Investment Treaty Law and the Fear for Sovereignty:
Transnational Challenges and Solutions

by Jan Kleinheisterkamp[*]

Introduction

Investment treaty arbitration is growing steadily - and so are the public voices questioning its legitimacy and its impact on sovereignty. A key feature of international investment agreements (IIA) is that they delegate judicial review of public acts affecting foreign investors to international arbitral tribunals and allow foreign investors directly to bring claims against host states.[1] But it is the combination of this procedural mechanism with the substantive law established by these IIA that really gives rise to concern. IIA establish international substantive standards of protection of foreign investors against state action or inaction. These standards constitute the yardstick against which the acts of the host state are measured in order to determine its liability to the foreign investor under international law. It is rather uncontroversial today that the degree of vagueness of these standards of judicial review such as fair and equitable treatment, full protection and security, and indirect expropriation, 'creates an especially difficult challenge'.[2] It is not too far-fetched to argue that these standards, as they currently stand, grant virtually unfettered discretion, if not even

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[*] Associate Professor of Law at the Law Department of the London School of Economics. Email: j.kleinheisterkamp@lse.ac.uk. Earlier versions of this paper have been presented at the LSE Transnational Law Project Workshop on 'Paradigms, Methods and Analogies in Investment Treaty Law' on 1 September 2010 and at the IALS WG Hart Legal Workshop on 'Sovereignty in Question' on 30 June 2011. I would like to thank Jacco Bomhoff, Jonathan Bonnitcha, Vladislav Djanic, Christian Djeffal, Monika Hlavkova, David Gaukrodger, Geoffrey Gertz, Noel Johnston, John Kline, Jan Komarek, Andrew Lang, Lauge Poulsen, Anthea Roberts, Joanne Scott, Taylor St John, Chris Thomas, Stephan Schill, Pallavi Sengupta, as well as all participants of the 2nd Investor-State Workshop at Essex Court Chambers on 24 March 2014, especially Toby Landau and Daniel Bethlehem, and finally the two anonymous reviewers for valuable comments. Any opinions or errors remain exclusive mine.

[1] For the conceptualisation see F Ortino, 'The Investment Treaty System as Judicial Review' (2013) 24(3) American Review of International Arbitration 437-468; for a leading critique of investment arbitration see G van Harten, *Investment Treaty Arbitration and Public Law* (OUP 2007).

[2] *Suez, Sociedad General de Aguas de Barcelona SA and InterAguas Servicios Integrales del Agua SA v Argentine Republic*, ICSID Case No ARB/03/17, Decision on Liability of 30 July 2010, ¶ 196. See also *Saluka Investments BV v Czech Republic* (UNCITRAL), Partial Award of 17 March 2006, ¶ 297 ('The "ordinary meaning" of the "fair and equitable treatment" standard can only be defined by terms of almost equal vagueness'); *CMS Gas Transmission Company v Argentine Republic*, ICSID Case No. ARB/01/8, Award of 12 May 2005 ¶ 273 ('Argentina's concern about [the Fair and Equitable Treatment standard] being somewhat vague is not entirely without merit'). See also Z Douglas, *The International Law of Investment Claims* (CUP 2009) ¶ 150; A von Aaken, 'International Investment Law between Commitment and Flexibility' (2009) 12(2) J Int'l Econ L 507, 514 and 527-531; S Schill, 'Enhancing International Investment Law's Legitimacy: Conceptual and Methodological Foundations of a New Public Law Approach' (2011) 52 Virginia J Int'l Law 57, 66-67.

‘quasi-legislative authority’ to arbitrators,[3] who are neither bound by any precedent and do not have to fear any meaningful review of their awards.[4] Issues of consistency and predictability become all the more problematic in view of the uncertainty not only regarding the rules applied but also the methods for applying them.[5]

These concerns, acerbated by the ever increasing magnitude of claims, have given rise to strong criticism against the investment treaty system, which is said to suffer a serious legitimacy crisis.[6] The question of legitimacy is linked to how the system’s current operation is perceived as not only limiting but also eroding the ‘policy space’ of countries hosting foreign investments, giving increasingly rise to fears for their sovereignty. What is striking, in any case, is the very limited consciousness of policy makers in the past of the degree to which the exercise of national sovereign powers of hosts states might actually be affected,[7] given that virtually every aspect of public regulation is susceptible of being scrutinised on such basis and potentially sanctioned through damages awards that are directly enforceable worldwide.

Given its efficiency, it is unlikely that the investor-state-arbitration mechanism, as presently implemented by IIAs in combination with the ICSID Convention, will be fundamentally overhauled or generally abandoned in the short or medium term. Investment treaty arbitration is here to stay, at least for quite some time, let alone because of the ‘survival clauses’ in most existing 3000 plus IIA that provide for continued protection for 10-20 years after their termination.[8] In the meanwhile, the existing regime will have a significant influence on the development of substantive investment law and is likely to raise more fears over its potential impact on host countries’ sovereignty and potentially on the notion of sovereignty all together. Some academics have argued that issues of adjudicatory consistency might be

[3] See, eg, CH Brower II, ‘Structure, Legitimacy, and NAFTA's Investment Chapter’, (2003) 30 Vanderbilt J Transnat’l L 37, 66; A Stone Sweet, ‘The New *Lex Mercatoria* and Transnational Governance’ (2006) 13 Journal of European Public Policy 627, 641; WMC Weidemaier, ‘Towards a Theory of Precedent in Arbitration’, (2009-10) 51 Wm & Mary L Rev 1895, 1940.
[4] *cf* Articles 52(1) and 53(1) ICSID Convention and Articles 34 UNCITRAL Model Law on International Commercial Arbitration and Article V(2)(b) of the UN Convention on the Recognition and Enforcement of Foreign Arbitral Awards.
[5] T Wälde, ‘Interpreting Investment Treaties: Experiences and Examples’, in C Binder et al (eds), International Investment Law for the 21st Century: Essays in Honour of Christopher Schreuer (2009) 724, 725 (‘Confusion, rather than clarity, prevails in today’s practice of investment arbitration’).
[6] For many see S Frank, ‘The Legitimacy Crisis in Investment Treaty Arbitration: Privatizing Public International Law Through Inconsistent Decisions’ (2005) 73 Fordham L Rev 1521, 1584-1587; M Sornarajah, ‘A Coming Crisis: Expansionary Trends in Investment Treaty Law’, in: K Sauvant (ed), *Appeals Mechanisms in International Investment Disputes* (OUP 2008) 39, 41; Schill, *IIL and Comparative Public Law* (n 2) 4-7.
[7] See L Poulsen and E Aisbett, ‘When the Claim Hits: Bilateral Investment Treaties and Bounded Rational Learning’, (2013) 65 World Politics 273-313.
[8] A Carska-Sheppard, ‘Issues Relevant to the Termination of Bilateral Investment Treaties’ 26(6) J Int’l Arb (2009) 755–71.

solved by the emergence of *de facto* or quasi precedential value of the arbitral case law;[9] others have questioned whether this is feasible and desirable.[10] In any case, the central question remaining: can – and how can – arbitrators in their decisions square the international investment regime with the public concerns relating to sovereignty in terms of *content*?

This article does not aim at exploring the actual meaning of notions like sovereignty and legitimacy. It parts from the understanding that a country's entering into IIA is, in itself, an exercise of its sovereignty, despite the already mentioned doubts as to the exact understanding of their meaning and consequences.[11] Rather, this article focuses on the underlying object and purpose of investment treaties as a key for addressing the shortcomings that give rise to much of the concern, and that through a revised understanding of how the IIA entered into need to be interpreted. The central premise is that the perceived clash between investment treaty law and sovereignty can and must be resolved by integrating the logic of public law, as a proxy for sovereignty, into investment treaty law,[12] and that in a transnational dimension.

Furthermore, this article concentrates on solutions *de lege lata* and does not expand to solutions de *lege ferenda* in the sense of rewriting existing treaties or overwriting them by new treaties, such as is now starting to happen especially in the context of the negotiations of the European Union. The analysis and solutions proposed here primarily regard the interpretation and application of existing treaties. The vast majority of these basically follow the simple lines of the 1967 OECD Draft on Convention on the Protection of Foreign Property, and are thus marked by remarkably succinct and open-textured provisions requiring arbitrators to engage in significant efforts of interpretation to give a specific meaning to those provisions.[13] This being said, the approach developed here would certainly also provide a much more scientifically grounded and reliable basis for the drafting of future IIA.[14]

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9 See especially Weidemaier (n 3) 1895 (referring to 'a mechanism for generating a robust system of privately made law'); see also TH Cheng, 'Precedent and Control in Investment Treaty Arbitration' (2006-2007) 30 Fordham Int'l LJ 1014-1049.

10 See, eg, IM Ten Cate, 'The Costs of Consistency: Precedent in Investment Treaty Arbitration' (2013) Colum J Transnat'l Law 419-478; and T Schultz, 'Against Consistency in Investment Arbitration' in J Pauwelyn, J Viñuales and Z Douglas (eds), *The Conceptual Foundations of International Investment Law* (OUP 2014) 297-315; for the debate see also proceedings of the Conference on International Arbitration at the Supreme Court of Singapore of 20 January 2010 in (2010) 25(1) ICSID Review 87-110.

11 See above n 7 and below n 90

12 For the comparative public law dimension see the seminal passage by T Wälde in *International Thunderbird Gaming Co v Mexico*, Award (UNCITRAL/NAFTA) – Wälde Separate Opinion 31 December 2005, paras 27-29; also Schill, *IIL and Comparative Public Law* (n 3) 10-17.

13 For a comprehensive historical analysis see KJ Vanvelde, *Bilateral Investment Treaties – History, Policy, and Interpretation* (2010) especially 195-199, 217, 287, 416.

14 See for the European context J Kleinheisterkamp, 'Financial Responsibility in European International Investment Policy' (2014) 63 ICLQ 449, 471-473.

Part I proposes to listen to the intuitions – rather than rationales – that give rise to the fears for sovereignty. It highlights some historic tensions between investor rights, international arbitration and sovereignty and analyses the reactions of traditional capital exporting states when hit themselves for the first time by investor claims. The analysis of this historical and political background of the arguments voiced against investment arbitration and the objections that it undermines host states' sovereignty gives insight into the core of what a new normative framework would have to address and that can provide a conceptualization a balanced approach to the investment treaties.[15]

For that purpose, Part II discusses how the international investment regime, including its perceived limitations on sovereignty, has developed and gained acceptance by capital importing countries under the premise that its fundamental *telos* is enhancing development. This explains that the international investment regime, for the sake of legal certainty, is designed to overcome the substantive and procedural deficiencies of public law in the host country – but not to over-compensate foreign investors as compared to the safeguards they enjoy in their home country. Put in abstract terms, the limitations to exercise of sovereignty by the host state resulting from bilateral investment treaty should be understood as being 'capped' at the level at which the investor's home state affirms its own exercise of sovereignty in balancing private and public interests.

Part III, however, shows that it is necessary to expand from a home-state to a transnational perspective. The operation of 'most-favoured-nations' clauses contained in most IIA, which offer foreign investors of different origin a level playing field at the highest level, impose the quest for a more adequate benchmark than the home-state standards. It is argued and developed that the vague treaty provisions must be interpreted in the light of the system's broader underlying *telos* of enhancing development and thus as not exceeding the degree of protection granted in the law and practice of the most advanced national public law systems, as distilled through comparative public law analysis.

