTO is reserved to member states even if businesses (in effect acting usually both as trading and investing companies) are often behind WTO litigation<sup>30</sup>. In investment arbitration, however, a legal revolution occurred in the 1980s and 1990s. Disputes can be initiated unilaterally by private investors, with states having limited screening or filtering control. This explains the explosion of investor-initiated investment disputes since the late 1990s. It has been driven by entrepreneurial cooperation between investors, specialized law firms and the arbitration community —an example of the «invisible hand» making private interests acting as «private attorney generals» to develop good-governance.

Many governments (including those in developed countries) do not seem to have expected that the rules they set up would actually be enforced; nor did they think it through that the general formulations of investment disciplines in the relevant treaties inevitably gave de-facto and in the longer term *de iure* law-making powers to arbitral tribunals<sup>31</sup>. It also explains the shocked reaction of older scholars who had grown up in the secure states-only paradigm of conventional international law up to the 1960s<sup>32</sup> and of younger scholars and NGO activists not ready to accept that states should be accountable for their conduct before the semi-privatized system of international justice that is investment arbitration. But the new facility of direct investor-state arbitration also means that in the search for remedies by aggrieved foreign investor the law is continuously tested, that analogies are sought from all cognate areas of law with similar language or a similar function<sup>33</sup>. To search for such analogies to help specify the still inchoate

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<sup>30</sup> SHAFFER (2003).

<sup>31</sup> On this also: PAUWELYN (2003).

<sup>32</sup> Perhaps most characteristic is the reaction of Professor Sornarajah who consistently advocates a minimalist and reductionist approach to investor rights. See generally and throughout, from beginning to end, SORNARAJAH (2004).

<sup>33</sup> I.e.: Traditional international law principles on discrimination; application of discrimination rules to further national (US) or international-regional economic integration; to further world trade (WTO, NAFTA), comparative constitutional and administrative law where principles of equality play a major role; human rights law —both general rules against discrimination of individuals and social and ethnic groups and specific rules on discrimination in an economic context; comparative

national treatment language is inevitable at this early stage of national treatment in investment law jurisprudence. My study is intended to contribute towards systematic thinking on the scope, but also limitations of specifying investment treaty language by analogy and in conformity with other areas of international economic law, in particular WTO law.

To face the manifold interpretative challenges that the national treatment clause raises, in a context that is usually markedly different from the trade law context<sup>34</sup>, there is usually little conventional legal support. So far, very little is known in terms of treaty-history («travaux») about specific purposes ascribed to the national treatment clause. We know that references to discrimination occurred as early as the Havana Charter, the first BIT and the Abs-Shawcross convention<sup>35</sup>, but rather as an adjunct to the then primary expropriation discipline. An exhaustive survey of the evolution of national treatment—from an expropriation adjunct to a self-standing key investment discipline—still remains to be done. Similarly, the *travaux* of the main multilateral treaties—Energy Charter Treaty, NAFTA<sup>36</sup>—have not as yet been made to reveal anything of substance to guide the interpretation. In this situation, one needs to rely on the formal intentions—the object, context and purpose in the sense of Art. 31 of the Vienna Convention on Treaties—of the treaties as they are indicated by the preambles and specific references to the objectives.

These objectives are quite broad. Thus, Art. 102 of the NAFTA—for example, speaks of the goal to «increase substantially investment opportunities» and «promote conditions of fair competition». Similarly, the Energy Charter Treaty<sup>37</sup>

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discrimination law (which is largely focused on ethnic, religious, political and social and now, in particular in developed countries, on gender and sexual-preference discrimination. On the similar tension in WTO law between a system of self-containment on one hand and, on the other, a harmonious evolution of the various subsystems of international (and international economic) law see PAUWELYN (2003).

<sup>34</sup> TRACHTMAN, report for UNCTAD, [http://www.unctad.org/en/docs/iteia20034\\_en.pdf](http://www.unctad.org/en/docs/iteia20034_en.pdf).

<sup>35</sup> Art. 2, *supra*.

<sup>36</sup> NAFTA history is still open only to a limited extent. There is no proper collection of the «travaux» for the Energy Charter Treaty nor are there specific «travaux» which would help to analyse the discussion of national treatment in the MAI. Bilateral treaties, as a rule, are negotiated on the basis of major-nation models (e.g. US, Germany, UK). We are not aware of a systematic discussion of the origin and intentions of the specific national treatment formulations in such BIT models and the actual BITs negotiated subsequently. This is quite different from the WTO where there is now a large literature on national treatment. The explanatory memoranda submitted to governments for ratification of both multilateral and bilateral investment treaties still remain to be mined for better insight into the official purpose for specific national treatment clauses though we suspect they will yield little of a specific insight with respect to national treatment.

<sup>37</sup> In the case of the ECT, one needs also to go back to its precursor «European Energy Charter» of 1991 which refers to a «high level of legal security», to transparency and non-discrimination.

affirms the goals of developing a «stable and transparent legal framework creating conditions for the development of energy resources» and to «catalyze economic growth by means of measures to liberalize investment and trade»

These objectives translate into an intent to apply liberal economic policies aimed at economic integration, promotion of foreign investment by protecting it extensively and a general emphasis on a level playing field between domestic and foreign competitors in a competitive market economy. To understand better how such quite general approaches should guide the interpretation of the national treatment discipline, it is necessary to visualize at least briefly the «political economy» of the interaction between governments, domestic (private and public) businesses and foreign investors. The statesmen, international economists and lawyers who set up the post-World War II international economic institutions realized that the normal political dynamics national economic policy-making leads to restrictions on foreign trade and investment —«domestic protectionism». The specific special interests threatened by foreign trade and investment and those which benefit from domestic privilege tend to have a greater influence over domestic political processes than either foreign traders and investors or the people at large; in the «logic of collective action» special interests of greater intensity with greater information and interest prevail<sup>38</sup>. This leads to an international zero-sum race for reciprocal barriers which disrupts and in the end destroys the potential for enhanced prosperity (plus often security) of international economic integration. The inter-war economic crises and escalating trade, investment and monetary restrictions with their concomitant contributions to international and national insecurity and instability are usually quoted as the best example. The main rationale for the development first of the Bretton Woods Institution after 1944 was to avoid the threat to prosperity and security that had plagued the inter-war years and to create a global legal and institutional framework which would unleash the potential of market capitalism. That indeed occurred, though with some imperfections: The failure of the investment treaty program of the Havana Charter in 1948<sup>39</sup>, the division of the world into the economically successful market economies, the economically and politically failing Communist countries and the politically wavering and only partially successful underdeveloped (developing, emerging) economies. But the unfinished business of the Havana Charter was taken up again in the 1950s —Abs-Shawcross and the beginning

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<sup>38</sup> OLSON (2000).

<sup>39</sup> The only relevant obligation from the Havana Charter is in art. 18: «to give due regard to the desirability of avoiding discrimination as between foreign investments» —which is to be seen as a adhortatory MFN— rather than a national treatment clause.

of the BIT movement in the 1960s. The OECD model conventions and the creation of ICSID, suffered a set-back in the 1970s —the «New International Economic Order»<sup>40</sup>— and revived from the mid-1980s —the creation of MIGA and the new model of pervasive BITs, NAFTA and ECT with direct investor-state arbitration<sup>41</sup>. It is currently suffering from a back-lash as governments realize they can in practice be sued and at times may lose investment arbitration, often combined with the realization that international law, treaties and disciplines can indeed reduce the «regulatory policy space». If such treaties can be effectively enforced without too much diplomatic filtering by states, then the disciplines on the domestic regulatory process can be more than a subject of inter-governmental conversation<sup>42</sup>.

## 2. THE CONTOURS OF A NATIONAL TREATMENT INQUIRY: GOOD GOVERNANCE AND THE CHALLENGE OF APPLICATION

The very extensive development of international «disciplines» on domestic economic policies, combined with international economic institutions, was intended to counteract the innate tendencies of domestic politics towards protectionism, both against trade and against investment. This role extends to virtually all international economic law, but it has been thought through most in-depth for the WTO conceptualized by Jan Tumlir<sup>43</sup>. It is equally relevant—indeed possible more so—for international investment law: While foreign traders/importers increase competition with domestic businesses for market share and sales profit, foreign investors increase competition for local companies not only to the extent they are involved in production and sales, but also in the identification and development of business opportunities. Business opportunities especially in many developing and transition countries usually involve close relationships between businesspeople and government (politicians, bureaucrats). Such close relationships tend to involve at best extensive patronage, at worst pervasive corruption —«crony capitalism» generating «political rent» for the «state classes». The harsh reality is that foreign investors disrupt such relationships. They endanger the advantage held by well established local business groups in terms of «captive» or closely

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<sup>40</sup> Prof Sornarajah —see most recently 2004, *op. cit. supra*— is a still surviving advocate of the «NIEO».

<sup>41</sup> WÄLDE (2005a).

<sup>42</sup> For a series of papers highlighting, mostly, the «regulatory policy space» than the other side of the coin, treaty-based investment protection, see the UNCTAD seminar in 2002: [http://www.unctad.org/en/docs/iteiia20034\\_en.pdf](http://www.unctad.org/en/docs/iteiia20034_en.pdf).

<sup>43</sup> See the extensive discussion in PETERSMANN in: HILF and PETERSMANN (1993).

linked government and the «political rent» enjoyed by the «state classes». They may be co-opted, but that usually takes place only over the long term and rather favours large multinational companies, but less so entrepreneurial companies with limited experience and local staying power.

The collusion that often exists between powerful local business groups (nationally or locally) and the relevant elements in the government are rarely fully visible. It is like a «black box» where one sees the result: that some do inexplicably very well out of the interaction with the government, while others—both domestic and in particular foreign investors— can not get a foot in the door however hard they try and however much they comply with the formal, visible and explicit local rules<sup>44</sup>. It is against this backdrop of the hidden confrontation of foreign investors with the «black box» of government-local business collusion that external disciplines are helpful to reduce the black-box effect by encouraging greater transparency in government-business relations, an essential pre-condition for a more equal playing field. It also explains why explicit (or *de jure*) discrimination is quite rare; legally explicit and visible discrimination is rather a sign of early and clumsy conduct by government (as by the Canadian Minister for Environment in the *Myers v. Canada* case). With growing awareness of the national treatment discipline's enforceability, discrimination—favouring the local businesses with political leverage—is likely to operate rather behind veils. The main investor complaint is therefore often about discrimination that only can be identified by its effects rather than by explicit manifestation. The protectionist and anti-foreign investor intent came out in the *Myers v. Canada* or the *Feldman v. Mexico* case quite late. In these cases the detailed factual discovery and examination that is part of the benefits of in-depth litigation indicated the powerful influence of domestic business groups keen to preserve a monopoly or at least a significant

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<sup>44</sup> I have developed this observation with particular respect to public energy monopolies, state- and privately owned: WÄELDE (2002). There is analysis from a business perspective on the role of domestic majority investors, but also minority investors in using their capture of the state's regulatory, administrative and political machinery to squeeze out foreign partners that are from far away—geographically, culturally, socially and ideologically—and who have little understanding and ability to influence such domestic governmental processes as effectively as well connected local businessmen—see: DESAI and MOEL (2004), p. 27 at note 62.: «Zeleshny's ability to control the value of CNTS arose, in part, from the ability to access Czech officials and court public opinion while CME was viewed as a remote entity. The CME example suggest that proximity to critical resources can lead to greater control and that remote owners may not retain the level of control indicated by their ownership shares». The *Feldman v. Mexico* tribunal seems also to have faced such a black box phenomenon, with enforcement more focused, rapid and effective against Feldman than against his Mexican competitors (where Mexico's economically most powerful businessman had a key role).



competitive advantage based on privileged relationships with government<sup>45</sup>. In this difficult situation —where the borders between the natural advantage of «local players» and exorbitant «crony capitalism» are not easy to distinguish—, the traditional core discipline of investment treaties —no expropriation without full compensation— only plays a marginal role. It is in the main the role of the revived «national treatment» discipline to help movement towards a more level playing field. Such a contribution can only be limited: Without radical affirmative action which is usually politically and practically not feasible, international disciplines even if vested with effective arbitration enforcement can only go so far in equalizing competition between foreign and domestic, large and smaller, entrepreneurial companies. There is a significant rest of «foreign handicap» —based on personal, cultural and institutional links and affinities— which is an unavoidable reflection of the fact that societies are not just legal and mechanical constructs, but living and with respect to the non-member distinct social communities. But the re-activation of the «national treatment» principle as a key component of the investment disciplines in modern investment treaties indicates the need for moving towards a more equal —never fully equal— playing field in light of the natural collusion between domestic business and captive government against foreign «newcomer» investors: the «new kid on the block» seen as disruptive to the established ways of playing profitable games.

This observation in turn raises the difficulty of applying a «national treatment» obligation effectively. There is a need to find a reasonable balance between the intrusion into national regulation and administrative practices —in itself an expression of the culture, good or bad, of national and then local communities— and a wise restraint respecting the limits of what is politically and practically feasible at a particular point of time and in a particular situation. Over the last years, intensive opposition has developed against the external intrusion into the domestic «regulatory space» by, first and foremost, WTO law; opposition against the lesser intrusion by international investment treaties is a companion, though investment treaties usually are focused on particular cases of affected individual investors<sup>46</sup>, rather on more generalized issues of anti-trade domestic policies. This opposition is part of the anti-globalization sentiment; many if not most NGOs, trade unions and industries anxious about losing domestic market power and the associated benefits. Intrusion into the domestic «regulatory space» is what international economic law does and is fully intended to do. The political

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<sup>45</sup> See also: PUIG, TDM 2004 (?) on the role of Carlos Slim, Mexico's most influential businessman, in the background of the *Feldman v. Mexico* dispute.

<sup>46</sup> On the difference between trade and investment disputes: TRACHTMAN, 2002, *op. cit. supra*.

legitimacy of such intrusion is based on the fact that countries with unfettered sovereignties have been economically —and politically— unsuccessful, indeed a threat to peace and security. Economic theory and experience suggest that open economies should do well and have done best, while closed economies should do badly and have fared worst. The economic and political success of the 50 years of EU integration has shown the benefit of external disciplines and institutions while the example of closed economies —the Communist countries in the past or the persisting examples of, say, North Korea or Belarus— show the association of closure with failure. The legal legitimacy of external disciplines on domestic regulation is based on voluntary consent and accession to the relevant trade and economic treaties. So «intrusion» into the «regulatory space» of national communities, governed more or less democratically, is not per se an argument against application of disciplines such as «national treatment». International law limits, and that is its function, the sovereignty of states as national law limits, and that is its function, unfettered freedom of individuals. However, there are limits on the scope of such intrusion. These are related to the social and political acceptability of external disciplines, and such de facto limits should be accommodated within the way the external disciplines are interpreted and applied in practice. Whatever the discussion between realism and idealism in international law, some realism is necessary in order to make international economic law practically effective rather than utopian.

It is helpful to appreciate the link between the potentially quite intrusive WTO restraints on national economic policy powers on one hand, the three-tier process of managing disputes (often with more than one phase) and the quite finely tuned system of remedies —as a rule ex-post and prospective, as a rule without direct financial liability for damages, and intended to encourage the defendant state to gradually move its regulatory and administrative system towards compliance<sup>47</sup>. This system of a very gradual adjudicatory process, leading not to huge damages for conduct in the past, but rather to pressure towards a prospective adjustment of regimes contrasts starkly with investment arbitration where a rigorous logic of systematically calculated damages can lead to massive damage awards for what could be seen as not fundamental infringements of the rules. The best illustration is the series of CME/Lauder cases where two respected tribunals on the basis of the same facts and with, each, a respectable reasoning came to either a dismissal of claim (Lauder v. Czech Republic) or

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<sup>47</sup> MAVROIDES (2000).

the award of a 350+ Million US \$ award<sup>48</sup>. Such stark differences between winning or losing a claim do not occur with WTO remedies. The application of conventional damages methodology combined with the usual wide range of valuations possible leads more easily to damage awards which can destabilize the investment arbitration system than in the WTO situation. If analogies are to be drawn between the WTO-based intrusion into the national policy space and investment arbitration, then one needs to take also into account the greater subtlety of WTO remedies. They allow a step-by-step encouragement of compliance in ways that move the disciplining effect forward, but only as much as it is politically acceptable without endangering the viability of the WTO system. This consideration should help to think about national treatment not in the usual legal separation between breach and damages, but to link the type of breach with the type of remedy that is suitable and most effective in making the national treatment discipline effective.

