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by H. Wöss

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Systemic Aspects and the Need for Codification of International Tort Law Standards in Investment Arbitration

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Abstract

International trade and investment law is characterized by two distinct models (the constitutional law model, as espoused by the WTO, and the tort law model) that both represent rules-based approaches to the peaceful settlement of disputes, replacing power diplomacy. In contrast with the development of WTO law that has been developed through the 'authentic' interpretation of rather precise behavioural rules driven and controlled by the contracting parties, standards contained in international investment agreements (IIAs) are the result of a 'dilatory formula compromise', that is, a formal compromise without agreement on its precise content. In this regard, this article underlines the need for legal certainty and predictability with respect to investment law standards in a tort law environment, which can only be achieved through the participation of the contracting parties via codification or authentic interpretation of such standards in order to avoid or remedy legitimacy issues. In particular, this contribution explores the efforts to codify international investment law standards in the Comprehensive Economic and Trade Agreement (CETA) and concludes in this respect that the CETA follows a conservative approach of adopting carefully selected strands of interpretation, together with the reasonable reduction of the scope of MFN to its core function and the abandoning of the umbrella clause. In addition, in spite of several flaws and even if it does not undertake a systemic overhaul, the CETA contributes to system building through the participation of the contracting parties, eliminating some of the excesses of arbitral tribunals caused by interpretations based on a lack of understanding of fundamental concepts of public international and international economic law.

Introduction[1]

International trade and investment law is characterized by two distinct models: the constitutional law model, as espoused by the World Trade Organization (WTO),[2] where the remedy is 'the bringing into conformity of the measure', and the tort law model, where international law standards establish the threshold for remedying delictive behaviour, in

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[1] Herfried Wöss, 'Legitimacy in WTO Law and Investment Arbitration: The Role of The Contracting Parties' (30 March 2015) Columbia FDI Perspective No 144.

[2] Ernst-Ulrich Petersmann, *Constitutional Functions and Constitutional Problems of International Economic Law* (Fribourg University Press 1988).

particular as regards interference in property rights, by damages.[3] Both models represent rules-based approaches to the peaceful settlement of disputes, replacing power diplomacy. They may be considered as the finest examples of the efficient application of rules of international law. Both of these sub-systems of international law are creations of treaties, which serve to control unreasonable political actors and positively affect regulatory governance even on a domestic level.

The development of the former General Agreement on Tariffs and Trade (GATT) and present WTO law has been driven and controlled by the contracting parties, through the rather automatic adoption of panel reports based on rather precise behavioural rules, which leads to an 'authentic' interpretation of such rules by Member States.[4] In contrast, standards contained in international investment agreements (IIAs) are the result of a 'dilatory formula compromise',[5] that is, a formal compromise without agreement on its precise content due to historical reasons, such as the North-South conflict that lasted until the early 1980s. These standards have, until recently, been developed to a large extent through interpretation by arbitral tribunals and scholarly writings, without achieving a sufficient level of precision to provide the legal certainty and predictability required for international tort. Save where codification efforts have been made in recent IIAs or more comprehensive trade and economic agreements, this development occurs without further involvement of the contracting parties, which raises legitimacy issues.[6] The absence of state involvement is also reflected in a rather underdeveloped customary international law with respect to the protection of property.[7] There is no evidence that states were aware, or should have been aware, of the potential widening of the scope of IIAs through the use of Most Favoured Nation (MFN) provisions, especially with regard to jurisdictional and procedural elements of such agreements. For example, IIAs do not contain criteria establishing the threshold for the violation of the Fair and Equitable Treatment standard based on the intensity of regulatory measures interfering with property rights. Nor do IIAs provide guidelines for the proper identification of comparators for discrimination in order to find a violation of the MFN and the National Treatment standards. These factors have a direct impact on the amount of damages to be awarded.

Arbitral awards and scholarly writings have contributed to the development of international law standards in a mostly balanced and increasingly sophisticated manner, though without achieving uniform interpretation. Arbitral awards are at best a subsidiary means of demonstrating rules of international law,[8] and their legal effect is limited to the parties to the arbitration.[9] Scholarly writings are only a subsidiary source of international law.[10] Both

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[3] Hersch Lauterpacht, *Private Law Sources and Analogies of Law* (Longmans 1927) 6; Borzu Sabahi, *Compensation and Restitution in Investor-State Arbitration* (Oxford University Press 2011) 15-42; Herfried Wöss and others, *Damages in International Arbitration under Complex Long-Term Contracts* (Oxford International Arbitration Series) (Oxford University Press 2014) 13-6, 18-9, 223-33, 236-44.

[4] Wolfgang Benedek, *Die Rechtsordnung des GATT aus völkerrechtlicher Sicht / GATT from an International Law Perspective* (Springer 1990) 142.

[5] Carl Schmitt, *Legalität und Legitimität* (Dunker-Humboldt 1932).

[6] Santiago Montt, *State Liability in Investment Treaty Arbitration, Global Constitutional and Administrative Law in the BIT Generation* (Hart Publishing 2012) 146-54.

[7] Martins Paparinskis, *The International Minimum Standard and Fair and Equitable Treatment* (Oxford Monographs in International Law) (Oxford University Press 2013) 171-80, 217-60.

[8] Todd Weiler, *The Interpretation of International Investment Law, Equality, Discrimination and Minimum Standards of Treatment in Historical Context* (Martinus Nijhoff 2013) 53.

[9] Gilbert Guillaume, 'The Use of Precedent by International Judges and Arbitrators' (2011) 2 JIDS 16.