The paper proposes in Part IV a practical way for translating these findings into an operable tool that is adapted to the nature and needs of international arbitration – by borrowing again from the world of international commercial transactions. Going beyond the formal understanding of 'general principles of law' as a source of international law, it suggests the practical elaboration of a transnational 'pre-statement' (i.e. going beyond a mere 'restatement') of international investment law. Dwelling on the experience with the

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[15] For a more theoretical approach see J Bonnitcha, 'Outline of a normative framework for evaluating interpretations of investment treaty protections' in C Brown & K Miles (eds), *Evolution in Investment Treaty Law and Arbitration* (CUP 2011) 117-144.

UNIDROIT Principles of International Commercial Contracts, such *Principles of Investment Protection* would be elaborated primarily on the basis of public comparative law, but also the existing case law of tribunals as well as other sources of international law. The combination of the techniques of comparative public law and comparative international law[16] would allow for the formulation of detailed principles designed to offer well-balanced and generally acceptable specifications of the multiple facets to which the vague principles found in investment treaties must be broken down. Such principles, if well-crafted and flanked with scientific analysis and commentary, could establish persuasive presumptions of how private investor rights and public interests of host states are to be balanced by arbitral tribunals when interpreting open-textured investment treaty provisions. This would, in turn, also provide investors and host states *ex ante* with benchmarks that supply much more certainty and reliability in practice as well as more reliable guidance for future treaty negotiations. The proposed approach would thus be an efficient means for bringing investment treaty arbitration in line with the expectations relating to the host states' sovereignty and perceptions of legitimacy. Part V concludes.

I. Foreign investor rights and the need to reaffirm sovereignty

The fears of the impact of any special regime protecting foreign investments on national sovereignty date far back in history and well known through the Calvo doctrine: foreigners should not be allowed to invoke greater rights in a host country than its nationals, especially regarding claims against the government; the foreigners' home state should not interfere in favour of its citizens; foreigners should be fully subject both to the substantive law and the jurisdiction of the courts in the host country.[17] The essence of this position is twofold: it rejects the phenomenon of 'reverse discrimination' of citizens of host states in comparison to foreign investors privileged under international law and it rejects any foreign interference with sovereign national policy space, be it by foreign powers or by international tribunals. Efforts to complement the Calvo doctrine by a legal shield to sovereignty against imperialist interventions of Western powers on behalf of their investors culminated – and arguably failed – with the Drago-Porter Convention of 1907 that was prompted by the Venezuelan crisis of 1903.[18] This was the first multilateral treaty to codify a prohibition of use of military force for

[16] For this concept see A Roberts, 'Comparative International Law? The Role of National Courts in International Law' (2010) 60(1) Int'l & Comp L Quarterly 57-92.

[17] C Calvo, *Le droit international théorique et pratique* (vol III, 5th edn 1896) 138-142; see also D Shea, *The Calvo Clause: A Problem of Inter-American and International Law and Diplomacy* (1955) 16-20.

[18] For a historical account of the military interventions to protect or enforce investor interests see Ch Lipson, *Standing Guard: Protecting Foreign Capital in the Nineteenth and Twentieth Century* (1985) 54.

the recovery of claims by foreign investors.[19] This prohibition, however, was made subject to the condition that the debtor state would accept international arbitration as the means for peacefully settling such claims[20] – a condition that Professor Jessup described as 'a loophole through which a fleet of warships could sail'.[21]

Against this background, the popularity of the Calvo doctrine and a traditional resistance against international arbitration especially in the Latin American countries is hardly surprising. Far from being 'dead' or 'deactivated',[22] Calvo's logic is very much alive in the resurgent rhetoric of investment arbitration as a tool of neo-imperialism, such as in Brazil's refusal to ratify any international investment agreement or the ICSID Convention and the recent wave of Latin American governments terminating their IIAs and leaving ICSID.[23] In a similar vein, other countries such as South Africa and Indonesia have been rethinking their IIA and envisaged their termination.[24] What is, however, more interesting for the present purposes are the manifestations of fear for, and the need to reaffirm, sovereignty by those countries that initiated and pushed the proliferation of this regime. The following highlights the developments in North America and Europe for the purpose of showing the emergence of a need to impose, in the name of protecting sovereignty, some kind of 'cap' on how far arbitral tribunals can go when interpreting IIA provisions. As will be shown in the following, this gives critical guidance for addressing the concerns raised and outlining the normative foundation for developing investment treaty law in the future.

1. The fears for sovereignty in North America

On the side of traditionally capital exporting countries, the *prise de conscience* of the political price to be paid for the perception of investment treaty law impacting on national sovereignty has given rise to similar reasoning. This became most evident when the USA was hit by claims by Canadian companies under Chapter 11 of the NAFTA, i.e. rules on foreign investment originally designed to protect US and Canadian interests in Mexico. Cases

[19] Article 1.1 of the Hague Convention respecting the limitation of the employment of force for the recovery of contract debts, signed at The Hague October 18, 1907, (1907) 36 Stat 2241; Treaty Series 537, C Bevans, *Treaties and Other International Agreements of the United States of America 1776-1949* (vol I, 1968) 607.
[20] *ibid* Article 1.2; see in detail LM Drago, 'State Loans in Their Relation to International Policy' (1907) 1 Am J Int'l L 692-726; also WMC Weidemaier, 'Contracting for State Intervention: the Origins of Sovereign Debt Arbitration' (2010) Law & Contemporary Problems 335, 347-348.
[21] Ph Jessup, *A Modern Law of Nations* (1948) 113.
[22] But see W Shan, 'Is Calvo Dead?' (2007) 55 Am J Comp L 123, 163.
[23] For the Brazilian position in detail see J Kleinheisterkamp, 'O Brasil e as disputas com investidores estrangeiros', in: R Di Sena Jr. & MT Costa Souza Cherem (eds), *Comércio Internacional e Desenvolvimento – Uma Perspectiva Brasileira* (2004) 156-187. For the claims of bias and neo-imperialism in other regions see M Sonarajah, 'The Climate of International Arbitration' (1991) 8(2) J Int'l Arb 47-86.
[24] B Bland, S Donnan, 'Indonesia to terminate more than 60 bilateral investment treaties' Financial Times 26 March 2014, http://www.ft.com/cms/s/0/3755c1b2-b4e2-11e3-af92-00144feabdc0.html; for South Africa see below n 90.

brought by Canadian investors against the U.S. like *Loewen*, *Methanex*[25] and *Mondev*, although all ultimately fruitless, had a very strong impact on the re-definition of the U.S. international investment policy owing to the public indignation and thus political pressure they created – just at the time when President Bush in 2001 had asked Congress to grant fast-track authority for negotiating trade agreements. The debates in both the House and the Senate evolved around two strings of objections that coincided with Calvo's position: the potentially better treatment of foreign investors in the US as compared to US citizens and the impact on US sovereignty.

Then Senator – and now Secretary of State – John Kerry was the driving force in the Senate for introducing restrictions to the mandates for negotiating future investment chapters in free trade agreements. Echoing numerous worries voiced in the House, he insisted that 'NAFTA was never intended to infringe on U.S. sovereignty in such a way',[26] 'that U.S. sovereignty must be protected',[27] and that the cases brought against the U.S. had 'everything to do with our sovereignty'.[28] Similarly, the co-sponsor of the amendment that the Senate ultimately adopt, Senator Baucus, insisted that '[i]n taking steps to protect U.S. investors abroad, we must not sacrifice the sovereignty of Federal, State, and local governments here at home'.[29] This political position translated – ultimately accepted by unanimity out of fear of Kerry's more radical amendments – into a Congressional directive to U.S. negotiators in the 2002 Trade Act, which has been reiterated since in the Bipartisan Trade Deal of 2007 when the 2002 trade promotion authority expired:[30]

> 'Recognizing that United States law on the whole provides a high level of protection for investment, consistent with or greater than the level required by international law, the principal negotiating objectives of the United States regarding foreign investment are to reduce or eliminate artificial or trade-distorting barriers to foreign investment, *while ensuring that foreign investors in the United States are not accorded greater substantive rights with respect to investment protections than United States investors in the United*

[25] *Methanex Corp v United States of America*, Final Award on Jurisdiction and Merits (UNCITRAL/NAFTA), 3 August 2005, (2005) 44 ILM 1345.
[26] *cf* M Roosevelt, 'A Canadian chemical firm says California's pollution controls violate NAFTA rules', Time Magazine 25 March 2002 (vol 159, no 12); but see the statement of Rep Gilman (NY), 147 Congr Rec E2257 (12 December 2001): 'To add insult to injury, the drafter of the provision, now in private practice [referring to Daniel Price], readily admits that it was an intended consequence of NAFTA, rather an unintended consequence as most people believed it to be.'
[27] 148 Congr Rec S4810 (23 May 2002).
[28] 148 Congr Rec S4595 (21 May 2002).
[29] 148 Congr Rec S4298 (14 May 2002).
[30] Office of the US Trade Representative, *Bipartisan Agreement on Trade Policy* (10 May 2007), http://www.ustr.gov/sites/default/files/uploads/factsheets/2007/asset_upload_file127_11319.pdf.

> *States*, and to secure for investors important rights comparable to those that would be available under United States legal principles and practice …'[31]

It is very clear that Congress' intention in 2002 was to shield U.S. sovereign regulatory powers by imposing a 'ceiling' on the possible interpretations that arbitral tribunals could be giving to the vague provisions in investment treaties. As explained by the co-sponsor of the bill Senator Baucus:

> 'It is our objective to negotiate agreements that protect the rights of U.S. persons abroad. But we are not willing to sacrifice the regulatory functions of our Government in order to obtain that objective… In other words, *the rights of U.S. investors under U.S. law define the ceiling. Negotiators must not enter into agreements that grant investor rights that breach that ceiling*.'[32]

This principle of capping had further repercussion, beyond finding its way into the preambles of the few FTAs concluded by the US since.[33] As already highlighted by Kerry in the Senate, such a cap could only be implemented by containing the risk resulting from the tandem of the very vague substantive standards and the procedural features of international arbitration. In this light, the U.S. government engaged in a process of revising its international investment policies. Most of the U.S. BITs still in place today are based on the simplistic 1984 model BIT, which had been patterned after the European models.[34] The policy review lead to a largely overhauled model BIT in 2004.[35] This new model implemented the 'no greater rights' policy in particular by capping the meaning of 'fair and equitable treatment' to its meaning under customary international law,[36] and by partially spelling out the standards of U.S. law, such as the definition of regulatory takings[37] (which, as it happens, itself has been criticized

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[31] PubL 107-210, 116 Stat 933 [H.R. 3009]; US Trade Promotion Authority Act, 19 USC § 3802(b)(3).
[32] Sen Baucus, 148 Congr Rec S4267-68 (13 May 2002) [emphasis added].
[33] US–Peru FTA, signed 12 April 2006; US–Colombia FTA, signed 22 November 2006; US–Panama FTA, signed 28 June 2007; US – South Korea FTA, signed 30 June 2007; all available at http://www.ustr.gov/trade-agreements/free-trade-agreements.
[34] For the 1984 U.S. Model BIT see P Gann, 'The U.S. Bilateral Investment Treaty Program' (1985) 21 Stanford J Int'l L 373; K Scot Gudgeon, 'United States Bilateral Investment Treaties: Comments on their Origin, Purposes, and General Treatment Standards' (1986) 4 Int'l Tax & Bus Lawyer / Berkeley J Int'l L 105; see also J Alvarez, 'Three Responses to "Proliferating" Tribunals', (2009) 41 NYU Int'l L & Pol 990, 999.
[35] 2004 U.S. Model Bilateral Investment Treaty, http://www.state.gov/documents/organization/117601.pdf ('2004 US Model BIT').
[36] See also, shortly after the end of oral hearings in the *Methanex* case, NAFTA Free Trade Commission, Notes of Interpretation of Certain Chapter 11 Provisions (31 July 2001) para B, http://www.state.gov/documents/organization/38790.pdf.
[37] 2004 US Model BIT (n 35), Annex B.3 & 4(a), spelling out the principle of *Penn Central Transportation Co v New York City* 438 US 104 (1978).

