Emerging Trends in ICSID: Proportionality Between Indirect Expropriation and the Right to Regulate

Polen Bayrak

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1. Introduction

States offer various protections for investors of a foreign country through Bilateral Investment Treaties (BITs) and Free Trade Agreements (FTAs) with investment chapters to attract foreign money and to strengthen their economies. A provision requiring host states to compensate for the expropriation of foreign direct investments is one of the few permanents contained within around 3200 investment treaties.[1]

The lack of definition in treaties, and in domestic legislations pushes arbitral tribunals to provide a legal content, if not a proper test. So far, the investment tribunals failed for their inconsistent understanding and application of the term.[2] The awards of the investor-state arbitral tribunals are widely critisized for their failiure to act impartial by favouring the investors against the host states, thus violating the international norm of the right to a fair trial. The host states have been left with the fear that any measure although for public purpose can hit the wall of the ICSID, and oblige them to pay compensation.

This attitude of the tribunals has faced a backlash recently.[3] Starting from the 2004 US Model BIT, host states when concluding an investment treaty add definitive criterias to the indirect expropriation provisions. This has been interpreted by the scholars as the host states reclaiming their right to regulate.[4] Nevertheless, the right to regulate is an attribute of state sovereignty and it always exists at the background.

Since these clarified indirect expropriation clauses introduced relatively recently, only one tribunal had an opportunity to interpret the new provision. This clause has come in front of the *Bear Creek v. Peru* tribunal.[5] This case will be analyzed to assess whether the tribunal has correctly balanced the interests in conformity with the intention of the parties which is implied from their clarification to the indirect expropriation clause with the aim of preserving the regulatory space of the host state. This article claims that these clarified indirect expropriation clauses may not be sufficient to achieve its aim based on the emerging ICSID practice.

In the first Section, the article will examine the character of the regulatory freedom to establish its normative value. Then, Section two will compare regulatory freedom and indirect expropriation norms to determine whether there is a normative hierarchy between them. In Section three, the general pattern used by the ICSID tribunals on indirect expropriation claims under the 'traditional BITs' has been analyzed. Thirdly, the clarified indirect expropriation clauses are introduced and divided into three sections in order to better examine their strengths and weaknesses. Then, *Bear*

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[1] Federico Ortino, ' Defining Indirect Expropriation: The TTIP Approach and the (Elusive) Search for 'Greater Certainty'' (2016) 43 Legal Issues of Economic Integration 351.

[2] See Malcolm Langford and Daniel Behn, 'Managing Backlash: The Evolving Investment Treaty Arbitrator?' (2018) The European Journal of International Law Vol. 29 no. 2; Michael Waibel, 'Backlash to Investment Arbitration: Three Causes' in Michael Waibel*, Backlash Against Investment Arbitration: Perceptions and Reality,* (1edn, 2010 Kluwer Law International).

[3] Michael Waibel, 'Backlash to Investment Arbitration: Three Causes' in Michael Waibel*, Backlash Against Investment Arbitration: Perceptions and Reality,* (1edn, 2010 Kluwer Law International).

[4] See Myriam Vander Stichele and Roos van Os 'BITs, FDI and Development' in Marc Maes and others, *Reclaiming Public Interest in Europe's International Investment Policy EU Investment Agreements in the Lisbon Treaty Era: A Reader* (SOMO 2010) 1, 26.

[5] *Bear Creek Mining Corporation v. Republic of Peru*, ICSID Case No. ARB/14/21, Award, 30 November 2017.

Creek Mining v. Republic of Peru which is the first and foremost tribunal to interpret the clarified indirect expropriation clause is critically analyzed.

2. Character of the Regulatory Freedom

With regards to the claims of indirect expropriation, the tribunals are frequently exposed to lay off the scope of the regulatory freedom of the host states. The investment agreements do not mention the regulatory freedom or any term equivalent. The answer to the question of to what extent the host states can adopt policies without being found to be in breach of the investment treaty is often left to the tribunals. In this respect, the tribunals have adopted a variety of approaches. Before analysing the past and current practices on indirect expropriation, the root of the regulatory freedom must be ascertained.

It is no doubt that states have a legal competence to regulate their economies within the boundaries of their territories.[6] Expropriating property, whether domestic or foreign, is one of the reflections of this right and a prominent attribute of being a sovereign state.[7]
The inherent rights comprising severeignty were recognized in the Declaration of the United Nations General Assembly on Friendly Relations in the following words: "Each state enjoys the rights inherent in full sovereignty."[8] This Declaration has been acknowledged as customary law on more than one occasion.[9]

For example, the International Court of Justice (ICJ) in *Nicaragua v United States of America*[10] referring to the possibility that *opinio juris* may be deduced from the attitude of states towards certain United Nations General Assembly resolutions, particularly the Declaration on Friendly Relations stated that:

> "[T]he effect of consent to the text of such resolutions cannot be understood as merely that of a "reiteration or elucidation" of the treaty commitment undertaken in the Charter. On the contrary, it may be understood as an acceptance of the validity of the rule or set of rules declared by the resolution by themselves."

The regulatory freedom is a fundamental attribute of state sovereignty. Since sovereignty is a customary norm in nature, its individual elements such as regulatory freedom should also be characterized as custom.[11] Yet, the regulatory freedom by itself can be characterized as custom by virtue of constant state practice and *opinio juris* which are the two essential elements for the formation of the customary international law.[12]

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[6] Martin Laughlin, *The Idea of Public Law* (OUP 2004), 84; Samantha Besson, 'Sovereignty' in Rüdiger Wolfrum (ed.) Max Planck Encyclopedia of Public International Law (OUP 2008) para 120.
[7] Ben A. Wortley, *Expropriation in International Law* (CUP 1959), 13, 14.
[8] UN General Assembly, *Declaration on Principles of International Law concerning Friendly Relations and Cooperation among States in accordance with the Charter of the United Nations,* 24 October 1970, A/RES/2625(XXV), available at: https://www.refworld.org/docid/3dda1f104.html [accessed 10 June 2021]
[9] *Military and Paramilitary Activities in and against Nicaragua* (Nicaragua v United States of America), 27 June 1986, 1986 ICJ Reports 14, para. 188; *Armed Activities on the Territory of the Congo* (Democratic Republic of the Congo v Uganda), Judgment of 19 December 2005, (2005) ICJ Reports 168, para. 162.
[10] ibid.
[11] Aniruddha Rajput, 'Chapter 6: Regulatory Freedom as Customary International Law', in Aniruddha Rajput, *Regulatory Freedom and Indirect Expropriation in Investment Arbitration*, (Kluwer Law International 2018) 109.
[12] Article 38, United Nations, *Statute of the International Court of Justice*, 18 April 1946.

The rules that made up customary international law are not written down or codified in any particular source.[13] They are implicitly incorporated as a source of law[14], whether or not they are explicitly referred to in the text of the treaty. Thus, a query about the existence of a rule requires an examination beyond the treaty.