[10] Statute of the International Court of Justice, art 38(1)(d).

arbitral awards and scholarly writings provide content for international law standards used in investment arbitration, but they do not necessarily create legitimacy, which may only be provided by the contracting parties through their treaty-making power, authentic interpretation, or state practice.[11] Legitimacy is an important aspect of fairness.[12]

Whereas it may be contended that, as a matter of legal policy, things should be left as they are,[13] there is a danger that the current investment protection regime will shrivel if it does not progress.

This article underlines the need for legal certainty and predictability with respect to investment law standards in a tort law environment. The author argues that the further development of international investment standards requires the participation of the contracting parties through codification or authentic interpretation of such standards, perhaps based on a uniform understanding or model law, which would also remedy the legitimacy deficit. Finally, the author examines the efforts to codify international investment law standards in the Comprehensive Economic and Trade Agreement (CETA).

1. The Need for Legal Certainty and Predictability in International Tort Law Standards

Investment protection standards are in essence international tort law standards.[14] The violation of those international tort law standards leads to damages in the form of restitution or compensation. The remedy of damages seems to be considerably more intrusive than the fairly soft remedies under the WTO system in the form of 'bringing into conformity of the measure' with mere prospective effects. There is a direct correlation between the intensity of the remedy and the requirement of certainty in the formulation of norms or standards of protection involved in establishing the threshold for delictive behaviour. As the intensity of the remedy increases so does the requirement of certainty, with the highest level of legal certainty being required in criminal law under the Roman law maxim of *nulla poena sine lege (no penalty without a law)*.[15]

The absence of the contracting parties in the development of investment treaty standards leads to legitimacy issues, which derive from the need for primary rules providing for legal certainty and predictability in international law standards, with respect to both content and form. In the absence of a sufficiently developed customary law of protection of property, the present situation may only be remedied through codification of treaty standards or authentic interpretation implementing greater specificity.

Assuming the proper application of methods established in customary international law for the analysis of damages related to income-generating assets or investments, the precision or

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[11] Wolfram Karl, *Vertrag und spätere Praxis im Völkerrecht / Treaty and Subsequent Practice in International Law* (Springer 1983).
[12] Thomas M Franck, 'Fairness in the International Legal and Institutional System' (1993) 240 Recueil de cours de l'Académie de La Haye 26.
[13] Charles N Brower and Sadie Blanchard, 'What's in a Meme? The Truth about Investor-State Arbitration: Why It Need Not, and Must Not Be Repossessed by States' (2014) Colum J Transn'l L 689.
[14] See Lauterpacht (n 3).
[15] Paul Johann Anselm Feuerbach, *Lehrbuch des gemeinen in Deutschland gültigen peinlichen Rechts* (GH Heyer 1801); Friedrich August Hayek, *The Market and Other Orders, The Political Ideal of the Rule of Law (1955)* in Bruce Caldwell (ed), *The Collected Works of FA Hayek* (University of Chicago Press 2014) 148.

imprecision in the formulation of international tort law standards has a direct impact on the amount of damages to be awarded. Damages are a reflection of the extent of the violation of the international law standard. Under the differential hypothesis, or 'but-for' premise,[16] damages are the compensation for the economic difference between the situation subject to the violation and the hypothetical economic situation without the violation. The lowering or raising of the threshold of the applicable standard therefore has a significant monetary effect. Uncertainties with respect to whether the MFN standard applies to jurisdictional or procedural aspects of IIAs, the intensity of regulatory measures' interference in property rights that is required to deem these measures illegal under the Fair and Equitable Treatment standard, or the proper identification of the comparators for discrimination in order to find a violation of the MFN and the National Treatment standards all have a direct impact on the amount of damages to be awarded.

The application of a standard, to a public administration, to act 'in a consistent manner, free from ambiguity and totally transparently in its ... regulations that will govern ... [an investor's] investments, as well as the goals of the relevant policies and administrative practices or directives, [in order for the investor] to be able to plan its investment and comply with such regulations' has been established in the *Tecmed* case.[17] This contrasts with the risk situation and reality typically determined by project finance experts when considering political risk for the risk matrix used in the planning of an infrastructure project in an emerging market or developing country.[18] The discrepancy between the standard and the reality may lead to a difference of millions of dollars in damages in an investment arbitration, provided that the damages analysis is properly made and reflected in the reasoning of the award. Hardly any investor in an emerging market or developing country would base its risk analysis on the ideal administration and stability of regulation throughout the investment period described in the *Tecmed* case. It is therefore not convincing that investors may claim expectations of an ideal administration as legitimate if they hardly considered such a scenario when planning their investment. The International Minimum and Fair and Equitable Treatment standards serve to establish the lower acceptable limit of treatment, but they do not impose a higher standard than many states are able to achieve. An arbitral tribunal applying a standard higher than that used by the experts who are setting the risk premium for the project may actually overcompensate the investor.[19]

In a pending telecommunications investment arbitration case, the issue at stake is the considerable reduction of interconnection tariffs for market participants. Some participants serve a business clientele based on long-term services contracts; others provide services for rural areas where considerable investments in infrastructure are necessary and where services

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[16] Friedrich Mommsen, *Beiträge zum Obligationenrecht, Zweite Abtheilung: Zur Lehre von dem Interesse [The Doctrine of Interest]* (EU Schwetschke und Sohn 1855) 3: 'We understand as interest in its technical meaning the numeric difference of the assets of a person at a certain moment, with and without the injuring event at precisely such moment'.

[17] International Centre for the Settlement of Investment Disputes, *Técnicas Medioambientales Tecmed, SA v The United Mexican States*, ARB (AF) 00/2, Award, 29 May 2003.

[18] Scott L Hoffman, *The Law and Business of International Project Finance* (3rd edn, Cambridge University Press 2008) §2.02.