by U.S. scholars as being excessively vague and ambiguous),[38] plus a clarification that echoed Kerry's claims for shielding U.S. policy space:[39]

> 'Except in rare circumstances, non-discriminatory regulatory actions by a Party that are designed and applied to protect legitimate public welfare objectives, such as public health, safety, and the environment, do not constitute indirect expropriations.'[40]

Another revision of the Model BIT in 2012 reaffirmed the line taken in 2004,[41] and it is worth noting that America's NAFTA partner Canada equally revised its BIT programme and introduced virtually the same changes in its 2004 Model Foreign Investment Protection Agreement (FIPA) with the aim of safeguarding its sovereign regulatory powers.[42]

3. Repercussions in Europe

In the EU, the prise de conscience of the potential impact of IIA on policy space of traditional capital exporting countries of the (now) EU dates back to the same time as the debates on the 2002 U.S. Trade Act with the accession negotiation with the Central and Eastern European countries, all of which had concluded many BITs after the fall of communism when in dire need of foreign investments. In a long development since, it has become quite clear that both intra- and extra-EU BITs have a potential for interfering with the effectiveness of the EU rules regulating the internal market.[43] The EU Commission's efforts over the last 5 years to start substituting the BITs of the EU member states – which make up for half of all BITs worldwide – by European IIA have generated an unprecedented public debate. Politically explosive investment cases such as the claims by Philip Morris against Australia and Uruguay because of their anti-tobacco laws, by Lone Pine against Canada because of provincial moratoria on fracking, and by Vattenfall against Germany because of its expedited exit from nuclear energy after Fukoshima, have the Parliament to discuss whether and to what degree rights of foreign investors could compromise EU regulatory policy space. The debates in the Parliament in 2013 showed a striking resemblance to those in the U.S. Congress a decade earlier, which culminated, indeed, in adopting the same solution.[44] The

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38 A Sanders, 'Of All Things Made in America: Why are We Exporting the Penn Central Test?' (2010) 30 NW J Int'l L & Bus 339, 360-66.
39 See Amendment 3430 to Amendment 3401, 148 Congressional Record S4529 (17 May 2002), § 2101(b)(3)(G).
40 2004 US Model BIT (n 35), Annex B.4(b); see also Article 20(3) on the carve-outs to arbitral jurisdiction regarding prudential measures regulating financial services.
41 2012 US Model Bilateral Investment Treaty, http://www.state.gov/documents/organization/188371.pdf.
42 *Agreement between Canada and ___ for the Promotion and Protection of Investments* [FIPA] of Fall 2003 http://www.international.gc.ca/trade-agreements-accords-commerciaux/assets/pdfs/2004-FIPA-model-en.pdf.
43 See in detail Kleinheisterkamp 'Financial Responsibility' (n 14) 454-456.
44 *Ibid* at 469-471.

Parliament inserted by unanimity (excluding only the small parties who oppose investment arbitration or the EU altogether) an amendment to the recitals of the regulation, which ultimately was – albeit only most reluctantly – accepted by the Commission and the Council in the trialogue negotiations:

> ‘Union agreements should afford foreign investors the same high level of protection as Union law and the general principles common to the laws of the Member States grant to investors from within the Union, *but not a higher level of protection*. Union agreements should ensure that the Union's legislative powers and right to regulate are respected and safeguarded.’[45]

The report of the Committee on International Trade, which laid the basis for this amendment, explained:

> ‘This recital underlines the need to keep financial responsibility of the Union within the well-established limits of the law of the Union and the common legal tradition of the Member States… *Unless framed restrictively, EU investment treaties will … allow arbitral tribunals to hold the Union liable to foreign investors for legislative acts where EU investors would have no claim under EU law*.’[46]

It remains to be seen how the European Commission will actually incorporate this ‘no greater rights’ logic into the ongoing negotiations of IIA. The point to be developed in the following is, however, that this principle cannot be brushes aside as mere rhetoric.

4. A basis for developing investment treaty law?

As questionable as these political reactions in the U.S. and in the EU may be, they lead to the heart of the legitimacy debate entangling international investment law and open an opportunity to address the underlying issues – and that without perpetuating the flaws inherent to the unilateralist ‘no greater rights’ approach. Despite their mere preambular

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[45] Recital 4 of Regulation (EU) No 912/2014 of the European Parliament and of the Council of 23 July 2014 establishing a framework for managing financial responsibility linked to investor-to-state dispute settlement tribunals established by international agreements to which the European Union is party, [2014] OJ L 257/121 (28 August 2014). For more detail see Kleinheisterkamp ‘Financial Responsibility’ (n 14) 469.

[46] INTA Committee Report of 26 March 2013, http://www.europarl.europa.eu/sides/getDoc.do?type=REPORT&reference=A7-2013-0124&language=EN (amendments 4 and 5) [emphasis added], adopted by the Plenary on 23 May 2013, http://www.europarl.europa.eu/sides/getDoc.do?type=TA&reference=P7-TA-2013-0219&language=EN&ring=A7-2013-0124.

nature, the 'no greater rights' affirmations on both sides of the Atlantic have not only a political but also a legal dimension. In reaction to the reciprocal dimension of IIA, they translate the fear for sovereign policy space in traditional capital exporting countries, as well as the political worries about reverse discrimination of their own nationals, into a bench-mark for the negotiation, framing and interpretation of future investment treaties. Their 'ceiling' or 'capping' logic poses two fundamental questions, the exploration of which should prove fruitful. More directly and practically: what exactly is that benchmark to which future IIA are to be subject, or rather, how is it to be determined? And more indirectly, and maybe more importantly: is there any deeper substance to this 'capping' logic that would allow drawing conclusions on the normative foundations for the developing investment treaty law and thus on the application of the still in force and probably long-time persisting existing IIA?

It is this latter question that shall be the starting point for developing a deeper understanding of the underpinnings of existing IIA and thus for sketching the way forward for answering the former question on how to frame future IIA. It is both practically and theoretically relevant that, largely irrespective of any future IIA, for the time being some 2,500 BITs will remain in force the overwhelmingly number of which enshrine broadly and vaguely framed standards of protection. These treaties can be expected to dominate the next two decades of investment arbitration and thus shape the development of investment treaty law – and will thus play a significant role for the practical exercise of state sovereignty. The following section analyses how the application of these open-textured standards by arbitral tribunals in their review of sovereign acts of host states is essentially dependent on sound construction and especially teleological interpretation. That in turn requires a much clearer picture of what the normative foundations for developing investment treaty law are.

II. The normative foundations for developing investment treaty law

The unilateralist 'no greater rights' logic of capping the investor rights granted under IIA aims at limiting the effect of investment treaties on national sovereignty. More specifically, this capping logic, as misguided as it may be in the current form, reveals that one of the major fears for the host state's (exercise of) sovereignty is, indeed, that the vagueness of largely unqualified investor protection provisions in IIA can allow for excessive unpredictable outcomes that do not sufficiently balance the private (investor) interests against the public (host state) interests and thus the latter's exercise of sovereignty.[47] The need for capping arises out of the insight that the success of an investor's claim, and thus the limitations that

[47] See above n 2.

the applied standards potentially imply for the host countries' sovereignty, essentially depend on how the open-textured and largely vague provisions of BITs are eventually constructed with respect to the detailed issues of the specific case.

As for the existing treaties, which will remain in force, this insight suggests that one way of addressing the issues arising from them is to focus on their interpretation, which is the central point of this section. The more vague the provisions the more need there is for a clear understanding of what the object and purpose of the treaty provisions is. This leads to the heart of both the normative foundations but also to the central practical challenge that IIA pose: the need to recur to the general object and purpose underlying these provisions is necessary for the proper determination of their exact scope by way of teleological interpretation. As shown in the following, the reflection on the *telos* of investment treaties is also crucial for understanding the inherent limitations that they carry with them – and without which their application cannot produce the necessary balance between private and public interests.

1. The role of teleological interpretation

Reservations against the teleological approach have primarily been formulated because of fears that 'placing undue emphasis on the "object and purpose" of a treaty [may lead to denying] the relevance of the original intention of the parties.'[48] Indeed, focusing on the 'object and purpose' of legal instruments means going beyond the original intention of the parties as derived from the *travaux préparatoires*, as acknowledged by Article 32 of the Vienna Convention on the Law of Treaties ('VCLT'). It aims at allowing for an interpretation that overcomes textual ambiguities dynamically in the light of unforeseen and new circumstances and practices. It prevents adjudicators from resorting to overly strict, narrow or literal interpretations. But does this mean that the intention of the contracting parties is eventually irrelevant? Or does this dynamic approach require the systematic expansion of the protection as provided for literally in the treaties? Practice in investment arbitration often has affirmed the latter – and thereby brought itself in the line of fire. Arbitral tribunals have quite naturally turned to the titles and preambles of the BITs whose provisions they had to interpret, finding there only reference to 'the promotion and reciprocal protection of investments' and the declared intention 'to create and maintain favourable conditions for

[48] I Sinclair, *The Vienna Convention of the Law of Treaties* (2nd edn, 1984) 130, endorsed in *Plama Consortium Ltd v Republic of Bulgaria*, ICSID Case No. ARB/03/24, Decision on Jurisdiction of 8 February 2005, para 193.

investments'. And most have stopped there;[49] some of them concluding that '[i]t is legitimate to resolve uncertainties in its interpretation so as to favour the protection of covered investments.'[50]

Some authors have similarly argued that the blame lies with governments which, in the negotiations of the treaties, have failed to include specific language in the preambles that recognises not only the protection of investment but also the prerogative of states to regulate in the public interest.[51] This argument difficult to square with what is known about the degree of understanding and thus the real intention of the state parties at the time of entering into IIA.[52] It also reveals an overly strict, narrow and literal approach that teleological interpretation is, by its definition, designed to counter-balance.[53] It is plainly counter-intuitive that explicit references to needs for sustainable development in the preambles will lead to goals now being considered under new BITs – but not under the former.[54] This reveals that the very basics of how to determine the 'object and purpose' is far from clear, and even more so what the actual *telos* eventually is.

2. Taking 'object and purpose' further

An analysis of IIA from the perspective of their impact on sovereignty could invite exploring to what degree the interpretation under Article 31 VCLT allows a presumption *in dubio mitius* in the sense that, in case of doubt, states cannot be expected to have wanted to transfer more sovereignty than they explicitly stated.[55] This approach is highly controversial,[56]

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[49] See, eg, *Romak v Uzbekistan*, PCA Case no AA280, Award of 26 November 2009, para 181; *HICEE v Slovak Republic*, PCA Case No 2009-11, Partial Award of 23 May 2011, para 120 (finding the wording chosen for the preamble of the Dutch-Czechoslovak BIT to be 'studiously neutral').

[50] *SGS v Philippines*, ICSID Case no ARB/02/6, Decision on Jurisdiction of 29 January 2004, (2004) 8 ICSID Reports 515 ¶ 116; see also *MTD v Chile,* ICSID Case no ARB/01/7, Award of 25 May 2004, para 104; *Siemens v Argentina*, ICSID Case no Arb/02/8, Decision on Jurisdiction of 3 August 2004, para 81 (claiming not to interpret the Treaty neither liberally nor restrictively); *HICEE v Slovak Republic* (n 49) Dissenting Opinion of Judge Brower, para 9; see also A von Aaken, 'International Investment Law between Commitment and Flexibility: A Contract Theory Analysis' (2009) 12(2) J Int'l Econ L 507, 528-529 n 91: 'most tribunals take a narrow view'.

