Transitional Governments and the Protection of Foreign Investments under International Law

A thesis submitted for the degree of Doctor of Philosophy in Law

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Declaration

I hereby declare that the thesis is based on my original work, except for quotations and citations which have been duly acknowledged. I also declare that it has not been previously or concurrently submitted for any other degree at Brunel University or other institutions.

Heba Yehia

Abstract

The thesis examines the international state responsibility towards foreign investments of transitional governments that take over State control through unconstitutional means. This study evaluates the potentials and limits of the application of several doctrines, including whether such governments can invoke the defence of state immunity; and state responsibility to avoid their international liability in the context of international investment. The thesis shows that international responsibility of transitional governments towards foreign investments remains uncertain because are contradictory tribunals' view in investment arbitration. The inconsistent arbitral awards can be described as; "there is fragmentation in international investment law." Therefore, this study's main contribution to the literature revolves around the application of both over-enforcement and under-enforcement theories to review the problem of fragmentation in international investment law. Both over-enforcement and under-enforcement theories point to institutional causes of uncertainty regarding the question of the responsibility of successor governments towards foreign investments. The thesis recommends the development of a unitary framework of international law and the establishment of a new international convention that like the VCLT (1969) codifies and progressively develops international investment law.

Keywords:
Fragmentation; customary international law; international investment law; ICSID arbitration, under-enforcement theory; over- enforcement theory, State responsibility, State immunity, State sovereignty, foreign investment

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Dedication

This PhD thesis in law is dedicated to my mum Kariman and my father H.E Minister Yehia Abdel Megeed who has always made me proud of his achievements and reaching the highest positions in Egypt. This time is for you my father to make you proud of your only daughter. I am delighted to hold your name with the doctor title. I promise to always raise your name.

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Heba Yehia Abdel Megid

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Abbreviations

Ampal	Ampal-American Israel Corporation
AOC	Arabian Oil Company:
Art.	Article
ARSIWA	Articles on Responsibility of States for Internationally Wrongful Acts
BIT	Bilateral investment treaty
Canadian Model FIPA	Canada Model Foreign Investment Protection and Protection Agreement
CERDS	Charter of Economic Rights and Duties of States
CEMIGA	Convention Establishing the Multilateral Investment Guarantee Agency
ECT	Energy Charter Treaty
EMG	Egyptian company Eastern Mediterranean Gas
EGOTH	Egyptian General Organization for Tourism and Hotels
EGPC	Egyptian General Petroleum Corporation
EGAS	Egyptian Natural Gas Holding Company
ECSI	European Convention on State Immunity
ECtHR	European Court of Human Rights
ECJ	European Court of Justice
FET	Fair and equitable treatment
FDI	Foreign Direct Investment
FSIA	Foreign Sovereign Immunities Act

FPS	Full Protection and Security Standard
ICSID	International Centre for Settlement of Investment Disputes convention
ICC	International Chamber of Commerce
ICA	International Commercial Arbitration
ICJ	International court of justice
ILAs	International Investment Agreements
IMF	International Monetary Fund
IRUSCT	Iran-United States Claims Tribunal
LIAMCO	Libyan American Oil Company
LAFICO	Libyan Arab Foreign Investment Company
MENA	Middle East and North Africa
MIT	Multilateral Investment Treaty
MFN	Most-Favored-Nation
NAFTA	The North American Free Trade Agreement
NIOC	National Iranian Oil Company
NPC	National Power Corporation
NIEO	New International Economic Order
OECD	Organization for Economic Co-operation and Development Draft
PSNR	Permanent Sovereignty over Natural Resources
PCIJ	Permanent Court of International Justice
PGI	Philippine Geothermal Inc
SRL	Sierra Rutile Limited
SPR	Single Presentation Requirement
SPP	Southern Pacific Properties (Middle East) Limited
SIA	Sovereign Immunity Act
SCC	Stockholm Chamber of Commerce
UK SIA 1978	United Kingdom State Immunity Act 1978
UNGA	United Nations General Assembly
UNCTAD	United Nations Conference on Trade and Development
UNCSI	United Nations Jurisdictional Immunities of States and their Property

UN	United Nations
UNCITRAL Arbitral Rules	United Nations Commission on International Trade Law Arbitration Rules
US	United States
UK	United Kingdom
USA Model BIT	United States of America Model Bilateral Investment Treaty
v.	Versus
VCLT	Vienna Convention on the Law of Treaties
WTO	World Trade Organization

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Chapter 1: General Background

It is essential to briefly introduce the history of the international law on foreign investment**.** Throughout the colonial period, investment did not need to be protected. This is because colonial legal systems were combined into the imperial system, which provided enough protection for such investments. In this sense, the need for an international law on foreign investment was minor. Within the imperial system, the protection of investments was ensured by Parliament and the imperial's court. After the colonial period ended, the need for a system to protect foreign investment was felt. This is because the period instantaneously after the end of colonialism witnessed antagonism and hostility towards the foreign investments that were made by former colonial powers. This resulted in nationalism; there was a need for newly independent states to recover control over important sectors of their economies from foreign investors. This resulted in the nationalisation of foreign property. Nationalism became a threat for foreign investments.[1]

However, because the existence of economic philosophy favored the liberalisation of foreign investment, neo-policies were promoted by International Monetary Fund (IMF) and the World Bank. This required the liberal entry of foreign investment, national treatment and protection against violation ensuring treatment standards and secure dispute settlement. These polices needed to be implemented for states to secure financial assistance from international financial institutions. Thus, states had to sign international investment agreements (IIAs.) that provided assurance for foreign investment protection. [2]

Currently, the most noteworthy progress in international law is the growth of IIAs. These agreements take the form of treaties between states that address matters related to cross-border investments for the promotion, protection and liberalisation of foreign investments. States that conclude ILAs commit themselves to following certain standards of the foreign investment's treatments within their territory. IIAs govern significant features of the relationship between foreign investors and host governments. For instance, the establishment, admission, operation and withdrawal of foreign-owned companies. Also,

[1] Muthucumaraswamy Sornarajah, The International Law on Foreign Investment (Cambridge University Press 2004)
[2] ibid

ILAs define procedures for settling disputes. The most common types of IIAs are bilateral investment treaties (BITs).[3]The United Nations Conference on Trade and Development (UNCTAD) defines BITs as "agreements between two countries for the reciprocal encouragement, promotion and protection of investments in each other's territories by companies based in either country."[4]

Simply, BIT is a legally binding agreement between two states that establishes mutual promotion and protection of investments in both states. BITs provide rights for investors in foreign jurisdictions. For instance, security against expropriation by governments; establishment of sufficient recompense in the event of government takings and the right to transfer money from the host state to another state without restriction. It provides the right to international adjudication for any disagreement that arises; limits on operation requirements; and the right to choose administrative staff.[5]

The main objective of BITs is to regulate international investment relationships between states. BITs provide definitions of investors and investments and address matters regarding foreign investors' admission and treatment. For example, BITs guarantee that foreign investors will receive fair and equitable treatment will be treated no less favorably than national investors. It provides the right for foreign investors to not have their investments expropriated without compensation and enjoy full protection and security. BIT also provides foreign investors access to arbitration[6] against the host state to bring claims for violation of treaty obligations. Thus, foreign investors can bypass domestic courts of host states and all local remedies that might be available through direct access to international investment arbitration.[7]

[3] Paul Alexander Haslam, 'The Evolution of the Foreign Direct Investment Regime in the Americas' (2010), 31 (7) Third World Quarterly.
[4] 'Investment Instruments Online—Bilateral Investment Treaties', United Nations Conference on Trade and Development [2008].
[5] Office of the United States Trade Representative, Bilateral Investment Treaties <http://www.ustr.gov/trade-agreements/bilateral-investment-treaties>.
[6] Arbitration, a form of alternative dispute resolution (ADR), is a way to resolve disputes outside the courts.

[7] Andrew Newcombe and Luis L Paradell, *Law and Practice of Investment Treaties* (Kluwer Law International 2009).

Generally, investment arbitration is limited to treaty claims and disputes that involve the state. There are limits for the jurisdiction of tribunals. The investor must establish that the relevant dispute relates to an investment.[8] Once an investor raises a claim under an investment treaty, a tribunal is constituted to adjudicate. Once the tribunal establishes its jurisdiction, it determines the disputed facts and applies the relevant law. If the state has violated the applicable treaty standard, the tribunal may award compensation to investors. This award is binding on the respondent state and investor. ICISD tribunal awards are enforced under the authority of the ICISD convention.[9] It is also protected from judicial review by national courts. Investment arbitration tribunals apply standards that limit sovereign acts of the state's judiciary, legislature and administration.[10]

Accordingly, BITs allow foreign investors to claim that judicial, administrative or legislative measures have violated the core principles of these treaties without exhausting local remedies in host states' courts.[11] As a result, foreign investors have been raising many claims against host states for different reasons such as banking sector reforms, environmental policies, responses to economic crisis, implementation of treaty obligations, termination of concession contracts, revocations of licences and application of tax laws.[12] This raises the question of what is the effect of BITs on new governments? Nevertheless, before discussing such effect it is important to note that there are constitutional changes of government that can only occur through national consensus, if possible, or by referendum. However, there can be unconstitutional changes of government, there are two types of it, the replacement and emplacement. The replacement is acquiring power illegally which includes rebel insurgency, mercenary intervention and coup d'état. Emplacement refers illegally acquiring the power through emplacement of someone else in a position power, as was done by President Hosni Mubarak of Egypt when he given his power to the Egyptian Military Council. [13]

[8] Santiago Montt, *State Liability in Investment Treaty Arbitration: Global Constitutional and Administrative Law in BIT Generation* (Hart Publishing 2009)
[9] 'Convention on the Settlement of Investment Disputes between States and Nationals of Other States', 575 (1965) UNTS 159 (hereinafter ICSID Convention).
[10] Montt, 'State Liability in Investment Treaty Arbitration' (n8).
[11] Kenneth J Vandevelde, 'US Bilateral Investment Treaties: The Second Wave' (1993) 14 Michigan Journal of International Law.
[12] Montt, 'State Liability in Investment Treaty Arbitration' (n8).
[13] See Lomé Declaration of July 2000 on the framework for an OAU response to unconstitutional changes of government (AHG/Decl.5 (XXXVI)

In all cases, as according to the argument of Kelsen a government which has come to power by revolution should be recognized as a valid government in the sense of international law, providing that it is able to secure a substantial observance of the norms which it has set up. Also, Kelsen excludes any difference between a revolution and a coup d'etat.[14] Thus, questioning legality of changes of government is irrelevant particularly in the modern arena of international investment law. This is because BITs limit the ability of new governments[15] to change the contractual arrangements governing foreign investments irrespective to the legality of new government. Since there are treaties that contain umbrella clauses that specify that any unilateral changes to investment contracts constitute a violation of the treaty. Although there are treaties that do not contain umbrella clauses, the fair and equitable treatment (FET) standard is interpreted as a guarantee of the legal framework stability that governs foreign investments. Also, under investment treaties, expropriation of a foreign investment requires fair market value compensation regardless of whether the investment was acquired on a fair market value basis. Moreover, some other treaties have stabilisation clauses that are used in international investment law to prohibit the risk of regulatory change of host states.[16]

This raises the issue of the legitimacy of states to regulate in the public interests. In this regard, any attempts of new governments to unilaterally change contracts or reform the legal framework that governs investments can increase the state's liability under investment treaties.[17] On the other hand, new governments[18] can argue that international law provides the right for the state to regulate in the public interest. Every state has the freedom to choose its economic, political and cultural systems according to the will of its people.[19]

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[14] Hans Kelsen, 'Pure Theory of Law, The - Its Method and Fundamental Concepts' (1934), 50 Law Quarterly Review 474

[15] Revolutionary governments arise when the former regime is overthrown and the power goes to the ones who have overthrown it. Under international law, the permissibility of revolution is interrelated with self-determination and human rights.

[16] For example, freezing clauses aim to protect foreign investors from any changes in domestic laws. Also, economic equilibrium clauses provide compensation for the state's acts. In addition, there is a hybrid clause that requires the state to restore the investor's position to what it was before the regulatory changes.

[17] Jonathan Bonnitcha, 'Investment Treaties and Transition from Authoritarian Rule' (2014), 965 The Journal of World Investment & Trade.

[18] Under international law, right of revolution is interrelated with self-determination and human rights

[19] The Charter of Economic Rights and Duties of States enshrines, in its Article 1, every state's 'sovereign and inalienable right to choose its economic system as well as its political, social and cultural systems in accordance with the will of its people, without outside interference, coercion or threat in any form whatsoever'. The 1961 Harvard Draft Convention on the International Responsibility of States acknowledges a number of classifications of actions whereby non-compensable taking could take place, i.e.: a) taxation; b) general changes

1.1. The problem of study

It appears that there is a tension between legal stability and political change. On one hand, incoming transitional governments that are moving from authoritarianism system to more democratic one or from conflict to reconciliation and peace face pressure to enact economic reforms to redress the control of the previous regimes.[20] Such demands are difficult to ignore. For this reason, the transitional phase requires incoming regimes to reconsider the benefits provided to cronies of previous regimes. This may require renegotiating concession contracts, terminating monopolies and renationalising state assets that have been illegitimately transferred into private hands. This cause major changes in general laws such as taxation, labour and the relationship between investors and the business communities in which they operate in. This create inconsistency with assurances granted by the previous regime. This result in a different regulatory environment to that anticipated by investors when they originally invested. On the other hand, investment treaties can hamper the consolidation and emergence of more democratic governments. Investment treaties can dissuade incoming governments from enacting economic reform for civilian coalition building or by requiring the incoming governments to pay compensation when they are involved in such economic reforms, thus placing a huge strain on stretched budgets.[21]

This raises the question of how arbitral tribunals address the tension between legal stability and political change. International investment law is a new development in international law. It relies on the roots of general international law, particularly in the traditional field of protection of aliens and their property. There is no central authority—the arbitral panel is decentralised and private. Arbitral tribunals have to establish concrete norms of state behaviour towards foreign investors. [22] This generates the need for an assessment tool to analyse how these arbitral tribunals interpret open-ended and abstract standards of investment treaties given the tension

in the value of a currency; c) maintenance of public order, health or morality; d) valid exercise of belligerent rights; or e) normal operation of the laws of the state, subject to certain conditions in the draft convention. The Harvard Draft Convention does not possess binding power; nevertheless, it has been cited by arbitral tribunals, which are authoritative sources.