According to the Lotus principle established by the International Court of Justice (ICJ) in *Bozkurt v. Lotus*[15], all attributes of sovereignty continue until there is a specific rule on the contrary in International law. The international law and the BITs do not prohibit expropriation completely. They only require conditions that must be satisfied to be a lawful expropriation. These are it must be for public purpose, conducted in a non-discriminatory manner, and with due process and accompanied by compensation paid to the adversely affected investor whose property has been expropriated. In practice, this seems to deprive the states of the regulatory prerogatives by obliging them to pay compensation even for measures taken for public purpose. However, it shall be noted that if these public motives are sufficiently strong and reasonably connected, then there may be no expropriation at all and therefore no right to compensation.[16]

If the expropriatory measure does not possess one of the required conditions, it would be regarded as unlawful expropriation.[17] The main difference between the lawful and the unlawful expropriation for the host states is the amount of compensation, which is higher for the unlawful expropriation.[18]

[13] See Brian D. Lepard, *Customary International Law: A New Theory and Practical Implications* (CUP 2010).
[14] Article 38 of the International Court of Justice (ICJ) Statute.
[15] *S.S. Lotus (Fr. v. Turk.),* 1927 P.C.I.J. (ser. A) No. 10 (Sept. 7), Publications of the Permanent Court of International Justice, Series A - No. 10; Collection of Judgments, A.W. Sijthoff's Publishing Company, Leyden, 1927.
[16] David Collins, *An Introduction to the International Investment Law,* (1edn, CUP 2016) 170.
[17] Yannick Radi, *Rules and PRactices of International Investment Law and Arbitration* (1edn, CUP 2020) 174.
[18] ibid, 181.

3. Regulatory Freedom v. Indirect Expropriation Norms

Investment treaties provide a guarantee against expropriation without compensation whether direct or indirect. However, traditionally they neither mention the right to regulate or what amounts to indirect expropriation.[19]

The right to regulate does not have to be explicitly referred to in the treaties, it is the police powers of the state and implicitly incorporated as part of customary international law[20], and stays in the backround ready for filling the gaps. The recent practice of specific reference to the right to regulate in investment agreements is merely a reaffirmation of the right in customary law[21], and perhaps it is a reminder to the ignorant tribunals that this right do exist.

International law is familiar with two types of expropriation: direct and indirect. Direct expopriation refers to the legal transfer of title to the property to the host state or a state-mandated third party, or its outright seizure. Direct expropriation was largely a move by newly independent states to regain control over their national assets. The nationalization of the foreign-owner companies commonly in the oil and gas sector by Libya in 1970s[22], and by Kuwait in 1980s, and by some Latin American countries in the 2000s are the typical examples.[23] Today, large-scale direct expropriations or nationalizations are exceptional, since precipitous seizure of property might endanger the reputation of the host state as a desirable location for FDIs.[24] On contrary, the mainstream practice is regulatory taking or indirect expropriation which results in the economic devastation of the investor without a formal taking of property but nevertheless has the same outcome as direct expropriation. The current rules recognise the legitimacy of such a move but imposes certain requirements including the payment of compensation to the investor who loses his business, investment and profit. In the same vein, a series of government measures as a composite act[25] might result in the substantial deprivation of the value of the investment, even though each by itself do not amount to expropriation, then it is an indirect expropriation. This is called "creeping expropriation".[26]

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[19] Based on a survey taken by the United Nations Conference on Trade and Development ("UNCTAD"), only 5% of the bilateral investment treaties signed before 2010 specify the criteria in indirect expropriatio clause. However, 42% of investment treaties concluded during 2011-2016 contain such provisions; See UNCTAD, *World Investment Report* 2017, 122, U.N. Doc. UNCTAD/WIR/ 2017 (2017), accesed at 27 August 2021 <https://unctad.org/system/files/official-document/wir2017_en.pdf >

[20] See Aniruddha Rajput, 'Chapter 7: Regulatory Freedom (Customary Norm) and Indirect Expropriation (Treaty Norm): Interaction of Norms', in Aniruddha Rajput, *Regulatory Freedom and Indirect Expropriation in Investment Arbitration*, (Kluwer Law International 2018).

[21] Aniruddha Rajput, 'Chapter 7: Regulatory Freedom (Customary Norm) and Indirect Expropriation (Treaty Norm): Interaction of Norms', in Aniruddha Rajput, *Regulatory Freedom and Indirect Expropriation in Investment Arbitration*, (Kluwer Law International 2018) 133, 138.

[22] See G. Winthrop Haight, ' Libyan Nationalization of British Petroleum Company Assets' (1972) 6,3 541. Libya nationalized its oil and gas industries against the foreign-owned companies including taking over the assets of the British Petroleum (BP) against the payment of fair compensation within three months.

[23] Ying Zhu' 'Do Clarified Indirect Expropriation Clauses in International Investment Treaties Preserve Environmental Regulatory Space' (2019) 60 Harv. Int'l LJ 377, 380.

[24] ibid.

[25] A composite act is aggregate of actions, omissions, or a combination of both which, taken together, violate the international obligation according to the International Law Commisson (ILC) Commentaries 2001 Articles on Responsibility of States for Internationally Wrongful Acts.

[26] Yannick Radi, *Rules and PRactices of International Investment Law and Arbitration* (1edn, CUP 2020) 158.

In order to decide whether is there a hierarchy between indirect expropriation and the regulatory freedom, and if so which concept is superior, we must first analyze the normative relationship. There is a tendency to assume that indirect expropriation has a higher normative value as compared to regulatory freedom because it is a treaty norm whereas the regulatory freedom is found in customary international law.[27] However, ICJ Statute Article 38 does not provide a hierachial order. The structure merely represents practical convenience based on ease of categorisation. The fact that the tribunals almost always look at the treaty first and refer to custom when necessary as a secondary step is not due to the higher hiearchy of a treaty norm, but because it is more convenient to look into a treaty first as it sets out rights and obligations of the state clearly and it is easy to locate the contents.[28] It does not follow that a treaty is superior than the customary law. They both are created by state consent whether explicit and implied.[29] Therefore, they are equivalent norms with binding force.[30] It is fallacious to assume that indirect expropriation due to its being a treaty norm will supersede the regulatory freedom which originates in customary international law.

Yet, Fitzmaurice challenges whether treaties can even be treated as a "source of law" because they merely create contractual rights and obligations for parties and thus, it would be, in fact, more appropriate to understood it as a "source of obligation".[31]

An interpretation rule for the treaties is found in Article 31(3)(c) of the Vienna Convention on the Law of Treaties (VCLT).[32] The article does not provide a discretion, but states adjudicators "shall" use relevant rules of international law as a tool of interpretation.[33] Therefore, in order to defer the operation of regulatory freedom emanating from customary international law, a clear rule to the contrary must exist, and the burden of proof would be upon the party that alleges the existence of a restriction upon sovereignty, or more specifically the regulotory prerogatives. Otherwise, it is the duty of the tribunals to take into account the regulatory freedom when interpreating a treaty. This is a natural consequence of the *exclusion unis est exclusion alterius* which means what is not barred by a treaty is allowed.[34] In the ELSI case, ICJ has used clear language by saying that:

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[27] Aniruddha Rajput, 'Chapter 7: Regulatory Freedom (Customary Norm) and Indirect Expropriation (Treaty Norm): Interaction of Norms', in Aniruddha Rajput, *Regulatory Freedom and Indirect Expropriation in Investment Arbitration*, (Kluwer Law International 2018) 134.