[51] A Newcombe & L Paradell, *Law and Practice of Investment Treaties: Standards of Treatment* (Kluwer 2009) 116.

[52] Poulsen & Aisbett (n 7).

[53] See also Douglas (n 2) para 150.

[54] But see *ibid*. See also A Newcombe, 'Sustainable Development and Investment Treaty Law' (2007) 8 J World Inv & Trade 357.

[55] See the position of the United States in *Methanex Corp v United States of America*, UNCITRAL Arbitration, 1st Partial Award of 7 Aug 2002, para 103; also *SGS v Pakistan*, ICSID Case no ARB/01/13, Decision of 6 August 2003 (2003) 18 ICSID Review 307, para 171; *Noble Ventures v Romania*, ICSID Case no ARB/01/11, Award of 12 October 2005, para 55. See also WTO Appellate Body Report, *EC Measures Concerning Meat and Meat Products (EC – Hormones)*, WT/DS26/AB/R, WT/DS48/AB/R, adopted 16 January 1998, para 165 n 154.

[56] See ICJ, Dispute Regarding Navigational and Related Rights (Costa Rica v Nicaragua), [2009] ICJ Reports 213, 236-8, para 48; for an extensive discussion see also Wälde (n 5) 733-736.

especially because of its alleged incompatibility with another interpretative principle: the *effet utile*.[57] There is, however, no need to pursue the *in dubio mitius* argument for present purposes precisely because it is the *effet utile* dimension that, as shown in the following, ultimately allows making the crucial point: teleological interpretation cannot follow a simplistic 'more [in favour of the protected party] is better' logic. Teleological interpretation addresses the need to shed new light on a textual ambiguity by putting the provisions into the broader context of the reasonable and balanced objects and purposes of the law, both to expand beyond textual limitations but also to restrict the breadth of unqualified wording.[58] This is all the more true when the task is that of fine-tuning the definition of specific rights and obligations on the basis of extremely broad standards as those found typically in BITs – an exercise that is widely acknowledged to approach a stage of judicial law making.[59] The design of specific legal rules in such a context is a balancing act that requires a much more comprehensive understanding of what the actual *telos* is than so far assumed by most tribunals and scholars.[60]

The need for a more holistic approach to the 'object and purpose' of BIT provisions becomes all the more evident when the teleological element is combined with the systematic element to form its corollary, the principle of effectiveness. The postulate that all provisions are to be interpreted so as to have their full effect – rather than depriving them of sense – is essentially dependent on the *telos* being determined so as to guide the entire instrument and thus allow giving all provisions maximum efficacy for the sake of the 'object and purpose'. The *effet utile* doctrine has played a crucial role in the highly dynamic consolidation and expansion of European Community law by the Court of Justice of the European Union (CJEU).[61] And it is from this European experience that investment treaty law can learn a great deal since the parallel is striking.

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[57] H Lauterpacht, 'De l'interprétation des traités. Rapport et projet de Résolution' (1950) 43-I Annuaire de l'Institut de Droit International 366, 372, 407.
[58] cf Wälde (n 5) 758-764 and 738-739.
[59] Above n 3.
[60] Admittedly, some tribunals have accepted that '[t]he protection of foreign investments is not the sole aim of the Treaty but rather a necessary element alongside the overall aim of encouraging foreign investments and extending and intensifying the parties' economic relationships' and that this 'calls for a balanced approach to the interpretation'; *Saluka Investments BV v Czech Republic,* UNCITRAL Arbitration, Partial Award of 17 March 2006, para 300; for such a 'balanced approach' see also *El Paso Energy v Argentina*, ICSID Case no ARB/03/15, Decision on Jurisdiction of 27 April 2006, paras 68-70, and *Mondev v United States*, ICSID Additional Facility Case ARB(AF)/99/2, Award of 11 October 2002, para 43. As pointed out by R Dolzer & C Schreuer, *Principles of Investment Treaty Law* (2008) 33 n 16, the tribunal's predilection for a particular (restrictive, expansive or neutral) approach is often eventually not reflected in the actual decision.
[61] See, eg, V Skouris, '*Effet Utile* v Legal Certainty: The Case-Law of the Court of Justice on the Direct Effect of Directives' (2006) 17:2 European Business Law Review 241-255; M Everson & J Eisner, *The Making of a European Constitution* (Routledge 2007) 53-55.

In many key decisions to expand the scope of application of the rather sketchy positive European law – frequently far beyond what the European member states ever imagined – the CJEU relied primarily on teleological arguments and the need to give full effectiveness to provisions according to the object and purposes of the EC Treaty (now TFEU), especially in order to give direct effect to rights of individuals against the national barriers to cross-border economic activity. This highly controversial expansionist approach in favour of 'Community interests',[62] however, cannot be appreciated in its entirety without having regard to the mechanisms for balancing private and public interests that the CJEU itself had to elaborate to safeguard its constructs' and its own legitimacy (against the potential backlash from the member states through restrictive revisions of the treaties). In the landmark *Cassis de Dijon* decision, the CJEU affirmed that 'in the absence of common rules on the production and marketing of alcohol ... it is for the Member States to regulate all [related] matters' and that resulting 'obstacles to movement within the Community ... must be accepted in so far as the provisions may be recognized as being necessary in order to satisfy mandatory requirements'.[63] The CJEU thereby expanded the grounds upon which member states can legitimately restrict trade beyond those – according to the literal understanding: exhaustively – listed in (what is now) Article 36 TFEU. This new turn of the case law became necessary so as to counter-balance the previous expansive interpretation in *Dassonville* of the prohibition of obstacles to trade in (what is now) Article 34 TFEU.[64] The only justification for taking an expansive approach to the interpretation of what constitute legitimate exceptions to the guarantee of free movement was, methodologically, the teleological interpretation based on a balanced understanding of the fundamental *telos* of the Union Treaties.[65] The *prima facie* most evident purpose is to establish a common market without internal barriers. Yet the CJEU clearly recognized that the broader objective of the treaty was not to establish an internal market *without any* regulatory obstacles to trade, but a space of economic freedom that is regulated *appropriately*, either by harmonised EU law or, in absence thereof, by national laws that protect public interest in the interest of the Union within the limits of proportionality. As put by Advocate General Tizziano, otherwise 'that would be tantamount to bending the Treaty to a purpose for which it was not intended: that is to say, not in order to

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[62] For the debate over judicial activism see, eg, M Cappelletti, 'Is the European Court of Justice "running wild"?' (1987) European Law Review 3-17, reviewing the seminal study by H Rassmussen, *On Law and Policy of the European Court of Justice: A Comparative Study in Judicial Policymaking* (Nijhoff 1986).

[63] ECJ Case 120/78 *Cassis de Dijon* [1979] ECJ I-649 para 8. This example is also referred to by S. Montt, *State Liability in Investment Treaty Arbitration* (2009) 77 n 205, citing M Poiares Maduro, *We The Court. The European Court of Justice and The European Economic Constitution. A Critical Reading of Article 30 of the EC Treaty* (Hart 1998) 71.

[64] ECJ Case C-8/74 *Dassonville* [1974] ECR 837 para 5, allowing allowed – and actually inviting – traders to attack 'all trading rules enacted by Member States which are capable of hindering, directly or indirectly, actually or potentially, intra-community trade'.

[65] See M Lasser, *Judicial Deliberations: a Comparative Analysis of Judicial Transparency and Legitimacy* (OUP 2004) 288 (referring to 'meta-teleology'); also J Bomhoff, 'Perfectionism in European Law' (2012) 14 Cambridge Yearbook of European Legal Studies 75, 89.

create an internal market in which conditions are similar to those of a single market and where operators can move freely, but in order to establish a market without rules'.[66] The crucial point made by the CJEU is that the programme of economic integration spelled out in the European Treaties is merely a tool for achieving a higher object and purpose. And going back to the origins suggests that this is a Europe of peace and prosperity, as devised by Jean Monnet and propagated by Robert Schumann in his historic declaration of 9 May 1950.[67] It is this broader vision, this *telos*, which, in case of doubt, must be the guideline for the legitimate interpretation of EU law – rather than a reductionist 'more is better' logic.

In short, teleological interpretation can lead to the feared excessive results that put the legitimacy of the entire system into question only if based on a superficial and one-sided determination of the 'object and purpose'. For investment treaties, the task of determining their object and purpose is admittedly more complex than for the (former) EC Treaty, which itself spelled out both in the Preamble and in Article 3 the objectives that sketch the much broader social and political picture within which the European 'economic constitution' is to be understood and interpreted. Nevertheless, it does not require too much abstraction to realize that the 'object and purpose' of a BIT cannot be reduced to optimized protection of foreign investments alone.

3. A glimpse at the (potential) intentions of the contracting parties

It may very well be that most BITs in force today have been negotiated by the main capital exporting countries, on the basis of their respective models, with the motivation of obtaining optimal guarantees for their investors. If this, however, were to be relevant, the 'object and purpose' of these investment treaties would mean little more than profit maximisation and put them in the tradition of 19th Century gunboat imperialism that constituted the historic origins of 'effective' investment and trade protection.[68]

Relevant are not the motivations of the individual contracting parties but their common intentions, at least to the degree that such intentions can be identified.[69] This leads to the question of the *quid pro quo*. Why would host countries accept to grant privileges to foreign investors that go far beyond those granted to their nationals? Why would they accept far

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[66] Advocat General Tizziano in ECJ Case C-442/02 *CaixaBank France* [2004] ECR I-8961 para 63; for a critical appreciation see F Scharpf, 'Legitimacy in the Multi-level European Polity', in M Loughlin and P Dobner (eds), *The Twilight of Constitutionalism?* (OUP 2010) 89, 111-17.
[67] Ninth and final draft of the Schuman Declaration (9 May 1950), http://www.ena.lu/ninth_final_draft_schuman_declaration_1950-2-7860.
[68] See in detail K Miles, *Origins of International Investment Law: Empire, Environment and the Saveguarding of Capital* (CUP 2012).
[69] *cf* Article 31(4) VCLT.

reaching limitations to their sovereign right to regulate, to their 'policy space'? As the development in the USA discussed above has already suggested, the answer can hardly be found in the formal argument of reciprocity: at the time of the conclusion of the vast majority of BITs, the probability of an investor from a developing country bringing a claim against a traditional capital exporting country seemed very unlikely. In any case, those countries that pushed the main wave of BIT conclusions did not intend the BITs concluded on the basis of their models to be relevant for that hypothesis, as the following observation by a former member of the team that elaborated the first generation US model BIT demonstrates:

> 'The BIT program resulted from the U.S. government's determination that a more favorable framework for U.S. investments in developing countries should be created. This new framework has a twofold purpose: to encourage as well as to protect such investments. From the United States' standpoint, the rights and duties under the BITs are redundant because investments in the United States already receive substantial and non-discriminatory protection.'[70]

Conversely, it can be doubted that traditional capital-importing 'developing' countries were offering the international standards privileging foreigners as a *quid pro quo* for the protection of their own investors' interests in a distant future when the capital export balance might be equilibrated or inversed. Even if that were to be the case, it is clear that yet another element must be considered: such equilibration or inversion of investment flows would be dependent on significant wealth building and thus economic development.

III. The Transnational Challenge

1. The relevance of the ICSID setting: 'multilateralization' and development

The importance of this element of 'development' in the *quid pro quo* equation becomes fully clear only if the broader context in which the vast number of BITs eventually were concluded is taken into consideration. The World Bank's initiative and support of creating and enhancing the investment treaty system through the elaboration of the Convention of Washington of 1965 and the subsequent establishment of ICSID has been crucial for the eventual success of the efforts of establishing international protection of investments on a global basis.[71] It is against this institutional background that most BITs have been negotiated

[70] Gann (n 34) 374; in the same sense Gudgeon (n 34) 111.
[71] See Wälde (n 5) 729; for historical detail T St John, *The Power of Modest Multilateralism: The International Centre for Settlement of Disputes (ICSID) 1964-1980* (forthcoming, on file with the author).

and framed, as evidenced in particular by the systematic reference to ICSID's arbitration facilities as an either exclusive or alternative dispute resolution mechanism available to investors seeking to enforce their rights. It is also against this broader contextual and historical background that the 'object and purpose' of these BITs has to be determined.