[19] Differences in the required quality of regulation based on the state of development of a WTO Member are expressly recognized in the preamble of the General Agreement on Trade in Services ((adopted 15 April 1994) 1869 UNTS 183), according to which Members of the WTO recognize 'the right ... to regulate, and to introduce new regulations, ... in order to meet national policy objectives, and given asymmetries existing with respect to the degree of development of services regulations in different countries, the particular need of developing countries to exercise this right'.

are subject to pre-paid cards. One of the market participants is an incumbent, or monopolist, with considerable market and political power. The competent authority significantly reduced tariffs in an apparently uniform manner; however, the reduction had different impacts on the participants depending on their different market segments. The incumbent has been compensated for the tariff reduction by tariff increases in a different telecommunications market. The participant doing business in rural areas has ended up with an income stream that does not cover costs and appears to violate basic guarantees in the concession agreement. That participant finally filed for investment arbitration.

Studies by the World Bank, OECD, and other renowned institutions provide guidelines for best practices, referring to the need for progressive tariff reduction in emerging market countries after the liberalization of the telecommunications market, the need to deal with the inevitable incumbent, and the need to establish a fair tariff structure.[20] As a basic premise, tariffs are to be reduced within a certain time frame according to the increase in efficiency of the new participants.

This telecommunications case raises a series of questions such as whether a tariff reduction of around 70% would represent a violation of the Fair and Equitable Treatment standard or indirect expropriation, how to determine the necessary comparator for discrimination as regards the compensation for the incumbent, and whether additional elements, such as a certain mode of treatment, in the form of arbitrary and abusive treatment, are required to establish illegality. Furthermore, the question arises of how much best practices established by international institutions influence the determination of the relevant benchmark for violation. If tariff reduction is part of best international regulatory practices, it may hardly be considered indirect expropriation or a violation of the Fair and Equitable Treatment standard, though it may be argued that participants in different market segments should be treated differently. As regards the damages analysis, the answer is found in a recent Oxford University Press monograph and further writings by its authors;[21] however, the damages case is contingent upon the liability case.

In case the arbitral tribunal would consider an excessive tariff reduction as indirect expropriation or violation of the Fair and Equitable Treatment standard, the next question would be where it would set the benchmark for illegality. If set at 50%, would the damages be in the amount corresponding to the 70% price reduction, or just 20% (i.e., the difference between 50% and 70%), or would the damages be the economic impact resulting from the discrimination as compared to the more favourable treatment of the incumbent? The choice of the suitable approach is likely to result in variations of millions of US dollars as compared to perhaps not so suitable approaches.

The answers to those questions may not be found easily. For the analysis of such a case, even experienced practitioners would need a team of research assistants, preferably at a specialized

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[20] Andrew Dymond, 'Telecommunications Challenges in Developing Countries, Asymmetric Interconnection Charges for Rural Areas' (2004) World Bank Working Paper No 27; *OECD Review of Telecommunication Policy and Regulation in Mexico* (OECD 2012); Robert J Shapiro, 'Foreign Direct Investment in Developing Nations: Issues in Telecommunications and the Modernization of Poland' (Council for European Investment Security April 2011).

[21] Wöss and others (n 3) ch V; Herfried Wöss and Adriana San Román Rivera, 'Damages in International Arbitration with Respect to Income Generating Assets or Investments in Commercial and Investment Arbitration', (2015) 2 Journal of Damages in International Arbitration 37; *Yukos Special*, [2015] 5 Transnational Dispute Management (ed Mark Kantor).

postgraduate level, in order to procure sufficient 'grinding power' to dig through decennial cases in order to find relevant or outcome-determinative *dicta* or *obiter dicta* to be used for legal argumentation. This process is not only highly inefficient, as reflected in the cost of investment arbitration, but it also provides little legal certainty as regards to the outcome. The case material and scholarly writings would be used as means of advocacy but not necessarily as evidence of the applicable rule of law, which in practice, leads to an *ex post* determination of the applicable rules of law instead of the 'subsumption' of the underlying facts within pre-established rules of law, in the sense of the prominent international and constitutional law scholar Hans Kelsen.[22] For each set of case material supporting a legal argument, experienced practitioners can find another set of cases showing the contrary. The outcome often seems to be determined by the size of the respective legal teams and their advocacy skills, rather than the proof of violation of clearly established legal standards based on the available evidence.

This is markedly different from the WTO system, where many of these legal issues do not even arise due to a rather detailed normative basis and standing 'jurisprudence', and where answers to principal issues may be found rather quickly in the WTO Analytical Index, which leads directly to the relevant case material. Whereas WTO law is characterized by the very limited scope of remedies available through its dispute settlement mechanism, which is based on prospective remedies to restore the *status quo ante* or the balance of tariffs or commitments,[23] international investment law leads to high-impact remedies in the form of damages through restitution or compensation. Uncertainty in the formulation of the applicable international tort standards leads to uncertainty in the amount of damages awarded due to the but-for premise used to determine the expectation interest, where damages are the economic equivalent to the situation but for the violation and are a mirror-image of the liability case.[24] Uncertainty at the liability level may lead to unfairness at the remedy level even when best practices for damages determination with respect to income-generating assets are applied. It is therefore of importance that international investment standards be sufficiently precise and predictable, though it is conceded that absolute precision with respect to rather general standards may never be achieved.

Arbitral practice often shows a penchant for creative law making on the liability side through generous use of the principles of effectiveness (*effet utile*) and *compétence de la compétence* to broaden the scope of international investment agreements.[25] This creativity with respect to liability is not infrequently contrasted with deficient damages analyses (e.g., *Gemplus v Mexico*[26]), where the damages case cannot be verified or 'falsified'[27] due to lack of proper reasoning in the arbitral award, which leads to unsatisfactory results.

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[22] Jörg Kammerhofer, *Uncertainty in International Law: A Kelsian Perspective* (Routledge 2011) 120-22.