[28]Karol Wolfke, 'Treaties and Custom: Aspects of Interrelation' in Jan Klabbers and René Lefeber (eds) Essays on the Law of Treaties: A Collection of Essays in Honour of Bert Vierdag, (The Hague, Boston: M. Nijhoff Publishers 1998), 37.

[29] Vladimir Duro Degan, *Sources of International Law* (The Netherlands: Martinus Nijhoff Publishers, 1997) 181.

[30] Mark Villiger, *Customary International Law and Treaties: A Manual on the Theory and Practice of the Interrelation of Sources* (Kluwer Law International 1997) 58,59; See also Luigi Condorelli, 'Customary International Law: The Yesterday, Today, and Tomorrow of General International Law' in Antonio Cassese (ed.) *Realizing Utopia: The Future of International Law* (Oxford University Press 2012), 149,150.

[31] Gerald Fitzmaurice, 'Some Problems Regarding the Formal Sources of International Law' in JHW. Vezjil (ed.) *'Symbolae Verzijl: présentées au professeur J.H.W. Verzijl à l'occasion de son LXXième anniversaire'* (Martinus Nijhodd 1958) 157, 158.

[32] Article 31(3)(c), United Nations, Vienna Convention on the Law of Treaties, 23 May 1969, United Nations, Treaty Series, vol. 1155, p. 331, available at <https://www.refworld.org/docid/3ae6b3a10.html> accessed 27 August 2021.

[33] ibid.

[34] "Expressio unius est exclusio alterius." *Merriam-Webster Legal Dictionary,* Merriam-Webster, https://www.merriam-webster.com/legal/expressio%20unius%20est%20exclusio%20alterius. Accessed 27 Aug. 2021.

"The Chamber has no doubt that the parties to a treaty can therein either agree that the local remedies rule shall not apply to claims based on alleged breaches of that treaty; or confirm that it shall apply. Yet the Chamber finds itself unable to accept that an important principle of customary international law should be held to have been tacitly dispensed with, in the absence of any words making clear an intention to do so."[35]

An argument stating that by entering into a treaty the host state party has confirmed to abonden the right to regulate cannot be accepted. As stated in the previous Section the right to regulate is an attribute of state sovereignty and by entering into international agreements the state only reinforces its sovereignty by directly using its attributes of entering into agreements at an international level.[36] The police powers doctrine arising from custom as a reflection of the state sovereignty suggests that the regulatory freedom is part of custom and must be applied equally conflicts with the decisions of the tribunals who opted for the "sole effects" doctrine. Under the latter the tribunals base their answer to the question of whether there is a regulatory taking on the effects of the relevant state conduct. However, up to the present, neither doctrine whether sole effects or police powers has steadily gained an edge over the other in arbitration practice.

In the hierarchical order, the sole effects is based on academic writings without any prior public practice. Thus, it has a lower normative value than treaties, customary law and general principles of law.[37]

A relevant question is does the sole effects doctrine evolve to be custom as stated in *Tecmed v. Mexico*, thus replace the right to regulate which is called police powers? In order to be regarded as a customary law rule, two elements need to be established: constant state practice and *opinio juris*.[38] It can be said that there is a state practice as the most tribunals apply the sole effects doctrine instead of police powers doctrine, and the awards are automatically enforced on the host states. However, a pyschological element that is a belief among states that the sole effects doctrine has become a legal obligation[39] is lacking. This is evidenced with the recent state practice to clarify indirect expropriation clauses by adding definitive elements to enhance their regulatory space in order to take measures in the public interest. Without *opinio juris*, a norm cannot reach the level of being a custom. Therefore, the claim of creation of custom based on the decisions of tribunals mandated by parties' agreement is farfetched.[40]

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[35] *Elettronica Sicula S.p.A. (ELSI) (United States of America v. Italy*), Judgement, 20 July 1989, para. 50.
[36] S.S. Wimbledon (U.K. v. Japan), 1923 P.C.I.J. (ser. A) No. 1 (Aug. 17), para. 35.
[37] Aniruddha Rajput, 'Chapter 7: Regulatory Freedom (Customary Norm) and Indirect Expropriation (Treaty Norm): Interaction of Norms', in Aniruddha Rajput, *Regulatory Freedom and Indirect Expropriation in Investment Arbitration*, (Kluwer Law International 2018) 150.
[38] Article 38, United Nations, Statute of the International Court of Justice, 18 April 1946, available at: <https://www.refworld.org/docid/3deb4b9c0.html> accessed 2 July 2021.
[39] David Bederman, *International Law Frameworks,* (Cambridge University Press 2001) 15,16.
[40] See Rudolph Dolzer, 'Indirect Expropriations: New Developments?' (2002) New York University Environmental Law Journal, 11 64, 90,92.

4. ICSID Practice So Far on Indirect Expropriation Claims

The traditional BITs are silent on what kind of state measures will amount to indirect expropriation. Domestic legislations on foreign direct investment (FDI) are usually mere repetitions of the BITs. Another important source is arbitration awards. The tribunals many times attempted to define what is meant by indirect expropriation, and often conducted a three-step analysis.

1. Does it have an expropriatable character?

Is this property an 'investment' to be protected for the purposes of the relevant IIA? If so, it will be protected as an investment thus subject to a guarantee against expropriation. Otherwise it is not protected under the BIT, and the investor cannot rely on the treaty neither for a substantive protection nor for arbitration as an alternative dispute resolution mechanism to the local courts of the host state.

2. What is the impact of the state measure on the investment?

The tribunals tempted to put a legal definition to indirect expropriation which more seems to be a threshold. It is often defined as the substantial devastation of the economic value of an investment or deprivation of the investor's abilities to control its property in a reasonable manner.[41] However, what is meant by substantial has not been clarified either in the text of the treaties nor by the tribunals. Only, the tribunal in *Tokios*[42] has suggested that "a reduction of 5% of the value of an investment will not be sufficient to find an expropriation, while a diminution of 95% would likely be sufficient". Nevertheless, the troublesome part is where the degree of interference is in between these percentages, such as 50%.[43]

Under the traditional BITs, most tribunals stick with the definition and merely look at the adverse effects of the state measure on the investment regardless of the nature, purpose or intent of the measure alleged to be expropriatory.[44] This is the 'sole effects' doctrine. The outcome of the application of this doctrine leads to a situation where the government measure has substantially diminished the value of the investor's business, it *per se* amounts to expropriation regardless of its public welfare objectives. It has been critisized as the state's *raison d'etre* which is the collective public interest is basically ignored by the international adjudicators that acceded by the parties' agreement.

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[41] However, what should be understood by substantial has not been clarified either in the treaty texts nor by the arbitral jurisprudence. In this respect, the Tokios tribunal expressed its views that a reduction of 5% of the value of an investment will not be sufficient to find an expropriation, while a diminution of %95 would likely be sufficient. Yet, the problem is still ongoing as the grey areas have left uncovered such as where the degree of interference resulted in around %60-70 diminution of the investment's value; See for example ,*Tokios Tokelés v Ukraine,* ICSID Case No ARB/02/18 at [120]; *Pope and Talbot Im v Canada*, UNCITRAL, Interim Award, 26 June 2000 at [102].

[42] *Tokios Tokelės v Ukraine*, ICSID Case No ARB/02/18, Award, 26 July 2007.

[43] The LG&E v. Argentina tribunal recalled that "in many arbitral decisions, compensation has been denied when the State's measure has not affected all or almost all the investment's economic value" LG&E v. Argentina, Decision on Liability, 3 October 2006, para. 191.