[20] Michał Lubina, Set the Torturers Free: Transitional Justice and Peace vs Justice Dilemma in Burma/Myanmar Polish Political science Yearbook, vol. 47(1) (2018)

[21] Bonnitcha, 'Investment Treaties and Transition from Authoritarian Rule' (n15).

[22] Montt, 'State Liability in Investment Treaty Arbitration' (n8).

between legal stability and political change. Sager, the prominent constitutional law scholar, developed the under-enforcement legal theory. The theory explains how in some instances, the law is not fully enforced.[23] Thus, under-enforcement theory can be an analytical tool to provide better understanding of how the law is interpreted among different tribunals. Generally, the under-enforcement theory leads to an examination of over-enforcement theory, the opposing theory, in which adjudicators extend statutes beyond their original understanding.[24] Both theories will be used as analytical tools to assess the law enforcement.

1.2. Aim of study

Nowadays, the world is unstable, especially in the Middle East and North Africa (MENA) since the Arab Spring in 2011.[25] More revolutions and new transitional regimes are anticipated. Transitional phase is reflective of the challenges generated for foreign investments when an unconstitutional takeover of power occurs within a State. However, the transitions can be non-violent, or violent but still the essence is their departure from the previous order to a completely different one, often accompanied by radically different policy values. Generally, transitional phase creates the tension between legal stability versus political change creates vagueness in defining the international liability of new governments towards foreign investment. It appears that international law is unclear about the responsibility of transitional governments in relation to foreign investments. In the meantime, neither new governments nor foreign investors can predict the outcomes of their future situations. Foreign investors will always argue that the state is responsible for safeguarding investments and is not allowed to make any unitary changes in policy under investment treaties. Nevertheless, the state will always argue that international law gives the state the right to regulate its public interests as a legal power. Also, recent claims resulting from revolutionary governments (the Arab Spring) have raised some questions. Firstly, can investment treaties constrain the incoming regime from taking the necessary economic and political measures to maintain the regime? Secondly, is the successor government bound by the investment treaty signed by the predecessor regime? Thirdly, to what

[23] Lawrence G Sager, *Justice in Plain Clothes: A Theory of American Constitutional Practice* (Yale University Press 2004).
[24] Henry P Monaghan, 'Constitutional Common Law' (1975), 89 Harv. L. Rev. 1 <https://scholarship.law.columbia.edu/faculty_scholarship/794>.
[25] Recent political revolutions by people against the governments in 2011-2012 in Egypt, Yemen, Tunisia and Libya were named the Arab Spring.

extent is the foreign investor provided with substantive protection from policy and legal changes by an incoming government?

Accordingly, the main objective of this research is to effectively understand international legal responsibility of new regimes towards foreign investments and arrive at evidence-based results. This thesis attempts to determine how international law deals with legal stability versus political change. This clarifies the vagueness of determining the international liability of new governments towards foreign investments in the light of international law. It requires examining the extent to which a transitional or new government can use different state defences under the laws of state immunity and state responsibility to avoid its international obligations. Also, the study will examine under the law of state responsibility the ability of revolutionary governments to make unitary changes to meet public demands that can negatively affect foreign investments. Thus, the doctrines that will be examined are state immunity, state necessity, force majeure and state responsibility.

Moreover, recent disputes resulting from new governments and other relevant cases will be examined to determine whether international investment law limits the incoming regime from taking necessary economic and political measures to maintain the regime. This raises the question about how tribunals interpret these standards in light of the tension between legal stability and political change. Thus, the study seeks to provide deeper analysis. Legal under-enforcement theory and its opposing theory, over-enforcement theory, will be applied as analytical tools to assess the enforceability of laws among different tribunals. The analysis will provide better understanding of how different tribunals interpret the law of states' international liability in international investment law. Generally, the main objective of this thesis is to fulfill the gap in the literature on this matter. It is expected that a thorough analysis of the existing international investment law, undertaken in this thesis, might provide an important building block for future regulation of international investment law. Thus, this research seeks to formulate new ideas and conclusions.

1.3. Importance of the study

Given the recent revolutions in Egypt, Yemen, Tunisia and Libya. In addition to the future political transitions are more likely to be subject to investment treaty claims resulting from political transitions. Thus, it is important for both foreign investors and host states to understand the international liability of revolutionary governments towards foreign investments in pre- and post-revolution times. This is important because foreign investors might be hesitant to invest in countries that experience revolution, which can affect them negatively because foreign direct investment (FDI) is important for economic growth. FDI has many advantages. FDI transfers scientific knowledge, increases revenue through expansion of the tax base; decreases reliance on national debt and international aid. It helps finding new methods for funding development and accessibility to scientific knowledge and the possibility of transferring it.[26]

1.4. Gap in the literature and research contribution

First, it is important to clarify that revolutionary or transitional government represent emergencies times in which economic, political and social forces are beyond the state's ability. An emergency time can involve political, economic and social crises. Thus, scholars have studied the state's liability towards foreign investments during emergency times from two perspectives. On the one hand, scholars have examined the doctrine of state necessity from the perception of the vagueness of using it as a necessity defence towards foreign investments during emergencies.[27] On the other hand, scholars have studied the topic from the perspective of the effect of treaty investment clauses on the state's limitation to take necessary measures during emergencies.[28] Thus, the originality of this thesis lies firstly in studying the state's

[26] U.N. LDC IV and OHRLLS, 'Harnessing the Positive Contribution of South-South Co-operation for Least Developed Countries' Development' (2011), 20, New Delhi.

[27] See Katia Yannaca-Small, "International Investment Perspectives: Freedom of Investment in a Changing World" in *Essential Security Interests under International Investment Law* (OECD 2007) 24.; Robert D Sloane, 'On the Use and Abuse of Necessity in the Law of State Responsibility', 106 The American Journal of International Law**;** David D Caron, 'The ILC Articles on State Responsibility : The Paradoxical Relationship between Form and Authority' (2002), 96 (4) The American Journal of International Law 857;); Jason Webb Yackee, 'Political Risk and International Investment Law' (2014), 24 (477])Duke J. Comp. & Int'l L. 477; Surendran R Subramanian, 'Too Similar or Too Different: State of Necessity as a Defence under Customary International Law and the Bilateral Investment Treaty and Their Relationship' (2012), 9 Manchester Journal of International Economic Law; 213. William W Burke-White, 'The Argentine Financial Crisis: State Liability under BITs and the Legitimacy of the ICSID System' (2008), Faculty Scholarship At Penn Law School

[28] Sotonye Frank, 'Stabilisation Clauses and Foreign Direct Investment: Presumptions versus Realities' (2015), The Journal of World Investment & Trade; Rudolf Dolze, 'The Impact of International Investment Treaties on

liability towards foreign investments during emergencies under the different doctrines of state immunity, state necessity, force majeure and state responsibility. The literature only focused on examining state responsibility under single doctrine of the state's necessity. In addition, this study adds to literature by focusing on the effect of investment treaties on revolutionary governments which was ignored on literature.

Most of literature focuses on addressing the effect of economic crises on foreign investment protection rather than on the political crisis. This study closes the gap on literature by addressing the effect of political crisis on foreign investment protection. The Argentines' economic crisis case has received much academic attention. Little academic attention was given to the claims that resulted from the revolutionary government's actions. Also, scholars have analysed the Iranian revolution, but there is a lack of analysis of claims resulting from the recent revolutionary governments. Accordingly, this research will fill this gap by studying these cases. Arab Spring cases are important because they have raised concerns about how international law deals with legal stability versus political change in modern international arena. Also, these cases have raised the concern that investment treaties limit the incoming regime from taking necessary economic and political measures for its maintenance.

Second, the research conducts deeper analysis on how the law is interpreted in light of the tension between legal stability and political change. This study is the first to use under-

Domestic Administrative Law' (2005), 37 New York University Journal of International & Politics 953; Julia G. Brown , 'International Investment Agreements: Regulatory Chill in the Face of Litigious Heat', (2013) 3 Western Journal of Legal Studies
Jonathan B Potts, 'Stabilizing the Role of Umbrella Clauses in Bilateral Investment Treaties': Intent, Reliance, and Internationalization' (2011), 51 (1005])Virginia Journal of International Law; Aleksandra Vonica, 'International Arbitration Agreements and their Adjustment Clauses: Are They in a State of Evolution?' (2016), International Arbitration Research Centre, University of Bucharest; Emmanuel Yaw Benneh, 'International Law, Sovereign Rights and Foreign Direct Investment: Directions from the Jurisprudence of International Arbitral Tribunals' (2002), 21 University of Ghana Law Journal**;** Dillon Fowler, 'Is This Really Necessary? The Scope of the Doctrine of Necessity in 21st Century Investment Treaties' (2016), 9 Creighton International and Comparative Law Journal; Jonathan Bonnitcha, 'Investment Treaties and Transition from Authoritarian Rule' (n15).Also see, Nasser Alreshaid, 'Revisiting the Notion of Full Protection and Security of Foreign Direct Investments in Post-Gadhafi Libya: Two Governments, Tribal Violence, Militias, and Plenty More' (2016) 28 Florida Journal of International Law 63; Pedro J Martinez-Fraga and Joaquin Moreno Pampin, 'Reconceptualizing the Statute of Limitations Doctrine in the International Law of Foreign Investment Protection: Reform beyond Historical Legacies' (2018) 50 New York University Journal of International Law and Politics 789; Commonwealth Secretariat ' mproving the recognition of foreign judgments: model law on the recognition and enforcement of Foreign Judgments' (2017) 43 Commonwealth Law Bulletin, 545-576; Arman Sarvarian'Codifying the Law of State Succession: A Futile Endeavour? ' (2016)3 European Journal of International Law 27; Laurence Boisson de Chazournes' International economic law and the quest for universality'(2019) 3Leiden Journal of International Law 32; timm Betz and amy Pond 'Foreign Financing and the international Sources of Property rights'(2019) World Politics A Quarterly Journal of International Relations 71

enforcement legal theory and its opposing over-enforcement theory to provide better understanding of how the international investment law is interpreted among different tribunals. Generally, using the under-enforcement theory can perform a valuable role in explaining the differences in award decisions. This theory has been applied in various areas of law[29], but not in international investment law, which brings originality to the study. Also, the relevance of using the under-enforcement theory comes from its constitutional law theory, in which both national constitutional law and investment treaties were established to limit states' sovereignty.

1.5. Scope and limitations of the study

This study generally considers three main areas of international law— law of state immunity, the law of state responsibility and international investment law, which is a sub-field of international law that integrates both public and private international law.[30]

However, it is important to highlight that this thesis examines international liability of revolutionary governments towards foreign investments under the laws of state immunity and state responsibility in international investment law context. This led to examine disputes between state-foreign investors in investment arbitration, which is a kind of global administrative law. Arbitral tribunals are established to do administrative law work. They determine the legality of states' acts, assess the fairness of governmental decision-making, provide remedies to individuals who are negatively affected by unlawful state acts and determine the appropriate content of property rights.[31] Also, investment arbitration can be described as a global constitutional law because both national constitutional law and

[29] Alexandra Natapoff, 'Underenforcement' (2006-2007) 75 Fordham L. Rev. 1715; 95.Bennett Capers, 'Crime, Legitimacy, and Testilying' (2008) 83 Indiana Law Journal 835; Paul MacMahon, 'Good Faith and Fair Dealing as an Under-enforced Legal Norm' (2014) 99 Minnesota Law Review 2051. Rev. 2051; Fionnuala Ní Aoláin and Eilish Rooney, 'Underenforcement and Intersectionality: Gendered Aspects of Transition for Women' (2007])1 International Journal of Transitional Justice 338.

[30] Barnali Choudhury, 'Recapturing Public Power: Is Investment Arbitration's Engagement of the Public Interest Contributing to the Democratic Deficit?' (2008) 41 Vanderbilt Journal of Transnational Law.775

[31] Gus Van Harten and Martin Loughlin, 'Investment Treaty Arbitration as a Species of Global Administrative Law' (2006), 17 (1) The European Journal of International Law.

investment treaties were established to limit states' sovereignty. Arbitral tribunals see these limits as matters of constitutional and administrative law. It appears that investment treaties delegate part of the jurisdiction of constitutional character to arbitral tribunals.[32] Therefore, the study's scope encompasses different areas of law.