[23] Frieder Roessler, 'The Scope of WTO Law Enforced through WTO Dispute Settlement Procedures' in Merit E Janow, Victoria Donaldson, and Alan Yanovich (eds), *The WTO: Governance, Dispute Settlement & Developing Countries* (Juris 2008) 332-33.

[24] Professor Rudolf von Ihering further developed Mommsen's 'interest' into 'expectation interest' and reliance interest'. Rudolf von Ihering, 'Culpa in contrahendo oder Schadensersatz bei nichtigen oder nicht zur Perfektion gelangten Verträgen', *Jahrbücher für die Dogmatik des heutigen römischen und deutschen Privatrechts IV* (1861) 1 ff.

[25] José E Alvarez, *International Organizations as Law-Makers* (Oxford University Press 2005) 66-108, 458-520.

[26] International Centre for the Settlement of Investment Disputes, *Gemplus, SA, SLP, SA de CV v The United Mexican States*, ARB (AF)/04/3, Award, 16 June 2010, <http://www.italaw.com/cases/480> accessed 28 November 2015.

[27] Sir Karl Raimund Popper, *The Logic of Scientific Discovery* (first published 1935 as *Logik der Forschung*, Routledge Classics 2002).

Legal certainty and predictability with respect to international tort standards may only be achieved through black-letter rules and codification, either through non-binding legal instruments such as model laws, a common understanding in the form of treaty negotiation,[28] authentic interpretation,[29] or a combination thereof, and should not depend on the advocacy skills of the parties or the sophistication of the arbitral tribunal.

2. The Need for the Development of Verifiable Standards through a Systemic Approach and Codification

In his recent, seminal analysis of the International Minimum and Fair and Equitable Treatment standards, Martins Paparinskis suggests that the interpretation and development of international law standards by arbitral tribunals and scholarly works does not necessarily follow rules of international law, and that customary law in the field of protection of property is rather underdeveloped as distinguished from a fairly advanced notion of denial of justice. Accordingly, 'It remains to be seen whether future practice will develop the law in line with the traditional approaches—as has been largely the case regarding denial of justice—or resolve legal complexities in a (sometimes perhaps excessive) innovative manner—as has been the case regarding the protection of property more broadly'.[30]

It does not appear likely that the current form of treaty interpretation by arbitral tribunals and scholarly works—often limited to the discussion of new strands of interpretation, whether based on a historical or contemporary approach, or even on changing the rules of interpretation as recently proposed—will lead to the sufficiently precise standards necessary for a tort law system in the near future. Nor is the current practice of *ex post* treaty interpretation by arbitral tribunals likely to change settled rules of law creation under public international law. Therefore, even if arbitral tribunals were to achieve a more or less harmonious interpretation of the principal international law standards, the flaws remain as regards law formation in the absence of the contracting parties.

With respect to indirect expropriation, Katia Yannaca-Small states that, 'The question that arises is to what extent a government may affect the value of property by regulation, either general in nature or by specific actions in the context of general regulations, for a legitimate purpose without effecting a "taking" and having to compensate a foreign owner or investor for this act. The definition of indirect expropriation in this context has become one of the dominant issues in international investment law'.[31] The lack of precision necessarily leads to different possible outcomes without prejudice to variations in the precise wording of different IIAs.

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[28] UNCTAD, *Investment Policy Framework for Sustainable Development* (United Nations 2012) 36-64.

[29] Lise Johnson and Merim Razbaeva, 'State Control over Interpretation of Investment Treaties' Columbia Center on Sustainable Investment Policy Paper, April 2014.

[30] Martins Paparinskis (n 7) 260.

[31] Katia Yannaca-Small 'Indirect Expropriation and the Right to Regulate: How to Draw the Line?' in Katia Yannaca-Small (ed), *Arbitration under International Investment Agreements, A Guide to the Key Issues* (Oxford University Press 2010) 446; Alejandro Faya Rodríguez, '¿Cómo se determina una expropiación indirecta bajo tratados internacionales en materia de inversión? Un análisis contemporáneo' in Sonia Rodríguez Jiménez and Herfried Wöss (eds), *Foro de Arbitraje en Materia de Inversión: Tendencias y Novedades* (Instituto de Investigaciones Jurídicas, Universidad Nacional Autónoma de México 2013).

Karl Sauvant and Professor Federico Ortino explain that, with respect to 'indirect expropriation' and 'any measure having an equivalent effect to expropriation'

> Various doctrines have been advanced by the parties and endorsed by the many investment tribunals, including the following three doctrines: a measure falls under the concept of indirect expropriation whenever it has substantially deprived a foreign investor of its investment; notwithstanding its adverse impact on foreign investment a measure cannot be defined as expropriatory if it pursues a non-discriminatory, bona fide and legitimate purpose; and a finding of indirect expropriation requires balancing various factors, including, principally, the measure's adverse effect on a foreign investment and the measure's public policy benefits.[32]

According to Professor Ursula Kriebaum, there are at least three approaches with respect to indirect expropriation, including the 'sole effects doctrine', where there is expropriation if a measure deprives the investor of all or most benefits permanently or for a substantial period of time; the 'police powers approach', where there is no expropriation if the interference is non-discriminatory and in accordance with due process requirements; and a balancing approach, where the interests of the investor are balanced against the public purpose of the interference.[33]

In cases of National Treatment and Most Favoured Nation treatment, in particular in cases involving origin-neutral measures that do not explicitly differentiate between domestic and foreign investors, the determination of the comparator is subject to different interpretations[34] left to the *ex post facto* determination of arbitral tribunals.[35] According to Professor Andrea Bjorklund, 'While there is no universally accepted approach to addressing a national treatment claim, a common essential element is the identification of the appropriate domestic comparator—the entity in "like circumstances"—against which to assess the treatment accorded the allegedly injured foreign investment (or investor). A part of that analysis requires identifying the treatment itself that is less favorable than that given the domestic comparator. A third inquiry usually involves an assessment of whether the host government had nondiscriminatory reasons that justified the difference in treatment'.[36] The issue is that there is no pre-defined approach and that an analogy to GATT is of limited use due to systemic differences.