Finally, one needs to relate the «national treatment» discipline to the investment promotion role of investment treaties. This central objective has been documented for the two main multilateral treaties. It is likely to be either an explicit or implicit function of every investment protection treaty. Their function is to encourage new investment (and maintaining of current investment, possibly even to encourage return of flight capital) by a credible promise of protection (conventionally mainly in terms of protection of property and sanctity of contract) but in the regulated, post-privatization economy it is protection from discriminatory practices which obstruct the «normal» running of a business operation. In the post-privatization regulated economy, it is less the protection of tangible ownership rights as the ability to run a business in a context of fair competition which determines the essence of the value of the assets<sup>49</sup>. Discrimination is then the main risk, much more than formal expropriation, against which protection is sought from external, impartially enforced disciplines. By providing such effectively enforceable guarantees, the host state enhances its reputation and «investment climate»; it increases the credibility of its promises and is able to correct to some extent the disincentive inherent in low-governance quality frequent in developing and transition economies; it signals to the international markets that it is serious about

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<sup>48</sup> The Svea Court of Appeals judgement is the end of the case and it summarizes the various cases and awards preceding it, published with a comment: T. Wälde, Introductory Comment to the CME/Lauder v. Czech Republic Litigation International Legal Materials, 2003: 42 ILM 811. One needs to add that such large awards have been rare and tribunals have in most cases been cautious with damage awards. For a more detailed discussion of remedies and compensation see my ILA report - *op. cit. supra*.

<sup>49</sup> WÄLDE and WOUTERS (1996).

its commitment to treat investors reasonably well, even after they have become «hostage» to the vagaries and volatilities of often difficult countries. This function—though often explicitly referred to in preambles and objectives statements of investment treaties—is rarely appreciated or even understood in academic literature, though analyzed in quite some depth by authoritative discussions of international rules by the World Bank<sup>50</sup>.

External disciplines—if taken serious, as they will be if there is a credible enforcement mechanism—will not only make host state policies more credible, but they will also make them more stable. If domestic economic reform is «anchored» in external disciplines, it will be more insulated from the vagaries of domestic politics, and the foreigner-bashing that comes naturally to opposition parties; agitation against foreign businesses is always a temptation in domestic politics, particularly if it finds support in politically favoured domestic competitors. But it can often result in lasting damage to the stability of property rights, of contracts and the perception of the domestic investment climate. External disciplines provide support to domestic forces opposed to short-term populism<sup>51</sup>, they create political and financial costs against the tearing up of contracts and other rights for short-term political gain and thus stabilize economic policies that are technically correct and wise from a longer-term perspective. National treatment is thus an external discipline to anchor good-governance more firmly than mere importation of foreign models subject to political process vagaries would do. Nowhere has this been better shown to work than in the EU. It represents the rationale underlying all fine balances in constitutional systems where the long-term interests of the nation—or union—have to co-exist with the short-term perceptions of interest and sentiment of an unfettered democratic process<sup>52</sup>. International investment law is therefore a projection of constitutional approaches to the governance of the global economy.

### 3. PRECEDENTIAL JURISPRUDENCE BY ANALOGY: CUSTOMARY INTERNATIONAL LAW, WTO, EU, US

There is no formal common law rule of precedent—*stare decisis*—in international investment law. This is even more so in international commercial arbitration

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<sup>50</sup> For example, World Bank Development Report, 2004, «A Better Investment Climate», chapters 5 and 9—compare, on the other hand, with Sornarajah, 2004 where dependency, neo-colonialism and exploitation are amply discussed and frequently insinuated, but where the investment promotion, good-governance and signaling functions are ignored.

<sup>51</sup> PUTNAM (1988).

<sup>52</sup> Alexis de Tocqueville on the US constitution; RAKOVE (1966).

with which investment arbitration shares similar procedural (but not substantive) tendencies<sup>53</sup>. In commercial arbitration, awards are as a rule not public; they are sometimes summarized in a sanitized way. As arbitrators are primarily appointed by and accountably only to the parties, with a contractual relationship to the parties, awards are not written with an eye towards precedential effect and persuasion of the public, but almost exclusively for the parties and with the intention of accommodating their views and sentiments. Such award styles are therefore not very suitable for developing precedent. Not surprisingly arbitration awards can differ dramatically from each other in style, substance, selection and interpretation of the law. It is only in rare cases that such divergences surface<sup>54</sup>.

Investment arbitration though is quite different. The similarities with commercial arbitration can be deceiving even though the attitudes brought in from commercial arbitration linger on. First, it is in most cases not two parties disputing about a contract, but it is a foreign investor claiming damages because of governmental measures. Public policy issues are always present; they are rarely directly relevant in commercial arbitration. The treaty obligations on which claims are based are very open-ended, with general language («Fair and equitable», «non-discrimination») far away from the very detailed text of modern international commercial contracts. These treaty terms can not be interpreted only on their own, but only in the context of the treaty. All this leads to the increasingly dominant role of precedent as the few awards of the past (say 15-20 from 1950 to 1980) and the historically distant mainly PCIJ and terse claims commission decisions, are now being gradually superseded in weight by the substantial increase of investment treaty cases since in the main 1995. Tribunals recognize that they are not dealing with commercial contracts, but treaty instruments under international law for which the interpretation methods of treaties —Art. 31-33 of the Vienna Convention on Treaties— are the one authoritative guideline. This leads to the established sources of international law as expressed in Art. 38 of the statute of the International Court of Justice, that is:

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<sup>53</sup> While investment arbitration comes with the styles, procedures, formats and to a significant extent personnel of commercial arbitration, it is in substance a form of international quasi-judicial review of administrative conduct so that in essential, not minor procedural issues, a look towards comparative constitutional and administrative law of judicial review and towards international forms of judicial review as exercised by the European Court of Justice or the WTO dispute system is more warranted.

<sup>54</sup> As in the *CME/Lauder v. Czech Republic* case which was not a commercial arbitration, but an investment arbitration using commercial arbitration forms.

- «international custom, as evidence of a general practice accepted by law»<sup>55</sup>
- «general principles of law recognized by civilized nations» and
- judicial decisions (as a subsidiary means).

All three categories allow authoritative arbitral awards to contribute, in a cumulative way rather than as distinct individual awards towards international law formed by a line of precedent<sup>56</sup>. Modern investment arbitral awards are increasingly publicly available, in response to general professional interest in useful precedent, but also to NGO pressure for greater transparency. Once they become public, they are subject to the usual ways of professional, academic and political quality control in terms of public discussion and critique<sup>57</sup>. As a result, the style of awards has gradually changed from one only intended to accommodate two disputing commercial parties to one that is comparable to judgments by senior national courts, the WTO Appellate Body, the ICJ, ECHR, ECJ and similar international courts.

Precedent and litigation dynamics also build momentum towards the emergence of a «persuasive precedent» role of individual awards and authoritative precedent role of principles that get confirmed and reinforced in a series of awards. In modern investment arbitration, a large amount of legal resources is deployed by both parties —counsel, experts, witnesses, discovery, cross-examination and several sequences of pleadings and hearings, sometimes now also amicus briefs— to persuade the tribunal. A tribunal with two members appointed by each party and the chair appointed by the parties or at least with the informal consent of the parties by an appointing authority—all keen to win re-appointments—, can

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<sup>55</sup> See here, for investment treaties, on common core content of modern investment treaties as contributing towards a contemporary definition of customary international law: LEBEN (1998: 248); HINDELANG (2004: 767); always contra: SORNARAJAH (2004: 104, 306, 319, 330) who claims the 2200+ (plus 2500+ equivalent of BITs in terms of ECT and NAFTA treaty relationships) are not specific enough to contribute to customary international law, but in other parts of his books complains about the surprisingly identical substantive content of African BITs and of BITs based on large-country models, and, after having highlighted the special character of BITs proceeds to discuss their content in general and generic terms. Critically also: GUZMAN (1998), but his argument that BITs have no sense of legal obligation because developing countries seek advantages is not persuasive as most or all treaties or legal obligations are accepted because advantages are being sought.

<sup>56</sup> On the role of authoritative soft law to guide the interpretation of open-ended language in investment treaties: WÄLDE (2004).

<sup>57</sup> Just note the publication of awards on: [www.worldbank.org/icsid](http://www.worldbank.org/icsid); [www.transnational-dispute-management.com](http://www.transnational-dispute-management.com); [www.investmentclaims.org](http://www.investmentclaims.org); <http://ita.law.uvic.ca> —in addition to conventional and often sanitized publication and comment in the publication vehicles of commercial arbitration.

not but be influenced by the arguments put forward by parties. The parties will seek—with extensive resources backing their advocacy—not to leave a stone unturned in their effort to find persuasive precedent to support their case. The litigation dynamics thus involves a search for both precedents in existing and emerging investment arbitral jurisprudence, but also an effort to dig up analogies wherever a credible reason can be found for such analogy. A tribunal, when faced with the challenge of interpreting a so far untested, open-ended treaty clause will naturally gravitate to seek support from any other authoritative, respected and reasonably cognate area of law, both to help it find its decision and, perhaps more importantly, for providing authority for its reasoning. Judges and arbitrators fear little more than being accused of «subjective and discretionary» decisions. The power of the tribunal—but also its accountability—«increases in direct proportion as the norms increase in generality»<sup>58</sup>. The more general the investment disciplines, the more tribunals will want and have to search for external authority that protects them from the «subjectivity» accusation. While such elements are part of the real-life decision-process, they will be overlaid by a reasoning that presents the decision as «objective», as «finding» rather than «creating» the law. The more an area is as yet unsettled, the farther will counsel and arbitrators reach out to cognate areas of law; the more a jurisprudence is settled, the less such far-reaching analogy will be necessary. The more «revolutionary» a judicial decision, the more the courts and tribunals will seek to present it as nothing but an application of well-established principles to a mildly novel factual situation.

To sum up, precedent plays a most significant role in investment arbitration. One can perhaps distinguish direct precedent—other arbitral awards interpreting a similar clause in a similar context—and more remote, indirect precedent—analogy from cognate, but distinct fields such as in particular WTO, ECJ and comparative jurisprudence. Should an award deviate from a well-established and directly precedential jurisprudence, then the burden of reasoning will be much larger—arguably sanctioned by Art. 52 (1) (4) of the ICSID annulment procedure and the rules for judicial review of arbitral awards in the case of non-ICSID awards.

As a starting point, the closest source of guidance for the application of national treatment in investment treaties is the jurisprudence on national treatment in GATT Article III. It is notable that this was the route taken by claimants and tribunals in the very first NAFTA cases that applied the national treatment Article 1102 such as *SD Myers* and *Pope & Talbot*. The language employed in GATT Article III (and especially GATT Article III.4) is similar in

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<sup>58</sup> MCKEAN (1983), also: PAUWELYN (2003).

certain respects to that adopted for national treatment in investment treaties. This is by no means unexpected considering that underlying concepts from the WTO were imported into various newly negotiated investment treaties including Chapter 11 of NAFTA, the Energy Charter Treaty and the aborted OECD Multilateral Agreement on Investment. Further, there is a commonality in purpose that unites these different arms of international economic law: the setting up of international controls on domestic economic policy making. It is thus understandable that the instinctive reaction of counsel and tribunals in the first NAFTA Article 1102 cases was to look towards the WTO, and to import WTO jurisprudence more automatically than the difference between both areas of law should allow. One import was the structure of analysis adopted in the GATT Articles III and XX approach: likeness? —different treatment?— justification? Then again, this structure is by no means limited to the WTO jurisprudence as it is a general approach that unites any general discrimination claim. It is also in the main the approach that two prominent NAFTA states (in particular US, also Canada) have suggested for investment treaties<sup>59</sup>.

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<sup>59</sup> See US/Canada Declaration on the ECT art. 10 NT standard (one should note both countries did in the end not sign the Treaty): «With respect to Article 10 Canada and the United States each affirm that they will apply the provisions of Article 10 in accordance with the following considerations:

For the purposes of assessing the treatment which must be accorded to Investors of other Contracting Parties and their Investments, the circumstances will need to be considered on a case-by-case basis. A comparison between the treatment accorded to Investors of one Contracting Party, or the Investments of Investors of one Contracting Party, and the Investments or Investors of another Contracting Party, is only valid if it is made between Investors and Investments in similar circumstances. In determining whether Differential treatment of Investors or Investments is consistent with Article 10, two basic factors must be taken into account. The first factor is the policy objectives of Contracting Parties in various fields insofar as they are consistent with the principles of non-discrimination set out in Article 10. Legitimate policy objectives may justify differential treatment of foreign Investors or their Investments in order to reflect a dissimilarity of relevant circumstances between those Investors and Investments and their domestic counterparts. For example, the objective of ensuring the integrity of a country's financial system would justify reasonable prudential measures with respect to foreign Investors or Investments, where such measures would be unnecessary to ensure the attainment of the same objectives insofar as domestic Investors or Investments are concerned. Those foreign Investors or their Investments would thus not be "in similar circumstances" to domestic Investors or their Investments. Thus, even if such a measure accorded differential treatment, it would not be contrary to Article 10. The second factor is the extent to which the measure is motivated by the fact that the relevant Investor or Investment is subject to foreign ownership or under foreign control. A measure aimed specifically at Investors because they are foreign, without sufficient countervailing policy reasons consistent with the preceding paragraph, would be contrary to the principles of Article 10. The foreign investor or Investment would be "in similar circumstances" to domestic investors and their investments, and the measure would be contrary to Article 10.



It is much more difficult to simply transpose specific WTO jurisprudence on questions such as the determination of «likeness». GATT Article III.4 for example speaks of «like products» whilst NAFTA Article 1102 uses the formulation «in like circumstances». There is also the very pertinent difference that exists between most investment treaties and the WTO compact. Unlike the WTO, most investment treaties do not contain a general exception from application in the form of a GATT Article XX. There are however good reasons why WTO jurisprudence should be examined closely for analogy. WTO Panels and the Appellate Body have grappled for decades in sometimes intensively debated and commented cases with the contours of a national treatment inquiry. In recent years, the jurisprudence has tackled the difficult task of identifying hidden discrimination in origin-neutral regulation. The criteria and reasoning developed in the WTO context thus should not be ignored in the task of developing a coherent approach to underpin national treatment as it applies in the investment treaty context.

At the same time, one must bear in mind key systemic differences between WTO and investment disputes. WTO disputes are inter-governmental only and there is no unscreened access by private claimants<sup>60</sup>. Investment remedies are mainly monetary damages. WTO remedies in contrast are prospective and try to encourage and move the non-complying state gradually into compliance. They have none of the financial impact of a multi-million dollar award often with compound interest that can be the result of an investment arbitration. There is also the issue of institutional structure and support of the dispute settlement process. The WTO secretariat is closely, some say too intrusively, involved with the award<sup>61</sup>. The WTO is also marked by a formal appeal process that is missing in the investment treaty context apart from the rudimentary ICSID annulment procedure.