It is also fundamental to note that the limitation of the study is the unavailability of recent case law. Little claims that resulted from the recent revolutionary government are not publicised. However, the study overcame this challenge by examining the limited publications available on ICISD cases. Also, the study overcomes such challenge by not being limited to only analysing cases resulting from revolutionary governments, but it also examines other relevant cases. It is also significant to note that although investment arbitration cases are the focus of the study, other relevant commercial arbitration cases[33] and national court cases will be examined can help answer research questions.

1.6. Research questions

It seems that international law is unclear about the international responsibility of transitional governments in relation to foreign investments. There is vagueness to what extent transitional government can use different state defences under the laws of state immunity and state responsibility to be exempted from its international obligations. Thus, this study seeks to determine international legal responsibility of transitional regimes towards foreign investments. The core question of this thesis is what does international law allow transitional governments to do with respect to foreign investments?

Other relevant sub-questions within this thesis are as follows:

1. Whether transitional governments immune under international law for measures they take against foreign investments?

[32] Montt, 'State Liability in Investment Treaty Arbitration' (n6).
[33] Commercial arbitration is limited to contract claims. In disputes between private parties, even when the state becomes a party to arbitration because it accepted the arbitration clause in a contract, it was acting in a private capacity. The arbitral awards are enforced under the New York convention.

2. Whether transitional governments allowed to use the law of state responsibility to accommodate changes for measures they take against foreign investments?

3. Whether transitional governments responsible under international law for protection and measures against foreign investments?

4. What are the conclusions and recommendations about what international law allows new governments to do with respect to foreign investments?

1.7. Methodology

The purpose of all research is to expand, refine and advance a body of knowledge, reach new conclusions and/or establish facts. Defining research's problem, questions and objectives is initial step to formulate research design to answer their research questions.[34] Generally, research methodology is the most important part of the research study. It determines the direction that the research will follow and tools that will be used in collecting and analysing the data.[35]

There are different research methods that can be used in every research. Nevertheless, it is important to select the right method that can help to answer research questions. Thus, to answer core research question of what does international law allow transitional governments to do with respect to foreign investments; appropriately, this thesis uses a combination of methodologies. It will use a doctrinal analysis approach. The word of doctrine means knowledge, instruction or learning.[36] Doctrinal analysis is the study of legal institution

[34] Denise Polit, CheryI Beck, *Nursing research: generating and assessing evidence for nursing practice* (Lippincott Williams & Wilkins, 2012)
[35] Michael Crotty, *the foundation of social research: meaning and perspective in the research process* (SAGE, 1998)
[36] Trischa Mann (ed), *AustralianLaw Dictionary* (Oxford University Press, 2010) 197.

through rational deduction or legal reasoning. It requires firstly locating the relevant sources of law and then analysis and interpreting the text.[37]

Also, scholars such as Kelsen explained that legal rules have a normative character as they order how individuals should behave. These rules do not attempt to predict, explain or understand human behaviour. [38] Thus, using doctrinal analysis can provide a systematic examination of the rules that govern certain legal category, clarify vagueness within rules, place them in a coherent and logical structure, possibly predict future developments and examine the relationship between rules.[39]

Nevertheless, doctrinal analysis requires the ability to reach a high level of critique and analysis. The researcher examines the sources to reach logical conclusions about what the law is. This requires description of certain inquiry being established whether it is evaluation, explanatory or conceptual. Generally, researcher analyzes the legislative provision, examines the situation and then decides if the situation comes within the rule.[40] It is important to note that sources of doctrinal research are typically conventional legal source. It includes analysis of legal principles and concepts of all types -rules, case laws and statutes.[41] Utmost of the doctrinal research sources are commentaries, periodicals and text books; however, they are not having the authority as the acts passed by state parliament and legislatures. Consequently, the quality of doctrinal research varies on the sources and materials that researcher relies on in the study. Currently, the doctrinal research plays essential role in the functioning of legal systems and research development. This is because doctrinal research has made many of outstanding research quality.[42]

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[37] Dennis Pearce, Enid Campbell and Don Harding ('Pearce Committee'), *Australian Law Schools: A Discipline Assessment for the Commonwealth Tertiary Education Commission* (Australian Government Publishing Service, 1987)
[38] Hans Kelsen, *Pure Theory of Law* (University of California Press, 1967)
[39] David Weisbrot, *Australian Lawyers* (Longman Cheshire, 1990)
[40] Christopher Enright, *Legal Reasoning* (Maitland Press, 2011)
[41] Mann (ed), *AustralianLaw Dictionary* (n32)

[42] Vijay M Gawas, 'Doctrinal legal research method a guiding principle in reforming the law and legal system towards the research development,' (2017) 3 International Journal of Law 5

It is significant to underline the importance of using doctrinal analysis in this study which is to acquire a logical examination of the rules, clarifies vagueness within rules, examine the relationship between rules and reach recommendations. Thus, doctrinal analysis can play role in assessing the main hypothesis of thesis which is that international law is unclear about the international responsibility of transitional governments in relation to foreign investments Therefore, doctrinal analysis will be used to analyze international responsibility of transitional governments under relevant three main areas of international law— law of state immunity, the law of state responsibility and international investment law. Thus, this study includes examining the doctrines of state immunity, state necessity, force majeure and state responsibility. It also involves textual analysis of relevant national laws, case laws, resolutions, treaties, conventions and legal academic writings.

Although the research focuses on studying investment arbitration cases, it is open to examining the relevant commercial arbitration[43] and domestic cases that can help answer the research questions. Also, the thesis studies the claims that resulted from transitional countries, but it will be open to examining other case law that can help answer research questions.

It is also important to mention that although methods of doctrinal research remain intact, legal scholars are trying to accommodate comparative analysis. Simply, comparative analysis is intellectual exercise that consider law as its substance and comparison as its process. [44] The first step to do comparative analysis is to define legal issue that will be examined in the study; subsequently, choice of comparators and sources.[45] Comparative analysis starts with the logical study of the differences and similarities between legal data points, then examine the reasons for the similarities and differences.[46] Mostly, comparative analysis helps to harmonise the law, support international unification and help adjudicators to fill gaps in law. This analysis method like any other legal analysis method aims to make improvement on how

[43] Commercial arbitration is limited to contract claims. In disputes between private parties, even when the state becomes a party to arbitration because it accepted the arbitration clause in a contract, it was acting in a private capacity. The arbitral awards are enforced under the New York convention.
[44] Gawas, 'Doctrinal legal research method a guiding principle in reforming the law and legal system towards the research development (n36)
[45] Geoffrey Samuel, *An Introduction to Comparative Law Theory and Method (Hart 2014)*
[46] Edward J. Eberle 'The Methodology of Comparative Law' (2011) 16 Roger Williams University Law Review

the law can be improved. It may act as a cause for legal changes, such as introducing a new policy.[47]

Thus, the study will employ little comparative analysis among different arbitral awards. It is an innovative way of treating the subject matter. The relevance of conducting little comparative analysis is exploring the differences and similarities between different tribunals. Particularly, to provide better understanding on how the law is interpreted among different tribunals. Thus, the findings of such a comparison may, therefore, be expected to yield a small contribution to the development of law in international investment law.

Furthermore, doctrinal analysis can refer to other areas where it can help in interpreting the results and defining research question.[48] Thus, this study will borrow constitutional theory to be applied into international investment law context. Constitutional theory helps to see the big picture. [49] Generally, a theory can be considered as a coherent explanation of certain phenomenon. A theory is created by a scholar where it can be seen as abstract entities taken from our social realism. It explains relations between matters. [50] Thus, this study will engage in theoretical analysis to acquire better understanding of the legal concepts and supports the study's findings.[51] This is because theoretical research raises complete understanding of the conceptual bases of legal principles.[52] Subsequently, under-enforcement legal theory and the opposing theory of over-enforcement are selected to be applied as analytical tools to assess law enforcement.

Ultimately, the research for the thesis depended mainly on primary sources that can answer core research question, the relevant national laws, case laws[53], statutes, judicial

[47] Samuel, *An Introduction to Comparative Law Theory and Method* (n43)
[48] Dave Owen and Caroline Noblet,' Interdisciplinary Research and Environmental Law' (2014) 41 ECOLOGY LAW QUARTERLY
[49] Thomas. Baker, 'Constitutional Theory in a Nutshell'(2004) 13 William & Mary Bill of Rights Journal
[50] Anne Taekema, 'Theoretical and Normative Frameworks for Legal Research: Putting Theory into Practice' (2018) The journal Law and Method
[51] Pearce, Campbell, Harding, *Australian Law Schools: A Discipline Assessment for the Commonwealth Tertiary Education Commission*,(n33)
[52] Dennis Pearce, Enid Campbell and Don Harding, *Australian Law Schools: A Discipline Assessment for the Commonwealth Tertiary Education Commission* (Australian Government Publishing Service, 1987)
[53] Major used cases: The Schooner Exch. v McFaddon, 11 U.S. 116, 3 L. Ed. 287, 1812 U.S. LEXIS 377, 7 Cranch 116 (U.S. Mar. 2, 1812); Trendtex Trading Corporation v Central Bank of Nigeria, [1977] 64 ILR 111; Societe Commerciale de Belgique (Belg. v. Greece), Judgment, 1939 P.C.I.J. (ser. AlB) No. 78; Gabcikovo-Nagumaros Project (Hung. v. Slovk.), 1997 I.C.J. 3 (Order of Feb. 5) para. 52 ; Unión Fenosa Gas, S.A. v. Arab

pronouncements, international treaties, conventions and resolutions.[54] Secondary sources[55] were journal articles and books, used as applicable.

Republic of Egypt; CMS Gas Transmission Company v Argentina Enron Corporation. v Argentina; Sempra Energy International v. Argentina; LAFICO v Burundi; AAPL v Sri Lanka, 4 ICSID Reports 246, Award of 21 June 1990; P Pantechniki SA Contractors & Engineers v Repub of Albania, ICSID Case No ARB/07/21, Award of 20 July 2009; AMT v Zaire, ICSID Case No ARB/93/1, Award of Feb 1997; Veolia Propreté v Arab Repub of Egypt, ICSID Case No ARB/12/15, Award of 25 May 2018; *Factory at Chorzów* Case (*Germany v Poland*) PCIJ, 1925; Starrett Housing Corporation, Starrett Systems, Inc. and others v. The Government of the Islamic Republic of Iran, Bank Markazi Iran and others IUSCT Case No. 24*SEDCO Inc v National Iranian Oil Co* (Award) [1985] 9 Iran-USCTR 248. Methanex v United States; *Philip Morris Brands Sàrl, Philip Morris Products SA and Abal Hermanos SA v Oriental Repub of Uruguay*, ICSID Case No ARB/10/7, Award of 8 July 2016.

[54] UNGA Charter of Economic Rights and Duties of States GA, Res. 3281(XXIX), UN GA'Res, 29th Sess., Supp. No. 31 (1974) 50; UN Convention on Jurisdictional Immunities of States and their Property of 2004 Caron, 'The ILC Articles on State Responsibility'; 9. ILC, 'Draft Articles on Responsibility of States for Internationally Wrongful Acts, with Commentaries' (2001)

[55] Major journals and books are Muthucumaraswamy Sornarajah, The Settlement of Foreign Investment Disputes (Kluwer Law International 2000); Clive M Schmitthoff, 'The Claim of Sovereign Immunity in the Law of International Trade' (July 1958) 7(3) The International and Comparative Law Quarterly 452;Hazel Fox, The Law of State Immunity (Oxford university press 2002). Christoph Schreuer, *State immunity: Some recent developments* (Grotius Publication 1988) 162; Robert Ago, Addendum to the Eighth Report on State Responsibility (Document A/CN. 4/318/ADD.5-7) (1980); Federica I Paddeu, 'A Genealogy of Force Majeure in International Law', in The British Yearbook of International Law The Author (Oxford University Press 2012) Federica I Paddeu, 'A Genealogy of Force Majeure in International Law', in The British Yearbook of International Law The Author (Oxford University Press 2012); Ian Brownlie, *System of the Law of Nations, State Responsibility, Part I* (Oxford University Press 1983).James Crawford, *The International Law Commission's Articles on State Responsibility: Introduction, Texts and Commentary* (Cambridge University Press 2002) 74. Christoph Schreuer, *The Protection of Investments in Armed Conflicts* (Cambridge University Press 2013); René Provost, State Responsibility in International Law Series (The Library of Essays in International Law) (1st edn, Routledge 2002); Santiago Montt, State Liability in Investment Treaty Arbitration: Global Constitutional and Administrative Law in BIT Generation (Hart Publishing 2009); Jonathan Bonnitcha, 'Investment Treaties and Transition from Authoritarian Rule' (2014), 965 The Journal of World Investment & Trade; Jeswald Salacuse, The Law of Investment Treaties (2nd edn, Oxford University Press 2010) 191; James Crawford, Brownlie's Principles of Public International Law (8th edn Oxford University Press 2012) 501; Ian Brownlie, System of the Law of Nations, State Responsibility, Part I (Oxford University Press 1983); Federica I Paddeu, A Genealogy of Force Majeure in International Law, in The British Yearbook of International Law The Author (Oxford University Press 2012) ;Dhisadee Chamlongrasdr, Foreign State Immunity and Arbitration (Cameron 2007); Christina Binder, 'Stability and Change in Times of Fragmentation: The Limits of Pacta Sunt Servanda Revisited' (2012) 25 Leiden Journal of international law 909; Robert D Sloane, 'On the Use and Abuse of Necessity in the Law of State Responsibility'(2012) 106 American Journal of International Law 447

1.8. Study outline

Chapter 2

This chapter brings the idea of under-enforced legal norms into international investment law. The theory explains how in some instances, the law is not fully enforced. Thus, under-enforcement is the relevant theory that can be used to assess the degree to which law is enforced. However, under-enforcement theory contradicts itself by being promptly over-enforced and under-enforced. This leads to an examination of over-enforcement theory, its opposing theory, in which adjudicators extend statutes beyond their original understanding. The purpose of this chapter is to simply explain both the under-enforcement and over-enforcement theories in preparation to be used as analytical tools to assess the laws enforcement in the next chapters.