The need to refer to such a broader context becomes also clear when considering the transnational dimension of investment treaty law. There is a strong argument that BITs cannot be seen as isolated individual instruments but that their operation must be understood in the light of the momentum of 'multilateralization' that is inherent to them.[72] From a legal point of view, this multilateralization is brought about primarily by the functioning of most-favoured-nation (MFN) clauses, the gateway in virtually every BIT that opens access to all substantive privileges granted in other IIAs concluded by the host country.[73] It becomes clear that these clauses would lack all legitimacy if they were to operate – like they did in the 19th Century era of imperialism – as a crude mechanism for reaping privileges.[74] MFN clauses can only legitimately be conceptualised, at best, as means for creating a level playing field and fair competition among investors.[75] Most importantly, such a conception of a level playing field also entails a balance between liberalisation and regulation for the higher goal of improving welfare. In consequence, given that MFN clauses link the definition of rights and obligations under a BIT to the higher sphere of the totality of potentially applicable agreements and practices of a host state,[76] it is necessary also to re-allocate the quest for the real 'object and purpose' guiding teleological interpretation at the broader, transnational level at which international investment treaty law eventually operates.

Whereas in the establishment of the world trading system in 1947 the idea of 'expanding the production and exchange of goods' was seemingly bluntly formulated as an end itself, without any reference to enhancing development,[77] this element of 'development' has been essential for the efforts to justify the creation of the modern system of investment protection

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[72] For a broad analysis of this phenomenon see S Schill, *The Multilateralization of International Investment Law* (2009) (in the following '*Multilateralization*').

[73] For a detailed analysis, especially as regarding the extension of rights to use arbitration, see *ibid* 121-196.

[74] See, e.g., FL Hawks, *Narrative of the Expedition of an American Squadron to the China Seas and Japan, Performed in the Years 1852, 1853, and 1854 Under the Command of Commodore M.C. Perry, United States Navy* (vol 1, Appleton 1856) 388: 'Since the foregoing was written the treaty with England has reached us. We subjoin it, with the expression of our regret that [the English] Admiral Stirling could not obtain more than he did, as all he might obtain beyond what we had, would, under article IX of our treaty, have inured at once to our benefit...'

[75] Schill, *Multilateralization* (n 72) 139 and 193; S Schill, 'Most-Favored-Nation Clauses as a Basis of Jurisdiction in Investment Treaty Arbitration: Arbitral Jurisprudence at a Crossroads' (2009) 10 J World Investment & Trade 189, 210; UNCTAD, 'Most Favoured Nation Treatment: A Sequel' (2010) UNCTAD/DIAE/IA/2010/1, 27; *contra* T Cole, 'The Boundaries of Most Favored Nation Treatment in International Investment Law' (2012) Michigan J Int'l Law 537, 541.

[76] c*f* Schill, *Multilateralization* (n 72) 129.

[77] General Agreement on Tariffs and Trade 1947, Preamble para 1.

through arbitral tribunals. When proposing the arbitration system of ICSID for the World Bank in 1961, Aaron Broches formulated what has been coined 'the classic theory':[78]

> 'International investments are universally recognized as a factor of crucial importance in the economic development of the less developed parts of the world... Unfortunately, private capital is not being transferred in sufficient volumes to the areas in need of capital, one of the most serious impediments for its transfer being the fear of investors that their investments will be exposed to political risks such as expropriation, government interference and the non-observation by the host government of the contractually assumed obligations on the basis of which the investments were made... The Bank thus asked itself if, in view of its reputation of integrity and its position of impartiality, it could not help in the task of removing these obstacles to private investments... The Bank concluded that the most promising option would be to tackle the problem of the unfavorable investment climate by the creation of a machinery offered on a voluntary basis for the conciliation and arbitration of investment disputes.'[79]

This reasoning was also adopted almost literally in the Preamble of the resulting ICSID Convention. And, indeed, this foundation of the modern system of investment arbitration is but a revival of the rhetoric found the drafting of the Havana Charta of 1948,[80] the predecessor of the GATT that failed in parts precisely because of this very rhetoric: its Article 12 on investment protection was placed in the Chapter on 'Economic Development and Reconstruction' and started by the recognition that 'international investment, both public and private, can be of great value in promoting economic development and reconstruction, and consequent social progress'.

The classic theory's postulate that enhanced investment would bring about enhanced economic and social development is, not surprisingly, disputed regarding its empirical foundations; and it is far from certain that international protection of investments actually produces the benefits the drafters of the ICSID Convention had in mind or that it even has an impact on investment decisions at all.[81] From a normative point of view, however, this uncertainty is actually irrelevant. What is relevant is that the *idea* of enhancing development

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[78] For a discussion of this classic theory as contrasting with the dependency theory see M Sornarajah, *The International Law of Foreign Investment* (3rd edn, 2010) 47-55.

[79] A Broches, Opening Address at the First Consultative Meeting of Legal Experts, Addis Ababa, 16-20 Dec 1963, in: *Convention on the Settlement of Investment Disputes between States and Nationals of Other States – Documents Concerning the Origin and the Formulation of the Convention (vol 2, 1968)* 239 (hereinafter 'ICSID Documents').

[80] Final Act of the United Nations Conference on Trade and Employment, UN Doc. E/Conf. 2/78 (Havana, 24 March 1948).

[81] See, eg, L Poulsen, 'The Importance of BITs for Foreign Direct Investment and Political Risk Insurance: Revisiting the Evidence' [2009/2010] Yearbook on International Investment Law & Policy 539-574.

was at the origin at what allowed turning investment treaty law into a global institution, namely the World Bank's support – coupled with '*its reputation of integrity and its position of impartiality*' – and the establishment of ICSID, as well as providing the legitimacy it needed to grow and prosper. This rationale implies by no means that foreign investments are or should be motivated by altruistic motives of developing the economy of the host states.[82] But it becomes clear that, as in any country or community, economic activity is harnessed, and thus stimulated – but also regulated – for a higher purpose of improving welfare.[83] This purpose cannot be ignored for investment treaty law just as it could not be ignored by the CJEU when relying on the *effet utile* doctrine for overcoming the vagueness of EU treaty provisions.[84]

It is therefore not too far-fetched to argue that international investment law essentially derives its normative legitimacy from the logic that investment should be protected not for the sake of individual economic interests but for the higher sake of contributing to enhancing social welfare. Translated in normative terms, this would mean that the ideal aimed at, the relevant *telos*, is that of an investment protection system that eventually enhances the equality of nations and thus grants privileges (translating into restrictions to the exercise of state sovereignty) *to the degree necessary* to obtain that goal – but not more. As it would with any constitutional system, any excess beyond this logic of necessity would directly call into question the legitimacy of the investment law system. It was already recognized by arbitration practitioners themselves early in the boom years of investment treaties that '[a] single incidence of an adventurist arbitrator going beyond the proper scope of his jurisdiction in a sensitive case may be sufficient to generate a [political] backlash.'[85] Even if making abstraction from a philanthropic meta-normative *telos* of 'development',[86] it becomes clear that investment treaty law must serve an objective beyond the optimisation of investment flows and profits but must be understood – and applied – as serving the establishment of an essentially fair investment environment that, in the words of McLachlan, provides for 'an appropriate balance between protection of the rights of foreign investors on the one hand, and recognition of the legitimate sphere of operation of the host State on the other.'[87]

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[82] *cf* Sornarajah (n 78) 292.
[83] See, eg, OECD Recommendation of the Council on Regulatory Policy and Governance (22 March 2012), http://www.oecd.org/gov/regulatory-policy/49990817.pdf: 'RECOGNISING that regulations are one of the key levers by which governments act to promote economic prosperity, enhance welfare and pursue the public interest'.
[84] See above n 61-73.
[85] J Paulsson, 'Arbitration Without Privity' (1995) 10 ICSID Review 232, 257.
[86] For a 'law & development approach' see F Ortino, 'Redefining the Content and Role of Investment "Rules" and "Standards": A New Approach to International Investment Treaty Making' (2013) 28(1) ICSID Review 152, 166.
[87] *cf* C McLachlan *et al*, *International Investment Arbitration – Substantive Principles* (OUP 2007) 21.

2. The link between investment treaty law and domestic public law

The aspect of constituting and thus constitutionalizing economic activity through a legal framework leads to another important precision: the investment protection system as devised by Broches and filled with substance by specific treaties is based on a logic of substitution. International investment treaty standards are more than 'functionally comparable to constitutional guarantees and administrative law principles at the domestic level.'[88] Investment treaty law was intended to be developed in the context of ICSID as a true functional *substitute* for the constitutional and administrative law rules and mechanisms in the host country that were distrusted by foreign investors as being insufficient in terms of sufficiency and transparency or accessibility by foreign investors. This logic of substitution is the key for specifying the consequences that derive from the proper definition of the 'object and purpose' of investment treaty law. By substituting for domestic legislation and jurisdiction because of their real or perceived lack of efficiency, trustworthiness or transparency, the international investment regime is designed to offer guarantees that are equivalent to those the investor would find in his home country. Similar to the European internal market logic, potential discrimination of foreign investors is overcome by offering conditions that allow them to operate as if they never left home. From the traditional developed-developing country perspective, that is the greatest degree of legal certainty an international investor could hope for to be induced to invest abroad – and that is also, in terms of *quid pro quo*, all that both home state and host state could really have had in mind in concluding a BIT or a FTA.

Admittedly, this is not an understanding that could have been officially accepted at the time by the developing, i.e. poor capital-importing, country, since nominally a *bilateral* investment treaty was entered into. As already mentioned, however, there strong evidence that developing countries – and, indeed, also some developed countries – were altogether not conscious about the actual legal consequences of the commitments entered into primarily for ceremonial reasons into after virtually no or hardly any negotiation.[89] Among others, the South African Government concluded:

> 'The Executive had not been fully apprised of all the possible consequences of BITs. While it was understood that the democratically elected government of the time had to demonstrate that the RSA was an investment friendly destination, the impact of BITs on future policies were not critically evaluated. As a result the Executive entered into agreements that were heavily stacked in favour of investors without the necessary

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88 Schill, *IIL and Comparative Public Law* (n 6) 28.
89 See above n 7

safeguards to preserve flexibility in a number of critical policy areas. In reviewing the *travaux préparatoires* of the various BITs entered into at the time, it became apparent that the inexperience of negotiators at that time and the lack of knowledge about investment law in general resulted in agreements that were not in the long term interest of the RSA.'[90]

Moreover, the traditional capital exporting countries considered the bilateral dimension of the BITs to be a mere ceremonial expression of respect for the other country's sovereignty, i.e. reciprocity was 'rather a matter of prestige … than reality.'[91] As mentioned before, also the US negotiators of the first BIT wave considered that 'the rights and duties under the BITs are redundant because investments in the United States already receive substantial and non-discriminatory protection'.[92] Similar understandings can equally be found today in Europe.[93]

A developed country with a firmly established constitutional and administrative jurisprudence and institutions that more or less effectively protect private property rights from excessive state intervention will hardly have intended to accord a higher level of protection to investors from less developed countries. After all, the entire point of establishing the international substitute regime was to overcome the real or perceived problems of the capital-importing country – not those of the capital-exporting country. This understanding of capping is most clearly expressed by the already discussed 'no greater rights' principle as enshrined in the 2002 U.S. Trade Act and the 2007 Bipartisan Trade Deal and as incorporated in the FTAs concluded by the US.[94] Other than the problems of reciprocity, the inversion of this unilateral and protectionist rule allows the unveiling of a more general normative conclusion: the reverse must also hold true, i.e. investors from a 'developed' country can be entitled to no greater rights that those granted by the law of their home country when investing in a foreign country.[95] The intuition underlying this logic has been strongly formulated by Montt:

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90 Government of South Africa, 'Bilateral Investment Treaty Policy Framework Review', Government Position Paper of 25 June 2009, http://www.pmg.org.za/files/docs/090626trade-bi-lateralpolicy.pdf; for Pakistan see L Peterson, 'Pakistan Attorney General advises states to scrutinize investment treaties carefully', Investment Treaty News (IISD) 1 December 2006, http://www.iisd.org/itn/wp-content/uploads/2010/10/itn_dec1_2006.pdf; in more detail Poulsen & Aisbett (n 7).