[44] See for example *Compañia del Desarrollo de Santa Elena, SA v The Republic of Costa Rica* (2000) 39 ILM 1317 at 1329; Tippetts(1984) 6 Iran-US CTR 219 at 225-26; Siemens A.G. v. The Argentine Republic, ICSID Case No. ARB/02/8; Biwater Gauff (Tanzania) Ltd. v. United Republic of Tanzania, ICSID Case No. ARB/05/22; Saipem S.p.A. v. The People's Republic of Bangladesh, ICSID Case No. ARB/05/07.

3. Is there a justifiable ground for expropriation, more specifically may a public policy goal legitimize substantial deprivation?

Some tribunals refer to the same definition of the substantial devastation of the investment's value or control, but they provide an exception that the measures that serve public purpose, taken in due process, and non-discriminatory fall within the ambit of the state's police powers, and are not indirect expropriation.[45] Thus, there is no obligation to pay compensation.[46] This is called the 'police powers' doctrine.[47] Since the concept is very broad and hard to define, it is difficult for a foreign investor to challenge this aspect.[48] In other words, it is really hard to find a state measure which the ultimate aim is not public good. If we can find one, it would probably be a targeted measure which discriminates the foreign investor. In this scenerio, the discriminatory measure would be outside the acceptable scope of the regulatory freedom.

It is salient to note that the police powers doctrine is far from being certain. The uncertainties are twofold. First relates to whether the doctrine exists to exclude certain measures from being classified as expropriatory.[49] Secondly, even if it is accepted as applicable, the exact scope is uncertain.[50]
An illustration of the two major doctrines in arbitration jurisprudence is given below.
The host state adopted a new policy requiring the companies which use X chemical to pay additional tax in order to protect the environment.

Doctrines / **Loss of Value**	**Sole Effects**	**Police Powers**
%5 loss of value	no expropriation no compensation	no expropriation no compensation
%90 loss of value	expropriation compensation required	no expropriation no compensation

Neither doctrine provides for a satisfactory balance for the competing values. Under the sole effects doctrine which seems to be the most preferred approach amongst the tribunals, the host state

[45] Noam Zamir, 'Police Powers Doctrine in International Investment Law' (2017) 14 318, 337.
[46] See for example, *Sedeo* (1985) 9 Iran-US CTR 248 at 275.
[47] Ben Mostafa, 'The Sole Effects Doctrine, Police Powers and Indirect Expropriation Under International Law' (2008) 15 Aust. Int. Law J. 279.
[48] David Collins, *An Introduction to the International Investment Law,* (1edn, CUP 2016) 170.
[49] Ben Mostafa, 'The Sole Effects Doctrine, Police Powers and Indirect Expropriation Under International Law' (2008) 15 Aust. Int. Law J. 267
[50] See for broader interpretation *Methanex Corporation v. United States*, Award, 9 August 2005, 44 ILM 1345*;* See also *Saluka Investments BV v. The Czech Republic*, Permanent Court of Arbitration (17 March 2006); *Marvin Roy Feldman Karpa v. United Mexican States,* ICSID Case No. ARB(AF)/99/1; Suez, Sociedad General de Aguas de Barcelona S.A v. The Argentine Republic, ICSID Case No. ARB/03/17; *Chemture v. Canada*, Award, 2 August 2010; Ben Mostafa, 'The Sole Effects Doctrine, Police Powers and Indirect Expropriation Under International Law' (2008) 15 Aust. Int. Law J. 267, 277; Simon Baughen, 'Expropriation and Environmental Regulation: The Lessons of NAFTA Chapter Eleven' (2006) 18 J. Environ. Law 207, 211; Jason Gudofsky, 'Shedding Light on Article 1110 of the North American Free Trade Agreement (NAFTA) Concerning Expropriations: An Environmental Case Study' (2000) 21 Northwest. J. Int. Law Bus. 243, 290.

cannot adopt a policy for environmental protection or any other public purpose without being accused by expropriation unless the investor's loss is just a fraction of money, as shown in the table. Whereas, under the police powers doctrine, any measure that serves a public purpose would be within the police powers of a state, and non-compensatable.

4. Can the proportionality or reasonableness test legitimize the host state measure[51]? Although originated in domestic administrative law field,[52] the proportionality analysis has evolved as an international judicial technique for reconciling between the competing values of protection of public and private rights.[53] The investment tribunals have increasingly taken into account the host state's regulatory freedom in their evaluation considering claims of indirect expropriation, acknowledging the need to balance between investor and host state interests. While there is no single established test in the proportionality analysis, the commonly used technique consists a preliminary appraisal of the legitimacy of the state measure's objective, then three steps of suitability, necessity and strict proportionality.[54]

The preliminary step of the assessment of the legitimacy of the measure's objective in terms of whether it serves the public good aims at excluding illegitimate purposes.[55] The suitability analysis requires requires a casual relationship between the measure and its objective. If the host state measure contributes to its public welfare objective, this stage is sufficiently secured.[56] The necessity step requires a host state to adopt a measure which imposes the least burden on the person whose rights will be adversely affected (the investor).[57] The most stringent stage of review, strict proportionality or proportionality *stricto sensu* requries a tribunal to conduct a cost-benefit balancing. In other words, the tribunals weighs two competing interests and reach a conclusion on whether the measure's impact is proportionate to the benefits that the public policy seeks to achieve.

[51] Jonathan Bonnitcha, *Substantive Protection Under Investment Treaties,* 255 (CUP 2014).
[52] Caroline Henckels, 'Indirect Expropriation and the Right to Regulate: Revising Proportionality Analysis and The Standard of Review in Investor-State Arbitration', (2012) Journal of International Economic Law 15(1) 223, 226.
[53] See Moshe Cohen-Eliya and Iddo Porat, 'American Balancing and German Proportionality: The Historical Origins', 8 International Journal of Constitutional Law (2010) 263; Jurgen Schwarze, 'The Principle of Proportionality and the Principle of Impartiality in European Administrative Law', Rivista Trimestrale di Diritto Pubblico (2003) 53, 55; Alec S. Sweet and Jud Matthews, 'Proportionality Balancing and Global Constitutionalism', 47 Columbia Journal of Transnational Law (2008) 72, 73-75.
[54] Caroline Henckels, 'Indirect Expropriation and the Right to Regulate: Revising Proportionality Analysis and The Standard of Review in Investor-State Arbitration', (2012) Journal of International Economic Law 15(1) 223, 227.
[55] Julian Rivers, 'Proportionality and Variable Intensity of Review', 65 Cambridge Law Journal (2006) 174, at 196.
[56] E.g. Jan Jans, 'Proportionality Revisited', 27 Legal Issues of Economic Integration (2000) 239, at 240, 244; George Bermann, 'Proportionality and Subsidiarity', in Catherine Barnard and Joanne Scott (eds), The Law of the Single European Market: Unpacking the Premises (Oxford: Hart, 2002) 75, at 80; Jeremy Gunn, 'Deconstructing Proportionality in Limitations Analysis', 19 Emory International Law Review (2005) 465, at 467; Tridimas, 'General Principles', above n 10, at 139; Andenas and Zleptnig, above n 10, at 388–89; Rivers, 'Variable Intensity', above n 11, at 198; Kumm, 'Political Liberalism', above n 7, at 138.
[57] Julian Rivers, 'Proportionality, Discretion and the Second Law of Balancing', in Pavlakos (ed), above n 7, 167, at 171, 177; Barak, above n 10, at 317, 320–21.