Chapter 3

This chapter examines the limits of unconstitutional transitional governments in invoking the sovereign immunity defence to avoid international state liability and claims in the international jurisdiction. This requires examining the doctrine of state immunity to understand the limits in which international law provides a state, freedom to act within its territory. Both the over- and under-enforcement theories are used to assess the law enforcement.

Chapter 4

This chapter examines whether unconstitutional transitional governments are allowed to use the law of state responsibility to accommodate changes for measures against foreign investments. Hence, it is necessary to assess the limits to which hostile governments can invoke the necessity and force majeure defences to avoid international state liability. Both the over- and under-enforcement theories are used as interpretative tools to study different tribunals' decisions.

Chapter 5

This chapter investigates whether unconstitutional transitional governments are responsible under international law for protection and measures against foreign investments. It studies the

requirements of the doctrine of state responsibility for internationally wrong acts. To achieve this, it has been necessary to analyse two phases—the limits of state's responsibility during the course of a revolution and after such an event. Also, both the over- and under-enforcement theories are used as interpretative tools to study different tribunals' decisions.

Chapter 6

This chapter concludes the previous chapters, with an emphasis on the outcome of this thesis. More significantly, this chapter focuses on the contributions of this research to literature.

Chapter 2: Theoretical framework Under-enforcement Legal Theory

2.1Introduction

This study has borrowed under-enforcement the constitutional theory to apply it in international investment law context, which brings originality to the research. The main significance of using the under-enforcement theory is that it is a constitutional theory. At the same time, investment arbitration is a type of global constitutional law. This is because both national constitutional law and investment treaties were established to limit states' sovereignty. As according to Hertig and Cottier the constitution does not provide complete regulatory for state. The national constitution is a partial constitution which is completed by the other levels of governance.[56]

It is vital to note that the use of underenforcement theory in the study is not advocate for full enforcement of the law but rather to assess how the laws of state immunity and state responsibility are enforced in international investment law context. Thus, the theory can provide a better understanding of the study outcomes. Generally, the under-enforcement theory leads to an examination of its contrary theory the 'overenforcement.' Hence, the chapter starts by introducing the under-enforcement legal theory and its strengths and weaknesses. It then examines over-enforcement theory and its strengths and weaknesses. Examining the strengths and weakness of both theories is to only understand their application. Thus, the purpose of this chapter is to simply explain both the under-enforcement and over-enforcement theories in preparation to be used as analytical tools to assess the laws enforcement in the next chapters.

2.2 Under-enforcement Legal Theory

Larry Sager is a prominent constitutional law scholar who introduced under-enforcement theory. Sager has made significant achievements in law through the publication of many

[56] Thomas Cottier and Maya Hertig, 'The Prospects of 21st Century Constitutionalism' (2003) 7 Max Planck Yearbook of United Nations Law 261, 303–4.

articles and books, such as 'Justice in Plainclothes.'[57] Sager defines under-enforcement theory as the circumstances in which the court fails to enforce constitutional provisions fully.[58]

Sager explained that primary purpose of this theory in which the court refuses to hold anyone liable for injurious rights violation is to justify the availability of alternative remedies whether its's based on institutional or analytical reasons.[59] Sager clarified the institutional reasons to limit enforcement based on institutional capacity, such as impropriety or the inability of the court to decide a particular issue. For example, when a federal judiciary system fails to determine claims that are constitutionally based due to judicial incompetence rather than considering any relevant clause or reading.[60]

On the other hand, the analytical reasons to limit enforcement 'based upon an understanding of the [underlying constitutional] concept itself'.[61] For example, congress can read the constitutional norm broader than the Supreme Court. Also, Sager explained there are some constitutional provisions are under-enforced because they are interpreted in a justice-seeking way.[62] Consequently, the textual analysis is portrayed in the literature as a tool to free judges from constraints. The role of the legislative authority is to choose statutory language. Nevertheless, legislators lack the power to bind judges to the intentions underlying those choices. This makes scholars such as Maltz to argue that judges should interpret the textual language based on their views of the meaning of words and direction of precedent. This provide that judges should do good interpretation on language based on their views about the meaning of words.[63]

Accordingly, modern scholars advocate under-enforcement theory in which courts can refuse to enforce the legal rules where the legislature intended to enact. Modernist scholars also argue that changes in values should affect statutory interpretation. Constitutional principles undergo under-enforced changes over time. For example, change between 1920 and today is that public has to accept the extensive role of government generally. The constitutional norms enforced in

[57] Sager,'Justice in Plain Clothes' (n23)
[58] ibid
[59] Maxwell Maltz, 'Rhetoric and Reality in the Theory of Statutory Interpretation: Underenforcement, Overenforcement, and the Problem of Legislative Supremacy' (1991) Boston University Law Review 767.
[60] Sager, 'Justice in Plain Clothes' (n23)

[61] David R Williams, Jr, 'In Defense of the Secular Status Quo' (2016) Virginia Law Rev.
[62] Sager, 'Justice in Plain Clothes' (n23)
[63] Maltz, 'Rhetoric and Reality in the Theory of Statutory Interpretation' (n 59).

1920 were different than the norms under-enforced in 1965. There can factors that affect decisions to under-enforce certain constitutional principles and demonstrate how these factors many change over time.[64] However, drawbacks from the change of social values in justifying interpretation will increase indeterminacy of process.[65]

It appears that institutional and analytical reasons are the main drivers for under-enforcement. Governing the law of the Internet is a good example that can better explain these considerations.[66] The large number of illegal downloads of copyrighted material occurs without arrests, investigation or prosecution; the police have under-enforced the law.[67] These crimes go unpunished because those responsible for its enforcement interpret the law on illegal download as not a crime, which is an analytical reason rather than an institutional one. Another reason for under-enforcement in the law of the internet is limited resources and the inherently open technical Internet structure, which are institutional reasons rather analytical ones.[68] Nevertheless, under-enforcement theory has its strengths and weaknesses that must be discussed to understand the proper application of the theory.

2.2.1 Strengths and weaknesses of under-enforcement theory.

Under-enforcement theory has several strengths. It can promote more justice. For example, the right to minimum welfare measure, which gets rid of deep-rooted social bias behaviours. It is reflected in *Plyler v Doe*[69] a Texas law prohibited free education to children who are illegally in the country. The District Court, the U.S Supreme Court and Fifth Circuit Court of Appeals under-enforced the law because it violated the Equal Protection Clause of the Fourteenth Amendment. The Supreme Court found that the significance of educating children, particularly those who are illegally in the country. This is because there is no fault of their part. The court outweighed unsubstantiated aspiration on the State's part to maintain educational resources or alleviate illegal immigration at the border.'[70]

[64] Ernest A Young, 'Popular Constitutionalism and the Underenforcement Problem: The Case of the National Healthcare Law' (2012) 75 LAW AND CONTEMPORARY PROBLEMS 157.
[65] Maltz, Rhetoric and Reality in the Theory of Statutory Interpretation' (n 59).
[66] Natapoff, 'Underenforcement' (n29)
[67] ibid.
[68] ibid.
[69] *Plyler v Doe*, 457 US 202 (1982) ('*Plyler*').
[70] ibid.

Another similar example of judicial under-enforcement is *Williamson v Lee Optical*,[71] in which opticians contested an Oklahoma statute on ground that it is unlawful for any person other than a licensed optometrist or ophthalmologist "to fit lenses to a face or to duplicate or replace into frames lenses or other optical appliances, except upon written prescriptive authority of an Oklahoma licensed ophthalmologist or optometrist."[72] The District Court held that because the law "prohibit[ed] the wearers of eyeglasses from exchanging their frames either to obtain more modern designs or because the former frames are broken, without first visiting an ophthalmologist or optometrist', the law's practical effect was to 'divert [] from the optician a very substantial, as well as profitable, part of his business."[73] The court reasoned that 'the knowledge necessary to perform these services is strictly artisan in character and can skillfully and accurately be performed without the professional knowledge and training essential to qualify as a licensed optometrist or ophthalmologist.'[74] The District Court under-enforced the statute because it was discriminatory and unreasonable and breached both Equal Protection Clauses. These judicial under-enforcement cases show how the under-enforcement of a law can result in more justice.

Another strength of under-enforcement theory is its consideration as providing proper balance between individual freedom and state coercive authority.[75] Darryl Brown defines the withholding of criminal sanctions as facilitating ongoing 'trust [and] cooperation' between government and businesses.[76] Responsive under-enforcement can benefit and empower individuals, enhancing their independence, dignity and potential growth where legal sanctions might otherwise destroy them. Also, scholars such as Margaret Raymond noted, there may be a social agreement that full enforcement of such laws would be unreasoning.[77] Such under-enforcement is a form of response to social demands.

For example, during civil disobedience, in which protesters often violate criminal laws, forces do not totally enforce the laws. This is because fully enforcing the laws in such case will negatively affect democracy if the protester is treated like a traditional criminal.[78] In this sense,

[71] *Williamson v Lee Optical Co.*, 348 US 483 (1955).
[72] ibid
[73] ibid
[74] ibid
[75] Natapoff, 'Underenforcement'(n29)
[76] Darryl K Brown, 'Street Crime, Corporate Crime, and the Contingency of Criminal Liability' (2001) 149 Univ. of Penn. Law Review 1295.
[77] Margaret Raymond, 'Penumbral Crimes', (2002) 39 American Criminal Law Review 1395, 1400 nn 16–18.
[78] ibid.

under-enforcement represents a reactive government that acknowledges not all laws should be enforced. It promotes political change and discourse. Also, it appears that under-enforcement theory addresses conflicting values by sending message that political activism, individual autonomy or free speech are more significant than routine enforcement of laws.[79]

Another example is internet laws. Scholars such as Sager have noted that cyberspace is the largest place of breaches of intellectual property law of anywhere in human history.[80] Under-enforcement in the cyberspace context can bring positive effects, such as enhancing the development of new technologies and creativity. However, one group's liberty may be another group's fetters. License and copyright holders perceive themselves sufferers of under-enforcement, and civil disobedience has its expenses. In the debate over Internet under-enforcement, the upside depends on who under-enforcement protects and who it disadvantages; in contrast, in the under-enforcement of homicide laws there is no upside.[81]

Another strength of under-enforcement theory is it can be benchmarked to assess law reforms, such as the domestic violence reform movement of the 1970s and 1980s, when there was widespread of public under-enforcement. It is a form of social dismissal and disadvantage. The aim of such reform efforts was to reduce under-enforcement and ensure that prosecutors and police enforced laws.[82] The outcome of these reform efforts is that, not merely are national violence laws more vigorously and routinely enforced today but also legal resources are dedicated to national violence issues.[83] Thus, fuller enforcement of anti-violence law serves as an important function of physical protection and value setback in which the state steps in to revise traditional male violent prerogatives and protect female violence.[84] Accordingly, under-enforcement shows the gap between state assurances under law and in with the way it utilises scare resources and political legality under the pressure of democratic groups.[85] It appears that under-enforcement theory draws a vital distinction between the law and enforcement. It helps to determine when another actor acts in impermissible way. Generally, under-enforcement

[79] ibid.
[80] Sager,'Justice in Plain Clothes' (n23)
[81] *See Edward K Cheng, 'Structural Laws and the Puzzle of Regulating Behavior' (2006) 100 Northwestern University Law Review 655, 714–15.*
[82] See G Kristian Miccio, 'A House Divided: Mandatory Arrest, Domestic Violence, and the Conservatization of the Battered Women's Movement' (2005) 42 Houston Law Review. 237, 239–241.
[83] Lisae C Jordan, 'Introduction to Special Issue on Domestic Violence' (2005) 39 Family Law Quarterly 1, 1–2 (documenting increased programs and expenditures on domestic violence).
[84] Natapoff, 'Underenforcement' (n 29)
[85] ibid.

theory is effective, however, only when there are relevant norms particularly suitable for under-enforcement; otherwise, the theory could have negative effects.