It is perhaps in the scope of operation that the most fundamental difference lies. WTO law relates to trade in goods and services. As such, it affects the conduct of traders who would like to be more active in the importing country but they are not exposed as yet to sizeable risk as investors who have entered the host state. While trade and investment can sometimes overlap, (in particular in services trade), there is still a fundamental difference. The investor has made the leap

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<sup>60</sup> This is not to say the decision to commence WTO processes is taken by reference to state interests alone. Indeed, some aspects of the WTO compact expressly contemplate the involvement of the domestic industry affected. This is most notable in the area of anti-dumping duties. Thus, Article 5.1 of the WTO Anti-Dumping Agreement provides that the regulator's investigation into whether dumping has occurred is initiated upon a written application by the affected domestic industry.

<sup>61</sup> See, e.g., J. WEILER in PORTER *et al.* (2001).

and, is exposed as a «hostage» to its host state that now can change its conduct and extract rent from the investor. A commercial entity in a trading relationship with an importer in the host state is rather looking prospectively into the future to develop opportunities rather than having to protect investments already made<sup>62</sup>. The need for protection for an investor will therefore in many cases be much greater than in a typical WTO dispute though with the links between investment and trade some convergence and parallel applicability of both trade and investment rules may occur.

The next proximate field for analogy should be international law on discrimination<sup>63</sup>. Since discrimination has been a standard item in international trade treaties since at least the 12th century, and presumably long before this<sup>64</sup>, one would expect relevant case law. There are however very few cases. The Oscar Chinn case<sup>65</sup> revolved around a guarantee of «commercial freedom and equality» in the Treaty of St. Germain of 1919. Otherwise, discrimination against foreigners in matters of economic policy has received little attention in international law. This is of course apart from the controversy of whether discrimination makes an otherwise legal expropriation illegal under international law. Home states, in particular in the context of decolonisation expropriations, have taken that position against host states and NIEO advocates<sup>66</sup>.

There is probably no general international law prohibition on discrimination against foreigners<sup>67</sup>. Indeed, there are many cases of discrimination —both for and against foreigners— which are largely accepted. On the other hand, there is a trend towards considering discrimination on the basis of race and certain other factors (religion, gender *et al.*) as illegal. In contrast, Professor Sornarajah considers «affirmative action» discrimination as acceptable<sup>68</sup>, meaning measures that discriminate in favour of indigenous or socially and economically disadvantaged

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<sup>62</sup> TRACHTMAN, UNCTAD report, 2002, *op cit.*

<sup>63</sup> Authoritatively: MCKEAN (1983); also: MANIRUZZAMAN (1998).

<sup>64</sup> ERLER (1954).

<sup>65</sup> PCIJ 1934 ser A/B. No. 63; case comment by T. WEILER in T. WEILER (Ed), 2005.

<sup>66</sup> See the discussion in MCKEAN (1983: 196-198) referring to the Anglo-Iran case, the Suez Canal nationalization and the Indonesian nationalizations of Dutch companies.

<sup>67</sup> Notably however, a senior US Court in the Sabbatino case made precisely such a claim. See 307 F2nd 845, 866 (1962), reversed by the US Supreme Court, 376 US 398, 433 (1964); 307 F2nd 845, 866 (1962), reversed by the US Supreme Court, 376 US 398, 433 (1964).

<sup>68</sup> SORNARAJAH (2004: 201).

people<sup>69</sup>. Discrimination based on racial hatred is considered illicit<sup>70</sup>; the question then arises of whether «racial hatred» can also include measures against «hated aliens»<sup>71</sup>. Most of the scholarly discussion and the little of jurisprudence on issue<sup>72</sup> suggests that «positive discrimination» may be permitted if reasonably effective to compensate factual inequalities. It also suggests that the key issue is if there are reasonable—and proportional—grounds for distinct treatment and that the difference in treatment is done without abuse and in good faith.

Whilst traditional international law presages the basic concepts of today's interpretative discussion, it does not seem to yield specific standards for applying current investment treaties. This is particularly the case as modern economic treaties are much more numerous, specific and are now faced with discrimination in the context of the post-privatisation regulatory state for which there is very little precedent<sup>73</sup>. Human rights treaties focus on individuals rather than businesses though the European Convention on Human Rights protects both juridical persons and property through its Additional Protocol<sup>74</sup>. The role of discrimination against foreigners in its jurisprudence is still to be properly researched. None the less, some of the criteria used—proportionate affirmative action to correct inequalities, good faith and absence of abuse—should be part of a standard inquiry into the existence of legitimate policy reasons in a national treatment test.

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<sup>69</sup> Also Art. 24 (2) of the ECT: Certain measures are exempted from the ECT's scope, such as: «Designed to benefit investors who are aboriginal people or socially or economically disadvantages individuals or groups [...]». That exemption is limited by non-discrimination between member state investors and by the absence of a «significant impact on that Contracting Party».

<sup>70</sup> MANIRUZZAMAN (1998) with reference to SORNARAJAH.

<sup>71</sup> Most references, e.g. SORNARAJAH (2004), select only relatively benevolent cases of affirmative action – e.g. for the Malay majority in Malaysia, for lower castes in India. The definitively not benevolent discrimination against Jews in Nazi Germany—the «Aryanization» of Jewish-owned business—is however rarely mentioned in this context: FRIEDLAENDER (1977). Then, as in the 1970s in the NIEO context, the principle of «absolute state sovereignty» was asserted against international rules and intervention (at p. 139).

<sup>72</sup> PCIJ advisory opinion on the minority schools in Albania; 1935 19 ser A/B NO. 64 and Advisory Opinion concerning German settlers in Poland, 1923 PCIJ 24, ser B No. 6.

<sup>73</sup> Apart from perhaps the Oscar Chinn case.

<sup>74</sup> There are reportedly over 45000 applications per year, though few of them deal with major matters of economic regulation affecting property rights; D. Anderson, Expert Opinion on Yukos case in Houston, February 2005, on: [www.transnational-dispute-management.com](http://www.transnational-dispute-management.com) 2005; on ECHR jurisprudence with respect to property protection: CONDORELLI (1995); ANDERSON (1999); SORNARAJAH (2004: 154), claims that the ECHR instruments «do not contain any reference to the right of property» to reject those who «scavenge for authority in the most unlikely quarters» for recognition of property as a universal human right—something that is hard to square with the significance of the Additional Protocol to the ECHR and increasing jurisprudence of the Latin American Convention, e.g. Banco de Lima case, *supra*.

The elimination of discrimination has constituted a key plank in the EU's successful integration effort. One can perhaps distinguish three dimensions of that anti-discrimination effort, although it often does not operate under the label of «discrimination», but under the category of «elimination of impediments to freedom of movement (capital, services)»<sup>75</sup>.

- Firstly, there is an absolute prohibition of discrimination (Art. 6, ex Art.7) on grounds of nationality. It has been widely interpreted: Any disadvantages —not only disadvantages suffered in the context of a competitive commercial context— are forbidden; special favours granted to one can be discriminatory disadvantages for others. Discrimination is covered that is explicit, but also that which is only indirect and de facto. But different treatment is not discrimination if it can be justified on reasonable grounds.
- On a second level, the equivalent of a discrimination rule is contained in the far-reaching prohibition on freedom of movement of goods, capital and services. These capture virtually all de-facto, by effect only, forms of disadvantages for foreign investors. The key debate here is usually less if forms of regulation and government conduct can be qualified as a restriction on intra-Union trade, but rather if they can be justified<sup>76</sup>. The debate and the fine points of ECJ jurisprudence tend to turn around issues of least-restrictiveness and proportionality, but also recognition of governmental discretion in assessing and shaping economic policies. That leaves some immunity for domestic cultural preferences and social and political needs<sup>77</sup>. In so far, EU trade law is much closer to WTO law than the use of different terminology suggests<sup>78</sup>.
- On a third level, there is the much more advanced and intensive level of integration intensity, as compared, for example, to the WTO and the NAFTA. This comprises positive action to develop common standards or mutual recognition and other pro-active measures to propel integration are continuously developed in a way that has no equal outside deeply federated states (such as the US). This is usually done by directly effective regulation or, in most cases, by EU directive. Much of the elimination

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<sup>75</sup> Summary: McKEAN (1983: 201-202).

<sup>76</sup> Hartley (1994).

<sup>77</sup> 1997 ECJ electricity import monopoly, EC Commission v. France *et al.* (C159/94) [1997] E.C.R. I-5815.

<sup>78</sup> WEILER (2000).

of discrimination of trade and investment between member states came about not by individual judicial decision, but by large-scale restructuring of the regulatory regimes for industry by directive. This instrument of intensive integration policy is neither available nor suitable under the low-integration levels of BITs.

The ECJ jurisprudence in turn largely reflects the deeper and more intensive level of integration than exists in most other international fora. It is thus unlikely to serve as a strong precedent for the much looser pre-integration aims and preconditions of investment treaties. On the other hand, the decades of jurisprudence developed with a pro-integrationist purpose, (whilst still balancing Community interests versus national identities) should not be ignored. The ECJ, in particular, has often developed subtle (if not always consistent) ways of moving integration forward step-by-step, while not going so far as to provoke a too radical counter-reaction. Measures that overshoot a reasonable underlying policy rationale are separated from those that can be legitimized. The Danish bottle case<sup>79</sup> is a good example of how discriminatory legislation was struck down where it overshot a legitimate underlying environmental objective. It is therefore in particular ECJ jurisprudence relating directly to discrimination (where there is no requirement of a competitive context) and relating to justification of restraints on intra-EU freedom of movement that should be relevant per analogy to our national treatment challenges. On these levels, EU law is not that far removed in terms of integration intensity from investment treaty situations, while on level three —positive action— the EU may serve as a laboratory for regional economic integration advocates, but not for current investment arbitration.

Comparative national law on judicial review of administrative acts —usually with claims that national constitutional guarantees of equality of treatment are breached— would be another natural area for analogy. Since investment arbitration is in effect quasi-judicial review of government conduct by affected investors, it is more comparable to judicial review than to commercial arbitration. Nevertheless, there are serious differences: National constitutional guarantees of equality play within a national context. There is less sensitivity over the national judiciary (including constitutional courts) intervening in national legislation than there is over foreign adjudicatory bodies intervening in domestic policy areas. On the other hand, investment treaties have the explicit purpose of encouraging investment and enhancing good-governance by protecting exposed foreign

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<sup>79</sup> Case 302/86 *Commission v. Denmark* (1988) ECR 4607, 1 CMLR 619 (1989). European Court of Justice, *Brasserie du Pecheur v. Germany*; *Regime v. Secretary of State for Transport, Ex Parte Factortame*, *The Times*, March 1996, p. 38.

investors. The closest that comparative judicial review comes to national treatment challenges in investment arbitration is probably where the federal courts (e.g. US Supreme Court) exercise economic integration roles similar to the one by the ECJ. The questions of discrimination for out-of-state businesses can at times raise issues quite similar to those arising under investment treaties<sup>80</sup>.

To sum up, there is good reason to look to precedent in other fora where judicial control is exercised over domestic economic policy-making and where equality —or discrimination— is used as the main interpretative standard. However, none of the sources considered in this article can be simply transposed into the investment treaty context. There are some similarities, in particular in areas where legal rules are used on a relatively low-intensity level of economic integration to strike out relatively direct and easily identifiable measures of discrimination. Such analogies, as tenuous as they often are, are also inevitable until a separate body of arbitral jurisprudence on national treatment has emerged. But every analogy that is proposed to tribunals or relied upon by them needs to be seen as a prop. That is, something that might yield an argument, a tested method of solving a dilemma but is not suitable for automatic application.

#### 4. OVERVIEW: TYPICAL NATIONAL TREATMENT CLAUSES IN MULTILATERAL AND BILATERAL INVESTMENT TREATIES

Although there are now over 2400 BIT (and another 1000 or so equivalent bilateral treaty investment protection relationships in operation, there are certain core commonalities and often very similar language that has emerged, in particular with treaties influenced by the modern US/UK model since 1990<sup>81</sup>. The multilateral treaties (and the newest US model) provide the most representative illustration. Multilateral treaties tend to be negotiated with more care and rely less on established models. They are therefore most instructive for the state of the art and state of development of modern investment treaty practice.

NAFTA Art. 1102 can perhaps be seen as the «mother» of all modern national treatment clauses in investment treaties: «Each Party shall accord to investors (Art. 1102 (2) refers to investments», i.e. domestic host state subsidiaries of foreign

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<sup>80</sup> The *Methanex v. US* case presumably raises quite related issues to NAFTA art. 1102 under the US inter-state commerce clause.

<sup>81</sup> SALACUSE/SULLIVAN 2005; on the new model: M. KANTOR, TDM 2004 (check); also: GANTZ in WEILER (Ed) 2004, NAFTA Chapter XI arbitration; for an overall survey of all sorts of formulations with respect to national treatment see UNCTAD, 1999 and 2005. They also describe issues not dealt with here such as pre-investment (access), sectoral and other restrictions; relationship with the MFN and other typical BIT clauses.

investors) of another party treatment no less favourable than that it accords, in like circumstances, to its own investors with respect to the establishment, acquisition, expansion, management, conduct, operation, and sale or other disposition of investments.»

Art. 1102 (3) is also of more interest than just the reference to sub national authorities: «The treatment accorded by a party [...] means, with respect to a state or province, treatment no less favourable than the *most* favourable treatment accorded, in like circumstances, by that state [...] to investors [...] and investments [...]».

National treatment in the NAFTA thus covers both «investors» and «investments» (foreign parent and domestic subsidiary). It is necessary to note the use of «like circumstances» which is textually different from the *identical* circumstances language as was proposed in the aborted UN Code of Conduct<sup>82</sup>. One should also note the possible qualification to «the establishment, acquisition, expansion, management, conduct, operation, and sale or other disposition of investments». There are other listings, such as in the 1992 World Bank Foreign Investment Guidelines which refer to permits, property rights, security, legal matters»; the draft MAI lists also «enjoyment» and the Asian Framework Agreement on Investment makes clear the list is only illustrative but not exhaustive<sup>83</sup>. It is difficult to see any relevant government action affecting foreign investment that is not covered — including merger regulation («acquisition», «sale») and the application of competition law principles («operation», «conduct»). Art. 1103 (3) is notable as it uses the term «most favourable» in the national treatment context, thus (arguably) contributing something on the disputed question if the comparator is «the most favourably treated domestic investor» or «the average treatment meted out to domestic investors».

In contrast, Article 10 of the Energy Charter Treaty has a not yet properly understood structure: It takes up the NAFTA formulation (no discrimination in specific areas of economic activity) but it adds a general national treatment obligation using the «most-favourable» as compared to domestic investors method:

Art. 10(1): [...] no Contracting Party shall in any way impair by unreasonable or discriminatory measures their management, maintenance, use, enjoyment or disposal.

Art. 10(3): Treatment” means treatment accorded by a Contracting Party which is no less favourable than that which it accords to its own Investors or

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<sup>82</sup> UNCTAD (2005: 171).

<sup>83</sup> Longer analysis: UNCTAD (1999: 31-32).

to Investors of any other Contracting Party or any third state, whichever is the most favourable.

Art. 10(7): Each Contracting Party shall accord to Investments in its Area of Investors of other Contracting Parties, and their related activities including management, maintenance, use, enjoyment or disposal, treatment no less favourable than that which it accords to Investments of its own Investors [...] and their related activities including management, maintenance, use, enjoyment or disposal, whichever is the most favourable.

It may be that at some time in the future parties in litigation will be able to squeeze different meanings out of these three references to national treatment (non-discrimination). At present, all we can surmise is that the more extensive version of national treatment in the ECT as compared to Art. 1102 NAFTA means that the drafters wanted both an «illustrative clause» (but not exhaustive as arguably in Art. 1102 NAFTA, though the scope there is very wide as well) and a general, all-encompassing clause encompassing any sort of national treatment. It may be also that Art. 10 (1) refers here to discrimination that is wider than a difference in treatment between foreigners and nationals (such as, possibly, ethnic, religious, etc discrimination). It requires a lot of imagination though come up with discrimination which is not caught by the national treatment obligation.