It is salient to note that these stages are successive, yet, described as a 'nested sequence of succesively more stringent tests.'[58] For example, the methodology followed in the *Tecmed* award (that is the first expropriation decision to have elaborated on the proportionality analysis as a means of determining whether a measure that have been taken in the exercise of police powers reflects a proper balance between the interests of the host state and investor) was flawed in proceeding directly to evalutating the measure's strict proportionality after the first step of legitimacy analysis without applying the second and third steps, suitability and necessity.[59]

Besides the proportionality analysis, Iran-US Claims tribunal proposed another line of approach, which suggests that indirect expropriation occurs where there is 'unreasonable interference' with the property rights of the investor. However, what is meant by 'unreasonable interference' or whether it established a brand-new legal test is uncertain.

There are four possible interpretations of this test:

(1) If the reasonableness of a measure is determined by the severity of its impact on the investment, then this approach would be in accordance with the *sole effects* doctrine.[60]

(2) If reasonableness refers to a weighing up of the objectives pursued by the measure against its negative impacts, it would provide a *proportionality* test.

(3) Weighing up test can lead to multiple outcomes. Where a measure produces an effect that reaches the substantial deprivation threshold, then if the measure is proportionate to the objective it pursues, the expropriation is not occurred; or

(4) Where the required threshold is not met, an expropriation may be held to occur[61] depending on the tribunal's methodological preferences.

[58] Don Regan, 'The Meaning of ''Necessary'' in GATT Article XX and GATS Article XIV: the Myth of Cost–Benefit Balancing', 6 World Trade Review (2007) 347, 351; Takis Tridimas, The General Principles of EU Law (OUP 2006) 139; Mads Andenas and Stefan Zleptnig, 'Proportionality: WTO Law in Comparative Perspective' 42 Texas International Law Journal (2006) 371, 388.

[59] Caroline Henckels, 'Indirect Expropriation and the Right to Regulate: Revising Proportionality Analysis and The Standard of Review in Investor-State Arbitration', (2012) Journal of International Economic Law 15(1) 223, 233.

[60] Ben Mostafa, 'The Sole Effects Doctrine, Police Powers and Indirect Expropriation Under International Law' (2008) 15 Aust. Int. Law J. 267, 282.

[61] See *James and others v. United Kingdom* [1986] ECHR 2.

5. Emerging Trends in International Investment Agreements

5.1 Clarified Indirect Expropriation Clauses

In order to introduce greater clarity and predictability in the BITs with regard to the concept of indirect expropriation, particularly to allow host states and investors to appreciate and comply with the rules applicable to their relationship and to decrease the high level of discretion currently entrusted on to ad hoc investment tribunals to decide the legitimacy of the host state public interest regulations[62], states began to add further clarification into their investment agreements. This has been done by adding clarification provision through an annex appended to the treaty or within the same article following the general prohibition on expropriation without compensation. There are mainly three categories of clarified expropriation clauses.

a. Model I: "Carving-out"[63]

Some BITs adopt a carving-out clause that excludes certain non-discriminatory measures to protect legitimate public welfare objectives from the scope of indirect expropriation. This practice appears to implicitly codify the concept of police powers in the investment treaties. This is based on Article XX of the General Agreement on Tariff and Trade (GATT) and Article XVI of the General Agreement on Trade and Services (GATS).

While this practice is pretty straight-forward, other type of BITs include a further assessment on proportionality. They provide that, to be exempted from indirect expropriation, measure should not be 'so severe in the light of their purpose that they cannot be reasonably viewed as having been adopted and applied in good faith.'[64]

The former type of carving-out clause establishes an exception to the general rule on expropriation, whereas the second type merely set forths a rebuttable presumption. It is a rebuttable presumption as even such measures that is to protect legitimate public welfare objectives may constitute indirect expropriation if that measure is so severe to the investor compared to the public benefits. This suggest that assessment will be done through the proportionality analysis. The former carving-out clause provides a flexible system where the host states can enact regulations for public welfare freely.

A related issue is there is no definition as to what should be understood by the concepts 'so severe', 'reasonableness' and 'good faith'. What needs to be established for a state measure to be defined as so severe in light of its purpose that cannot be reasonably adopted in good faith? In the same vein, what is the applicable test to determine whether a state measure is to protect legitimate public welfare objectives? An option is the state conduct at issue be a good faith initiative to address a

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[62] European Parliament Resolution on the Future of the European International Investment Policy (6 April 2011) 2010/2203(INI), para 24.; Federico Ortino, *The Origin and Evolution of Investment Treaty Standards: Stability, Value, and Reasonableness,* (Oxford University Press 2019) 49.

[63] Ying Zhu' 'Do Clarified Indirect Expropriation Clauses in International Investment Treaties Preserve Environmental Regulatory Space' (2019) 60 Harv. Int'l LJ 377, 403.

[64] See Agreement for the Promotion and Protection of Investment, Austria-Taj., art. 7(4), Dec. 15, 2010; Agreement for the Promotion and Protection of Investment, Austria-Kyrg., art. 7(4), Apr. 22, 2016 [hereinafter Austria-Kyrgyzstan BIT); Agreement for the Promotion and Protection of Investment, Austria-Nigeria, art, 7(4), Aug. 4, 2013.

legitimate public concern. The second option is reasonableness which suggest a rational connection with the state conduct and the end pursued. The third option is necessity which puts a higher threshold when scrutinising the state conduct. The tribunal then have to determine whether is there a measure that imposes lower burden on the investor for the state to achieve the same public policy objective.

b. Model II: 'Case-by-case analysis'

Article 8(1) of the 2014 ASEAN-India BIT reads as follows:

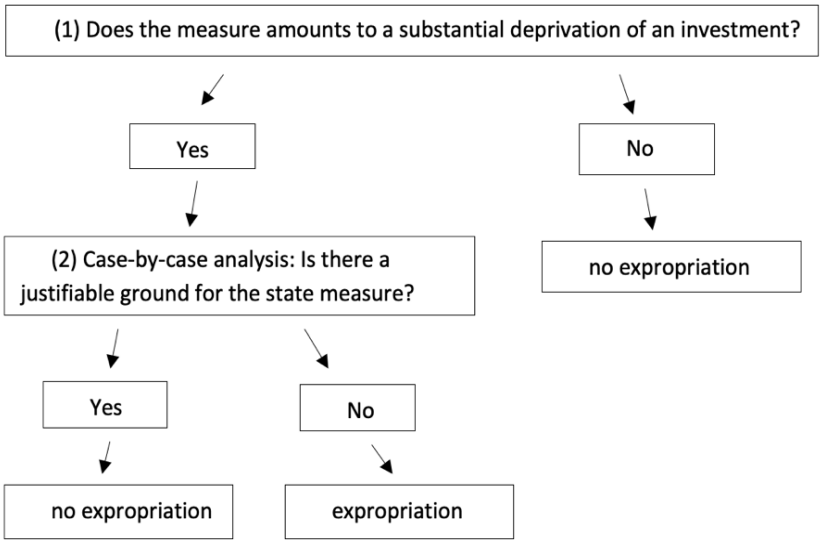
> A Party shall not expropriate or nationalise investments as referred to in subparagraph 1(b) of Article 1 (Scope) either directly or through measures equivalent to expropriation or nationalisation.