Under-enforcement has weakness. It can create mistrust of law enforcement, exacerbate crime and increase illegal act activities. Under-enforcement undermines the effectiveness of law enforcement.[86] It might result in harmful judicial errors.[87] Judicial errors might arise when under-enforcement fails to provide the right judgment. Judicial under-enforcement also may undermine the value of legitimacy because it obliges the judiciary to say one thing and do another, so that courts that under-enforce will be seen as illegitimate.[88]

Furthermore, it weakens the strength and equality of the law. It can be considered a form of official disrespect for under-protected groups and an unequal distribution of resources. One of the clearest examples of the harmful effect of under-enforcement is urban under-enforcement. Sociological research found that high standard neighbourhoods have low crime rates compared to minority neighbourhoods with high crime rates. It appears that forces provide less service to victims.[89] In urban communities there is high crime where police fail to respond to crime, residents recognize that their complaints may be answered to inadequately or not at all. Urban under-enforcement takes many forms, including allowed open-air drug markets, unsolved homicides slow or non-existent responses, and the public disorder and property crimes. The sources of the under-enforcement are varied for instance: disorder in politically weak neighbourhoods, inadequate funding for urban area services, and residents' distrust of police.[90]

Also, underenforcement has resulted to grave crimes in central cities, for example in Los Angeles, there have been 11,000 homicides since 1988, almost 6,000 with no arrests. Three-quarters of those homicides are focused in one-quarter of the city. In the neighbourhood now recognized as South L.A., most of killers are not ever caught. Unresolved homicide rates are related not merely to racial segregation and neighbourhood poverty but also weak police forces, reflecting an unequal distribution of public resources.[91] Thus, under-enforcement can be

[86] ibid
[87] Abimbola Olowofoyeku, 'When Courts Get It Wrong: Judicial Errors and Common Law Underenforcement' (2018) 134 The Law Quarterly Review 450-477
[88] Williams, 'In Defense of the Secular Status Quo' (n61).
[89] Sara Stoutland, 'The Multiple Dimensions of Trust in Resident/Police Relations in Boston' (2001) 38 Journal of Research in Crime and Delinquency: SAGE 226, 231
[90] Natapoff, 'Underenforcement' (n 27)
[91] Jill Leovy and Doug Smith, 'Mortal Wounds: Getting Away With Murder in South L.A.'s Killing Zone', *L.A. Times* (1 January 2004).

considered a type of discrimination and a barrier to the neutrality of law. Governmental officials discriminate deliberately against helpless groups by withholding legal protection.[92]

Moreover, under-enforcement exemplifies relationships and experiences, whereby decisions are made from a relational perspective rather than enforcing the law on experience.[93] Therefore, applying this theory fails to protect certain victims, more so victims of insecurity and violence, and often protect the perpetrators. Consequently, the democratic legitimacy of the legal system is called into question because actualizing the theory highlights the legal failure observed through the discrimination and undemocratic treatment of the poor.[94]

Another example of negative effects of under-enforcement is undocumented workers in the United States. There are an estimated nine million undocumented immigrants, and the underground economy in which they normally work undocumented immigrants work in construction, restaurants, individual homes, restaurants and manufacturing. They are employed by prominent political figures and major corporations. They pay billions of dollars to federal taxes and state. At the core phenomenon of undocumented worker lies a tangle of official practices including the selective under-enforcement of labour, criminal and immigration laws.[95]

Government officials acknowledge that the government cannot entirely enforce immigration laws. It is unlawful for employers to hire undocumented workers, but immigration officers openly recognize they do not enforce these provisions; instead, the government ignored immigration violations in the work place. US policymakers acknowledge that full enforcement of restrictive entry law could damage the economy. Workplaces are deeply regulated areas, protected by labour and wage standards and safety, health and anti-discrimination laws. US Congress noted that the Fair Labor Standards Act, Title VII and the National Labor Relations Act apply to all workers, irrespective of immigration status.[96] These laws, nevertheless, are under-enforced as well.

[92] John Hart Ely, 'Democracy and Distrust: A Theory of Judicial Review' (1980) 15 Valparaiso University Law Review 76–77
[93] Lawrence G Sager, 'Thin Constitutions and the Good Society' (2000) 69 Fordham L.Rev. 1989.
[94] Deborah Tuerkheimer, 'Underenforcement as Unequal Protection' (2016) 57 Boston College Law Review1287
[95] ibid.
[96] ibid.

Nevertheless, undocumented workers are typically paid below minimum wage and are racially discriminated against, work in unsafe conditions, are fired for their language and race, and are fired for practicing their rights to organize or join unions.[97] Immigrants are also victimized by workplace conditions and employers that breach criminal and labour laws. The under-enforcement of these protective laws contributes to the lawless and dangerous conditions that characterize undocumented immigrant life.[98] Such workers suffer from domestic violence, rape, theft and homicide. They experience racial discrimination, sexual harassment and hate crimes. The police recognize they cannot play their customary role if they are seen as immigration enforcers.[99] Undocumented workers do not obtain full protection of criminal law because they have strained relations with police.[100]

Thus, the under-enforcement of labour, public welfare and criminal laws define the conflicting relationship that the US legal system has with these workers. Under-enforcement is a selective enforcement tool that subsidises illegal acts of employers and industries who rely on undocumented workers. At the same time, it diminishes the rights and dignity of workers by bearing their personal and economic victimization in breach of current laws. The selective enforcement results in a lawless atmosphere.

Under-enforcement also can prohibit certain individuals from accessing basic functions, such as work or healthcare. This is seen in urban communities where individuals have trouble obtaining education and jobs. Similar to undocumented workers, under-enforcement avoids them from participating in fundamental public activities, such as collective bargaining and joining unions, to which they otherwise are legally allowed.[101]

Consequently, the under-enforcement is not suitable for every situation. As such, it is more effective when used with other mechanisms that check for unreasonable contractual conduct, such as good faith and fair dealing. Also, the under-enforcement can be seen to be solved by the over-enforcement of laws.[102] It shows that under-enforcement theory contradicts itself as being simultaneously over-policed and under-policed, whereby communities are classified into

[97] Lori A. Nessel, 'Undocumented Immigrants in the Workplace: The Fallacy of Labor Protection and the Need for Reform' (2001) 36 Harvard Civil Rights-Civil Liberties Law Review. 345, 360
[98] Natapoff, 'Underenforcement' (n 27)
[99] ibid.
[100] See, e.g. Solomon Moore, 'LAPD Enlisted in Fight on Human Smuggling', *L.A. Times* (25 January 2005).
[101] Natapoff, 'Underenforcement' (n 27)
[102] Young, 'Popular Constitutionalism and the Underenforcement Problem' (n 40).

criminal and victim classes from which the law can be administered.[103] This shed the light on the need to examine the phenomena of over-enforcement.

2.3 Over-enforcement Legal Theory

Henry Monaghan identified the phenomenon of overenforcement—as adjudicators extending statutes beyond the original legislative intent, it is the opposite of under-enforcement.[104] For example, in *Jones v Alfred H Mayer Co*.[105] The plaintiff claimed that a real estate company in St. Louis County (Missouri) did not agree to sell him a home in a certain neighbourhood due to his race. The plaintiff raised a claim in federal court, asserting racial discrimination under 42 USC § 1982.[106] The lower courts dismissed the complaint concluding "that § 1982 applies only to state action, and does not reach private refusals to sell."[107] Nonetheless, the Supreme Court expanded the scope of the Fourteenth Amendment, holding "that § 1982 bars all racial discrimination, private as well as public, in the sale or rental of property, and that the statute, thus construed, is a valid exercise of the power of Congress to enforce the Thirteenth Amendment."[108] Therefore, over-enforcement resulted from interpreting laws in an extended way.

Over-enforcement also can occur when the legal system enforces rules that are hard to fulfill to minimize law violations. Likewise, legal system can enforce sanctions that exceed the normal optimal deterrence for the violation.[109] Such is the case when a legal system erroneously imposes a hefty fine on a legal violation at a level that is unnecessarily high, say by imposing a $10,000 fine on all drivers who exceed the speed limit of sixty miles per hour. It is beyond the normal deterrence. However, over-enforcement theory, like under-enforcement theory, has its strengths and weaknesses.

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[103] MacMahon, Good Faith and Fair Dealing as an Underenforced Legal Norm' (n27)

[104] Monaghan, 'Constitutional Common Law' (n24)

[105] *Jones v Alfred H. Mayer Co.*, 392 US 409 (1968) ('*Jones*').

[106] 42 USC § 1982. Derived from the Civil Rights Act of 1866, section 1982 provides that '[a]ll citizens . . . shall have the same right . . ., as enjoyed by white citizens . . ., to inherit, purchase, lease, sell, hold, and convey real and personal property'.

[107] *Jones v Alfred H. Mayer* (n 105).

[108] ibid

[109] Abner S Greene, 'Can We Be Legal Positivists Without Being Constitutional Positivists' (2004) 73 Fordham L.Rev. 1401.

2.3.1 Strengths and Weaknesses of Over-enforcement Theory

So far as strengths, over-enforcement can increase the deterrence level that substantive liability standards cannot remedy. It creates fear, which minimizes the number of criminal offenses committed due to the hefty fines imposed on violators. Over-enforcement theory is supported by political processes, which create an environment that authorizes harsh punishments.[110] Moreover, judicial over-enforcement can promote more justice as seen in *Jones*.[111]

On the other hand, over-enforcement theory has weaknesses. Scholars such as smith argued that over-enforcement or in other word the over criminalization provide disproportional punishment for offenses. It can degrade the quality of law and justice. Generally, over-enforcement happens more in undefined wrongdoings where it results to interpretive flaws. There can be extensive interpretation because of laws ambiguity. It allows people to be convicted based on judicial determinations behind the scope of law.[112]

Moreover, over-enforcement theory has weaknesses, with effects similar to under-enforcement theory, such as, group victimization, social distrust and increased violence.[113] For example, officials can use over-enforcement to target criminals who are poor and lack the resources to fight for their rights; hence, after trials, they are remanded because they lack the resources to pay the fines. This is seen in urban law enforcement where it is known for its over-enforcement, racial profiling and police disrespect.[114] Also, in cases where rich people are involved, over-enforcement might send the wrong message that the rich people can freely commit crimes because they can pay the fines imposed for committing the crime.[115] This can be reflected on states since there are rich and poor states.

In the end, negative effects of both theories can be summarized that the state can be abandoning its caretaking responsibilities, by either over-punishing or under-protecting. Generally, under-enforcement and over-enforcement establish a gap between community and police. It discourages citizens from going to the police since they fear the forces will mistreat them and will not protect them from crime. It is cycle in which under-enforcement makes communities

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[110] ibid.
[111] *Jones v Alfred H. Mayer* (n81).
[112] Stephen F. Smith, Overcoming Overcriminalization' (2013) 102 Journal Criminal Law & Criminology 537. 3
[113] Natapoff, 'Underenforcement' (n 27)
[114] Young, 'Popular Constitutionalism and the Underenforcement Problem' (n 40).
[115]Rachel Barkow, 'Overseeing Agency Enforcement' (2016) 84(5) George Washington Law Review 1130.

with high crime in turn, justifies even more punitive over-enforcement.[116] The difference between bad and good over or under-enforcement turns on relationships, intentions and consequences of police practice. Accordingly, both theories are introduced with their purposes, strengths and weakness. This is raising the question of what we can reach from both theories?

2.4 Under-enforcement Theory Versus Over-enforcement Theory

It seems that underenforcement and overenforcement theories can occur when adjudicators are applying the law. Also, government might decide to over or underenforced the law in certain areas. Both theories have strengths and weaknesses, depending on their application. In some cases, under-enforcement may solve over-enforcement problems, though the solution to under-enforcement often will be more arrests or more policing. In other cases, over-enforcement and under-enforcement are not mutual alternatives; instead, they are double symptoms of the breakdown in relations between community and law enforcement.[117] Nevertheless, events, conditions and public attitudes dictate when and how under-enforcement and over-enforcement patterns are used to exercise justice. These changing patterns depend on the case in question. Generally, over or under-enforcement generally reflects adjudicators opinion of its own institutional ability to define rules that may be over-enforced or under-enforced at different times depending on changing political circumstances, historical circumstances and attitudes.[118]

It is also significant to note that the use of under-enforcement or over-enforcement theory to assess law enforcement requires certain technique. For illustration, there are some constitutional principles that have a determinate meaning. For example, the president must be at least thirty-five years old. In these circumstances, it would be easy to identify whether the provision is over-enforced or under-enforced. Other constitutional principles are less determinate in term of text and oblige judges to establish doctrinal rules and implement them

[116] ibid
[117] See Wayne A Logan, 'Criminal Law Sanctuaries' (2003) 38 Harvard Civil Rights-Civil Liberties Law Review.321
[118] Natapoff, 'Underenforcement' (n 27)

in certain situations. The prediction for over-enforcement and under-enforcement thus arises in situations where we likely reach agreement on the meaning of fundamental concepts.[119]

A requirement of specific definition would eventually be self-defeating because under-enforcement arises in those areas where the fundamental norms are most problematic to define with precision. For instance, it is uncommon that the Constitution identifies a sole, accurate meaning for balancing norms such as the separation of powers and federalism. This is similar to investment treaties, do not create concrete rules but merely abstract standards and open ended. This can attribute to the problems of under-defined law where broad law that invites selective enforcement. These vague laws allow enforcement authorities to select from many potential offenders behind the scope of the statute.[120]

Accordingly, broad laws blur the line between illegal and legal. Judges will choose to let many individuals breach the law and sanction others for the same conduct.[121] Discretion is a problem; there are no guidelines, and few criteria make law enforcement subjective and open to many different interpretations that depend on the judge's opinions rather than actual culpability and legislative definition.[122] Adjudicators might over or under-enforce the law because they are trying to square the law with the facts of the case to render their own notion of justice. This is going to be reflected while using the theories as interpretative tools in studying different tribunal decisions. Nevertheless, it's important to note the relevance of employing the selected theories into the study.

2.5 Relevance of Under-enforcement Legal Theory in the Study

Under-enforcement theory clarifies how laws are not fully enforced for various reasons in particular situations. Thus, the theory can illustrate how laws are enforced in the international investment context. The idea of an enforcement gap between legal duties and available

[119] Young, 'Popular Constitutionalism and the Underenforcement Problem' (n 40).