The most recent «model» formulation in the 2004 model US BIT is mostly based on Art. 1102 NAFTA, though it contains an interesting omission. The reference to the «most favourable treatment» in Art. 1103 (3) is gone. This omission is most likely explicable due to the experience of the NAFTA member states in cases such as *Methanex v. US* where respondent states have raised as a defence the fact that other domestic investors were also not treated as well as the «best treated» domestic investor<sup>84</sup>.

It is also useful to have the main text of the comparable GATT and GATS articles readily available:

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<sup>84</sup> 1. Each Party shall accord to investors of the other Party treatment no less favourable than that it accords, in like circumstances, to its own investors with respect to the establishment, acquisition, expansion, management, conduct, operation, and sale or other disposition of investments in its territory.

2. Each Party shall accord to covered investments treatment no less favorable than that it accords, in like circumstances, to investments in its territory of its own investors with respect to the establishment, acquisition, expansion, management, conduct, operation, and sale or other disposition of investments.

3. The treatment to be accorded by a Party under paragraphs 1 and 2 means, with respect to a regional level of government, treatment no less favorable than the treatment accorded, in like circumstances, by that regional level of government to natural persons resident in and enterprises constituted under the laws of other regional levels of government of the Party of which it forms a part, and to their respective investments.



GATT Art. III: 4:

«The products of the territory of any contracting party imported into the territory of any other contracting party shall be accorded treatment no less favourable than that accorded to like products of national origin in respect of all laws, regulations and requirements affecting their internal sale, offering for sale, purchase, transportation, distribution or use.»

Article XVII of the GATS:

«1. In the sectors inscribed in its Schedule, and subject to any conditions and qualifications set out therein, each Member shall accord to services and service suppliers of any other Member, in respect of all measures affecting the supply of services, treatment no less favourable than that it accords to its own like services and service suppliers. 2. A Member may meet the requirement of paragraph 1 by according to services and service suppliers of any other Member, either formally identical treatment or formally different treatment to that it accords to its own like services and service suppliers. 3. Formally identical or formally different treatment shall be considered to be less favourable if it modifies the conditions of competition in favour of services or service suppliers of the Member compared to like services or service suppliers of any other Member.»

There is, we suggest, a link in the formulation of national treatment as it appears in the GATT and GATS and its role in modern investment treaties. This is by no means absolute as there are also clear textual differences in the two divergent strands of international economic law. For one thing, the GATT national treatment formulation has the benefit of a textual direction as to its role in suppressing protectionism in the form of GATT Article III.1. There is no similar guide as to the overall purpose of the national treatment inquiry in the investment treaty context. This absence is largely ignored in the jurisprudence of investment arbitral tribunals that tend on the whole to mechanically attempt to transplant GATT Article III jurisprudence onto national treatment in investment treaties. There remains the unresolved question as to the overall purpose of national treatment in investment treaties. One cannot simply assume the goal should necessarily be the suppression of protectionism (howsoever defined but most likely requiring a pre-condition of competition) as it is equally plausible to conceive national treatment as an inquiry into broader forms of discrimination.

An important point in coming to an understanding on the purpose of national treatment as it applies to foreign investors is the difference when individual investors are exposed as «hostages» to the vagaries of host state economic policy as against the more distant relationship experienced by exporting entities to a importing state. The survey of the perhaps most influential treaty formulations help to be aware of the issues of WTO-to-investment treaties import, but can not resolve it.

## 5. CURRENT INTERPRETATIVE CHALLENGES UNDER INVESTMENT TREATIES

A cursory review of the issues and solutions from cognate areas may be relevant to draw upon pertinent issues that seem to pose significant interpretative challenges. This list is not exhaustive; life is richer than legal drafting can envisage it and new challenges are therefore likely to emerge over time. The four issues that seem particular pertinent are:

1. The overall structure of national treatment test;
2. The determination of «likeness»;
3. The meaning of the trigger requirement of «less favourable treatment»;
4. Whether and when to justify discrimination for legitimate public policy reasons.

reasons.

Each of these issues will be considered in turn.

### 5.1 Overall structure of National Treatment test

The first step in every discrimination analysis is the search for the appropriate comparison between the domestic business entity and the claimant foreign investor. That search is roughly comparable to the role of «likeness» in the WTO jurisprudence. While it is far from clear that absolutely the same criteria should determine the «likeness» for investors under investment treaties as the «likeness» under the GATT and GATS, it is structurally the first step in the national treatment analysis. The overall structure of the WTO approach has been considered applicable in the joint declaration of both Canada and the US included in the Final Act of the Energy Charter Treaty in 1994<sup>85</sup>:

«For the purposes of assessing the treatment which must be accorded to Investors of other Contracting Parties and their Investments, the circumstances will need to be considered on a case-by-case basis. A comparison between the treatment accorded to Investors of one Contracting Party, or the Investments of Investors of one Contracting Party, and the

Investments or Investors of another Contracting Party, is only valid if it is made between Investors and Investments in *similar circumstances*. In determining whether differential treatment of Investors or Investments is consistent with Article 10, two basic factors must be taken into account.

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<sup>85</sup> Reprinted in: WÄLDE (Ed), 1996, pp. 617, 618. Note that neither the US nor Canada signed or ratified the ECT. The declaration is therefore rather an expression of how two, and one principal, negotiating party understood the meaning of national treatment in 1994.

The first factor is the policy objectives of Contracting Parties in various fields insofar as they are consistent with the principles of non-discrimination set out in Article 10.

*Legitimate policy objectives* may justify differential treatment of foreign Investors or their Investments in order to reflect a dissimilarity of relevant circumstances between those

Investors and Investments and their domestic counterparts<sup>86</sup>. The second factor is the extent to which the measure is motivated by the fact that the relevant Investor or Investment is subject to foreign ownership or under foreign control. A measure *aimed specifically at Investors because they are foreign*, without sufficient countervailing policy reasons consistent with the preceding paragraph, would be contrary to the principles of Article 10. The foreign Investor or Investment would be «in similar circumstances» to domestic Investors and their Investments, and the measure would be contrary to Article 10.»

This statement —reflected in submission by the US and Canada to NAFTA tribunals<sup>87</sup>— is compatible with the general structure of the GATT Articles III and XX test which essentially requires:

Determination of «likeness» —for which claimant bears burden of proof;

Determination of a differentiated treatment —for which claimant also bears burden of proof, and, last

Determination if there are «legitimate policy reasons» which justify such differentiation —for which the respondent government bears the burden of proof<sup>88</sup>.

This three-step test (with its concomitant burden of proof) has been accepted as the basic structure of the national treatment test in a variety of arbitral cases<sup>89</sup>. The difficulty, however, is less with the structure of the test, but rather the legal definition of each of the three steps and their application to a specific factual situation.

The basic structure of the discrimination test and the burden of proof allocation rather reflects the way any lawyer —or reasonable person— will

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<sup>86</sup> It continues: «For example, the objective of ensuring the integrity of a country's financial system would justify reasonable prudential measures with respect to foreign Investors or Investments, where such measures would be unnecessary to ensure the attainment of the same objectives insofar as domestic Investors or Investments are concerned. Those foreign Investors or their Investments would thus not be «in similar circumstances» to domestic Investors or their Investments. Thus, even if such a measure accorded differential treatment, it would not be contrary to Article 10».

<sup>87</sup> <www.naftaclaims.com>.

<sup>88</sup> See also: T. WEILER (2004).

<sup>89</sup> Nykomb v. Latvia, 2003; Myers v. Canada, 2001; Feldman Karpa v. Mexico (2002); has it also been used in Occidental v. Peru.

approach a claim of discrimination. It is likely to be found in international and national law (customary, human rights) instruments on discrimination (ethnic, political, religious, gender, sexual). While there is sometimes a reference a «detailed, fact-based investigation», a mere reference to an in-depth factual examination does not by itself solve the underlying problems. While it is often useful to have a wide factual understanding, one needs legal criteria to understand which facts may be relevant and how they should be weighed. A direction to a simple factual investigation without guiding principles merely camouflages the wish to give the arbitral tribunal wide discretion to decide subjectively what constitutes discrimination.

The most difficult question is that of determining whether the foreign investor is treated differently and worse *because* it is foreign. Respondent governments—as the three NAFTA governments or the joint US/Canadian declaration to Art. 10 of the ECT— will prefer such a more limitative approach. This suggests as a condition for breach the existence of a subjective element underlying the incriminated government measure. Different treatment in turn would not be a breach if it were motivated by other factors, for example, that the investor brought the disadvantages on himself by unlucky or unskilful ways of interaction with government agencies. Inexperienced and unskilful foreign investors will probably often get a worse deal simply because they have not mastered the skill of domestic government relations. Lack of investor skills in government relations management should not normally constitute a breach by the government of its non-discrimination duty—except if there is some duty to assist, or at least clarify, to the investor what government policies are— an element of transparency and good-faith obligation one finds in a number of recent cases dealing with legitimate expectations of the investor<sup>90</sup>.

Yet, any requirement of subjective factors such as intent is usually hard if not impossible to prove. Government officials may publicly or privately be heard to express negative opinions about foreign investors in general or a specific foreign company. Politicians will frequently engage in foreigner-bashing to attract instinctive anti-alien sentiment prevailing in every society or they may express sympathy with local interests (companies, trade unions) to secure their support<sup>91</sup>. Such public utterances do not necessarily mean that the conduct was truly motivated by an anti-foreigner sentiment as it may have been purely for

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<sup>90</sup> Metalclad v. Mexico; Tecmed v. Mexico; Waste Management II v. Mexico; Occidental v. Peru; MTD v. Chile;

<sup>91</sup> E.g. the well demonstrated Canadian environment minister's public support for anti-US-investor regulations in the Myers v. Canada case — «Canadian business for Canadians», the «buy America» formal policies in the ADF case or the support to ethanol in its competition for methanol «bought»

public consumption. On the other hand, the absence of a «smoking anti-foreigner gun» may not indicate that discrimination of foreign investors and helping domestic investors was not at the heart of the design of government policy. It may just have been designed, implemented and camouflaged more skilfully. Hidden discrimination will as a rule not be publicly explained as such nor be found in explicit rules, but rather in the way the rules are applied. Focusing the national treatment simply on unskilful discrimination and immunising more skilful discrimination therefore makes little sense. That would mean catching the fool and letting the cunning escape. The adage: «Ye shall recognize them by their fruits»<sup>92</sup> —and not by their words and pretensions— should therefore guide the interpretation.

## 5.2 Likeness

The first step in the examination of discrimination —favouring of domestic businesses as compared to the claiming foreign investor— is to ascertain «likeness». As the claimant is individually defined, it is a matter of identifying domestic companies (investors) that can and should be compared<sup>93</sup>. Everything in life can be compared depending on the criteria («comparators») used. The choice of the relevant criteria to define what can be compared is the key methodological issue which usually will determine the outcome of a national treatment case. If advocates or tribunals wish to achieve a certain result for whatever reason, they will manipulate the criteria for comparison so they yield the desired result. It is therefore essential to define what the relevant comparator should be.

As a starting point, one aspect of the «likeness» or «similarity» standard should be noted. There is no requirement as was contained in the draft UN Code of Conduct of investors being in an «identical» situation. At most «likeness»<sup>94</sup> suggests a similarity, an easy comparability with respect to major qualities of a situation or a person. Various dispute settlement bodies have shrunk from making explicit the choice of comparability criteria by relying on what appears as an automatic, mechanistic application of «likeness», devoid of subjective judgement. This for

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by ethanol producer Archer Daniels through campaign contributions to the governor of California in the *Methanex v. US* case.

<sup>92</sup> Sermon of the Mount, Bible, Matthew 7:16.

<sup>93</sup> They are sometimes named «comparators», though a technically more correct terminology would be to talk of «compared» domestic investors, with comparators meaning the criteria on which the comparison is to take place.

<sup>94</sup> «Similar, nearly equal in any respect, resembling», are mentioned (Chambers dictionary), though «identical» is also mentioned. Our sense, however, is that «likeness» is not «identical» with «identical».

example can on one view be seen in the GATT Article III jurisprudence. GATT and later WTO dispute settlement organs have historically taken a market-based approach to the question of «like products» by emphasizing factors that indicate a competitive relationship between the imported and domestic product in the domestic market-place. Factors such as physical similarities, common end-uses and consumer tastes and habits have been historically been taken as probative of this relationship<sup>95</sup>. The blunt, market-based approach to likeness in the context of GATT Article III has been heavily criticized<sup>96</sup>; it does, though, have advantages: A product that is physical very similar on most counts is most likely to be «like» and has an immediate persuasion effect through plausibility.

It is not however easy to simply adapt the GATT approach that emphasizes certain physical similarities between products to the comparison between a foreign and one or several domestic investors. There may be certain «objective» characteristics that tend to be seen by observers with familiarity of a certain industry as making two investors (or «investment operations») as similar enough. For example, in the *Nykomb v. Latvia* case, a foreign-owned, modern electricity co-generation plant was seen by the tribunal as sufficiently similar to Latvian-owned co-generation plants with a similar production capacity, similar technology and built in a similar time period (2-3 years) based on incentives derived from the same law. These plants were not «identical»: the colour, an undoubtedly here irrelevant criterium, might have been different; the location was different (which is likely to have been a factor on competition between the plants), but for the tribunal the very tangible characteristic of «co-generation», together with the criterium of «similar time period» and the legal-financial criterium of being based on incentives in the same law were enough to assume «likeness» —and thus allow a comparison of treatment between the foreign-owned and the domestically owned plants. The *Nykomb* tribunal did not engage in the next test— was there direct substitutability and competition (probably not since the state energy monopoly was the only possible purchaser and was under a purchase obligation) nor did it look for a specific, to be proved «protectionist» or «discriminatory» intent;

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<sup>95</sup> These criteria pre-date the establishment of the WTO and are drawn from a GATT working party on border tax adjustment. Working Party Report, Border Tax Adjustments, BISD 18S/97, 2 December 1970. For specific WTO cases that have affirmed the relevance of these criteria (and reacted against broader criteria such as regulatory purpose), see *Japan-Taxes on Alcoholic Beverages*, Report of the Appellate Body, WT/DS8/AB/R, WT/DS10/AB/R, WT/DS11/AB/R, Oct. 4, 1996 and *Chile-Taxes on Alcoholic Beverages*, Report of the Appellate Body, WT/DS87/AB/R, WT/DS110/AB/R, Dec. 13, 1999.

<sup>96</sup> See, e.g., Donald REGAN, *Regulatory Purpose and «Like Products» in Article III.4 of the GATT* (With Additional Remarks on Article III.2), in 36 (3) J. WORLD TRADE 443 (2002); HOWSE & TUERK (2006); REGAN (2003); VERHOOSSEL (2002).

reasonably so, as such intent is hard to prove and if it exists it rather indicates clumsiness on the part of the governmental designers and commercial lobbyists for a privileging measure than anything else. The physical or rather «industry» and «technical characteristics» approach is therefore likely to stay, and perhaps constitutes the base point and the most plausible method of defining «likeness». One should not succumb too easily to professorial sophistication over allegedly too «literal» and «simplistic» adjudicators. It is a method that has a persuasive, presentational and intuitive advantage over more complex methods and thus also serves for external legitimating. When it looks similar to a reasonably industry-trained eye, it may well be similar.