With respect to the Fair and Equitable Treatment standard, there is a significant difference in the threshold triggering liability amongst cases. For instance, *Tecmed* establishes the rather utopian standard of perfect administration whereas *Saluka v Czech Republic*[37] takes a more

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[32] Karl P Sauvant and Federico Ortino, *Improving the International Investment Law and Policy Regime: Options for the Future* (FORMIN Finland 2014), 66-67 (footnotes omitted).
[33] Ursula Kriebaum, 'FET and Expropriation in the (Invisible) EU Model BIT' (2014) 15 Journal of World Investment & Trade 454, 459-62 (footnotes omitted).
[34] Federico Ortino, 'Non-Discriminatory Treatment in Investment Disputes' in Pierre-Marie Dupuy, Francesco Francioni, and Ernst-Ulrich Petersmann (eds), *Human Rights in International Investment Law and Arbitration* (Oxford University Press 2009) 364.
[35] Rudolf Dolzer and Christoph Schreuer, *Principles of International Investment Law* (2nd edn, Oxford University Press 2012) 199.
[36] Andrea Bjorklund, 'The National Treatment Obligation' in Katia Yannaca-Small (ed), *Arbitration under International Investment Agreements, A Guide to the Key Issues* (Oxford University Press 2010) 419.
[37] Nicolás M Perrone, 'The International Investment Regime at a Crossroad: Should We Be Rethinking Foreign Investment Governance?' *International Institute for Sustainable Development* (19 February 2015).

reasonable approach, referring to a 'balanced approach to the interpretation of the Treaty's substantive provisions for the protection of investments'.[38] The standard is subject to different formulations.[39] There are different approaches with respect to the preservation of legal stability and the protection of legitimate expectations and the state's right to regulate. Further uncertainty is added where IIAs contain express references to customary international law, which 'is as at least as imprecise as the fair and equitable treatment standard'.[40] In particular, it does not appear that Fair and Equitable Treatment has an 'ordinary meaning' in international law.[41]

The amorphous notion of 'legitimate expectation' originally imported from GATT law is of concern when used beyond the scope of ensuring the predictability of rights expressly granted by the state to an investor. WTO and GATT law aims to maintain legitimate expectations arising from tariff concessions and other commitments, which allow the suspension of benefits even in case of non-violation complaints.[42] The WTO Appellate Body has repeatedly denied the application of the principle of protection of legitimate expectations outside the scope of tariff concessions, such as in the context of The Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS) because of its subjective nature.[43] Both TRIPS and GATS establish positive rights, which are systemically different from traditional tariff concessions, and as a result, notions applicable to such tariff concessions may not be transferred to such positive rights.[44] The notion of legitimate expectations, therefore, should be dealt with carefully[45] in the course of defining the Fair and Equitable Treatment standard. In particular, the notion of legitimate expectations is used in different contexts under the Fair and Equitable Treatment standard—it is used both as an important element in the definition of the standard and as a means to grant particular rights to the investor. According to Martins Paparinskis, 'The legitimate or reasonable expectations of the investors have been accepted in case law as a key and probably the most far-reaching element of the international standard. Unlike arbitrariness, discrimination and procedural propriety, anchored in the traditional practice, the source of the rules on expectations is less obvious. ... While the role of expectations seems broadly accepted in mainstream decisions and writings, the systemic uniqueness of investment law in focusing on expectations raises the question of whether this perspective fulfils a useful function that could not be addressed otherwise'.[46] The notion of legitimate expectations, in particular where they convert private law obligations into treaty violations in the absence of an umbrella clause, is highly questionable as it compensates for the lack of definition of an international standard by reference to obligations that are not international law. This notion has to be distinguished from the notion of legitimate

[38] UNCITRAL, *Saluka v The Czech Republic*, Partial Award, 17 March 2006, paras 300, 305-307.
[39] Jeswald W Salacuse, *The Law of Investment Treaties* (Oxford University Press 2010) 222-28.
[40] Kriebaum, 'FET and Expropriation' (n 33) 472.
[41] Paparinskis (n 7) 111-15.
[42] Edmond McGovern, *International Trade Regulation*, para 2.272 (July 2014).
[43] WTO, *The EC-LAN Case* (5 June 1998), AB-1998, WT/DS62/AB/R, WT/DS67/AB/R, WT/DS68/AB/R; Thomas Cottier and Krista Nadakavukaren Schefer, 'Good Faith and the Protection of Legitimate Expectations in the WTO' in Thomas Cottier (ed), *The Challenge of WTO Law: Collected Essays* (Cameron May 2007) 136-39.
[44] Frederick M Abbott, 'WTO Dispute Settlement and the Agreement on Trade-Related Aspects of Intellectual Property Rights' in Ernst-Ulrich Petersmann (ed), *International Trade Law and the GATT/WTO Dispute Settlement System* (Kluwer Law International 1997) 433-34; Herfried Wöss, 'The Application of TRIPS to the Authorisation by Health Authorities of the Using, Making and Selling of Pharmaceutical Drugs' (2002) 3 Journal of International Trade Law and Regulation 82.
[45] Søren J Schønberg, *Legitimate Expectations in Administrative Law* (Oxford University Press 2000).
[46] Paparinskis (n 7) 251, 259 (footnotes omitted).

expectations as a synonym for legal certainty and the predictability of a legal norm. The existence of the notion of legitimate expectations under international law would have to be examined and justified in each of the different contexts where it is being used within investment arbitration. The fact that some states do use legitimate expectations with respect to the protection of property does not automatically mean that this use forms part of international law.