[120] Cynthia Godsoe, 'Recasting Vagueness: The Case of Teen Sex Statutes' (2017) 74 Washington and Lee Law Review 173.
[121] ibid.
[122] ibid.

sanctions helps to make sense of how international adjudicators talks about 'international liability' in the international investment law. This can establish the link between under-enforcement theory and study. The theory can bring a better understanding of study outcomes. Also, it is significant to highlight that use of theory is not a call for full enforcement of the law but rather to assess the laws of state immunity and state responsibility are enforced in the international investment law context.

Generally, Under-enforcement theory can bring originality into this thesis. This is because under-enforcement theory applies in various area of the law, including criminal justice, transitional justice, various aspects of US constitutional law, the role of prosecutors, good faith contracts, judicial harmful errors consequences,[123] corporate law,[124] antitrust law[125] and healthcare law.[126] However, under-enforcement theory has yet to be applied in international investment law. Also, as previously mentioned under-enforcement theory leads to an examination of its contrary theory the 'over-enforcement.' Like this, both the under-enforcement and over-enforcement theories will be used as analytical tools in assessing the law enforcement in the next chapters.

2.6 Concluding Remarks

This chapter brings the idea of under-enforced legal norms into international investment law context. The under-enforcement legal theory is developed by Sager the prominent constitutional law scholar. The theory explains how in some instances the law is not fully enforced. The idea of an enforcement gap between legal duties and available sanctions helps to understand of how international adjudicators talks about 'international liability' in the international investment law. Thus, under-enforcement theory is the relevant theory that can be used in this study as an analytical tool to assess the law enforcement. Also, the main

[123] Haywood Jefferson Powell, 'Reasoning about the Irrational: The Roberts Court and the Future of Constitutional Law' (2011) Wash.L.Rev.Assoc.
[124] MacMahon, Good Faith and Fair Dealing as an Underenforced Legal Norm' (n27)
[125] Howard A Shelanski, 'Information, Innovation, and Competition Policy for the Internet' (2013) 161 The University of Pennsylvania Law 1663, 1664
[126] Young, 'Popular Constitutionalism and the Underenforcement Problem' (n 40).

relevance of using the under-enforcement theory into the study comes from the fact that it was applied to constitutional law. At the same time, investment arbitration is a type of global constitutional law. This is because both national constitutional law and investment treaties were established to limit states' sovereignty.

The underenforcement theory has been applied in various areas of law but not in international investment law, which brings originality to the study. The Under-enforcement theory also leads to an examination of over-enforcement theory, its contrary theory, in which adjudicators extend statutes beyond their original understanding. Over-enforcement of the law can also occur when the legal system enforces rules that are hard to fulfill to minimize law violation. Over-enforcement can increase the deterrence level that substantive liability standards cannot remedy.

Like this, both theories will be used as analytical tools to assess the law enforcement in the next chapters. Thus, this chapter introduces both legal theories—Underenforcement and Overenforcement—and their purpose, strengths, weaknesses and means of application. It finds there can be good and bad overenforcement and underenforcement, depending on the application. However, this study is not focused on examining bad or good ones. The study is focused on using both theories as analytical tools to explain how the laws of state immunity and state responsibility are enforced in the international investment law context. Also, the use of theories is not a call for full enforcement of the law but rather to provide a better understanding of how the laws of state immunity and state responsibility are enforced in international investment law context.

However, the uses of under-enforcement or over-enforcement theory to assess law enforcement require certain technique. Some rules do have a determinate meaning. In these circumstances, it would be easy to identify whether the provision is over-enforced or under-enforced. Other rules are less determinate in term of text and oblige judges to establish doctrinal rules and implement them in certain situations. The predication for over-enforcement and under-enforcement thus arises in situations where we likely reach agreement on the meaning of fundamental concepts. This is similar to investment treaties, do not create concrete rules but only abstract standards and open ended. This has led to the problem of under-defined where

broad law that invites selective enforcement. Adjudicators might over or under-enforce the law because they are trying to square the law with the facts of the case to render their own notion of justice. This is going to be reflected into the study. Finally, the next chapter applies both under-enforcement and over-enforcement theories to assess how the law of state immunity is enforced in international investment law context.

Chapter 3: Whether transitional governments immune under international law for measures they take against foreign investments?

3.1 Introduction

State immunity is a principle of customary law in which the sovereign state cannot be sued without its consent. It provides states to have freedom in their interactions with foreign investors within their territories. States have the right to decide their method of management of their social, economic and political system over their territories without the interference of foreign investors. [127] In this sense, the host state can argue that it should be exempted from its international liability towards foreign investments during transitional times. This means that foreign investments can face different challenges due to state sovereignty acts. Hence, it made it important for foreign investors to understand the limitation of state sovereignty acts towards foreign investments; especially since host states can always invoke sovereignty arguments. Thus, this chapter tries to answer the question of whether transitional governments immune under international law for measures they take against foreign investments? This requires examining when successor governments Could invoke the sovereign immunity defence to avoid international state liability, specifically under the current international arena? Accordingly, this chapter examines the doctrine of state immunity in international investment law context. This chapter uses both over- and under-enforcement theories as interpretative tools to assess how the law of state immunity is enforced in international investment law context.

3.2 Doctrine of state immunity

State immunity is an establishment of customary international law, treaty law and domestic law. [128] It made the state to be immune from suit regarding wrongful acts in certain

[127] UNGA Charter of Economic Rights and Duties of States GA, Res. 3281(XXIX), UN GA'Res, 29th Sess., Supp. No. 31 (1974) 50 art. 1 and 2

[128] The international court of justice recognize that state immunity derives from the principle of sovereign equality of states. As the Statute of the International Court of Justice in 38 lists "the general principles of law recognized by civilized nations" as a source of international law. Additionally, sovereign immunity can be seen in the domestic laws. For example, in the United States, the FSIA is the primary statute that determines whether the American national court will afford a foreign state immunity. It contains a commercial exception. Further, the United Kingdom, Australia, South Africa, Singapore, Argentina, Japan, Israel, Canada and Pakistan have passed a legislation similar to the FSIA. See Winston P Nagan and Joshua L Root,The Emerging Restrictions on

circumstances, leaving sufferers of such acts with no redress. This doctrine excuses a state from the foreign domestic court's jurisdiction.[129] In general, state has the authority to pass legislation, conclude treaties, enforce judgments, enforce taxes, assume public debt, define property rights and so on.[130] Critically, state sovereignty empowers the state to take decisions over its territory without prior consultation with anyone. States as sovereigns have exclusive control of all spaces on their territories, including the social, economic and political aspects of these spaces.[131]

This appears that states as sovereigns have freedom to interact with foreign investors in their territories and shape the rules and practices of any such interactions. Salacuse demonstrated that states are granted the right to regulate both national and foreign investors' activities within their borders.[132] This is seen in some of the investment treaties.[133] It is also seen in fundamentals of international relations which is reflected in United Nations Charter of Economic Rights and Duties of States (UNCERDS). It was adopted by the UN General Assembly (UNGA) in 1974 states in Article 1 that: "Every State has the sovereign and inalienable right to choose its economic system as well as its political, social and cultural system in accordance with the will of its people, without outside interference, coercion or threat in any form whatsoever."[134] Further, Article 2 provides that:

> "Every State has the right (a) to regulate and exercise authority over foreign investment within its national jurisdiction in accordance with its laws and regulations and in conformity with its national objectives and priorities. No State shall be compelled to grant preferential treatment to foreign investment; (b) to regulate and supervise the

Sovereign Immunity: Peremptory Norms of International Law, the U.N. Charter, and the Application of Modern Communications Theory38 (2013) ؛ North Carolina Journal of International Law and Commercial Regulation 375

[129] Yearbook of the International Law Commission 1986; see Art 6. State immunity'; also, see United Nations Convention on Jurisdictional Immunities of States and their Property (the "U.N. Convention") Art 5: State immunity

[130] Gus van Harten, 'The Public-Private Distinction in The International Arbitration of Individual Claims Against The State' (2007) 56(2) International and Comparative Law Quarterly

[131] Weiss TD Hubert, *The Responsibility to Protect: Research, Bibliography, Background Supplementary Volume to the Report of the International Commission on Intervention and State Sovereignly* (The International Development Research Centre 2001)

[132] Jeswald Salacuse, *The Law of Investment Treaties* (2nd edn, Oxford University Press 2010) 191

[133] BIT (Egypt – Spain) (1992) Art 3(1), 1(2) and 1(2)[5] states that "[e]ach Party shall protect in its territory the investments made in accordance with its laws and regulations," and defines protected investments as "any kind of assets, such as goods and rights of all sorts, acquired under the law of the host country of the investment and in particular, […] rights to engage in economic and commercial activities authorized by law or by virtue of a contract, particularly those rights to search for […] or exploit natural resources, in accordance with existing laws and regulations"

[134] UNGA Charter of Economic Rights and Duties of States art 1 (n127)

> activities of transnational corporations within its national jurisdiction and take measures to ensure that such activities comply with its law, rules and regulations and conform to its economic and social policies. Transnational Corporations shall not intervene in the internal affairs of a host State. Every State should, with full regard for its sovereign right, cooperate with other States in the exercise of the right set forth in this subparagraph."[135]

We can infer from this that Article 1 is more direct than Article 2; it does not cause confusion. On the contrary, Article 2 causes confusion because it shows that each state is granted the authority to regulate foreign investments in a way that reflects its domestic affairs. This might result in the states misusing this authority to escape their international obligations. This vagueness can allow adjudicators in cases to over or under-enforce the law because they are trying to square the law with the facts of the case to render their own notion of justice. Thus, this Article 2 needs to be more precise and should provide detailed criteria. Nevertheless, we can also infer from Article 2 that international law allows states a wide margin of appreciation in the control of entry, operational activity, termination and exist of things and people from its territory. [136]

This raises the question of what exactly are the limits, if any, of these sovereign rights and immunities of states, particularly, in relations to immunity defences under international investment law. Put differently, has international law developed appropriate legal tools/muscles to flex against the public law doctrine of state sovereignty that dominates almost every sphere of inter-state relation? In almost all cases of hostile interference with foreign investments, host states always invoke sovereignty arguments. In the Anglo-Iranian Oil Co. case,[137] Iran argued that it was a sovereign act to change the international agreement for public interest. Thus, it should be exempted from any of the international obligations that were established by its predecessor regime, an argument similar to Egypt's argument in the *Ampal* case, which held that the dispute was "an act of sovereignty and a matter of Egyptian national security."[138]

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[135] UNGA Charter of Economic Rights and Duties of States, art 2 (n127)
[136] ibid
[137] *Mobil Oil Iran Inc. and Others v Government of the Islamic Republic of Iran*, partial award (July 14, 1987)
[138] *Ampal-American Israel Corporation and Others v Arab Republic of Egypt*, ICSID Case No ARB/12/1, Decision on Liability and Heads of Loss of. 21 Feb. 2017

Consequently, we can infer that in international disputes states use the sovereignty defence to avoid international obligations. It appears that state is given the right to maintain its public interest over private interest. However, it should have a valid sovereign purpose rather than attempt to avoid its international obligations. Laws should be clear on elaborating the criteria for the state to use the sovereign defence. This sheds light on the necessity of understanding the relationship between state sovereignty and foreign investments. When a state becomes a party to any investment agreement, it has the right to stipulate the conditions that match with its sovereign interests over any commercial matters. This is shown in fundamentals of international relations that is seen in the principle of sovereignty in Article 2 of the 1974 UNCERDS. States have the right to decide the method of management of their social, social and political system over their territories without the interference of foreign investors. This includes the right of state to supervise foreign-financed projects to guarantee compliance with environmental matters, domestic socioeconomic requirements and national laws.[139] This raises the question of sovereign rights in the administrative investment mandates.

3.3 State sovereignty rights regarding administrative investment mandates

Administrative investment contracts are always signed by a host state for the purpose of providing public service.[140] This type of contract has its origins in French administrative law. It gained practice among civil law countries, including Egypt where foreign investors ask recompense for adverse intervention of the state and national courts evaluate the legitimacy of state acts. The principle of legitimacy in administrative law obliges the existing national law and international law and regulations to be observed in order to recompense the investor. [141] Thus, it is crucial for foreign investors to know what is meant by the public order for a state and its authority limitations. Arbitration plays an important role for dispute settlement when the state does not agree to redress the claimant for the sovereign acts inimical to his investment.

[139] UNGA Charter of Economic Rights and Duties of States, art 2 (n127)
[140] Mansour Al-Saeed, 'Legal Protection of Economic Development Agreements' (2002) 17(2) Arab Law Quarterly
[141] See Muthucumaraswamy Sornarajah, *The Settlement of Foreign Investment Disputes* (Kluwer Law International 2000)

However, host states are permitted to regulate and monitor the foreign investment projects on their territories.[142]

3.3.1 The state has the right to amend the contractual terms

In general, the contractual parties are not allowed to make any unilateral changes in the agreement after it is made. Nevertheless, a state can change the terms of an administrative contract depending on the circumstances. As foreign investors enter international investment contracts to meet business interests while the state must protect its public interest, a balance must be continued between public and private interests. The case of Compagnie Générale Française des Tramways (1910)[143] and Compagnie Nouvelle du Gaz de Deville-lès-Rouen (1902)[144] reflected France's supreme administrative court's clarification on the matter of administrative contracts under public law. The state permitted to use its public power to change contractual terms. A state is given the right to unilaterally change the terms of the contract for public interest's subject to full compensation payment.