It is worth recalling that ultimately much of the GATT Article III jurisprudence has turned on whether the imported and domestic product are in a competitive relationship<sup>97</sup>. Products that may be quite different in physical characteristics (colour, material, shape, production process, use) may be in direct competition to each other. The boundary of the «competition area» is not a sharp bright line, but rather a gradual greying until competition is rather potential and its effect increasingly weaker. Consumer preferences —their readiness to buy rather motorcycles than scooters if price and convenience change— are relied upon in such a competition analysis. The method seems very similar to the «relevant market» definition of competition law, in particular for the concept of «abuse of a dominant position» and for measuring the anti-competitive impact of mergers<sup>98</sup>. Elements such as price convergence, constraints of one product's terms on the sales of another, geographic dimension, demand substitution, reactions of customers and «potential» competition with low barriers of entry play here a role. However, can one just transfer this method from trade and competition law to investment treaties? The Energy Charter treaty considers the promotion of workable, regulated competition as one of its objectives (Preamble, Art. 6). Similar, the NAFTA (Preamble, Art. 102) include as their general objectives «fair competition» and «competitiveness». Given the link between market economy, liberalisation and economic progress on one hand and competition on the other, it is therefore legitimate to link investment treaties with the goal

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<sup>97</sup> Consider the Appellate Body's perspective on interpreting «like products» in the context of GATT Article III.4: Likeness is viewed as «fundamentally, a determination about the nature and extent of a competitive relationship between and among products». European Communities -Measures Affecting Asbestos and Asbestos-Containing Products, Report of the Appellate Body, WT/DS135/AB/R, March 12, 2001, para 99. In Asbestos, the Appellate Body considers the health risks associated with carcinogenic asbestos fibers as probative of likeness not as a separate criterion (such the regulatory purpose underlying the product distinction with non-asbestos substitutes such as the protection of health) but within the prism of the physical properties of such fibers. See *para* 114.

<sup>98</sup> FAULL/NIKPAY (1999).

of competition. Interference by government in the free play of competition on the side of the domestic investor is therefore something that should fall properly under the non-discrimination rule. This is even more so as the black-box collusion between government and powerful domestic business —on a national or local level— creates considerable competitive handicaps for a foreign investor not part of the «in-group» and thus can severely restrict competition, and indeed does so<sup>99</sup>. There is therefore nothing intrinsically wrong to adopt a market-based approach that focuses on the competitive relationship between market participants rather than simply their output in products and services.

Companies do, however, not compete only with their «products» and «services» in a defined market; they also compete in a much wider sense for «business opportunities» and criteria of commercial strength: sales, profits, strategic position. This competition seems not covered in a traditional competition law analysis nor in a WTO-derived analysis of competition not between companies, but between products and services. A company that is helped here by friends in government and politics to win and develop profitably new opportunities may not compete from the start with the foreign company with the same or even substitutable products and services, but rather gain entry to new businesses. That situation is not captured in WTO law and its relevance in competition law still needs to be examined more closely. A company that can move from one business to acquire another will generate profits and loyalties (politics, civil servants, trade unions, employees) that a foreign company without such influence assets can not obtain. As a result, the competition in the market that could develop —putting competitive pressure on local companies to improve their pure commercial competencies and to provide goods and services of greater quality at lower price to local consumers— does not develop. In consequence, the investment treaty concept of «competitive markets» has to be much wider, and appropriate for the competition for new business opportunities between foreign and domestic firms in cahoots with the government apparatus, other influential domestic social forces and monopoly-like situations. «Likeness» should here be assumed when a foreign company meets opposition from domestic companies in the contest for business opportunities. This is at present a rather tentative conclusion as we have neither seen research nor precedents that discuss the competition for business opportunities rather than simply in the traditional competition and WTO prism the competition between goods and services. What I suggest here is a more «holistic» concept of competitive relationship and likeness, and one

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<sup>99</sup> *Financial Times*, 9 or so May 2005: «Slovenia prevents foreign supermarkets to enter to protect influential local supermarket group».



that reflects more closely the way business is carried out in societies with a close intermingling of business and politics<sup>100</sup>.

«Likeness» may also not be limited—as in WTO jurisprudence—to situations where there is a competition of any sort between the foreign and domestic companies. In *Nykomb v. Latvia*, for example, the better treated domestic co-generators were not in competition with Nykomb. All co-generators supplied power to the state monopoly which was under a purchase commitment. Nor was there any particular indication of a «competition for business opportunities», at least not in a more direct sense. The tribunal, without further analysis, relied mainly on the test of «industrial comparability»—co-generation, similar capacity, similar period of construction, similar or identical incentives based on the same law. The rationale underlying such reasoning was not that the government measure (i.e. state energy monopoly's refusal to honour special tariff commitment) interfered in the competitive relationship between the co-generators and buyers (i.e. where buyers and sellers meet), but rather that there was no good reason for the state enterprise in a monopoly position not to honour the government's special promotional tariff promise. This was especially the case given that it did in the end honour a similar promise towards local companies. In *Feldman v. Mexico*, the tribunal did not rely on the competition-interference analysis, but saw two companies in essentially the same business: A domestic company with very influential Mexican businessmen on board, and a smallish foreign company, both engaged in cigarette re-sale and exporting. It is possible, but not certain that denial of tax rebates and tax audit harassment of Feldman might have increased the relative cigarettes export share of its Mexican competitor. However, for the tribunal, the essential similarity was not the competition between the two, but rather that in industry terms both were engaged in the same business so that a different treatment was hard to justify on purely objective grounds. In *Occidental v. Peru*, again, there was no competition between Ecuadorean oil producers and Ecuadorean flower producers; the tribunal here jumped over the industrial sector boundaries<sup>101</sup>; it found that the flower exporters tax rebate should also be available to oil exporters.

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<sup>100</sup> HOFFMAN (2003); there relationships between business and politics everywhere (note the well discussed relationships between US presidents and the US/Texas oil industry), but I suggest that in developing and transition countries such relationship is often more close and inevitable while businesses in developed countries can operate in many (though not all) industries with a greater distance and detachment from the political process in normal times.

<sup>101</sup> Which is in itself problematic — see the OECD *National Treatment for Foreign-Controlled Enterprises* 22 (1993) which suggests that «likeness» can only be established within the same industrial sector.

One can envisage situations where companies can be legitimately compared even across sectoral boundaries, that is, when one sector is predominantly foreign-owned and the preferred sector predominantly locally owned. Here, the design of the measure suggests that investors get a worse deal because they are foreigners. Indeed, objective indications of a discriminatory targeting of foreign businesses are inferable from the way rules are designed and implemented and as such, can be used to link companies even from different sectors into a «likeness» comparability. That likeness does not necessarily require a competitive context can also be supported by traditional international law on discrimination. A competitive context may allow with greater ease to pinpoint discrimination as a way to help always supportive local friends against foreign competition, but it is not necessary: Racial, ethnic and other types of discrimination do not require a context of business competition (though it sometimes exists and usually intensifies pressures for discrimination<sup>102</sup>).

An unresolved issue is the right domestic comparator: Is it the «best treated» domestic company<sup>103</sup>, is it the «worst treated» domestic company or is it some average of treatment meted out by the host state to its domestic companies. It will be normal that some domestic companies have much less trouble of «capturing» politics and bureaucracy, usually if they can exercise significant capturing power — local politics, links with politicians and bureaucrats, outright bribery or influence through substantial and well-placed financial contributions<sup>104</sup>. Each country and culture has its own ways by which businesses can exercise political and regulatory influence, by campaign contributions, by bribery, by close personal, educational and institutional ties, by employment

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<sup>102</sup> On this in particular: CHUA (2002), on the stoking of ethnic hatred leading to governmental capture and discrimination against commercially successful and visible ethnic minorities and foreigners.

<sup>103</sup> WEILER, in: WEILER (Ed), 2003 with a discussion of the treatment of this issue in Myers, Pope-Talbot and other NAFTA cases.

<sup>104</sup> The Methanex v. US final award —dismissing the claim— discussed the implication of Methanex competitor Archer Daniels making 300 000+ \$ contribution to governor Davis of California before he issued the Californian pro-ethanol and anti-methanol regulation. In essence, the tribunal considered that a meeting between the governor and Archer Daniels was —as per the testimony of its participant— not suspect and that the history of the making of the regulation was transparent enough to suggest it was a bona-fide environmental regulation. The tribunal's award is consistent with general arbitration practice in terms of inferring certain conduct (my black-box theory) by drawing «lines» between «dots» —see POLKINGHORNE, in TDM, 2005. The Methanex tribunal: «The tribunal is not averse to trying to «connect the dots» as a way of testing Methanex's hypothesis», and: «inference is an appropriate mode of decision in circumstances in which firmer evidence is not available» (Part III, B, *para.* 57). Possibly and arguably, it may be used as a precedent for a required higher threshold of proof of bribery as it was ready to accept the Archer Daniels executives' testimony at their face-value.

of people close associated with government staff or employment of government staff during or after their public service tenure. Differences within a host state will therefore be frequent; this is even more so where, as again is normal, local political-administrative-business collusion operate against any newcomer, be it from another city, province, state or country. The *Feldman v. Mexico* tribunal, dealing with in the main only one domestic comparator, chose the «best» treated domestic business as comparator. The OECD and UNCTAD<sup>105</sup> identify the issue, but seem to leave it open (or vary their positions over the years). Under the NAFTA, Art. 1102 (3) provide a in our eyes clear solution: In case the relevant conduct emanates from a sub national authority, the country owes « the most favourable treatment» which strongly suggests it is the best treated investor, not the worst and not an average that is the right comparator. A country's responsibility under international treaties for the conduct of autonomous sometimes less<sup>106</sup> than for the conduct of the government's central institutions. If in case of a subnational body's conduct the best-treated investor (presumably an in-state company with influence over that federated state's policies) is the comparator, then that principle must apply to the same extent, or even more, for central government conduct<sup>107</sup>.

To sum up, there is a core of likeness which is relatively easy to grasp: different treatment of what are essentially highly comparable companies in the same industrial sector operating under highly similar conditions, investors engaged in a competitive race for new business opportunities and companies engaged in direct competition in the relevant market. But likeness can also exist across sectoral borders, in particular when the differentiation of treatment seems to be characterized by anti-foreigner sentiment, by attitudes that are usually considered in other areas of anti-discrimination law as unacceptable. One should never forget, as lawyers often do when digging themselves deep into the mountains of a complex legal text, the purpose of the national treatment discipline. It is to increase the quality of governance and thereby attract investment (in the end

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<sup>105</sup> OECD, Mid-Term Report on the 1976 Declaration and Decisions Annex v. (1982) at p. 58; the subsequent OECD report *National Treatment for Foreign-Controlled Enterprises* 22 (1993) avoids dealing with the issue. I am grateful to Juergen Kurtz, Hague Academy Report, 2006, forthcoming, for calling this to my attention. UNCTAD, 1999, p. 33 seems to favor the interpretation that it is the one «best-treated» foreign investors that is relevant for the comparison: «it may be presumed that the comparable treatment should be with the best treated out-of-state» United States investor, otherwise the treatment would be «less favorable».

<sup>106</sup> For example, the ECT provides for a defendant state option to pay only financial compensation for justified claims based on subnational misconduct, art. 26 (8) ECT;

<sup>107</sup> I can not follow UNCTAD, 1999, p. 33 which reads art. 1102 (3) of the NAFTA to allow «for differential treatment as between different out-of-sub-division investors of the host country».

both foreign and national). If a differentiation even across industry sectors would be seen as unacceptable in the major legal systems of economically successful countries, then it would make sense to apply the same yardstick —developed out of comparative law in the «successful and well governed economies»<sup>108</sup>— to countries signing up to a higher standard of governance quality precisely to attract companies from such countries.

The «likeness» test —though embedded in the three-tier structure of likeness, differentiation, justification— can not be mechanically and sequentially applied without taking the type of differentiation and the justification available into account. The three categories are inter-related. While lawyers tend to operate in categories that are completely distinct from each other, like filling one formula item without attention to how the previous item was filled out, there is an inextricable link between the three categories and, we suggest, even the remedies following the breach. The farther away from manifest likeness and the more into the grey zone, the higher the requirements for a clear showing of substantial differentiation of treatment and for an absence of any reasonable justification. The more blatant a finding for the claimant in one element of the test, the lower the threshold in the other elements, and vice versa. On the other hand, the more explicit, direct, with indications of intentionality both likeness and different treatment, the higher the threshold for necessary justification. The same relationship of proportion between severity of the breach and extent of remedies can be proposed. It is far from unheard in international law that the more severe, visible and unjustified breach leads to more stringent sanctions<sup>109</sup>.

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<sup>108</sup> Perhaps a revival of the concept of «civilized nations» of the ICJ statute, see *supra*. I have suggested in another study (Hague Academy 2004 report, forthcoming in 2006, preliminary version on TDM 2005) that the now somewhat embarrassing concept of «civilized nations» is being reborn (e.g. in the US model BIT of 2004's reference to «principal legal systems of the world» and essentially denotes today general and recognized forms of quality governance as identifiable from reasonably similar state practice in the area of economic regulation.

<sup>109</sup> For example, there have been precedents and suggestions that expropriation which is not only without compensation, but discriminatory and against previous stabilization promises should result in a higher level of compensation. Punitive practices are as a rule implicitly or explicitly not accepted (art. 1135 (3) of the NAFTA). But de facto, given the discretion in assessing damages and the usual valuation ranges which can not be managed without discretion, it is likely that arbitral tribunals will, consciously or not, apply penalization elements in determining compensation, for example in the case of breaches that are egregious and «shocking» rather than more of a technical character. See here my ILA report 2005 (*op. cit*) and B. SABAHI, Hague 2004 Research Seminar, forthcoming in 2006.

### 5.3 Different Treatment

The second step in the national treatment test is that there must be different and more unfavourable treatment for the foreign investor. Again, one needs to realize that the three steps in the standard national treatment test are not distinct, but inter-related. Tribunals in looking from facts to law and from law to the facts will be influenced by their determination of likeness when examining if companies in a «like» situation are treated differently, and they will already take into account what they see in terms of different treatment when they carry out the «likeness» test.

As in the stage of «likeness» determination, a tribunal will have the challenge to identify the criteria for determining which element of state conduct towards the compared domestic investor(s) and foreign investor is relevant and which is not. The selection of the criteria is decisive for the outcome. The two «like» cases will always be treated in some way similarly and in other ways dissimilarly. In investment cases, with businesses—and not products or services—being compared, there will be more differences. It is very hard, if not impossible, to develop an objective or quantitative approach for determining mechanistically which different treatment is relevant and which is not. The discretion for tribunals in investment cases is therefore considerably larger than in WTO situations. I suggest that in practice tribunals will mostly or always take a holistic view, and then fit their overall approach into the way they select those criteria of differentiation

As in the «likeness» examination, the test is much more complex than in conventional national treatment analysis under the WTO, in particular for internal taxes. In the case of taxes, it should be possible to calculate the financial impact of tax regimes on domestic as against imported products for a number of standard scenarios even if the tax rules are different<sup>110</sup>. But in the case of investment disputes, the first task is to define which elements of governmental conduct need to be compared. First, if the foreign and domestic investors, are involved in actual competition then the well-developed criteria in comparative competition law and WTO jurisprudence<sup>111</sup> might provide guidance. The first level of relevant government conduct should consist of trade regulation as in the *Pope-Talbot v. Canada* claim and the *Myers v. Canada* NAFTA award.

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<sup>110</sup> This has Art III (1) of the GATT: «The contracting parties recognize that internal taxes and other internal charges, and laws, regulations and requirements affecting the internal sale, offering for sale, purchase, transportation, distribution or use of products, and internal quantitative regulations requiring the mixture, processing or use of products in specified amounts or proportions, should not be applied to imported or domestic products so as to afford protection to domestic production.

<sup>111</sup> FAULL-NIKPAY (1999).