An immediate reaction to this article is that there is no change compared with the text of the traditional investment agreements. The aim pursued by Model II is to diminish the ambiguity related to the traditional indirect expropriation clauses. However, it might be failed to bring clarity as the clarified clause provides a wide margin of appreciation to the tribunals by emphasising on the case-by-case analysis. The same provision adds the following language:

> The determination of whether a measure or series of related measures by a Party, in a specific fact situation, constitutes an expropriation of the type referred to in subparagraph 2(b) of this Article requires a case-by-case, fact-based inquiry that considers, among other factors:
> (a) the economic impact of the government measure, although the fact that a measure or series of related measures by a Party has an adverse effect on the economic value of an investment,standing alone, does not establish that such an expropriation has occurred;
> (b) whether the government measure breaches the government's prior binding written commitment to the investor whether by contract, licence or other legal document; and
> (c) the character of the government measure, including its objectives and whether the measure is disproportionate to the public purpose.

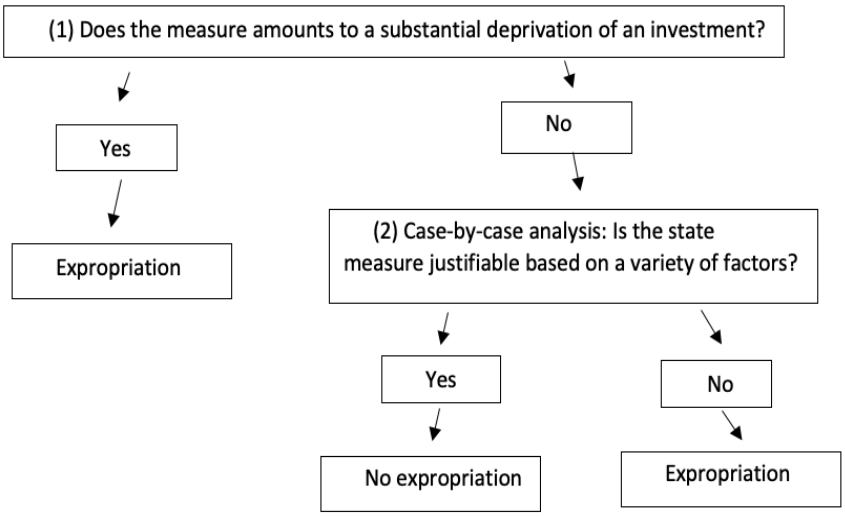
The first question revolves around the relationship between the general rule on expropriation and the case-by-case analysis mostly included in the appendix.

Option 1: ***Rule v Exception***



A first option is a 'rule v exception' relation.[65] The substantial deprivation of the economic value of an investment will lead to the finding of indirect expropriation unless a case-by-case analysis reveals that the public interest goal pursued by the state legitimizes the government measure under review.[66] When compared to the traditional view of expropriation where compensation is due regardless, this gives host states more regulatory sphere by entrusting the arbitrators the duty to analyze whether there is a justifiable ground that legitimizes the government conduct which otherwise be regarded expropriatory.

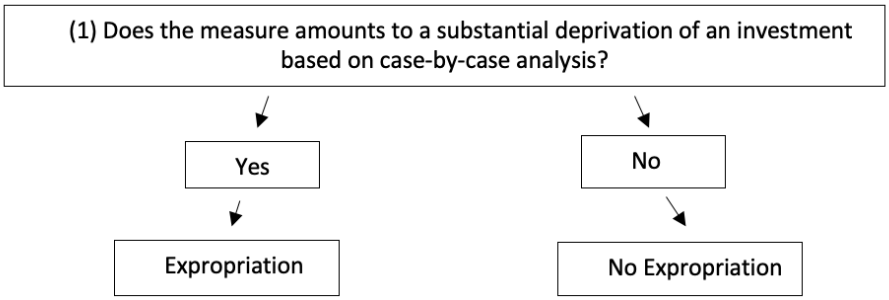
Option 2: ***Per se Taking v Rule of Reason***



[65] Federico Ortino, ' Defining Indirect Expropriation: The TTIP Approach and the (Elusive) Search for 'Greater Certainty'' (2016) 43 Legal Issues of Economic Integration 351.
[66] ibid; Crompton (Chemtura) Corp. v. Government of Canada, PCA Case No. 2008-01, Award, 2 August 2010, para. 249.

A second option is '*per se* taking v rule of reason' relationship.[67] A substantial deprivation will inevitably lead to a finding of indirect expropriation. A case-by-case analysis will be performed where there is lesser degree of deprivation which does not result in indirect expropriation.[68]

Option 3: Subsuming 'substantial deprivation' into 'case-by-case analysis'



A third option is the read 'substantial deprivation' and 'case-by-case analysis' altogether by subsuming the former into the latter. This test would include, as a matter of fact, considering the economic impact of the measure. Thus, in practice it would not alter the current interpretation of the traditional investment agreements by the arbitral tribunals.
The second question revolves around the very nature of the 'case-by-case' inquiry. There is no objective criteria. Thus, there is no clue as to what kind of case-by-case analysis will be conducted by the arbitral tribunals. The jurisprudence will not be reliable even in similar cases as there is no *stare decisis* in international investment law. Such an unclear language may involve various tests that involves different levels of interference with the host state's capacity to regulate.

The reading of indicative factors that will be taken into account in the analysis that include both the economic impact and the character of the state measure together suggests that the test is proportionality. A first option is strict proportionality. The strict proportionality regards the balance between costs undertaken by the investor's investment due to the public policy measure and the benefits of that measure. The tribunal will assess whether the adverse effect is proportional to the benefits of the measure. Another inquiry is what will the tribunal decide about the question of which will take precedence individual rights or public interest. There is no criteria and the outcome of the awards is inconsistent. It would be challenging to reach a conclusion on a point that will eventually affect millions of citizen in a country.

A second option is principle of proportionality which is a broader concept. It consists of three elements. The first element is suitability which requires a rational connection between a state measure and the public interest objective sought to be achieved. In other words, the measure should contribute to the chosen policy objective. The second element is necessity which requires the measure to impose the lowest possible burden on the investor. If there is another measure that is equally plausable to reach the public objective being pursued with the least interference on the

[67] ibid.
[68] This option reflects the American way on regulatory takings as put forward in Parvanov and Kantor. See Parvan Parvanov & Mark Kantor, Comparing US Law and Recent US Investment Agreements: Much More Similar than you Would Expect, in Yearbook on InternationalInvestment Law and Policy 2010-2011 767 (Andrea Bjorklund ed., OUP 2012).

investor, that measure should be preferred. The third element is strict proportionality which requires the cost and benefit balancing.