Also, in the case of force majeure, a state's acts are legitimate as necessity for public interest protection. In this necessity case, the public body of the state can take control of the project without wrongdoing on the part of the investor-contractor. In such domestic urgency times, the investment project can be either seized by a unilateral decision of the state or another contractor or public body can operate the project at the expense of the replaced party.[145]

3.3.2 The state has the right to terminate administrative contracts

The investment administrative law permits host states to terminate the contract. Regarding the administrative contract, a state has the executive power to unilaterally terminate the contract without the necessity of misconduct or error on the part of the other contracting party.[146] This

[142] ibid

[143] *Compagnie nouvelle du gaz de Deville-lès-Rouen* (Conseil d'Etat 10 January 1902) (France)
[144] *Compagnie générale française des tramways* (Conseil d'Etat 21 March 1910) (France)

[145] Suleiman El Tamawi, *The Administrative Contracts: Comparative Study* (Ain Shams University Publications 1984); Suleiman El Tamawi, The Effect of the Prince Theory and the Theory of Unforeseen Physical Circumstances (Ain Shams University Publications 1991) 653
[146] Ibid.

is demonstrated when Egyptian Administrative Court differentiated between administrative and civil jurisdictions:

"The administrative contract has its own features that distinguish them from the civil contracts; that feature is that the administrative contracts are connected directly to the needs of the public utilities which targeted by this kind of contracts. These [administrative] contracts seek to give the priority to the public interest rather than private one. According to that feature, the public authority has the right to terminate the contract if it sees that the public interest should be applied. The compensation is the only right to the other party."[147]

It seems that the state has inherent legal authority to terminate an agreement in case the administrative contract does not meet public welfare at any time. The administrative contract prioritises public interest over private interest. The other party has only the right to compensation.[148] Also, in case of an administrative failure by the foreign investor, there can be sanctions or contract termination.[149] Accordingly, we can infer that the state enjoys practicing its sovereignty rights regarding administrative investment mandates. It appears that the state is given the right to maintain its public welfare even through it can be inimical to the foreign investor's interests, but the state will be subject to compensation. This raised the question of the other sovereign acts that foreign investors might face apart from investment administrative contracts.

3.4 The challenges of state sovereignty towards foreign investments

An open economic plan obliges the host state to create its political and legal structure in a manner that can attract investments. It provides a stable investment environment for the investors. This can help the host state in gaining more economic benefit from the foreign investments. However, there are state sovereign challenges in the investment climate that might negatively affect the interests of foreign investors. Sovereign challenges can be categorised as legal, political and economic.

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[147] The Supreme Administrative Court (Egyptian Council d'Etat) decision No. 1227 (Translated)

[148] ibid
[149] ibid

3.4.1 The legal sovereignty of host states

The first type of legal sovereignty is that the state is given the right to amend its domestic law. It has the inherent authority to regulate its territory, which could negatively affect the interests of foreign investors. Foreign investors rely on a stabilisation clause to overcome the challenge that they may encounter following the States use its sovereign power to amend its domestic law. This stabilisation clause can be placed in the investment contract or in the BIT as a safeguard against adverse state interventions.[150] Stabilisation clauses limit the state sovereignty act and bind the state not to alter the relevant regulations and laws in a way that would negatively affect investors' interests. As foreign investors expect fair and adequate regulatory systems when practicing their businesses, these investors uses stabilisation clauses for protection against the state's sovereign authority.[151]

For instance, in the case of the *AGIP SPA v Congo,*[152] the claimant used the stabilisation clauses in the dispute to argue that this clause should be protecting investments from the sovereign actions of the host state but they still suffered from the state's sovereignty actions.[153] The concession agreement between AGIP SPA and the Congolese government, Article 4 asserts that:

"The government would not apply certain ordinances and decrees as well as all other ordinances and subsequent decrees. This clause aimed to ensure that state would not change the law regarding the private joint stock company thus, protecting it from expropriation." Article (11) added:

> "In the event of modifications being made to the company laws, appropriate provisions would be enacted to ensure that these modifications did not affect the structure and composition of the organs of the Company provided for in the Agreement and the

[150] The stabilisation clause means that the state cannot change the relevant laws during the time of the investment project.
[151] Van Harten, 'The Public-Private Distinction in The International Arbitration of Individual Claims Against The State' (n 130)
[152] *AGIP S.P.A. v People's Republic of the Congo,* ICSID Case No. ARB/77/1, Award of 30 Nov. 1977

[153] ibid

> Articles of the Association of the latter, which provide a duration for the Company of 99 years."[154]

The government of Congo decreed that all the company's assets and shares would be moved to a state-owned company without paying a fair compensation. The ICSID tribunal held its decision that there was a conflict between the investment agreement and the Congolese domestic law. The tribunal required Congo to pay compensation for the damages that were caused by its unlawful expropriation decisions. [155] Another similar case is *the Libyan American Oil Company (LIAMCO) v Government of the Libyan Arab Republic*.[156] LIAMCO attained three concessions for oil exploration and exploitation in Libya. The petroleum minister of Libya provided an agreement with the stabilisation clause to protect the interests of LIAMCO. The concession agreement between LIAMCO and the Government of Libya states:

> "(1) The government of Libya, the commission and the appropriate provincial authorities will take all steps necessary to ensure that the company enjoys all the rights conferred by this concession. The contractual rights expressly created by this concession shall not be altered except by mutual consent of the parties; (2) This concession shall throughout the period of its validity be construed in accordance with the petroleum law and the regulation in force on the date of execution of the agreement of amendment by which this paragraph was incorporated into this concession Agreement. Any amendment to or repeal of such Regulations shall not affect the contractual rights of the company without its consent."

This clause seemingly prohibits any changes in the national petroleum laws following the date of the contract should not have any effect on the company's contractual rights. However, the principle of state sovereignty allowed the Libyan government to make new laws and change the pre-existing regulations for public policy and interest. This negatively affected LIAMCO's interests. In 1969, there was a regime change and a new government under President Moammar Alkhadafi came to power. In 1973, the revolutionary command council of Libya practiced its unilateral sovereign power and issued law No. 66 for the purpose of expropriating 51% of the concession agreement with LIAMCO. After a year the remaining 49% was nationalised.

[154] ibid
[155] ibid

[156] *Libyan American Oil company v Government of the Libyan Arab Republic*, award of 12 April 1977

LIAMCO went to international arbitration due to the insufficient compensation stipulated in the concession agreement. The tribunal noted that the concession agreement was made with the previous government. All the legal principles were accepted in national and international law. It appears that there was a breach of obligations because of the stabilisation clause.[157] Therefore, the state had to fulfil its obligations and pay compensation. In general, damage determination is according to "the general principles of law", and the level of state responsibility affects the compensation measurement.[158]

Another example is the arbitration award of Texaco in 1977. Libya made an oil concession agreement with foreign companies in 1955; it had to fulfil its obligations under a 50-year oil concession agreement based on the stabilisation clause. This meant that the Libyan government could not change anything without the agreement of the mutual parties. The concession agreement throughout its validity period had to be interpreted according to the petroleum law and regulations. Following the Gaddafi-led Libyan revolution in 1969, Libya made an aggressive bargain with foreign oil firms. By 1973, Libya enacted a decree to nationalise the properties of California Asiatic Oil and Texaco overseas petroleum companies.[159]

This prompted the foreign oil companies to go to international arbitration to sue Gaddafi's government for rejecting participation. The sole arbitrator in the case interpreted the concession agreement and examined the application of the stabilisation clause to the nationalisation acts of Libya. The arbitrator concluded that the previous government of Libya had a contractual obligation that limited Libya's sovereign acts for the long term including the nationalisation acts that are taken by the post-revolutionary government. The arbitrator justified that this contract limited the state of Libya's sovereignty as the concessionary agreement is an international agreement separated from the state's domestic law.[160] We can infer from the previous cases that stabilization clause made adjudicators to under-enforce Art 2 of the 1974 UNCERDS. [161]

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[157] Stabilisation clause means that the state cannot amend its national laws within the time frame of the foreign investments made.

[158] *LIAMCO v Government of the Libyan Arab Republic* (n 156)

[159] Texaco Overseas Petroleum Co & California Asiatic Oil Co v Government of the Libyan Arab Republic (Merits) (19 Jan 1977) 17 ILM 4 [hereinafter Texaco]

[160] ibid

[161] Art 2 of the 1974 UNCERDS provides that each state is granted the authority to regulate foreign investments in a way that reflect its domestic affairs.

However, other adjudicators did not under-enforce Article 2 of the 1974 UNCERDS. The state is allowed to have room in amending its national laws despite the existence of stabilization clause. For instance, in the *Parkerings-Compagniet v Lithuania* case, the tribunal found that the state has to exercise its sovereign authority in amending or cancelling a law even though there can be a stabilisation clause in the investment agreement, according to which a state cannot change the regulatory framework during the time foreign investors make their investments. However, the tribunal clarified that state is not allowed only to act inequitably, unreasonably and unfairly in the exercise of its legislative authority.[162]

It appears that the interaction between Article 2 of the 1974 UNCERDS (representing fundamentals of international relations) and stabilization clause is problematic. Both over and under-enforcement theories can explain that stabilization clause is interpreted differently among different tribunals. It appears that stabilization clause is interpreted either broadly or narrowly based on tribunal's discretion. This might be because tribunals are trying to square the law with the facts of the case to render their own notion of justice.

The second type of legal sovereignty act is in the administrative regulation bureaucracy system in the public sector. Feiler described state bureaucracy as procedures, practices and actions aimed to shape the governmental policies implemented by public servants. A state can highly exercise its sovereignty in its civil administration, but this can negatively impact both the interests of the investors and the state. For example, a delay in the renewal of a commercial license for an investor will adversely affect the entire project operation. In addition, it can lead to revenue loss for both parties. Also, corruption in civil administration is always a problem in the investment climate. [163] A state can completely terminate the agreement if it was encouraged

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[162] *Parkerings-Compagniet As v Republic Of Lithuania*, ICSID Arbitration Case No. ARB/05/8, Award of 11 September 2007

[163] Gil Feiler, *Economic Relations between Egypt and the Gulf Oil States, Petro Wealth and Patterns of Influence* (Sussex Academic Press 2003) 90

to sign the agreement through bribery. The legitimate practise of the sovereignty defence exempts by some of the state acts is because they are representing the people.[164]

This can be seen in the recent dispute cases that stemmed from the Egyptian revolution in 2011. There was an alleged suspension of gas supplies by the government to foreign companies. Egypt claimed that the previous government had made agreement for exporting natural gas to Israel based on profitability and bribery.[165] This made the new government of Egypt terminate the agreement which led to many disputes.[166] For example, in the *Ampal* case, Egypt claimed to annul the agreement on the grounds of bribery. Egypt held that the dispute was "an act of sovereignty and a matter of Egyptian national security."[167] However, the tribunal rejected the claim due to lack of evidence for criminal charges against claimant.

Similarly, the case of Unión *Fenosa Gas, S.A. v. Arab Republic of Egypt.* Egypt claimed that the contract was based on corrupt act which is contrary to the international public policy and Egyptian law.[168] The tribunal confirmed that there will be a violation to the international public policy and Egyptian law if corruption was proven. It would be fatal in this arbitration regards admissibility, merits and jurisdiction. However, tribunal rejected the respondent's claim due to lack of evidence for criminal charges against claimant.[169] Accordingly, the international community should put more pressure on prompting good governance and there should be incentives for states with best practice.

3.4.2 Economic sovereign decisions of host states

Economic stability is extremely important for attracting foreign investments. Foreign investors can suffer from the economic sovereign decisions of the host states. Thus, the host state's sovereignty and its impact on foreign investments should be considered. For example, in the

[164] Andrew Reding, "U.S. Must Not Handicap Artistide" *NEWSDAY* (22 September 1994) <http://www.worldpolicy.org/sites/default/files/uploaded/image/Newsday-1994US%20Must%20Not%20Handicap%20Aristide.pdf>; Currently, this defence has not been invoked in arbitration. *Id.* at 330.
[165] *Unión Fenosa Gas, S.A. v. Arab Republic of Egypt,* ICSID Case No. ARB/14/4, Award of 31 Aug. 2018
[166] See *Ampal-American Israel Corporation and others v Arab Republic of Egypt* (n138)
[167] Ibid.
[168] *Unión Fenosa Gas, S.A. v. Arab Republic of Egypt* (n165)
[169] ibid.

Continental Casualty Company v the Argentine Republic case[170] the state took certain measures to enhance its economy. In 2001, Argentina suffered from a financial crisis. It had to go for an economic recovery, which required certain decisions such as restrictions on transfers that adversely affected Continental's interests. These decisions caused a devaluation of Argentina's currency. This economic sovereign decision negatively affected the interest of foreign companies.

The Continental company found that the interest rate was compromised in the BIT between Argentina and America. [171] Hence, in 2003, the Continental Casualty Company raised an arbitration request in the International Centre for Settlement of Investment Disputes (ICISID) against Argentina. The company claimed that Argentina violated its rights under the 1991 BIT. The value of the converted assets was less in the real US dollars, and the capital gain was overtaxed at the statutory rate. The tribunal held that Argentina had to pay compensation to the company, it was regarded as the treasury bills claim.[172] Over-enforcement theory can explain that *Continental* tribunal did extensive interpretation to the law. It did not consider the state's poor circumstances. Generally, it is important to note that sovereign defences can lead the necessity state defence to figure out the extent to which the state has valid purposes for breaching its international obligations.