The question arises of how, *de lege ferenda*, the lack of precision in international standards of investment protection may be remedied through the participation of the contracting states. A multilateral convention on the definition of primary rules of investment protection may be discarded in the light of the discussion of the necessity of investor-state dispute settlement (ISDS) in the Transatlantic Trade and Investment Partnership (TTIP) and the Trans-Pacific Partnership (TPP), and the apparent lack of international consensus. An appeals body based on multiple bilateral and regional IIAs simply adds another layer of arbitral jurisdiction and, though an interesting proposal, does not seem solve the underlying legitimacy deficit caused by the absence of the contracting parties and would simply lead to the body picking of one of the various strands of interpretation developed by arbitral tribunals. The new proposal of the investment tribunal under Article 8.27 of CETA in combination with the appellate tribunal might have a guiding effect on law formation due to the higher degree of institutionalization. However and as Article 8.41 of CETA clearly establishes, 'An award issued pursuant to this Section shall be binding between the disputing parties and in respect of that particular case', which limits the legal effect of any arbitral award *de lege lata*.

A solution that may be feasible, albeit not in the near future, is the formulation of a non-binding common understanding of all states, both capital exporting and importing, that are currently or likely to be involved in investment arbitration on a definition of the principal investment protection standards, which could take place under the auspices of the UN Commission on International Trade Law (UNCITRAL) with the participation of other international organizations such as the Organization for Economic Co-operation and Development (OECD) and the UN Conference on Trade and Development (UNCTAD), perhaps in the form of a model law. The agreed principles could then be incorporated by the contracting states into the various IIAs through authentic interpretation as established in Article 8.31(3) of CETA or by using their treaty-making powers to amend existing IIAs. Direct codification could occur through the contracting parties using their treaty-making powers for the formulation of modern investment protection standards in comprehensive economic trade and services agreements such as CETA, which would likely provide a benchmark and model for other IIAs.

As regards the content of the principal international investment standards, it is necessary to reduce the multiple interpretations made by arbitral and scholarly practice to the key elements of such standards: International investment law standards, in essence, circle around a few notions such as (i) the intensity of a measure and its effect on the property rights or other rights protected, (ii) discrimination, (iii) the mode of the measure (arbitrariness, unreasonableness, or abuse of rights), and (iv) procedure, including the procedural aspects of denial of justice. The current complexity of arbitral 'jurisprudence' and the variety of legal opinions could, therefore, be reduced to a few principles aiming at systemic consistency.

As regards its systematic aspects, the benchmark for investment protection standards should be illegal expropriation, which seems to be the most settled notion under public international law. The difficulty of establishing the threshold for illegal interference in property rights

necessarily leads to an emphasis on discrimination. The standards of discrimination have to be further defined using international practice and experience. Overlapping notions, including confusion between discrimination and arbitrariness, should be duly avoided. The limits are, in any case, well-established notions of denial of justice and arbitrariness under the Fair and Equitable Treatment standard and international customary law.

As regards the Fair and Equitable Treatment standard, an analogy to human rights law as proposed by various authors would certainly provide a more balanced approach.[47] There does not seem to be a justification for using the notion of indirect expropriation as this phenomenon could easily be dealt with under the Fair and Equitable Treatment standard. Expropriation requires, from the outset, a transfer of property, which is not present in cases of indirect expropriation. Applying the term 'expropriation' to a measure not leading to a transfer of property results in systemic inconsistency. The importation by arbitral tribunals of the domestic law concepts of a limited number of contracting states, such as the notion of 'takings', without respecting the rules of law formation in international law should be duly avoided.

Particular emphasis should be placed on the risk profile of host states, as used by investors, multilateral development banks, or international organizations in cases where a determination of legitimate expectations cannot be avoided due to express usage of the term in IIAs. Unless there are express promises or obligations, expectations may not exceed the reasonable expectations of a knowledgeable investor when planning its investment in a given country. The function of international investment protection standards seems to be to protect against excesses but not to punish states for failing to achieve a utopian standard of ideal administration and efficiency. This is without prejudice to the limits established by the International Minimum standard under customary international law.

The solution with respect to a more uniform and rules-based regime lies in the codification of international investment standards either through treaty-making or authentic interpretation. While a detailed proposal for the proper formulation of investment protection standards that goes beyond a mere sketch is outside the scope of this article, the starting point for such a proposal would be the discussion of the proper formulation of primary rules of investment protection standards[48] and their systemic aspects by state representatives, international organizations and institutions, and scholarly works. This enquiry would be more helpful than the discussion of technical aspects of arbitral awards, which does not necessarily contribute to the formulation of a concise system of investment protection standards in order to achieve reasonable legal certainty and predictability. The understanding of international investment protection standards as international tort law standards and the understanding of the remedial mechanism are of utmost importance for system formation. International investment protection law may not be properly understood without an insight into the remedial mechanism. As regards the issue of proper damages analysis and quantification in the

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[47] Ursula Kriebaum, 'Nationality and the Protection of Property under the European Convention for the Protection of Human Rights' in Isabelle Buffard and others (eds), *International Law between Universalism and Fragmentation: Festschrift in Honour of Gerhard Hafner* (Martinus Nijhoff 2008); Christoph Schreuer and Ursula Kriebaum, 'The Concept of Property in Human Rights Law and Investment Protection Law' in Stephan Breitenmoser and others (eds), *Human Rights, Democracy and the Rule of Law: Liber Amicorum Luzius Wildhaber* (Dike 2007) 754-55.