Many clarified BITs consist of legitimate expectations caused by written commitments as a factor to be taken into account in a case-by-case analysis. The third question is how much weight will be given to the legitimate expectations? For example, what will happen when a measure has passed the proportionality test due to its strong public benefits with a minimum adverse effect on the investor but at the same time the investor has been given binding written commitments from a government authority? Because legitimate expectations do not seem compatible with the proportionality test, will it be considered as a conclusive element by itself? However, the fact that it is listed next to the other factors which will cumulatively be taken into account when deciding on whether the measure is found to be an indirect expropriation does not support this view.

c. Model III: 'Carving-out' + 'Case-by-case analysis'

Most investment treaties clarifying indirect expropriation clauses combine Models I and II by requiring a case-by-case inquiry of indirect expropriation and at the same time carving out public welfare regulations from constituting indirect expropriation.[69] For instance, the Annex 812.1 of Canada-Peru FTA reads as follows:

> (b) The determination of whether a measure or series of measures of a Party constitutes an indirect expropriation requires a case-by-case, fact- based inquiry that considers, among other factors:
> (i) 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,
> (ii) the extent to which the measure or series of measures interferes with distinct, reasonable investment-backed expectations, and
> (iii) the character of the measure or series of measures;
> (c) Except in rare circumstances, such as when a measure or series of measures is so severe in the light of its purpose that it cannot be reasonably viewed as having been adopted and applied in good faith, 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 expropriation.

However, how the tribunals should interpret the *combined clause* is far from being clear. Should the tribunals conduct a case-by-case analysis for the purposes of determining whether a host state measure falls under the category that is described as a 'non-discriminatory measures that are designed and applied to protect legitimate public welfare objectives' or more specifically in order to determine a rare circumstance?

[69] Ying Zhu, 'Do clarified indirect expropriation clauses in international investment treaties preserve environmental regulatory space?' (2019) Harvard international law journal (60 (2) 377, 405.

The former interpretation gives a more restrictive regulatory domain to the host states whereas the latter provides *bona fide* regulations to be within the police powers of the host state by totally excluding them within the scope of indirect expropriation.

In *Bear Creek Mining v Republic of Peru*, the Government of Canada has expressed his views on the interpretation of a Model III clause found in 2008 Canada-Peru Free Trade Agreement. Canada has stated that after being identified a measure as an alleged indirect expropriation where it caused a substantial deprivation of the economic value of an investment, a case-by-case inquiry shall be carried out whether a host state conduct constitutes a non-discrimatory regulatory measure designed to protect public welfare. The guidance is best taken from its own words:

> *[...] In the case of an alleged indirect expropriation, Annex 812.1 provides guidance on how to distinguish between whether an indirect expropriation and bona fide regulation that does not amount to an expropriation. Whether a measure constitutes a nondiscriminatory, regulatory measure designed to protect public welfare – as opposed to an indirect expropriation – requires a case-by-case, fact based inquiry that considers various factors. The Parties have articulated certain of these factors in Annex 812.1 to guide the Tribunal, including the economic impact of the measure or series of measures, the extent to which the measure or series of measures interferes with distinct, reasonable investment-backed expectations, and the character of the measure or series of measures (for example if the measure is general in nature as opposed to targeting a particular investment). None of these factors will be determinative on its own. Together, they must be weighed along with any other relevant factors. A State is not required to compensate an investment for any loss sustained by the imposition of a non-discriminatory, regulatory measure designed and applied to protect legitimate public welfare objectives.*[70]

Although, the definition of the 'rare circumstances' is not resolved by Canada in its submission, the statements as a whole seem to acknowledge the police powers of a state only if the benefits pursued by a measure is proportional to the burden imposed by the investor. Based on the guidance provided by Canada, the provision should have been codified to give the desired meaning in the following way:

> (b) The determination of whether a non-discriminatory measure or series of measures of a Party that are designed and applied to protect legitimate public welfare objectives, such as health, safety and the environment constitutes an indirect expropriation requires a case-by-case, fact- based inquiry **based on the principle of proportionality** that considers, among other factors:
> (i) 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,
> (ii) the extent to which the measure or series of measures interferes with distinct, reasonable investment-backed expectations,
> (iii) the character of the measure or series of measures.

[70] Submission of Canada Pursuant to Article 832 of the Canada-Peru Free Trade Agreement (Jun. 9, 2016)

5.2. General Exceptions Clause

The second trend concerns the incorporation of a general exceptions clause in the investment agreements. The general exceptions clause is relatively clear in terms of creating *lex generalis* that excludes certain matters from the scope of the application of the protections contained within the investment agreement. How to reconcile the general exceptions clause with the clarified indirect expropriation clause where there is a government measure that falls within the scope of both provisions? For instance, a state measure adopted to protect public health, and public health is regulated as a general exception to the treaty and also as an exception to finding an indirect expropriation.

In this respect, the clarified indirect expropriation clause is *lex specialis* that specifically deal with the same subject. The maxim 'special law repeals general laws' is applicable as a method of interpreting and resolving conflicts of rules. It means that whenever there are two or more standards that deal with the same subject, priority should be given to the most specific standard. Therefore, the clarified indirect expropriation clause takes precedence over the general exceptions clause.

6. Bear Creek Mining Corporation v. Republic of Peru

The current debate is are the clarified indirect expropriation clause effectively preserve state's regulatory space? In order to answer this question, this article will analyze a recent ICSID award: *Bear Creek Mining Corporation* v. *Republic of Peru.* This case in worth-mentioning as it is the first tribunal to comment on a clarified indirect expropriation clause within an investment agreement. This thesis will focus on this case as it is the only award that a tribunal has reviewed a clarified indirect expropriation clause of those that have been made public.

6.1. Background

The case concerns silver mining deposits located close to the Peru-Bolivian border. According to the Constitution of the Republic of Peru there must be 'public necessity' is needed in order for foreign nationals to obtain mining concessions which must be determined by an executive decree.[71]
In order to 'secure' the mining rights, claimant agreed with his local national employee that she would herself apply for these mining rights in her own name, while Bear Creek requested and obtained the authorization required as a foreigner.[72] Then, Ms. Villavicencio and the Bear Creek Mining company entered into few Option Agreements for the future transfer of the mining concessions should Bear Creek satisfy Peruvian legal requirements. On late 2007, after a year-long review and consideration, the Government enacted Supreme Decree 083 authorizing Bear Creek to acquire the seven mining concessions, and subsequently Bear Creek acquired the consessions from its employee.[73]

In 2008, the opposition to the Santa Ana Projects was expressed clearly and repeatedly by the local community.[74] The opposition was based on concerns about unequal distribution of the benefits of the Santa Ana Project and the adverse environmental effects.[75] social unrest has showed itself by attacks and threatening of the staff members of the Bear Creek. In 2011, the several community leaders submitted a memorial to the President requesting the permanent withdrawal of the Bear Creek Mining Company. The discontent has continued for three years. On 28 May 2011, the Government issued the Supreme Decree 028 to suspend the review of the claimant's ESIA and the 1-year suspension of the granting of mining concessions in the Puno area. These failed to quell the protests. The protests continued until the Government enacted Supreme Decree 032 on 24 June 2011. Supreme Decree 032 has derogated the Supreme Decree 083 which lead to the cancellation of the mining consessions given to the claimant previously.

[71] Article 71, the Constitution of Peru, enacted on 31 December 1993
[72] *Bear Creek Mining Corporation v Republic of Peru*, ICSID Case No ARB/14/21, Award (30 November 2017), paras. 126-132.
[73] ibid paras. 149 , 150.
[74] See Nicolas M. Perrone, 'The International Investment Regime and Local Populations: Are the Weakest Voices Unheard?' (2016) 7 TLT 383.
[75] *Bear Creek Mining Corporation v Republic of Peru*, ICSID Case No ARB/14/21, Award (30 November 2017), paras. 152-169.