It is not overly difficult to identify such regulation. A claim by an investor will indicate the likelihood that such regulation affects the investor's competitive equality. What is, however, much more difficult is to find out if the same GATT tests —affecting the competitive ability of products and services— can also apply to investors. Investors have made their investment and are therefore exposed much more than exporters to a host state particularly if regulations change, thus springing a surprise on the investor. Of course, investors can and have to assess investment conditions with due diligence before investing<sup>112</sup>. It is especially damaging to a foreign investor if a regulation —and even more so the application— changes after it has made its move into the country and the domestic investors mobilizes its friends in politics and public administration to defend its position. It seems what is most problematic for investors is de-facto administrative conduct. Transparent regulations can be assessed with normal due diligence. It is much more difficult to ascertain beforehand how a regulation or tax rule will be applied in practice. Even the best due diligence, including close consultation with local experts on factual practices will rarely reveal how administrative and tax practices change once domestic companies in an entrenched position face competition and react by activating their political leverage. Such domestic companies will inevitably lean towards using their better links to the state to develop administrative protection rather than formal, easily identifiable and visible regulatory protection. It is a regular feature of discrimination claim that the interpretation and administration of the law changes, rather than that the law is changed<sup>113</sup>. It is for these reason that the examination of national treatment is likely to have to be much more fact-intensive in investment disputes than in trade disputes<sup>114</sup>. Such greater fact-intensity makes the dispute more costly, harder to predict, but it also gives the tribunal much more subjective discretion in fact selection and fact weighing.

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<sup>112</sup> Note, for example, the *MTD v. Chile* ICSID award where the tribunal sanctioned what it considered as insufficient due diligence by in effect halving the compensation due.

<sup>113</sup> For example, in the disputes between Russian oil company Yukos and the government of Russia, the complaints did not relate to a change in the law, but a change in the interpretation of tax law (from a formal to a substantive approach), the composition and political control of the relevant courts and administrative services and the non-application of the law (as re-interpreted) to other companies in a similar position as Yukos contrasted with a most rigorous, efficient and lightning-like application of the law, judicial, administrative and tax procedures to Yukos, see report by the rapporteur for the Parliamentary Assembly of the Council of Europe, Leutheusser-Schnarrenberger, [http://assembly.coe.int/EMB\\_NewsView.asp?ID=592](http://assembly.coe.int/EMB_NewsView.asp?ID=592).

<sup>114</sup> The over 300 pages of the *Methanex v. US* award illustrate this —required— approach though in *Methanex* the issue was a publicly available regulation, rather than a particular way law is applied in practice.

National treatment in investment law can, as we have seen earlier, go beyond a situation of impact on competitive conditions. This is especially pertinent in situations where the government visibly or surreptitiously helps domestic companies to prevail over foreign investors—even if not direct competitors in classical «relevant market analysis». Governmental regulatory and licensing rules—and in particular their actual conduct—can take the form of demanding foreign companies to overcome a much higher threshold of requirements be they information, disclosure, financial securities, technical quality, environmental and health safety—than is required, in law or in fact, from domestic companies<sup>115</sup>. In the *Nykomb v. Latvia* case, without any direct competition, the tribunal considered that the state energy monopoly discriminated against a Swedish co-generator because it paid (though reluctantly and compelled by the national courts) a promised incentive tariff to Latvian co-generators, but not to the foreign one. It was influenced here by the fact that the foreign investors had a «double tariff» contractual commitment which the domestic courts had validated in disputes between the state energy monopoly and local co-generators; it did not consider the foreign co-generator should have lost treaty protection because it preferred to have recourse to an international treaty (ECT) rather than to local courts. In *Feldman v. Mexico* and *Occidental v. Peru*, the less favorable differentiation consisted in the fact that tax rebates were in practice made available to domestic companies, but not to the foreign investors—though, in the *Occidental* case, outside a context of direct competition. In *Myers v. Canada*—where we have a competitive context—the government used its import regulation powers to obstruct Myers strategy to ship hazardous waste to its geographically closer, but across the border located, environmentally more efficient plant. It tried by using its regulatory and licensing powers to move the business of processing hazardous waste rather to an environmentally less efficient Canadian than a geographically closer and environmentally preferable US plant.

The existing jurisprudence (with some cautious analogy with conventional international law and ECJ jurisprudence) suggests that differentiation in treatment outside a direct competitive context has to be more blatant and associated with unacceptable discriminatory attitudes (such as unfavourable treatment because the investor is a foreigner), even more so if it is also in a group that is discriminated for reasons that are condemned in authoritative human rights instruments—race, religion and origin in particular. It is possible to conceive of a range of types of conduct that reaches from discrimination in a competitive context based on the

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<sup>115</sup> E.g. the Italian Central Bank's (May 11, 2005 *Financial Times*) delaying of a bid by ABN AMRO for the Italian Antonveneto bank in order to favor competing tenders by local banks.

foreign nationality of the investor on one end, and distinct treatment of foreign investors outside competitive contexts, without a reasonable or inferable nexus to the foreign nationality and rather by incidental impact on the other. The question is of how far the reach of the national treatment discipline should go. Lawyers' instincts are based on a binary (yes/no) habit of judgment that attempts to draw a bright line on one point of that particular range. The point of that bright line would depend on the relative integration intensity of the treaty, but also on the intention and effect of the treaty in signalling good governance and investment promotion. Investment-treaty based national treatment has therefore less place in situations where there is little need for investor protection, where the treaty has a high level of integration intensity and where there are no serious issues of good-governance and government misconduct at issue; BIT-based national treatment is not —and not yet— an appropriate legal basis for something close to the wide ranging economic integration jurisprudence of the ECJ or the US Supreme Court<sup>116</sup>. Other ways of providing a more subtle application of the discipline is to require a higher threshold of justification and less far-reaching, more prospective remedies in case of «weaker» cases of discrimination as compared to the more egregious cases.

There is no doubt that the national treatment discipline covers both *de iure*, (explicit, usually regulatory and written-rule based discrimination), but also *de facto* discrimination, (unfavourable differentiation in treatment that is not immediately visible, but has to be inferred from its effects). That has been recognized throughout —in customary international law<sup>117</sup>, WTO law<sup>118</sup>, EU integration law<sup>119</sup> and statements by recent investment tribunals<sup>120</sup>. It would be wrong to consider *de iure* discrimination as more serious than *de facto* discrimination: *De iure* is easier to catch, while *de facto* is more surreptitious, more characteristic of the black-box state-local business collusion and it tends to occur more out of often informal if not secretive ways the state apparatus carries out its action.

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<sup>116</sup> HARTLEY (1994).

<sup>117</sup> McKEAN (1983); MANIRUZZAMAN (1998); see also the dissent in the Oscar Chinn case, see the case study by T. WEILER (2004).

<sup>118</sup> Canada —Certain Measures Affecting the Automotive Industry, WT/DS139/AB/R, WT/DS142/AB/R, 31 May 31, 2000, at para. 78.

<sup>119</sup> EU law, as developed by the ECJ, goes beyond «de-facto discrimination» and covers also «indistinctly applicable rules» provided they obstruct the free movement (for our analogy mainly capital and services) not justified as a necessary and proportional measure by legitimate policy reasons (e.g. public policy, public security and public health), for a recent extended analysis: WEISS & WOOLDRIDGE (2002).

<sup>120</sup> Feldman v. Mexico; in Myers v. Canada, both a discriminatory intent and a discriminatory effect was easily identified. J. Kurtz, in: Hague Academy, forthcoming 2006. Discussion at notes 36-38.



It is recognized that the discriminatory treatment must be in principle «because» of the foreign nationality<sup>121</sup>. In the less integration-intensive world of investment protection treaties the discrimination principle can not be directed by a wide-ranging pro-integration policy as for example by the ECJ; it needs rather to focus on the question if the foreign investor is treated worse because it is foreign (and not because it would enhance economic integration or compensate for the foreign investor's lack of skill and luck in running its business abroad). The problem is to apply this in practice because only rarely will such anti-foreigner motivation become apparent and provable. The Myers-case, where the Canadian Minister of the Environment publicly went about advocating a «Canadian garbage for Canadian business» approach is rare, and will become much more so as awareness of the disciplining effect of investment arbitration sets in. Tribunals have therefore, in cases where a discrimination «because of being foreign» was not apparent (as it was in *Myers v. Canada*), operated a system of presumptions: *Feldman v. Mexico* argued, rightly, that requiring full proof of not only an intention to discriminate, but also «because of the foreign nationality» would invalidate the effectiveness of the national treatment clause<sup>122</sup>. It then operated a reversal of the burden of proof method. Once «likeness» and «different treatment» were shown by claimant, respondent government has to prove that the discrimination is not because of the foreign nationality. That appears to us at this time the correct approach. It broadly mirrors the methodology in WTO and ECJ jurisprudence<sup>123</sup>. Such analogy appears justified because in both of these analogous situations the treaty rules intend to prevent discrimination that is related to the foreign nationality, but which is hard to prove and where the evidence for a subjective intent to discriminate is largely under the control of the defendant state; the control of evidence is in arbitration jurisprudence a reason to reverse the burden of proof and to infer their likely content from claimant's allegation if the respondent does not reveal them<sup>124</sup>. The WTO Appeal Body gave up the

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<sup>121</sup> US/Canada statement on ECT, *supra*; US Canadian position in NAFTA cases, available from [www.naftaclaims.com](http://www.naftaclaims.com); discussion of this in *Feldman v. Mexico*, *para* 169.

<sup>122</sup> *Paras.* 181 ff.

<sup>123</sup> J. KURTZ, 2006, forthcoming, *op. cit.*

<sup>124</sup> *Kalkosch US-Mexican Claims Commission case cited in SANDIFER (1975[1939])*; POLKINGHORNE (2004: 13-16), forthcoming in *Fordham Law Review*. Most recently: *Methanex v. US*, p. 154, *para* 56: «the burden of proof... shifted to Methanex, yet Methanex elected not to call the relevant partners of the unnamed law firm whose testimony might have clarified the issue. The Tribunal is unable to see why these partners could not have testified before it». Similar at p. 155 (*para* 58), the tribunal again draws an inference from the fact that the relevant person «was not called by Methanex as a witness... was made aware of these proceedings and could have testified, Methanex provided no satisfactory explanation for his absence as a witness».

requirement of a subjective intention («aims and effect test») to discriminate and replaced this —always hard to prove criterium— with the requirement that there be an «objective design» that can be inferred from the architecture of the measure<sup>125</sup>. This «objective design» does not seem that different from the way the Feldman–Mexico tribunal dealt with the requirement that the discrimination be related to the investor’s foreign nationality.

«Treatment» also means in essence conduct by the state (including all state organs, including sub national governments, independent regulatory and licensing agencies and the judicial system<sup>126</sup>. The conduct of the state must be reasonably directly relate to both the foreign and domestic investor; jurisprudence is here not quite developed<sup>127</sup>. But the requirement that the discrimination must in principle relate to the foreign nationality of the investor suggests that a discriminatory impact that is not a reasonably direct result of the incriminated government conduct is unlikely to have been intended. One also needs as always in investment arbitration a «filtering» or «screening» facility to avoid that investment arbitration becomes recourse for any grievance against the host state and an external appeal for any matter where domestic courts have not satisfied the investor. A particular difficulty arises if the host state’s conduct does not just, in a unilateral direction, affect the domestic and foreign investors as complete passive objects, but if the discriminatory impact emerges out of an interaction between these three key players. In practice, that will be the rule. What if the state asserts, and can prove it, that there was no particular intention to treat the foreign investor less favourably, but that the less favourable situation is in fact due to the foreign investor’s conduct? This might constitute an unsuccessful or clearly ignorant strategy of negotiating with government authorities or an equally luckless and unfortunate litigation strategy? These cases —which are rather the norm than the more theoretical exception— are difficult to disentangle. The foreign investor can not use the national treatment clause to in effect shift a «normal» government relations, licensing and litigation risk to the state via the investment treaty. On the other hand, the black-box operation of the local state-business alliance against foreign intruders tends to work mainly through the way administrative and judicial processes operate. We need more jurisprudence to

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<sup>125</sup> WTO AB in the Asbestos case European Communities-Measures Affecting Asbestos and Asbestos-Containing Products, Report of the Appellate Body, WT/DS135/AB/R, March 12, 2001.

<sup>126</sup> Article 4 of the ILC Articles on State Responsibility, and commentary, published in: J. CRAWFORD, Cambridge University Press 2002.

<sup>127</sup> Through reference to direct and not too remote: MCKEAN, *op. cit.*; Methanex v. US, Jurisdictional award, 2002 at *para.* 138; also WEILER (2004), discussing the directness requirement in the WTO decisions examined.

get a better understanding of how to solve this dilemma. At present, the proper approach seems to be to require the government to prove that a de-facto worse treatment is not due to the nationality of the foreign investor and to raise this threshold as circumstances suggesting the plausibility of collusion between the state and foreign investors become known.

In these cases, the investor should have to prove that there are credible and plausible indicators that somewhere in the administrative and judicial process there was a definitive preference for a local competitor, or a definitive resentment against the foreign investor; upon such proof, the state has then to prove that the administrative and judicial system operated as it normally does and that mishaps that happened have nothing to do with the foreign nationality. This is largely the way the *Feldman v. Mexico* tribunal cut a path through the jungle of internal workings of the Mexican tax administration. It is here that it is difficult to avoid recognising substantial discretion of the tribunal in terms of determining the relevancy of facts and the weight of indicators in one direction or the other. Investors cannot be simply absolved of co-responsibility: While treaties provide in effect a certain measure of «affirmative action» to investors to compensate for their «foreigner handicap», they cannot free the investor from a reasonable due diligence and skill requirements in operating in a foreign context. Definitive under-performance in terms of acquiring the relevant foreign operating skills can either negate the finding of discrimination or it can be taken into account in less blatant cases through reduction of damages because of contributory negligence<sup>128</sup>. An arrogant foreign investor insulting local sensitivities cannot expect to then seek justice from an investment treaty for the expected resentment and bureaucratic and political blockade of its investment proposals. On the other hand, one can not go so far as to expect a foreign investor in the game to become an acceptable local player to adopt practices that are outlawed under domestic and international law, such as bribery. Compelling foreign investors to play exactly like local players—the implication of the «caveat investor» concept sometimes proposed—would undermine the «good-governance» signal to come international economic treaties. It would be incompatible with the objectives of «liberalisation» and «promotion of investment» under principles of «transparency» and «rule of law». How to strike the right balance here, with a realistic appreciation of the implications, has as yet not been thought through at all in the various proposals to enhance the «right to regulate», the due-diligence and «caveat investor» obligations or suggestions to define international treaty obligations in light of domestic conditions. In somewhat simplistic terms: Reducing an internationally anchored and enforceable

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<sup>128</sup> So the *MTD v. Chile* tribunal.

«rule of law» effect in treaties is most likely to result, in practice, in encouraging corruption. Rule of law and corruption (including related, not always illegal methods such as political contributions, patronage and other features of crony capitalism) are alternative approaches to government relations; weakening one means enhancing the relevance of the other<sup>129</sup>.

The unfavourable differentiation must also have a reasonably substantial weight. Investment treaties are not made for minor grievances. The investment arbitral machinery is heavy and should not be activated for minor grievances as they tend to occur in any business. Nor is it meant to avoid «learning costs» that any foreign investor has to accept when entering into an unfamiliar new business context. The national treatment discipline is also not intended to let investors—or counsel—exploit minor discriminations against foreigners on new turf to engage in litigation gambling or to pressure governments to pay-off litigious foreign lawyers in order to avoid arbitral trouble-making. A *de minimis* rule has to apply<sup>130</sup>. Minor bureaucratic obstruction is a business challenge in every place and investment treaties would lose their value if they are not limited to discriminatory government conduct of some seriousness in terms of the incriminated conduct and the impact on the foreign investor. Discrimination is parallel to the other major treaty disciplines: expropriation and fair and equitable treatment. In the case of expropriation—direct or indirect—a very substantial economic impact has to occur which in economic terms at least «deprives» the investor of the investment; in the disciplines under «fair and equitable treatment», «denial of justice», a breach of the «umbrella clause» requiring respect for commitments or the «international minimum standard», minor bureaucratic harassment, difficulty making or putting bureaucratic and judicial roadblocks into the way is not enough. One can argue about how high the threshold of «shocking behaviour» and «glaring misdemeanour» has to be<sup>131</sup> but it has to be substantially higher than a frequently occurring breach of internal procedural rules or otherwise

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<sup>129</sup> I refer here to discussions following the 9 September BIICL Conference in London on the good-faith principle in international law on the OGEMID internet forum, all available and searchable on the OGEMID archive (mainly after September 9 on TDM 2005 ([www.transnational-dispute-management.com](http://www.transnational-dispute-management.com))).