[48] The Draft Articles on Responsibility of States for Internationally Wrongful Acts ('Report of the International Law Commission on the Work of Its Fifty-Third Session' (2001) UN Doc A/56/10, 43 (Articles on State Responsibility)) are limited to secondary rules without further defining any primary tort law standards.

telecommunications case raised above, the answer is found in the damages doctrine for income-generating assets or investments formulated in a recent Oxford University Press monograph, which has actually been espoused by the landmark *Yukos v Russia* awards.[49]

3. CETA and the Codification of International Tort Law Standards

As confirmed in a recent study authored, amongst others, by one of the most renowned former functionaries of the European Commission, Roderick Abbott, it is clear that investors in the European Union are by far the most active users of ISDS. EU countries have many more bilateral investment treaties (BITs) with ISDS provisions than, for instance, the United States. EU investors' complaints represent more than half of the entire complaints filed at international investment tribunals in the past decade. Many EU countries are, in some sectors and areas, acting in a way that undermines foreign investors. And they are more likely to do so if there is no investment protection agreement that constrains potential government abuse. As with many other international agreements and contracts, IIAs' main achievement is not to facilitate dispute settlement when such a need occurs but to establish a framework to prevent disputes from occurring at all. From the viewpoint of political economy, the role of a BIT is often to counterbalance those actors within a government that prefer to act without taking notice of potentially negative consequences for other countries or foreign investors.[50]

CETA aims to affirm the right of the contracting parties to regulate and to achieve legitimate policies including those relating to public health, safety, the environment, public morals, and the promotion and protection of cultural diversity. CETA contains a definition of the Fair and Equitable Treatment standard and adds further language to clarify what constitutes 'indirect expropriation', which excludes claims against legitimate public policy measures, save when the measure is manifestly excessive. Under CETA, the European Union and Canada may issue binding interpretations that provide the contracting parties with 'ultimate control' over interpretation. According to Article 8.31(3) of CETA, 'Where serious concerns arise as regards matters of interpretation that may affect investments, the Committee on Services and Investment may pursuant to Article 8.44.3(a) recommend to the CETA Joint Committee the adoption of interpretations of this Agreement. An interpretation adopted by the CETA Joint Committee shall be binding on a Tribunal established under this Section. The CETA Joint Committee may decide that an interpretation shall have binding effect from a specific date'. CETA does not include any guarantee of a 'stable business environment', an outcome that derives from the right to regulate established under Article 8.9 (Investment and regulatory measures) of CETA. In order to avoid 'unwarranted' interpretations, the Fair and Equitable Treatment standard in Article 8.10 (Treatment of investors and of covered investments) of CETA has been limited to a closed list of behavioural norms consistent with consolidated judicial views in the European Union, such as denial of justice, arbitrary conduct, and breach of due process.[51]

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[49] Wöss and others (n 3) chs V, VI, VII; Wöss and San Román Rivera (n 21); *Yukos Special* (n 21); Ko-Yung Tung, Book Review of *Damages in International Arbitration under Complex Long-Term Contracts* by Herfried Wöss and others (2014) 29 ICSID Review 1; Aníbal Sabater, Book Review of *Damages in International Arbitration under Complex Long-Term Contracts* by Herfried Wöss and others, *Global Arbitration Review* (14 November 2014).

[50] Roderick Abbott, Fredrik Erikson, and Martina Francesca Ferracane, 'Demystifying Investor-State Dispute Settlement (SDS)' (2014) ECIPE Occasional Paper No. 5/2014, 2, 21.

[51] Commission, 'Investment in TTIP and beyond—the Path for Reform: Enhancing the Right to Regulate and Moving from Current Ad Hoc Arbitration to an Investment Court' (5 May 2015) <http://trade.ec.europa.eu/doclib/docs/2015/may/tradoc_153408.PDF> accessed 28 November 2015.

Apart from such improvements, CETA does not depart from traditional notions developed by arbitral tribunals, or contain a major effort to codify international investment standards. In particular, the definition of 'investment' in Article 8.1 (Definitions)[52] does not clarify the distinction between pure contractual claims, which ought not to be considered investments, and complex long-term contracts based on income stream, which are income-generating assets or investments, or so-called synallagmatic triallagmas.[53]

The definition of expropriation reflects international customary law. The notion of indirect expropriation established in Article 8.12(1) of CETA, and Annex 8-A (Expropriation) requires 'an effect equivalent to direct expropriation, in that it substantially deprives the investor of the fundamental attributes of property in its investment, including the right to use, enjoy and dispose of its investment, without formal transfer of title or outright seizure'. This is further clarified in Annex 8-A(2) of CETA, according to which

> The determination of whether a measure or series of measures of a Party, in a specific fact situation, constitutes an indirect expropriation requires a case-by-case, fact-based inquiry that considers, among other factors:
>
> (a) the economic impact of the measure or series of measures, although the sole fact that a measure or series of measures of a Party has an adverse effect on the economic value of an investment does not establish that an indirect expropriation has occurred;
> (b) the duration of the measure or series of measures by a Party;
> (c) the extent to which the measure or series of measures interferes with distinct, reasonable investment-backed expectations; and
> (d) the character of the measure or series of measures, notably their object, context and intent.

According to Paragraph 3, and for greater certainty, '[E]xcept in the rare circumstance when the impact of the measure or series of measures is so severe in light of its purpose that it appears manifestly excessive, non-discriminatory measures of a Party that are designed and applied to protect legitimate public welfare objectives, such as health, safety and the environment, do not constitute indirect expropriations'.

CETA contains an ample definition of the Fair and Equitable Treatment standard:

> Article 8.10
>
> Treatment of investors and of covered investments
>
> 1. Each Party shall accord in its territory to covered investments of the other Party and to investors with respect to their covered investments fair and equitable treatment and full protection and security in accordance with paragraphs 2 through 6.