The question in front of the *Bear Creek v Republic of Peru* tribunal revolves around whether the Supreme Decree 032[76] effected an indirect expropriation.

6.2. Evaluation of the Clarified Indirect Expropriation and the General Exceptions Clauses

The reading of the case reveals that the tribunal adopted a flawed methodology. The tribunal "jumped" to apply the Annex 812.1 on indirect expropriation before clarifying whether there is an expropriation that substantially deprives of the economic value of the investment. Perhaps, this can be explained by the fact that the express derogation of the previous decree (that is Supreme Decree 083) that gave the mining concessions makes it obsolete that the investment has been completely annihilated. Nevertheless, for the sake of clarity, the tribunal should have demonstrated how it reached from point A to point B. This would also prevent any possibility of the future annullment of the award.

More fundamentally, the tribunal did not deal with subsection(c) of the Annex 8.12 which states 'except in rare circumstances, such as when a measure or series of measures is so severe in the light of its purpose that it cannot be reasonably viewed as having been adopted and applied in good faith, 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 expropriation'. This statement creates a presumption that non-discriminatory regulatory measures do not constitute indirect expropriation. This is to give host states more regulatory freedom. Instead, the tribunal first examined whether the alleged expropriatiory measure (Supreme Decree 032) fall under the "factors" in the Annex 812.1.

However, The tribunal should have first applied the section(c) of the Annex 8.12. Canada's guidance on the interpretation of Canada-Peru FTA also supports that by stating that the factors given for the case-by-case analysis is investigated to decide whether the measure is non-discriminatory and applied to protect legitimate public welfare objectives that are referred to in 812.1(c). Thus, subsection (c) take precedence over subsection (b). If an accurate methodology would be followed, the most important issue would be whether the Decree 032 is discriminatory. However, the tribunal did not conduct a detailed analysis on the question of discrimination. It found that it is a discriminatory measure based on unknown reasons. The Respondent's arguments are enlightening:

> Supreme Decree 032 is not discriminatory. Rather, Respondent took a specific action related to Santa Ana based on its unique circumstances, namely, its dubious acquisition and its status as a lightning rod for protest.473 Although Claimant points out that no other mining company lost its right to own and operate mining concessions, Claimant does not identify a single comparable mining company that was the target of protests or that used a scheme similar to Claimant's to acquire concession rights. Unless and until Claimant can identify another mining company in similar circumstances, its discrimination argument merits no consideration.474 The protests in

[76] Supreme Decree No 032-2011-EM, published in the Official Journal of the Peruvian State: http://www.minem.gob.pe/minem/archivos/DS%20N%C3%82%C2%BA%20032-2011-EM.pdf.

southern Puno focused directly on the Santa Ana Project and, therefore, taking actions with respect to Santa Ana in particular was a rational regulatory choice.

The tribunal disregarded the subsection (c) completely, and it has given an insufficient reason for its disregard by absurdly saying that because the FTA contained very detailed provisions concerning expropriation as well as a general exemption clause for the investment chapter, no other exceptions from general international law or otherwise would apply. The overall reading of the case reveals that tribunal stated this to mean that it did not have to discuss the police powers doctrine as argued by the parties, however this does not explain why it did not consider subsection (c) which is not arising from the police powers doctrine but it is clearly within the text of the treaty. Furthermore, the existence of a general exceptions clause cannot disqualify this section or take precedence of it.[77] Yet, as a general principle of legal methodology *lex specialis derogat legi generali,* specific provisions take precedence over the more general one such as in this case general exemption clause.

With regard to the application of the general exemption clause, the tribunal stated that Peru's measure might come within the exception relating to measures necessary to protect human health or life. However, the tribunal noted that Peru had not explained why it was necessary for the protection of human life not to offer compensation. This does not seem the sound interpretation of the general exceptions clause. Because should the duty to pay compensation would still be applicable even the host state measure falls within the exemption clause, then what is the rational of introducing this clause in the text? As the name implies, it should exempt the party from an obligation if his action or measure falls within one of the exceptions provided. Concluding otherwise would conflict with the parties' clear intentions in the treaty. The general exemption clause reflects article XX of GATT in WTO. The tribunal did not refer to WTO case law for interpreting what is the legal interpretation of necessary and non-discriminatory.

Although the parties make clear what is meant by indirect expropriation by excluding measures that are taken in a non-discriminatory manner for the public interest, the tribunal did not take the clear wording in the treaty into account. By stating that it cannot be interpreted in a way that gives less protection than the customary international law. In my opinion, when there is a clear words reflecting the parties' intention it is not up to the tribunal to second guess or do not believe what the parties have actually made clear. Even this clear language is not sufficient for tribunals to give more regulatory freedom for the host state to take measures on behalf of their citizens. This explains the reason why few states have signed out the icsid convention.

[77] Andrew Newcombe, 'General Exceptions in International Investment Agreements' in Marie-Claire Cordonier Segger, Markus W. Gehring and Andrew Newcombe (eds), *Sustainable Development in World Investment Law* (Kluwer Law International 2011) 351, 368.

7. Conclusion

The dissatisfaction with the current investment arbitration regime is twofold. Firstly, the traditional investment agreements and domestic legislations have failed to provide a definition for indirect expropriation. This together with the lack of *stare decisis* has led the application of the indirect expropriation clauses by the arbitral tribunals in an inconsistent manner. Secondly, the arbitral tribunals have adopted a pro-investor approach when deciding on indirect expropriation and often ignored the public interest goals pursued by the state measures by obliging states to pay huge amounts of compensation to the adversely affected investors.

Since relatively recently, the states have began to add definitive elements to their newly concluded BITs to decrease the current margin of appreciation entrusted to the tribunals. The clarified indirect expropriation clauses has emerged in three different models. Each model offers different levels of regulatory sphere to the host states. There are doubts about whether the clarified indirect expropriation clauses effectively preserve the regulatory sphere of the host state as there are several interpretation options for each. The fact that it is not possible to know in advance which option will be adopted by the arbitral tribunal brings about the same inconsistency critisism against the investment law regime. Another line of approach by the host states is the introduction of the general exceptions clause. However, the tribunal in *Bear Creek Mining v Republic of Peru* has demonstrated that even the clear words within the general exception clause is not sufficient to preserve the regulatory freedom of the host states.

In *Bear Creek Mining v Republic of Peru,* the methodology adopted by the tribunal was fallacious. This has lead to concerns about the future of the investment law in the eyes of both host states and investors. Although, the clarified indirect expropriation clauses has been emerged to balance the public and private interests, this case has compeletely ignored the public policy objectives pursued. The tribunal was of the view that the general exceptions clause does not offer any waiver from the obligation to compensate for the expropriation. However, this approach renders the rationale behing the general exceptions provision meaningless. The right to regulate which arises from customary international law cannot be a secondary source because there is a treaty provisions. Instead, both of them shall be applied mutually as set forth in the ICJ Statute. The case law has proved that a future reform for the concept of indirect expropriation is needed. The indirect expropriation clauses shall incorporate a legal test to balance the interests correctly.

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