91 FA Mann, 'British Treaties for the Promotion and Protection of Investments' [1981] British YB Int'l L 241. For a more recent example of such merely ceremonial affirmation of reciprocity see below n 99.

92 Gann (n 70) 374.

93 See, eg, the opinion of AG Jääskinen of 15 March 2011 in ECJ Case C-264/09, *Commission v Slovak Republic (Swiss BIT)*, [2011] ECR I-0000 [61] and [63] (internal citations omitted, emphasis added): '[T]he detailed provisions contained in Directive 2003/54 and interpreted in detail in VEMW cannot be overridden by the more general provisions contained in the Energy Charter Treaty… *EU energy law as it stands … cannot be considered as failing to achieve the standards required by the Energy Charter Treaty….*'

94 See above text accompanying nn 31-41.

95 But see Sen. Gramm (Tex), 21 May 2002 Congressional Record – Senate S4529: 'whatever protections we pledge to apply to foreign investors in America are going to apply to our investors [abroad]… [W]e would be stripping away the protections that American investment now have. We would be hurting American companies.'

> 'It is indeed somewhat shocking ... that a US investor may lose a case against its government in the US Supreme court, a German investor may lose the same case in the *Bundesverfassungsgericht* (Constitutional Court), and a French investor may lose it in the *Conseil d'Etat*; but, nevertheless, any of them may win it against a developing country before an investment treaty tribunal.'[96]

It thus follows from the broader 'object and purpose' of investment treaties (as elaborated above) that there is also an important inherent limitation deriving from proper teleological interpretation: whatever protection a capital-exporting country obtained for its investors in a BIT with a developing country would not have been intended to exceed what the domestic public law offered at home. This teleological reduction – as the counter-piece to the filling of gaps through analogy – to the exact level and modalities of protection derived from the BIT standards is therefore a crucial first step for construing the normative basis of the international investment regime. But it is necessarily only a first step.

3. The need for comparative public law

Indeed, the traditional distinction between capital importing or exporting countries is vanishing with the increasing financial power of investors from the BRIC, the Gulf and other former developing countries and, moreover, is put into question by an emerging new generation of 'South-South' agreements.[97] In times in which Portugal encourages Angola to invest in its public utilities and infrastructures,[98] one cannot ignore the perspective of the foreign investor from a country with low public law standards of protection. Translating this need for reciprocity also into legal terms – and not merely affirming it for ceremonial reasons such as in the FTA between the USA and Colombia[99] – leads to serious problems if one were to accept a bilateralization of the 'no greater rights' doctrine or even the adoption of a 'home

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[96] Montt (n 64) 76, also pointing out that the general principle of *allegans contraria non est audiendus* has been accepted by international tribunals to preclude claims that would have been considered too remote by the investor's home jurisdiction in the state-to-state context of diplomatic protection; *cf.* Bin Cheng, *General Principles of Law: As Applied by International Courts and Tribunals* (1987) 143.

[97] For the development of 'South-South' treaties see L Poulsen, 'The Politics of South-South Bilateral Investment Treaties' in: T Broude et al (eds.) *The Politics of International Economic Law* (CUP 2011) 186-210; UNCTAD, South-South Cooperation in International Investment Arrangements (UN 2005), http://unctad.org/en/docs/iteiit20053_en.pdf.

[98] P Wise, 'Portugal appeals to Angola for funds', Financial Times 17 November 2011.

[99] Preamble of the U.S. – Colombia FTA, signed 22 November 2006, http://www.ustr.gov/trade-agreements/free-trade-agreements/colombia-fta/final-text: 'The Government of the United States of America and the Government of the Republic of Colombia, resolved to […] AGREE that foreign investors are not hereby accorded greater substantive rights with respect to investment protections than domestic investors under domestic law where, as in the United States, protections of investor rights under domestic law equal or exceed those set forth in this Agreement; RECOGNIZE that Article 226 of the Colombian Constitution provides that Colombia shall promote its international relations based *on the principle of reciprocity*'.

state' standard. The former, for example, would mean that also a US investor in Colombia should not obtain more than Colombian law grants Colombian investors. Reciprocity taken seriously would then undermine the whole purpose of concluding an investment chapter in the FTA since it eliminates the substitution logic underlying the international investment regime. The direct application of a 'home state' standard, in turn, would even lead to a complete race to the bottom: Colombian investors would then not only be limited to the cap of US law but even to the cap of Colombian law. Interpreting the investment provisions in this sense would lead to an ultimately absurd situation.[100]

It follows that a broader normative basis for construing and expanding BIT standards so as to allow for efficient investor protection – but only to the degree necessary for obtaining the object and purpose of the BITs – requires a more sophisticated approach that goes beyond the simple 'home state' logic. This also becomes evident when considering the multilateralizing effect of MFN clauses. By operating as virtual – and practical – gateways to the protection granted under any other BIT ratified by the same host country, the bilateral dimension of the BIT fades away. The respective intention of the contracting states regarding the individual standards, as well as the potentially more limited bilateral conception of their underlying object and purpose, lose relevance. By accepting the operation of MFN clauses, the contracting states place their treaty into the broader multilateralized context of a dynamic system of international investment protection. This multilateralization dissolves the relevance of the respective investor's origin and raises the issue to a higher, trans-national level that is reflected in Montt's central thesis:

> '[U]nless an explicit textual provision is to the contrary, investment treaty jurisprudence should not crystallise rules and norms for protection of property rights in terms more rigorous than those generally applied by domestic courts in developed countries.'[101]

Montt's postulate seems to capture, at least in principle, the consequence that need to be drawn from the more refined definition of the *telos* that should guide the development of investment treaty law *de lege lata*. And, indeed, some arbitrators have at least in principle accepted this logic when, for example, recognizing the need to cap the reach of the FET standard under NAFTA to the 'ordinary standards applied in the NAFTA countries'.[102] The resulting implications coincide largely with Schill's plea for the application of 'principles of

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[100] But may actually be irrelevant to decisions on whether to invest in practice; see J Darby *et al*, 'Does Public Governance Always Matter? How Experience of Poor Institutional Quality Influences FDI to the South', CESifo Working Paper Series No. 3290 (2010), http://ssrn.com/abstract=1738168.
[101] Montt (n 64) 82.
[102] *Pope & Talbot v Government of Canada*, Merits Phase 2 (10 April 2001), (2002) 13(4) World Trade and Arbitration Materials 61, para 118.

the emerging global administrative law'[103] – but go beyond by showing that the introduction of comparative public law as a not only *useful* but actually *necessary* means for construing and constraining investment treaty law.[104]

Comparative public law needs to guide the interpretation and application of the vague BIT standards: it must inform the elaboration of their specific ramifications and, moreover, their limits that will allow building a legal system of investment protection that actually can strike 'an appropriate balance between protection of the rights of foreign investors on the one hand, and recognition of the legitimate sphere of operation of the host State on the other.'[105] This quest for the balance of private and public interests is, indeed, at the core of any national public law system as crystallized in constitutional and administrative law and the law of state liability. Legitimacy of any public power requires protecting individual rights against disproportionate state intervention while ensuring the collective capacity to regulate society for the public welfare. As a consequence, in all developed legal systems courts and legislators have acknowledged the need for limiting the individual's rights of redress against the State.

One example is the English common law of citizens' right to administrative redress, which allows for liability of public entities only in rather rare circumstances;[106] the Law Commission's proposal to liberalise the law was vehemently rejected by the UK Government and leading senior judges with reference to the excessive burden on the public purse and the chilling effect on public administration.[107] Another common law example is the modification of contractual liability when a public entity is involved by denying contractual estoppel against a public entity's defence of having contracts *ultra vires*: '[T]here can be no power under administrative law for public bodies themselves to create new powers by representing that they have such powers',[108] a proposition that international lawyers and tribunals have resisted in the name of 'security of international trade and investment'.[109] Similarly, policy-

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[103] See B Kingsbury & S Schill, 'Investor-State Arbitration as Governance: Fair and Equitable Treatment, Proportionality and Emerging Global Administrative Law' (2009), http://lsr.nellco.org/nyu_plltwp/146, and Schill, *IIL and Comparative Public Law* (n 6).
[104] Montt (n 64) 344 and 371-372.
[105] *cf* McLachlan *et al* (n 87) 21.
[106] See Law Commission, 'Administrative Redress: Public Bodies and the Citizen' Consultation Paper No 187 (3 July 2008), http://lawcommission.justice.gov.uk/docs/cp187_Administrative_Redress_Consultation.pdf, 6-53
[107] See Law Commission, 'Administrative Redress: Public Bodies and the Citizen – Analysis of Consultation Responses' (28 May 2010), http://lawcommission.justice.gov.uk/docs/lc322_Administrative_Redress_responses.pdf, paras 4.2 and 5.1-2; Lord Hoffmann, 'Reforming the Law of Public Authority Negligence', Bar Council Law Reform Lecture (17 November 2009), http://www.barcouncil.org.uk/media/100362/lord_hoffmann_s_transcript_171109.pdf, paras 20-23.
[108] *Haugesund Kommune & Anor v DEPFA ACS Bank* [2009] EWHC 2227 (Comm) para 172, relying also on Harman J in *Rhyl UDC v Rhyl Amusements Ltd* [1959] 1 WLR 465, 474-475.
[109] See already T Meron, 'Repudiation of *ultra vires* State Contracts and the International Responsibility of States' (1957) 6(2) ICLQ 273, 289.

based and carefully defined prohibitions in the common law[110] – and most national legal systems – on shareholder damages claims for reflective loss of their companies are at odds with the practice of arbitral tribunals admitting shareholder claims against states and thus allowing treaty shopping.[111] Landmark decisions on state liability of the German Constitutional Court and the Court of Justice of the European Union (the latter explicitly referring to the common tradition of the EU member states) have not only conditioned state liability to prior attempts to obtain judicial setting aside of illegality state acts,[112] but also significantly limited state liability for acts that were legal under the respective constitutional law but nevertheless caused losses to private economic activity – insisting on the need to avoid administrative or legislative regulatory chill.[113]

What this shows is that national laws and the richness of national courts cases have much to say about the striking of the proper balance of private and public interests. It is equally clear that the proper introduction of the much more sophisticated tool of comparative public law is needed for directing also the development of investment treaty law towards a more legitimate basis. The proposition to construe the normative foundations for the interpretation of BIT standards by abstracting from the individual treaty certainly challenges the orthodoxy of the traditional rules of treaty interpretation, let alone because the public law dimension was probably not in the minds of those who negotiated the individual treaties. It is, however, the only approach capable of properly capturing the transnational dimension of the existing international investment law system of which each BIT is part and which cannot be understood without the context of the ICSID Convention and, at the same time, offer a perspective for reconciling this system's practical operation with the foundational 'object and purpose' from which it ultimately derives its legitimacy.