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[52] Commission, 'Consolidated CETA Text' (29 February 2016) <http://trade.ec.europa.eu/doclib/docs/2016/february/tradoc_154329.pdf> accessed 20 March 2016.
[53] See comments 28 to 31 of Article 36 of the Articles on State Responsibility (n 48); Wöss and San Román Rivera (n 21); *Yukos Special* (n 21).

2. A Party breaches the obligation of fair and equitable treatment referenced in paragraph 1 where a measure or series of measures constitutes:

(a) denial of justice in criminal, civil or administrative proceedings;
(b) fundamental breach of due process, including a fundamental breach of transparency, in judicial and administrative proceedings;
(c) manifest arbitrariness;
(d) targeted discrimination on manifestly wrongful grounds, such as gender, race or religious belief;
(e) abusive treatment of investors, such as coercion, duress and harassment; or
(f) a breach of any further elements of the fair and equitable treatment obligation adopted by the Parties in accordance with paragraph 3 of this Article.

3. The Parties shall regularly, or upon request of a Party, review the content of the obligation to provide fair and equitable treatment. The Committee on Services and Investment ... may develop recommendations in this regard and submit them to the Trade Committee for decision.

4. When applying the above fair and equitable treatment obligation, a Tribunal may take into account whether a Party made a specific representation to an investor to induce a covered investment, that created a legitimate expectation, and upon which the investor relied in deciding to make or maintain the covered investment, but that the Party subsequently frustrated.

5. For greater certainty, 'full protection and security' refers to the Party's obligations relating to physical security of investors and covered investments.

6. For greater certainty, a breach of another provision of this Agreement, or of a separate international Agreement does not establish that there has been a breach of this Article.

7. For greater certainty, the fact that a measure breaches domestic law does not, in and of itself, establish a breach of this Article. In order to ascertain whether the measure breaches this Article, a Tribunal must consider whether a Party has acted inconsistently with the obligations in paragraph 1.

This provision has been commented on in detail by Ursula Kriebaum in the *Transnational Dispute Management* special issue on CETA and is subject to review and clarification by the contracting parties under Articles 8.31 (Applicable law and interpretation) and 8.44(3)(a) (Committee on Services and Investment) of CETA. As stated by Professor August Reinisch, 'Obviously, the negotiators have tried to navigate between the Scylla of over-determination and the Charybdis of vagueness. At the same time this is an interesting example of the potential feedback between treaty-makers and investment tribunals. It is evident that the CETA drafters have incorporated many elements found in arbitration practice, but it is also

clear that they have, presumably intentionally, not adopted all of these elements'.[54] CETA does not refer to the element of stability.[55]

The National Treatment clause in Article 8.6 now expressly refers to 'treatment no less favourable, than the treatment it accords, in like situations to its own investors and to their investments with respect to the establishment, acquisition, expansion, conduct, operation, management, maintenance, use, enjoyment, and sale or disposal of their investments in its territory', thereby establishing a fairly precise comparator, including factors such as market access and establishment, which is effectively the same as in NAFTA and subsequent US and Canadian treaties. With respect to MFN treatment, Article 8.7(4) of CETA clarifies that 'For greater certainty, the "treatment" referred to in Paragraph 1 and 2 does not include investor-to-state dispute settlement procedures provided for in other international investment treaties and other trade agreements. Substantive obligations in other international investment treaties and other trade agreements do not in themselves constitute "treatment", and thus cannot give rise to a breach of this article, absent measures adopted by a Party pursuant to such obligations'. This provision most certainly represents major progress toward achieving legal certainty and predictability as regards the proper application of the MFN standard. In particular, MFN was not meant to serve as a tool to import into one treaty better treatment stipulated under other investment treaties.[56]

Finally, CETA does not contain any umbrella clause, thereby abandoning one of the most controversial notions of international investment law,[57] which parallels the limitation of legitimate expectations to specific written obligations under the Fair and Equitable Treatment provision.

Conclusions

CETA is, without a doubt and in spite of several flaws analyzed above, a landmark agreement with respect to the further codification and development of international investment protection standards. It follows a conservative approach of adopting carefully selected strands of interpretation, together with the reasonable reduction of the scope of MFN to its core function and the abandoning of the umbrella clause. CETA does not undertake a systemic overhaul, but it certainly contributes to system building through the participation of the contracting parties, eliminating some of the excesses of arbitral tribunals caused by interpretations based on a lack of understanding of fundamental concepts of public international and international economic law. It will certainly trigger further discussion of how to design a system of investment protection led by states and in accordance with the rules of law formation under public international law.

Investment protection law, similarly to the Bretton Woods organizations, the foundation of the European Communities, and the WTO, serves to replace power diplomacy through a rules-based system. It may be incidental, but it is precisely the existence of these peace-

[54] August Reinisch, '"Putting the Pieces Together ... an EU Model BIT"' (2014) 15 Journal of World Investment & Trade 692.
[55] Kriebaum, 'FET and Expropriation' (n 33) 470-72.
[56] Reinisch (n 54) 696.
[57] The original function of umbrella clauses was to neutralize unreliable legal systems by having a breach of contract 'straightaway considered to be a violation of international law': see Hersch Lauterpacht, 'Some Aspects of International Concession Agreements' (1959) 1 Bulletin of the Harvard International Law Club 6.

creating institutions that may explain why the Western world has experienced the longest period of peace in its history.[58] A globalized world is unthinkable without these institutions and a fairly developed system of investment protection.

[58] 'The Bretton Woods Agreements: The 70 year Itch' *The Economist* (5 July 2014). The second longest period of peace in Europe was between 1872 and 1914: see Stefan Zweig, *The World of Yesterday* (Viking Press 1943).