<sup>130</sup> It would be desirable to review arbitral awards in particularly with respect to the national treatment discipline for a *de minimis* principle, though such a principle may have been applied under different labels or in the way the two disciplines are applied. The idea of national conduct in the administration of justice to have to be «shocking» or «egregious»—under the fair and equitable treatment principle, contains already a *de minimis* rule, I. LAIRD, «Betrayal, Shock and Outrage», in: T. WEILER (Ed) (2004: 49-76); SCHREUER (2005: 357). Arguably, this is a general principle of all treaty investment disciplines and not only FET-specific.

<sup>131</sup> Pope-Talbot v. Canada, Award on the Merits; I. Laird, *supra*.

technical illegality. All other investment treaty rules assume a certain threshold for governmental misconduct —intensity of breach, of impact on the investor and scope of injury suffered and this rule of «sufficient substantiality» must also apply to national treatment.

#### 5.4 Justification by legitimate reasons

The third leg in the national treatment test is the justification of what has been proven by the investor as discrimination. It is not absolutely clear that this third step is necessary or allowed. Some authors have suggested in the context of GATT Article III that two products may not be in a «like» situation if the regulator has a legitimate non-protectionist purpose in treating the foreign product differently such as for health and safety reasons<sup>132</sup>. The third leg in the test — justification by legitimate reasons —thereby becomes part of the second part— «likeness». If two products are treated differently, but such difference can be justified, then there are not considered as «like». This approach shifts the burden of proof to the claimant —rather than, as in the standard GATT Article XX justification— to the defendant government. It does seem clear though that the general approach in most analogous sources of precedent (be that customary international law, the WTO and ECJ jurisprudence) is to search instead for a specific legitimate underlying policy reasons which justify a finding of discriminatory difference in treatment<sup>133</sup>.

The reference to «legitimate» reasons which can justify different treatment of investors in otherwise like situations is unavoidable. As the likeness test provides tribunal discretion in terms of selecting the criteria for factual comparison, so the justification test provides an even larger discretionary leeway. The challenge for tribunals is to sort between the many reasons respondent governments will have come up with during the regulatory and administrative process to justify

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<sup>132</sup> REGAN (2002).

<sup>133</sup> Also, for the application of the non-discrimination article under the European Convention on Human Rights (ECHR) in the seminal Belgian Linguistic case, Merits A 6 (1968): «[...] the principle of equality of treatment is violated if the distinction has no reasonable and objective justification. The existence of such a justification must be assessed in relation to the aim and effects of the measure under consideration, regard being had to the principles which normally prevail in democratic societies. A difference of treatment in the exercise of a right... must not only pursue a legitimate aim: art. 14 is likewise violated when it is clearly established that there is no reasonable relationship of proportionality between the means employed and the aim sought to be realised». HARRIS (1995). The ECHR does not focus specifically on discrimination against foreigners, but the authoritative quotation should be seen as describing the standard approach towards discrimination. For the justification of discrimination in EU law of freedom of movement, see WEISS (2002: 82).

the measure. Similarly, tribunals have to distinguish between reasons put forward which are merely and demonstrably pretences to cover other intentions as against the «true causes», the objective policy and if ascertainable the real intentions behind such measures. Not even individual persons have often clear and stable intentions or can distinguish well between what they pretend to themselves about their true intentions and a shifting reality; it is so much more difficult to do this when political, regulatory and administrative processes involving many disjointed organisations and individuals are at issue. Tribunals will therefore prefer to rather lean towards the more «objectified» approach of the WTO Appellate Body which looks less at specific individualized intentions than at the objective design that can be inferred from the architecture of the measure<sup>134</sup>. On the other hand, such an analogy may not be appropriate to the much more individualized situation of a claimant investor: The issue here is as a rule much less of a general regulatory policy affecting a group of trader as WTO law than of governmental policies and specific measures directed against a specific investor. As such conduct can be rather qualified with the perspective of tort law; individualized intentions may therefore be more relevant, in particular in the case of specific administrative measures hitting an individual investor only<sup>135</sup>.

It is important to understand the litigation dynamics of «justification». It is up to the respondent government to assert, in a substantiated way, that there are legitimate reasons for the differentiation and prove any pertinent facts. Respondent governments have in several cases simply failed to do this: in *Nykomb v. Latvia*<sup>136</sup>, the government did not come up with substantiated, detailed and factually proven reasons —e.g. that the other Latvian co-generators had undertaken obligations that were over and above those that Nykomb assumed; that their individual case histories were sufficiently different from Nykomb's or that other factors (e.g. more difficult location; different quid-pro-quo context; availability of subsidies available to Nykomb that were not available to the Latvian co-generators) required, or at least reasonably justified a different treatment. The fact that local courts had repeatedly and consistently

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<sup>134</sup> Compare *Japan-Taxes on Alcoholic Beverages*, Report of the Appellate Body, WT/DS8/AB/R, WT/DS10/AB/R, WT/DS11/AB/R, Oct. 4, 1996, at 28-9 (generally rejecting regulatory intent as the determinative test for breach of Article III.2 (second sentence) but affirming the relevance of objective expressions of intent such as the design and structure) with *Chile-Taxes on Alcoholic Beverages*, Report of the Appellate Body, WT/DS87/AB/R, WT/DS110/AB/R, Dec. 13, 1999, ¶ 41 (affirming such objective evidence of intent as «intensely pertinent» to determining protective application). For a more general analysis of WTO case law: G. Verhoosel, 2002, *op. cit.*

<sup>135</sup> That would also be the consequence of the distinction between WTO and BIT disputes as identified by J. TRACHTMAN, 2002.

<sup>136</sup> Case is published on TDM, with a case comment by WETTERFORS (2005).

answered the legal issue underlying the dispute —the validity of the double-tariff for co-generators promise by the state company— in favour of Latvian co-generators, also increased the weight of the presumption and thus the height of the justification threshold for Latvia. The award thus illustrates the much more complex and wide-ranging consideration of factual elements than in a typical WTO «products» case that may strengthen or weaken the case for a breach of the national treatment. There is no real or even apparent automaticity of the three-level test. In *Feldman v. Mexico*, the government essentially did not come up with a substantiated, detailed and fact-based statement on why the Mexican competitor of Feldman was —clearly— significantly favoured<sup>137</sup>. While the tribunal could not identify —as is normal— a clearly identifiable intention to go after Feldman because it was a foreigner, it found a number of factors that suggested that Feldman's character as a foreign investor and its conduct as a foreign investor (raising a NAFTA Chapter XI claim) could well have been the reason why the Mexican tax authorities singled it out.

Similarly, in the *Myers v. Canada* and *Occidental v. Ecuador* case, the government did not focus on submitting both legal reasoning and factual proof on justification. Perhaps, these cases indicate that the proper way of managing national treatment disputes is at present not yet well established so that respondents focus rather on the «likeness» and other investment treaty defences than on the justification of differentiated treatment. The real reasons for discrimination may be politically too sensitive and potentially embarrassing for the respondent government defence teams to be able to focus properly —as, for example, when the real reason is that powerful local businesses are in cahoots with and have in one form or other captured the administrative agency in charge. Government defence teams may here be under greater de-facto strictures with respect to full advocacy than a private investor claimant.

In WTO jurisprudence, justifications have to be sought primarily within the operation of Art. XX (also XXI) of the GATT. These articles set out a very restricted group of exempted regulatory conditions reflecting the political and economic realities of the late 1940s. A general review of the application of Art. XX and XXI suggests that a measure can in particular be justified if it can be linked to a legal or quasi-legal rule of an authoritative character, either between the parties or of a global nature. In the *Tuna-Dolphin* cases, for example, reasonable compliance with international soft-law rules and guidelines<sup>138</sup> was

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<sup>137</sup> Note *paras.* 168 ff.

<sup>138</sup> On the tuna/dolphin and shrimp/turtle cases: CAMERON & GRAY (2001); *Idem*, in: WARD & BRACK (2000, 2003); international authoritative codes —*Codex Alimentarius*, respected technical

considered to provide a legitimate reason. Such precedent may be helpful for investment claims where a regulation as such is the main cause for the claim. But again, investment arbitration is different: In WTO litigation, there is no specific, already heavily exposed investor interest to protect. In investment arbitration a regulation imposing a differentiated treatment may gain some legitimacy from the fact it constitutes reasonable modern governance practice, but the inquiry has to go deeper: Did the regulation at issue, for example, breach a pre-existing «legitimate expectation» of the investor<sup>139</sup>? Was the enactment of the regulation —or of ensuing administrative conduct— with its discriminatory intention and/or effect an unexpected and not reasonably foreseeable surprise for the foreign investor? That would diminish the force of the legitimate reason. In particular, was the international guideline rather a pretence and was it used to favour a domestic investor —or was the action against the foreign investor and the ensuing advantage conferred on domestic businesses an unavoidable consequence of modernising domestic legislation?

The risk with the defence of «compliance with international rules» is that such rules get misused for protectionist purposes. That is so in particular when the international rules are not very specific and provide discretionary leeway, or when they allow transition periods to protect existing operations from a too sudden reversal of the regulatory framework. The WTO (and ECJ) practice provide some precedent: Under the «chapeau» of Art. XX, there must be a relationship, broadly, of proportionality (least-restrictiveness, necessity)<sup>140</sup> between the legitimate cause and the discriminatory measure. If the discriminatory measure against a foreign investor is out of proportion with the accepted legitimate objective, then the justification effect disappears. This is even more so when the discriminatory measure is imposed in a way that the domestic investors' competitive position is improved —e.g. by selective enforcement or by taking into account habitual non-compliance of domestic businesses or when the discretionary leeway in implementation by regulation and administrative conduct is otherwise biased against the foreign investor. In *Myers v. Canada*, for example, Canada sought

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industry guidelines (e.g. by the American Petroleum Institute or the UK Society of Petroleum Engineers)— can provide the starting point for a careful examination if they provide —true rather than disguised, necessary and proportionate legitimate reasons. See on this also: M. ORELLANA, *The Role of Solid Science in Investment Disputes*, Hague Academy 2006, forthcoming; T. WEILER (2003: 229).

<sup>139</sup> The legitimate expectation concept is also relevant in WTO law: See J. CAMERON (2001); PANIZZON (2005).

<sup>140</sup> From Art. XX of the GATT: «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 [...]».



reliance on international environmental treaties concerning the transportation of hazardous waste; but the tribunal's analysis indicated that such treaties did not require the discriminatory action against Myers and thus were rather used as a pretence and camouflage cover for the discrimination. Proportionality indeed emerges not only in WTO and ECJ jurisprudence<sup>141</sup>, but also in some investment awards as a principle controlling government conduct<sup>142</sup>.

A «legitimate reason» for differentiated treatment is not simply what the tribunal subjective thinks but what the tribunal can identify as proper and legitimate reasons in authoritative instruments, be they treaties, authoritative soft-law guidelines and codes<sup>143</sup> or good-governance practices that can be identified with reasonable comparability to the situation at issue. Human rights treaties and international customary law probably justify a certain element of «affirmative action» in favour of disadvantaged local peoples, minorities or majorities<sup>144</sup> provided the aim is to compensate for existing handicaps, and not to express ethnic (or anti-foreigner) hatred and resentment. Art. 24 (2)(b)(iii) Energy Charter Treaty, for example, provides for the acceptability of «affirmative action» for «socially or economically disadvantaged individuals and groups», but it subjects such affirmative action to a notification requirement and a requirement that «normal domestic investors» bear the same burden. The rule is here that «affirmative action» can justify differentiated treatment, but not only or mainly at the cost of the foreign investor. Such rules are also found in other investment treaties<sup>145</sup>.

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<sup>141</sup> USHER (1998: 37, 55 ff); Sophia Tobler, the standard of judicial review of administrative agencies in the US and EU, 22 BC Int 213 (1999). To quote from the ECHR Bourrimi case: (Bourrimi v. The Netherlands; Application number 5 00028369/95. Date of Judgment: October 3, 2000.

«Under Article 14, a difference in treatment is discriminatory “if it has no objective and reasonable justification, that is if it does not pursue a legitimate aim or if there is not a reasonable relationship of proportionality between the means employed and the aim sought to be realized.” In addition, States “enjoy a margin of appreciation in assessing whether and to what extent differences in otherwise similar situations justify a different treatment”. The Court found that while the protection of other heirs may constitute a legitimate aim, in this case the child's exclusion from his father's inheritance was “disproportionate” and in violation of Article 14 taken in conjunction with Article 8».

<sup>142</sup> Svembalt case: HOBER, OGEL 5-2003, p. 37, 28; Tecmed v. Mexico, *para* 122.

<sup>143</sup> WÄLDE (2004b).

<sup>144</sup> SORNARAJAH (2004) as great advocate, see p. 119 ff. and throughout.

<sup>145</sup> The U.S. model agreement maintains an exception to NT in Annex 2, “Minority Affairs”. The United States reserves the right to adopt or maintain any measure according rights or preferences to socially or economically disadvantaged minorities, including corporations organized under the laws of the State of Alaska in accordance with the Alaska Native Claims Settlement Act.

Uruguay took a similar exception in their recent BIT with the US. Australia took the following reservation in their FTA with the US:

All international courts charged with exercising controls over domestic regulatory powers have recognized their limits: The ECHR and the ECJ have expressed respect for a measure of governmental discretion —both in assessing and developing an image of the regulated factual reality and in fashioning a regulatory policy response. Modern social sciences do not provide a single, uniquely true picture of reality; biases, interests, cultures allow developing multiple pictures of factual realities as the on-going public debate in countries where it is allowed shows. This applies even more to «social engineering»: It is virtually impossible to know what social and economic impact a specific policy measure will have in society, and the longer-term the perspective, the greater the uncertainty. Courts and tribunals are not well equipped to deal with a social-sciences' based assessment of both present reality and the future impact of policies<sup>146</sup>. The «margin of appreciation and policy-making» is therefore a necessary part of controlling governmental policy-making —not dissimilar from judicial restraint and «act of state» doctrines. The exercise of judicial restraint emerges also from a cognate area: The application of EU competition rules (in particular Art. 86) to state-licensed or supported monopolies —primarily a discrimination issue. Here, different treatment can be justified if it is «necessary» to carry out an essential public service function<sup>147</sup>. The ECJ has here as a rule carried out a detailed factual assessment

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Australia reserves the right to adopt or maintain any measure according preferences to any indigenous person or organisation or providing for the favourable treatment of any indigenous person or organisation in relation to acquisition, establishment or operation of any commercial or industrial undertaking in the service sector. Australia reserves the right to adopt or maintain any measure with respect to investment that accords preferences to any indigenous person or organisation or providing for the favourable treatment of any indigenous person or organisation.

Canada, the United States and Mexico have each adopted various reservations to National or MFN Treatment for Aboriginal Affairs or Minority Affairs in Annex II of NAFTA. For example, Canada's reservation reads:

“Canada reserves the right to adopt or maintain any measure denying investors of another Party and their investments, or service providers of another Party, any rights or preferences provided to aboriginal peoples”.

The US reservation is similar, but applies to “socially or economically disadvantaged minorities”. These model treaty amendments reflect US experience with litigation over the direct effect of the US-Japan FCN treaty. See: *Sumitomo v. Avagliano*, 457 US 176 (1982); *Fortino v. Quasar*, 950 F.2d 389 (1991); see also *LASH* (1991).