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[110] *Johnson v Gore Wood & Co* [2002] 2 AC 1, 62.

[111] See in detail D Gaukrodger & K Gordon, 'Investor-State Dispute Settlement: A Scoping Paper for the Investment Policy Community', OECD Working Papers on International Investment 2012/03, http://dx.doi.org/10.1787/5k46b1r85j6f-en; D Gaukrodger, 'Investment Treaties as Corporate Law' OECD Working Papers on International Investment 2013/03, http://www.oecd.org/corporate/WP-2013_3.pdf.

[112] For the EU see Case C-446/06 *Danske Slagterier* [2009] ECR I-2119, para 61, referring to Joined Cases C-104/89 and C-37/90 *Mulder and Others v Council and Commission* [1992] ECR I-3061, para 33, and Joined Cases C-46/93 and C-48/93 *Brasserie du Pêcheur* and *Factortame* [1996] ECR I-1029 para 85. For Germany see Bundesverfassungsgericht 1 BvL 77/78 *Naßauskiesung*, decision of 15 July 1981, BVerfGE 58 (1981) 300, 322-324.

[113] For the EU see Joined Cases C-120/06 and C-121/06 *FIAMM* and *Fedon* [2008] ECR I-6513, paras 170 and 175; Joined Cases 83/76, 94/76, 4/77, 15/77 and 40/77 *Bayerische HNL Vermehrungsbetriebe* and *Others v Council and Commission* [1978] ECR 1209, para 5; Joined Cases C-46/93 and C-48/93 *Brasserie du Pêcheur* and *Factortame* [1996] ECR I-1029, para 45; see Kleinheisterkamp 'Financial Responsibility' (n 14) 459-464; M Perkams, 'The Concept of Indirect Expropriation in Comparative Public Law' in Schill, *IIL and Comparative Public Law* (n 6) 107, 130-137 and 143-147.

IV. A Transnational Solution

1. The classic approaches to implementing comparative public law

The question remains how exactly this comparative public law approach can be efficiently implemented so as to have a real impact on the future development of investment treaty law. Both Schill and Montt refer primarily to the classic doctrinal roots of comparative law in public international law, which is the reference in Article 38(1)(c) of the ICJ Statute to the 'general principles of law recognized by civilized nations' as a source of international law that is applicable to general treaty interpretation via Article 31(3)(c) VCLT.[114] Furthermore, Schill points out that comparative law studies can be the basis for calls for political reform of the present system; for raising arbitrators' awareness of the spectrum of available solutions; and directly for the interpretative task when construing broad treaty standards. All of these are more or less promising ways in which comparative public law can gain an increasing influence in the investment treaty world. And there might even be some chances of success in the investment treaty field, since the impressive amounts at stake, and thus the more generous budgets for legal fees, may stimulate lawyers to engage with comparative studies or even commission them so as to enrich and fortify their pleadings.

The problems with the suggested approaches are, however, not negligible. On the one hand, the technical notion of 'general principles of law' is a rather restrictive one; for numerous questions, it will frequently simply not be possible to evidence the crystallisation of a true common core in all major legal systems so as to be able to identify a true 'general principle of law'. Moreover, different from uniform international commercial law, investment treaties have not been elaborated on the basis of comparative studies, so that there is little experience with the comparative method and much of the work is still to be done from scratch – although Schill has laid the grounds for this in his 'International Investment Law and Comparative Public Law' volume.[115] On the other hand, the sound use of the comparative method is a highly sophisticated task and, due to its dependence on the prudent selection of legal orders and materials, particularly prone to both negligently poor execution and manipulation in bad faith. The practice of commercial arbitration suggests that arbitrators – like judges in state courts – are not infrequently overwhelmed by the task and eventually tempted to resort to more comfortable and simplistic patterns avoiding the complexity by embracing simplistic 'transnational' solutions.[116] The superficiality with which tribunals have approached the

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[114] Schill, *IIL and Comparative Public Law* (n 6) 26-31; Montt (n 64) 372.
[115] Schill, *IIL and Comparative Public Law* (n 6).
[116] For examples see J Kleinheisterkamp, 'The Review of Arbitrators' Interpretation of International Contracts – Transnational Law as a Dangerous Short-Cut' (2011) 29(2) ASA Bulletin 474-486; *id*, 'Lord Mustill and the Courts of Tennis – *Dallah v Pakistan* in England, France and Utopia' 75(4) Modern Law Review 639-654.

determination of the 'object and purpose' in the context of treaty interpretation leaves little hope that the comparative law task analysis will be approached with more much sophistication and care.[117]

2. Complementing transnational procedure with transnational substantive principles

If comparative law, despite its theoretical paramount importance, cannot be offered to the practitioner world in a sufficiently attractive manner the risk is that its use remains marginal and that practice will continue business as usual. What is needed is a vehicle that will provide practice with a ready-to-use elaborate final product of the comparative approach. Inspiration for such a vehicle can be found again – after the borrowing of the mechanism of international arbitration – in the world of international commercial transactions. Following the difficulties of unifying commercial law at a global scale through treaty ratification or harmonising it through the adoption of model laws, as well as the conceptual and practical failure the mythical *lex mercatoria* as propagated since the 1960, the idea of a transnational 'general part' of international commercial law, of a 'uniform international commercial code' has led to probably the most successful practical comparative law project in modern times: the UNIDROIT Principles of International Commercial Contracts (PICC), which in 2011 have now been published in their third edition (after 1994 and 2004).

As regards the working method for the elaboration of uniform international rules, it was clear from the outset that the starting point would be comparative law studies of numerous national legal systems, their legislation, case law and academic literature.[118] Insofar as it was possible to find coinciding national solutions for specific contractual problems, this allowed the reformulation of truly general principles which would reflect the common core of international contract law. In that respect the PICC are, similar to the US Restatements, not a primary source of law, but a secondary source that allows the cognition of internationally accepted principles of contract law as restated in the PICC and made accessible in a systematic manner.

It was also clear from the outset that in many instances it would not be possible to find the necessary congruence between national solutions. Accordingly, the PICC intend primarily 'to provide a satisfactory set of rules for those relationships that come about, by definition, across national frontiers, whereas the traditional national laws are essentially based on the requirements of normal internal relationships; ... [consequently] the code should not attempt

[117] See, *eg*, *Total S.A. v Argentine Republic*, ICSID Case No. ARB/04/1, Decision on Liability, 27 December 2010, paras 128-130.
[118] See S Vogenauer, 'Introduction' in: S Vogenauer & J Kleinheisterkamp, *Commentary on the UNIDROIT Principles of International Commercial Contracts* (OUP 2009) 9.

chiefly to reconcile the latter, but rather to lay down the principles and solutions which seem to be best adapted to the special requirements of international trade'.[119] In line with this logic, many provisions of the PICC do not restate principles that are already broadly accepted, but instead have to be understood as propositions, or 'pre-statements' for what should be considered the best solutions for specific problems of contract law which, by proving inherently convincing and thus being highly acceptable in practice irrespective of the cultural background of the parties, could grow into new general principles.

The advantages of such a non-binding transnational code of commercial contracts have proven to be manifold. The PICC can be applied as the substantive law governing contracts if chosen by the parties in conjunction with arbitration.[120] But beyond this positive function as 'applicable law', the PICC are of ever growing importance as a universally accepted benchmark for rules on international transactions. They have been of much use to arbitrators by facilitating a first appreciation of the fundamental legal problems of a case where an unknown foreign law is applicable; they are increasingly been applied both by international tribunals and state courts for the interpretation of national law which is frequently incomplete or partially not suitable regarding international transactions; they are the primary source when parties or arbitrators have opted to apply 'general principles' or even the *lex mercatoria* to solve the dispute; and they are broadly accepted as the single most useful tool for the interpretation and complementation of international uniform law instruments, such as especially the Vienna Convention on the International Sale of Goods (CISG).[121]

This experience could – and should – be made very fertile for the efficient implementation of comparative public law as a key element in investment treaty arbitration. In view of the numerous cases in which investment tribunals come to squarely opposite results in application of either similarly worded or even identical provisions,[122] it is simply not probable that the interpretations of the extremely vague standards in the vast host of investment treaties will actually converge in the near or not too distant future, even if tribunals were to embrace the idea of comparative public law. Such convergence will not come without the guidance by some unifying authority that is generally accepted as impartial and legitimate. It is equally unlikely that there will be sufficient international consensus on the need for structural reforms so as to establish a permanent appeals body or a comparable institution ensuring the consistency of international investment law. Instead, a central

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[119] UNIDROIT Study L – DOCUMENT 15 (1979) 8.
[120] See, e.g., the English Arbitration Act 1996 in s. 46(1)(b).
[121] See, eg, J Felemegas (ed), *An International Approach to the Interpretation of the United Nations Convention on Contracts for the International Sale of Goods (1980) as Uniform Sales Law* (CUP 2007).
[122] See, eg, C Schreuer, 'Diversity and Harmonization of Treaty Interpretation in Investment Arbitration' (2006) 3(2) Transnational Dispute Management 1, 16-17.

authority driving the necessary convergence on the basis of the postulate of comparative public law could be the persuasive authority of some *Principles of Investment Protection* elaborated by a working group of legal experts – possibly including government representatives – from a representative number of legal backgrounds, ideally united under the auspices of, and provided by a mandate from, an internationally recognised and neutral institution or organisation.[123]

As with the PICC, the elaboration of such *Principles* would aim at formulating carefully drafted and optimally balanced specific provisions that address all essential details necessary for legal certainty in international investments. Based on specific comparative studies, these provisions would represent the already existing common core of the constitutional guarantees and administrative standards of countries with the most stable and consolidated tradition of efficiently protecting property rights – but with due considerations for the specific legitimate needs for flexibility of developing countries and for the specificities of cross-border dimension as partially already elaborated at the international law level. Where such common core cannot be found, the comparative studies would provide insight into best practices and experiences, both at the domestic as well as the international law level. This comparative approach would allow the working group, by fusing domestic and international legal considerations,[124] to devise the best available solutions that ideally incorporate the postulated sound balance between the private interests of investors and the public interests of host states. Such *Principles* would ultimately be formulated like a legal code – without any claim to being legally binding or necessarily representing 'general principles of law' in the formal sense – and would contain specific rules that address the different facets and ramifications arising under the different general standards as found in investment treaties as well as domestic and regional legal instruments (such as especially under human rights conventions).

3. A methodological sketch

In practical terms, in order to incorporate the above elements, such project could be structured two-fold so as to allow the interplay between a top-down analysis relating to

[123] For past attempts to draft 'balanced' codes on investment protection at the UN and OECD level, albeit not on a comparative public law basis, see I Shihata, *The World Bank in a Changing World: Selected Essays* (1991) 247-250; see also *ibid* (ed), Legal Treatment of Foreign Investments – The World Bank Guidelines (1993) as well as the recent UNCTAD Investment Policy Framework for Sustainable Development in UNCTAD, *World Development Report 2012* (2012) 97-163; see also unsuccessful attempt of the International Law Association Committee on International Law of Foreign investments (2003-2008), http://www.ila-hq.org/en/committees/index.cfm/cid/1015.

[124] See also S Schill, 'Deference in Investment Treaty Arbitration: Re-Conceptualizing the Standard of Review Through Comparative Public Law', paper presented at the 3rd Biennial Global Conference of the Society of International Economic Law, 28 June 2012, available at http://ssrn.com/abstract=2095334 (visited 29 August 2012).

consolidating the knowledge about international investment law as found in IIA and other relevant international instruments, such as especially human rights treaties, as well as in international case law; and a bottom-up logic relating to extracting the rich national experiences with government intervention with private investor interests through from comparative analysis of national public and constitutional legislation and case law. The top-down analysis could first facilitate the identification of the various areas and their respective issues as they arise from treaties and investment arbitration. The investment arbitration cases more specifically will allow identifying the fact patterns and legal constellations of cases that have given rise to problems in the application of IIA provisions. Along the lines of the case study method proposed by Rudolf Schlesinger for comparative contract law,[125] they can provide the raw material for sampling test cases that, after eliminating the original international dimension and context, can then be given to national experts from selected jurisdictions to solve under their respective national legislation, case law and doctrine on public law and state liability. This treatment of the cases as if they were purely domestic would allow identifying the various national solutions in situations in which there is no discrimination on the basis of nationality, which, after all, is one of the main aims of investment treaty law. This 'domestification' of the cases may also lead to introduce certain distortions as compared to international cases but this can be controlled for at a later stage when confronting the comparative law analysis of the national country reports with the solutions found or discussed at the international level. The preliminary findings of such a first round of comparative law analysis based on the case study method will then inform the further mapping of the issues to be studied as well as a second round of comparative analysis based on highly detailed questionnaires that are again answered by national public law experts in country reports. These country reports then should allow the rapporteurs in charge of the different subjects of the study to elaborate, as in other restatement projects, their reports with a first draft of principles: on the one hand, the common core principles identified in the comparative analysis, including extensive comments and comparative law references, and, on the other hand, principles for which no common core could be identified but that could be formulated on the basis of the comparative law experience either as compromises or as new solutions that strike a fair balance between private (investor) interests and public (host state) interests. This first draft of principles would then be contrasted and tested against the solutions found in 'comparative international law',[126] i.e. especially in the case law of arbitral tribunals but, to the degree possible, also in the human rights instruments and their case law and doctrine. This step would then allow a critical reflection on the draft principle, their re-thinking an fine-tuning and the elaboration of alternative, especially so as to cater for specificities that only arise out of the international dimension of the problem. This back and

[125] RB Schlesinger, *Formation of Contract – A Study of the Common Core of Legal Systems* (vol 1, 1968) 5-41.
[126] See above n 16.

forth between the international investment sphere and the comparative public law sphere should ultimately allow making the choices and perfecting the drafting of the specific principles so as to finally end up with a code-like, detailed and richly commented set of rules that embody a re- and, probably more so, a pre-statement of Principles of Investment Protection that can be operational.

4. Applicability and Feasibility

Regarding their practical use in investment treaty arbitration, such *Principles* consolidating the best solutions of comparative public law and international law would, in the simplest of cases, operate as a starting point of argumentation. The positive 'hook' for their consideration could, at the simplest level, be their reflection of 'general principles of law' in the sense Article 38(1)(c) of the Statue of the ICJ – with the limitation inherent to such a pre-statement project that not all of its provisions could claim having the authority of reflecting technically such general principles of law. But as argued above, the stronger reason for considering such a pre-statement based on comparative public law in an investment arbitration is the need to resort to the object and purpose of the IIA provisions for their interpretation – and thus also for their teleological reduction. Such teleological interpretation for determining the actual meaning of the vague IIA provisions needs to be contextualized in the light of the logic of substitution of the host countries legislation and jurisdiction, following the steps that have been elaborated in this paper: (1) the object and purpose of IIA provisions is not – and was never intended to – offer protection to foreign investors beyond what is necessary to stimulate investments that contribute to the host country's development; (2) this implies the acceptance that the object and purpose is to provide a capped level of protection, which (a) in a first interim step can be pinned to the level of protection that the foreign investor can expect in its host country; but (b) owing to the multi-lateralizing effect of MFN clauses ultimately needs to be measured against the level of protection that is common to the countries with the highest levels of investment protection. The *Principles* suggested here, as re- and pre-statements of the detailed rules that can be distilled from comparative public law, would provide for a practical tool for navigating the rough sea of comparative law. Their true practical value would essentially derive from the persuasiveness of the (hopefully) superior quality and general acceptability of their provisions as well as the reputation of the members of the Working Group and of the organisation sponsoring it. If these conditions are met, the arbitral tribunal could proceed on the basis of a simple presumption that specific solutions spelled out in those *Principles* represent the most appropriate solutions for the problems of interpretation and complementation of the treaty standards in question – unless, of course, where the treaty provisions specifically clarify otherwise. The party challenging the appropriateness of the provisions in question would bear the persuasive, rather than evidential, burden of having to convince the tribunal of what the superior solution should be – which would inevitably require even more elaborate comparative arguments.[127]

As regards the feasibility of such a project, the failure of the attempts to draft a multilateral agreement on investment under the auspices of the OECD as well as of the subsequent attempt to establish multilateral uniform investment rules in the context of the WTO should not be taken as a bad omen. First of all, their formally non-binding nature of a soft-law instrument would distinguish them fundamentally from the previous efforts of codifying international investment law in binding treaties (and even linking them to the powerful enforcement mechanisms in the latter attempt). The very method of their elaboration would be based on the understanding that comparative law must be relied upon to establish the necessary constraints for the development of investment treaty law. Moreover, and that is probably the greatest challenge, their provisions would have to reflect convincingly a fundamentally sound balance between the protection of private rights and the public interests in regulation that follows from the 'object and purpose' of international investment law as developed above. If that can be achieved, such *Principles of Investment Protection* could be a significant contribution to ensuring the future legitimacy of investment treaty arbitration and to laying the basis for developing a truly global standard of judicial review of government interference with private investments that offers sufficient consideration for the legitimate exercise of sovereignty of a host state.

Finally, it should be noted that also the UNIDROIT Principles and their method of elaboration have not been free of problems and criticism.[128] Some concern inevitable individual weaknesses, such as especially those resulting from lacking co-ordination between rapporteurs of different sections and the resulting difficulties for their consistent application; others concern the challenges of uniform application without a centralized adjudication;[129] more fundamentally, questions of legitimacy arise relating to the composition of the Working Group and thus the comparative law sample, resulting in a lack of representation of developing countries; finally, there are important question arise about entrusting academics – rather than mandated public authorities – with a quasi-legislative task as well as the degree of involvement of government officials; the role and use of such transnational soft-law literally

[127] The same logic was considered in the discussions on the potential alternative forms of operation of the ILC Draft Articles on the Responsibility of States for Wrongful Acts if not adopted in form of a convention but in form of a declaration; see D Caron, 'The ILC Articles on State Responsibility: The Paradoxical Relationship between Form and Authority' (2002) 96 Am J Int'l L 857, 865-866.
[128] *cf* P Deumier, 'Les Principes Unidroit ont 10 ans : bilan en demi teinte' [2004] Revue des Contrats 774-783; see also HD Gabriel, 'UNIDROIT Principles as a Source for Global Sales Law' (2013) 58 Villanova Law Review 661, 666-672.
[129] See, e.g., JM Perillo, 'UNIDROIT Principles of International Commercial Contracts: The Black Letter Text and a Review' (1994) 63 Fordham Law Journal 281, 317.

beyond the State, as well as is not unproblematic as such and merits deeper reflection, as does the role of private initiatives in defining public interests. Yet none of these issues or shortcomings have put into question the general suitability of the working method. Much work is certainly needed to think through and confront similar issues in the context of the project suggested here;[130] indeed, also the negative experiences with the UNIDROIT Principles would provide valuable guidance and would need to be taken into account in specifying the working method in the investment context.

V. Conclusion

The aim of the article is both normative and operational, the former conditioning and being necessary for the latter. The starting premise is that, for arbitral tribunals to be able to strike the right balance between private (investor) interests and public (host state) interests in the application of the overwhelmingly vague and open-textured IIA provisions –and thus for both host states and investors to obtain proper legal certainty about their rights and obligations, it is necessary to understand the fears for sovereignty underlying the debate about the legitimacy of investment arbitration.

The finding of a need for 'capping' the extent of investor protection as well as from taking the *telos* or the object and purpose of IIA seriously allows drawing an important normative conclusion: any interpretation of IIA provisions cannot lead to granting foreign investors more protection than they could legitimately expect in a properly regulated market. While in a first step it could be argued that such properly regulated market would be that of their home country, out of which they are supposed to be attracted to other markets, the multi-lateralizing effect of MFN clauses in most IIA requires taking a transnational view on how to define the benchmark against which the level of protection enshrined in the vague treaty provisions is to be defined in detail and thus qualified. Only comparative public law can offer the basis for the elaboration of such benchmark which sets the cap on the interpretative scope: teleological interpretation requires understanding the commonly accepted maximum level of investor protection in the most advanced jurisdictions. Any higher level of protection would mean over-compensating foreign investors for the political risk that is merely supposed to be off-set so as to stimulate cross-border investment flows for the purpose of enhancing development – and thus violate the IIA's object and purpose as well as undermine the legitimacy of the current investment treaty regime.

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[130] For a poignant critique see J Kammerhofer, 'Law-Making by Scholarship? The Dark Side of 21st Century International Legal "Methodology"' (2012) 3 *Selected Proceedings of the European Society of International Law 2010* 115-126.

The finding that investment tribunals need to engage with comparative public law for their exercise of treaty interpretation leads to, and forms the basis for, the operational proposal of this article of how this task can be facilitated against the odds and complications of the *ad hoc* use of comparative law. For this, the article suggests to push the logic of borrowing tools from international commercial law a bit further: whereas international arbitration has given the current investment regime the procedural dimension required for its success in terms of efficiency and proliferation, the substantive dimension for ensuring its success in terms of legal certainty and legitimacy should be taken from the methods of creating transnational uniform law, building especially on the experience with the UNIDROIT Principles of International Commercial Contracts. In emulation of that method of restatement and pre-statement, the suggestion is an academic project of distilling the common core from the laws and case law of the countries with the highest level of investment protection – and controlling against a reasonable sample of other jurisdictions as well as existing international case law – and, where such common core cannot be found, to build on that comparative law findings of the national experiences so as to devise the best possible specific principles that strike a sound balance between the private and public interests. The so elaborated *Principles of Investment Protection*, which would spell out in much more detail the different facets of the law of investment protection, could serve as persuasive authority that would serve tribunals as an operational starting point of a (rebuttable) presumption of how to interpret vague IIA provisions. Importantly, in line with the 'capping' logic elaborated earlier, the suggested method is not designed to tell arbitrators what exactly the respective treaty provisions mean but what they do not mean, i.e. establishing a threshold beyond which investor protection cannot be expanded through interpretation without losing legitimacy. Up to that threshold, the *Principles* can inform of what vague treaty provisions can mean in the best of cases, and potentially with certain discounts to cater for the discrepancy of capacity and means of public administration in the most advanced countries and those which are typically at the receiving end of investor claims. The aim is to construe on a scientific basis persuasive authority that is better (than arbitral precedent) founded on the object and purpose of investment treaties and better informed by the rich experience of protecting economic interests against state interference and defining the scope of regulatory powers at the national level – and thus more persuasive for developing investment law in a manner that does not raise issues of legitimacy.

This may appear, at first sight, as a legislative project in interpretative disguise. Indeed, where arbitral tribunals accept comparative law arguments based on such *Principles* and make them the basis for their decisions, such rules expounded by academics may have a legislative character. It is, however, important to note that the aim is not to supersede the actual meaning of IIA provisions but to allow working out their normative content on the basis of a method that respects their underlying *telos*. It is about teleological interpretation and helping arbitrators to understand better and properly apply the law that the states that ratified those IIA gave them to apply. The result would be allow arbitrators to concentrate on the jurisdictional – as opposed to law-making – role and to provide both investors and host state more of what should be the real currency of international investment law: legal certainty.