<sup>146</sup> ECJ, *EU Com v. France*, 1997; US Supreme Court *LINGLE V. CHEVRON U.S. A. INC.* (04-163) 363 F.3d 846, reversed and remanded.

<sup>147</sup> 2. Undertakings entrusted with the operation of services of general economic interest or having the character of a revenue producing monopoly shall be subject to the rules contained in this Treaty, in particular to the rules on competition, insofar as the application of such rules does not obstruct the performance, in law or in fact, of the particular tasks assigned to them. The development of trade must not be affected to such an extent as would be contrary to the interests of the Community.

if the restrictions —typically by a state enterprise favouring its internal services or domestic companies— are «necessary» to achieve the legitimate purpose, but accepting reasonable cause-effect relationships<sup>148</sup>.

If investment claims are largely about the effects of general governmental policies on foreign investors, then such «arbitral restraint» makes perfect sense. On the other hand, if the issue is rather specific conduct of public agencies against individual investors, there is less reason for «arbitral restraint» when facts emerge that indicate that the foreign investor is treated worse than the domestic comparator. The reason here is that for general policy the presumption should be rather for arbitral/judicial restraint with respect to policy-making, but for the specific case of an investor directly affected by administrative action, the presumption should rather be for taking a close look at what happened and comes out of the «black-box» of government-domestic-business collusion against the foreign newcomer.

A very difficult issue is to square domestic judicial-decision making with the national treatment discipline. It has been argued at times in investment claims that discrimination does not exist if the foreign claimant had a full opportunity, untainted by manifest «denial of justice», to litigate his case before domestic courts. Lack of success in that situation before domestic courts is then advocated to constitute either a «justification» or to reject —with equivalent effect— «likeness». There is no doubt that domestic courts in international law have no privileged position: They are part of the state; their conduct is fully attributed to the state under established rules of state responsibility<sup>149</sup>. There is, however, a relationship to be understood with respect to domestic courts: Between the «denial of justice» concept, now considered part of the «fair and equitable treatment» discipline<sup>150</sup> and national treatment. While «denial of justice» is reasonably well established, the application of the national treatment/non-discrimination discipline to domestic courts is so far utterly unexplored and untested. Courts can discriminate against foreign investors in the same way as any government agency can. Such discrimination if it occurs is likely to occur in the same context as discrimination otherwise: Judges are part of the local and national culture, integrated with local and national politics, bureaucrats and

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For jurisprudence on art. 86 (2): Faull/Nikpay; cases: Campus oil (Irish security of supply interest) versus Greek Refinery (no necessity).

<sup>148</sup> Commission Decision on La Poste, EC Official Journal of 23 October 2001; Belgian and Austrian postal/ magazine cases — compare with UPS v. Canada.

<sup>149</sup> Art 4 ILC articles on state responsibility with Commentary, J. CRAWFORD, *op. cit. supra*.

<sup>150</sup> PAULSSON (2005); cases: Loewen v. US.; Azinian v. Mexico; references/obiter in SGS v. Philippines.

business interests. True independence is rare in most developing and transition countries<sup>151</sup>. Only in relatively few jurisdictions with a clear focus on attracting capital and legal business for a competitive local legal services industry is there a relative lack of bias against foreign litigants. A judge's independence and professionalism can not emerge as an isolated personality trait; it must be formed, encouraged and sanctioned by the local legal culture. These factors advocate the application of normal non-discrimination standard to domestic judicial decision-making. On the other hand, there is a habit, perhaps in substance, but certainly in form, of courts and tribunals showing to some extent collegial respect and deference to each other. No judicial or arbitral system is perfect; collegiality hence involves a greater respect than would be shown by tribunals to administrative services of the government. The breach of national treatment is possibly much harder to detect with courts than with administrative agencies: All cases depend on facts and rules which are inevitably linked to subjective selectivity and presentation. Litigation depends everywhere on skills both of a technical and a more cultural-social character. Who is to say —if the court is reasonably competent in presenting its reasoning as objective— if a judgement was made against a foreign litigant because it is foreign —or because the facts, the law, its choice of counsel, of litigation strategy or «Lady Luck» were not favourable enough?

It is interesting to see how tribunals have been coping with these dilemmas. In *Nykomb v. Latvia*, the tribunal seems to have supported its finding of not justified discrimination by pointing out that domestic courts had decided the same issue in favour of domestic investors. The conduct by domestic courts thus gave comfort to the tribunal in its interpretation of domestic law to the extent it was relevant; but it also reinforced the impression that the domestic system —state enterprise, government, regulator, the courts— tended to lean towards the domestic investors. The situation was different in *Azinian v. Mexico*: Here, Mexican courts had rejected all appeals by the US investor for breaches of contract against the Mexican municipality it had contracted with. The tribunal found no indication that there was something biased about these cases —a test much lower than the very high-threshold test of «denial of justice»; also, the investor had not raised any criticism of the domestic courts. In the *Azinian* case, the impression emerges that the tribunal saw its own impression of a legally dubious claim confirmed by its own summary review of the domestic judgments. There

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<sup>151</sup> Jan Paulsson's *Denial of Justice in International Law* provides extensive case material throughout the last 150 years; for a current case: Report for the Council of Europe by Ms Leutheusser-Schnarrenberger on the Yukos affair, *op. cit. supra*.

was, hence, no «cognitive dissonance» between the tribunal and the domestic courts. This made it easy for the tribunal to reject the Azinian claim. In other cases in international arbitration, there was clearly a «cognitive dissonance»: In *Lucchetti v. Peru*, the tribunal, with one arbitrator also present in the earlier Azinian claim, seems to have considered with suspicion domestic judgements in favour of claimant. This made it easier for the tribunal to reject the idea that the dispute had been definitively solved by domestic courts. In the well-known *Hilmarton and Chromalloy cases*<sup>152</sup> a suspicion —short of definitive proof— of dubious integrity of the domestic courts seems to have made it easier for the tribunal to disregard such judgements.

The conclusion to be drawn is that, first, domestic courts are subject to the non-discrimination discipline, though breaches are harder to identify. Second, that the conduct of a state has to be judged in totality —with courts being integral part of the state, though enjoying some greater measure of respect and deference from arbitral tribunals, at least in form. Third, that the judgements of domestic courts are «taken into account» by tribunals when determining if an overall assessment of the government conduct —in law and more importantly in fact— leads to a finding of unjustified discrimination. If there are no plausible indicators that domestic courts were influenced by anti-foreigner bias and if their reasoning strikes a cord with the arbitrators, then tribunals in such situation of «cognitive consonance» are more likely to heed domestic courts. If, however, there are suspicions or a significant divergence in the tribunal's assessment from that of the domestic court, the weight given to domestic courts will be less. There are also practical considerations. Treaty tribunals are not intended to function as another layer of appeal and litigation for investors that have tried their luck with domestic courts and have, without any indication of bias, lost. A credible local court's definition of the applicable law will and should weigh heavily on the tribunal's mind. The threshold of differentiation for the claimant to prove will be higher, and the threshold of justification for the respondent government to prove will be lower if domestic courts have spoken credibly. This quite fluid situation requires from counsel and the tribunal examination of the authority and quality of domestic courts (which will rarely be fully disclosed), of challenges and criticism (if any) by the losing claimant with respect to decisions by domestic courts and of the particular role of the domestic court and its applicable law in the national treatment test. Domestic courts applying discriminatory law will not require much attention;

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<sup>152</sup> *Chromalloy Aeroservices v. Egypt XXII YBCA 1001 (1997)*; *Omnium v. Hilmarton, Rev. Arb 315 (1993)*; See: LEW (2003).

credible domestic courts which validate the application of non-discriminatory legislation will be much more relevant, but their position should not preclude an independent investigation by the tribunal.

In conclusion, precedents from the WTO and EU non-discrimination jurisprudence on the question of justification are of some, but limited value. They suggest lines of inquiry and relevant criteria. But in investment claims, there can not be—and is not—the literal automaticity that is usually claimed by the WTO Appellate Body nor the careful—and politically palatable—dissection of a government measure into legal and illegal components typical for the ECJ. Rather, tribunals have to understand the factual situation of the generally very individualized claimant much better; they do not only adjudicate for the future (as does the WTO system and to a significant extent the EU judicial system), but they adjudicate for the past, to compensate an investor who suffered for—reasonable—miscalculations with respect to government conduct. Standards that are used in other investment disciplines—denial of justice/due process, legitimate expectations, but also required due diligence—legitimately play a much bigger role in investment than in trade cases. Discrimination that is contrary to a legitimate expectation weights much heavier than a different treatment that is linked to a legitimate government reason and was well known or knowable to the investor before undertaking the investment. This is the «protective» dimension of investment protection that is largely absent in trade regulation—with a retrospective rather than an only prospective vision. There is therefore less of a «bright line test»—which is at least pretended to exist by the WTO Appellate Body, than a grey zone where the intensity, severity and proportionality of the difference in treatment, the seriousness of justification and the credible direct link between the discrimination and legitimate reasons and the indications for bias and discriminatory intention have to be weighed. The national treatment for investment claims assessment is therefore much more individualized rather than the generic treatment in the WTO. If the conduct at issue is consonant with good governance standards as they should be applicable to foreign investment under the respective «integration intensity» of the treaty relationship, then justification is more likely. But if the discrimination is blatant and severe, the link to justificatory policy reasons tenuous and the damage done serious, then the finding of breach with sanctions should be the proper response by the tribunal.

## 6. TOWARDS A MORE FLEXIBLE, MODULATED AND SUBTLE HANDLING OF THE NATIONAL TREATMENT DISCIPLINE IN MODERN INVESTMENT TREATIES

The conclusions of this study do not suggest that there is a «bright-line» test for identifying either likeness, different treatment or justification. The national treatment test in investment treaties has some basis in much older treaties and customary international law than WTO or economic integration law. While it is no doubt related to the application in WTO or economic integration law, it is quite distinct as the underlying situation, the remedies and the dispute resolution methods are not at all the same. At most, one can see a similar purpose—liberalisation, gradual (but lower-intensity) economic integration between countries, creation of more level playing fields between competitors—at work. Discrimination in investment dispute has a link with traditional international law and comparative discrimination law in so far as its demand for equality is not only relevant in a situation of competition (for markets, goods, services), but also business opportunities and even access to governmental regulatory, licensing, tax and administrative powers. It also expresses the idea that foreigners, even outside a widely defined competitive context, should not be treated by governments worse because they are foreigners. Lastly, there is an overall good-governance approach inherent in investment treaties: That having external disciplines like non-discrimination is in the end beneficial for a country's governance, first directly with respect to foreign investors, but in the end also in its dealings with its own people.

To bring these approaches to bear through interpretation of quite general treaty rules and application of usually complex factual situations is substantially more difficult than in most WTO situations. The reason is that the comparability between investors («likeness»), the determination of the relevant elements for «different/ discriminatory treatment» and for justification has to take into account many more, and typically qualitative elements than is usually required in WTO disputes. Tribunals are not well equipped for that task though they may struggle valiantly as, for example, in the detailed investigation undertaken by the *Myers v. Canada* tribunal. National treatment analysis in investment claims requires probably a much wider net for facts and criteria for selecting facts as relevant that operates with more tribunal discretion. There are some similarities with more modern WTO or EU integration cases on regulatory non-tariff barriers, services with a longer-term investment component or longer-term movement of capital and services. But none of these analogous situations of international economic law controls can provide a clear solution to the challenges now arising in the only emerging investment treaty jurisprudence on national treatment.

Lawyers use a methodology that splits up a case into distinct elements, each of which is usually examined in a «binary» (yes-no) way and then proceeds sequentially from one condition to the next one. This can lead to substantial risks in terms of the legitimacy of overall results reached when applied in a formalistic and outcome-wise blind way. For example, there may be a positive, but relatively weak finding on likeness; an existing, but not substantial discrimination; some reasons for discrimination but not strong enough to justify the different treatment. If these elements are combined and lead to a massive damages calculation, we can have a situation where the legal foundation is stretched beyond what the treaty intended and what makes sense, in terms of treaty objectives, context and political legitimacy. Most tribunals temper legal rigor with pragmatism and will avoid that situation. But that is not guaranteed—and hard to correct by way of annulment, appeal or judicial review.

The analysis here therefore suggests that in this early stage of discrimination jurisprudence in investment treaties tribunals should be very careful. This not to invite them to shun from making a decision as some think the *Loewen v. US* tribunal has done, but also not to rush into awards with massive damages as some think the *CME v. Czech Republic* tribunal has done. The model of arbitral progress with restraint should rather be the approach underlying one of the most famous US constitutional cases, *Marbury v. Madison*<sup>153</sup>. In this case, the US Supreme Court advanced the later crucial doctrine of judicial and constitutional review over acts of the legislature, but it did not go so far to strike down, for the first time ever, the particular piece of legislation at stake. The same combination of progress with caution will be observable with all of the other influential international courts—the European Court of Justice and the WTO Appeals Body<sup>154</sup>. The way to thus advance boldly and with caution is to take an «integrated», rather than an isolated, step-by-step look at a claim: To align the intensity, scope and impact of the remedy with the level of integration the treaty intends to achieve and, with the overall intensity of a breach. The intensity of a breach should be determined by looking at how self-evident likeness is, how serious and conspicuous the discrimination and how strong or weak the justification. Most senior courts and experienced tribunals will do this anyway—but usually not be explicit about it. Tribunals should therefore not refrain from finding a breach, even if it is not egregious and even if the treaty has a low level of integration intensity; but they should consider responding to low-level breaches carefully. One should therefore try to identify if such breaches could be sanctioned by prospective, rather than retrospective, large-amount damage awards.

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<sup>153</sup> 5 US (1 Cranch) 137 (1803).

<sup>154</sup> BELLO (1996); VAN DEN BROEK (2001).



The main objective should be to encourage the respondent state to work hard to improve its governance quality in particular where the breach occurred, while still providing enough compensatory incentives to investors to bring the case. The more egregious the case, the more should prospective and governance-enhancing remedies be complemented by true and sufficiently serious compensatory remedies. The tribunal should both —as does the WTO Appellate Body and the European Court of Justice, look for justice for the affected claimant, but also towards emitting effective good-governance signals to the respondent state. Breaches of the national treatment discipline that were in the main procedural should be corrected in the main by procedural remedies<sup>155</sup>. This could include obligating the state to re-enact the challenged conduct in a procedurally proper way, with compensatory damages only as a complement and with care not to choose the damages theory which produces the most dramatic outcome. The more a breach is serious, its impact for the investor substantial and not part of normal business risk or remediable and the more there are indications that it targets the foreign investor specifically because of state-domestic business collusion against foreign newcomers, the more prospective, good-governance signalling remedies should be combined with direct compensatory measures. Remedies and compensation should therefore not be determined in isolation after a breach has been found, but they should respond to the nature, impact, target and the target's conduct relating to the breach. Breach of other disciplines —e.g. fair and equitable treatment, minimum standard (in essence a modern minimum good-governance standard), legitimate expectations and due process should count in the ultimate decision on type and scope of remedy—, while excusatory factors —level of development, economic crisis, political upheaval— should equally count. Prospective good-governance signalling should be made as effective as possible, and retroactive damages compensation be as much as is necessary —but without providing an incentive for speculative treaty claims litigation and without providing a no-fault insurance for foreign investor's accidents in a naturally risky business. The tests here developed are therefore not white-black, win-lose standards, but rather a set of balancing criteria for chiaroscuro situations. Nor are they unfamiliar to lawyers: In criminal law, for example, the seriousness of an offense and the weakness of exculpatory factors may not be decisive for the question if an offense has been committed, but they determine for any reasonable court within its discretionary range the weight of the penalty imposed. It is suggested that this approach best describes the implicit practice of enlightened legally competent and politically sensitive international investment arbitration tribunals.

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<sup>155</sup> This proposal is developed in more detail in my IIA report on remedies and compensation; also PAULSSON (2005: 2007 ff.)

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