3.4.3 Political sovereignty of host states

Political sovereignty means that governments make their own laws and social and economic plans. However, this can cause a conflict with their international obligations in the investment agreements. Indeed, a state is given the right to make its own political decisions. Therefore, poor political planning will bring instability to the host state's political and investment environment. It can be described as a political risk. [173] It can negatively impact on multinational

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[170] *Continental Casualty Company v the Argentine Republic*, ICSID Case No. ARB/03/9,Award of 5 Sep 2008

[171] Argentina-United States: Treaty Concerning the Reciprocal Encouragement and Protection of Investment, Washington (14 November 1991) 31 ILM 124 (1992), art. VIII

[172] *Continental Casualty v the Argentine Republic* (n 170)

[173] Philipp Harms, *International Investment, Political Risk and Growth* (Kluwer Academic Publishing 2000) 72; Multilateral Investment Guarantee Agency, *World Investment and Political Risk 2010* (World Bank 2011) 19

enterprises in the host state's territory as sovereign decisions can cause financial and political risks for both investors and the host state.

There are three types of political sovereignty risks. The first type of political sovereignty of the host state is the overthrow of the previous contracting regime. It is related to the research's main question, which is whether a revolutionary government can be exempted from its international obligations towards foreign investments. This type of political sovereignty is the act of a national military or opposition group replacing the government through a revolution for social, political or economic goals. This can negatively affect the international investment agreements where the host state's previous regime had signed contracts with foreign investors and they face a risk from these social, economic and political reforms. One of these risks can be the termination of an investment agreement, which can cause tremendous loss for the foreign investments.[174]

For instance, in the 1979 Iranian revolution, the Western stand with the Shah group was removed by the Islamic authorities after two years of protests and turmoil. Under the Shah government, Iran had worked for a long time with Western companies and their affiliates. In 1973, negotiations resulted in a twenty-year agreement with Western companies for the sale and purchase of crude oil. However, the 1979 Iranian revolution resulted in the withdrawal of all foreign associations for safety reasons and the oil production was distributed by the state. This resulted in damages and losses for the foreign investment projects. Especially in 1980, the international investment agreements were terminated by the new Iranian government once it came to power.

This raised international claims such as in *Mobil Oil Iran Inc. v Government of the Islamic Republic of Iran* case,[175] the tribunal was created to figure out the investors' claim for compensation as these investors refused to consider that Iran was acting of state sovereignty on force majeure event. On the other hand, new Iranian regime claimed that its decision was a practice of state sovereignty 'force majeure event' and it should be exempted from its

[174] ibid

[175] *Mobil Oil Iran Inc. and Others v Government of the Islamic Republic of Iran*, Iran-U.S. Claims Commission. Award No. 311-74/76/81/150-3, on 14 July 1987 16 Iran-U.S. CI

international liability. Consequently, the tribunal held rejected the state defence due absence of link between state act and revolution. The tribunal held that the Iranian state conducted an expropriation of the assets and properties of foreign investors and Iran had to pay fair compensations.[176]

Another related example is the *Elf Aquitaine Iran (France) v National Iranian Oil Company (NIOC)* case,[177] the NIOC argued that the contract for the production and exploration of oil by ELF was rendered void by the Islamic Republic Revolution. A special committee was appointed by the Ministry of Oil. It considered all the oil agreements contrary to the nationalisation of the Iranian oil industry to be null and void. [178]Also, the committee considered that all claims arising from these agreements should be settled through the commission.[179] Iran claimed that it was in public interest as its national law provisions did not permit initiating an agreement with foreign parties without parliamentary approval. [180]

As a result, the government could not comply with the arbitration clause on the grounds of state sovereignty. The claim was refused, and the argument did not prevent the arbitration clause execution. The arbitration obligation remains even when the national law restricts the legal capacity to agree on such a matter.[181] Accordingly, the national laws that prohibit the agreement terms in international contract that limit the state sovereignty, but such a prohibition is more likely to not be recognised as enforceable.[182] Also, Article 27 of the Vienna Convention (1969) does not allow states from "invok[ing] the provision of its internal law as justification for its failure to perform a treaty."[183] Hence, a new government is obliged under international law to respect the obligations of the previous regime. Otherwise it has to pay compensation for foreign investors.[184]

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[176] ibid
[177] *Elf Aquitaine Iran (France) v National Iranian Oil Company* (14 January 1982)Ad Hoc-Award
[178] Article 139 of the Constitutional Law noted that arbitration claims related to the state property must be based on informing the Council of Ministers and the Assembly of these issues.
[179] Iranian Revolutionary Council, *The Single Article Act*, (8 January 1980); *Amoco International Finance Corporation v the Government of the Islamic Republic of Iran* (1987) Award No. 310-56-3
[180] ibid
[181] *Elf Aquitaine Iran (France) v National Iranian Oil Company* Ad Hoc-Award 14 January 1982 Yearbook XI Yearbook Commercial Arbitration 1986
[182] Jan Paulsson,'May a State Invoke Its Internal Law to Repudiate Consent to International Arbitration' (1986) 2 Arb.Int'l 90
[183] Vienna Convention on the Law of Treaties Signed at Vienna, 23 May 1969
[184]Doak R.Bishop, James Crawford and William Reisman, Foreign Investment Disputes: Cases, Materials and Commentary (Kluwer Law International 2005) 918

The second type of political sovereignty of the host state is civil war. It means that people fight for their needs. For example, fighting to make a new government or to rebalance the power between regional and central authorities. This can result in the government conducting sovereign, economic, military and political acts for its continuity. As a result, foreign investments might be negatively affected from such an act. Although this should not result in any expropriation acts as the host state will then be required to pay fair compensation to honour investment agreements under international law.[185]

For example, the American company, *Nord Resources Corporation*, based in Tucson. It owned 50% of *Sierra Rutile Holding Limited,* the sole shareholder of *Sierra Rutile Limited (SRL).* Rutile is sand for the use of industrial purposes. *SRL* owned a project in Sierra Leone, and their profits represented 40% of the country's foreign exchange revenues. In 1991, civil war broke out in the state and in 1995 the rebels stopped the project. However, at the end *SRL* regained site control, but in the intervening period of civil war the project incurred heavy losses; hence, it was subject to compensation.[186]

A similar case happened in the 1870s and 1980s in Philippines, which faced political turmoil because of the civil war that resulted from personal, regional and religious tensions. Philippine Geothermal Inc. (PGI) is an energy company owned by the American-based Chevron. In 1971, the company entered a service contract with a state-owned company in the Philippines, the National Power Corporation (NPC). The role of the foreign company was to provide support such as expertise, money and technology to NPC for the exploitation and exploration of geothermal energy resources in the territory of the host state. In 1987, the transmission towers owned by the NPC were damaged by the rebellious group and the government was incapable to take any action because of the ongoing civil war. The NPC was not able to operate its power to generate facilities, which prohibited the PGI from receiving its payment under the contract.[187] Hence, in civil war cases, the state is responsible for not providing sufficient protection for foreign investments and subject to compensation.

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[185] ibid

[186] *OPIC Memorandum of Determination (*14 May 1998) Political Violence Claim of Nord Resources Corporation, Sierra Leon, Contract of Insurance No. A628 (cited and related in Bishop and others (n178)

[187] *OPIC Memorandum of Determination* 10 August 1984 Contract of Insurance No. 8577

The third political sovereignty of the host state is hostile action. These actions are not always considered as war. However, these acts can cause instability in the investment climate and create difficulty in securing foreign investments. For instance, in the case of *F.C. Schaffer & Associates*. The American engineering company's project was negatively affected by the hostile acts between Eritrea and Ethiopia.[188] In 1998, the Eritrea government stopped the passage of Ethiopian imports over its territory. The project was seized by Eritrea. In general, Ethiopia had the right to use its sovereignty to protect its territory against threats from bordering states. One of the outcomes was the ban[189] as it was essential for Ethiopia's interests to prevent the claimant from operating the project successfully.[190] Thus, sovereign acts are lawful if they are conducted in public interest and in good faith, not planned to damage the foreign investor's interest. This is consistent with Article 1 of UNCERDS 1974 states:

"Every State has the sovereign and inalienable right to choose its economic system as well as its political, social and cultural system in accordance with the will of its people, without outside interference, coercion or threat in any form whatsoever."

Accordingly, we can infer that there are many challenges regarding the relation between state sovereignty and foreign investment. Hence, it is crucial to understand the development of the whole concept of state sovereign immunity to examine the degree to which the international investment law allows unconstitutional transitional governments to use the state sovereign immunity defence towards foreign investment.

[188] This project was based in Ethiopia. All the supplies that were needed for the project had to be sent to the closest port located in Eritrea. Its performance was negatively affected by the armed forces of Eritrea and Ethiopia who were involved in hostile action.

[189] *OPIC Action Memorandum* 18 June 1999 Political Violence Claim of F.C. Schaffer & Associates

[190] ibid

3.5 Theories of the development of state sovereign immunity

The law of state immunity has changed as there have been important changes in both the doctrine and its practice over the last 100 years. Also, many of the important decisions made by international and national courts have developed the law further. The development of state immunity can be divided into two theories.

3.5.1 Theory of absolute state immunity

It is old theory in customary international law. Absolute immunity from another state's court jurisdiction is similar to the concept of the monarch as a sovereign over his or her people and territory in medieval Europe. Kings were immune from courts; since the Westphalia treaty, the jurisdictional immunity principle has been undebatable.[191] This theory depends on the concept that a state cannot be sued without its agreement. A state does not lose its immunity by participating in commercial activities. A state will be exempted from liability in other jurisdictions. The state property will be protected from seizure and the state vessels will be protected from arrest.[192]

For example, the case of *McFaddon v Schooner Exchange*[193] was about the federal court's jurisdiction over a French foreign friendly military ship visiting the port of America that had been arrested. The court interpreted the customary international law and found no jurisdiction. Chief Justice Marshall concluded that the government of France was allowed to state immunity; thus, it could retain the vessel. The reason behind this is the power of the US to assert judicial jurisdiction over its own property and territory could be nullified by the foreign sovereign jurisdiction immunity. [194]The importance of this case is that its decision can be

[191]Nagan and Root, 'The Emerging Restrictions on Sovereign Immunity'(n128)

[192] Christopher C Joyner, *International Law in the 21st Century: Rules for Global Governance* (Rowman & Littlefield Publishing Group 2005) 51

[193] *The Schooner Exch. v McFaddon*, 11 U.S. 116, 3 L. Ed. 287, 1812 U.S. LEXIS 377, 7 Cranch 116 (U.S. Mar. 2, 1812)

[194] Marshall concluded that sovereignty means that state has an absolute power within its own territory.

considered the "first definitive statement of the doctrine of foreign state immunity." In addition to the inability of the court to find jurisdiction led to the great respect by the court to the traditional state immunity.[195]

Also, in the 1849 *Spanish Government v Lambege et Pujol* decision,[196] the French Supreme Court explained that the state's independence is a universal principle of international law that should be respected. The French Supreme Court stated that:

> "The reciprocal independence of states is one of the most universally respected principles of international law, and it follows as a result therefrom that a government cannot be subjected to the jurisdiction of another against its will, and that the right of jurisdiction of one government over litigation arising from its own acts is a right inherent to its sovereignty that another government cannot seize without impairing their mutual relations."[197]

These cases reflect absolute state sovereignty and jurisdictional independence. Over-enforcement theory can explain that rules of state sovereignty were stipulated in restrictive way. The justification might be to protect state's interests above any other interests. According to the sovereignty doctrine, foreign investors are obliged to get the host government's consent in order to pursue redress. This made foreign investors depend on their domicile to protect their investments through diplomatic means but this was inefficient. As before the creation of BIT, foreign investors used to suffer from resolving their claims against host state governments. It is noted that the traditional international law principles used to protect national authorities from foreign investors.[198] However, currently, the theory of absolute immunity is not universally accepted.[199] In the globalisation environment, the principles of absolute immunity are under-enforced and the principles of restricted immunity have taken their place.

[195] ibid
[196] *Spanish Government v Lambege et Pujol* (1849) CC (France), D. 1
[197] ibid
[198] Olivia Chung, 'Lopsided International Investment Law Regime and Its Effect on the Future of Investor-State Arbitration' (2006-2007) 47 Virginia Journal of International Law 953
[199] ibid

3.5.2 Theory of restrictive state immunity

There was significant effort in the nineteenth century to move from absolute immunity to restrictive sovereign immunity. States became involved in international commerce through private enterprise partnership, quasi-governmental bodies or independently. This undermines the absolute sovereignty theory as the state has to give up a part of its power for the benefit of the new trade climate.[200] Sovereign immunity restriction in commercial disputes has become widely accepted. For example, the 1873 case of *Charkieh*[201], a vessel was used for merchant trading owned by the Khedive of Egypt. The master, owner and crew of Batavier filed a claim against the vessel for causing damage. Egypt's Khedive and his Minister of Marine claimed that Charkieh was the Khedive's property, which meant that it was ruled by the sovereign state of Egypt. A governmental vessel of a semi-sovereign state is not liable to be arrested. However, Charkieh bore the flag of the Ottoman navy. It came with cargo to England and paid the customs like normal merchant vessels. This vessel was engaged in a collision on the River Thames in England. The court concluded that the Khedive was not entitled to the sovereign prince privilege.[202]

In the High Court of Admiralty, the judge Sir Robert Phillimore illustrated the necessity of restricted sovereign immunity. Phillimore explained that under the sovereignty principle there might be many activities that should not be covered by sovereign immunity. This is because of the growth of commercial activities among states as in the *Chatkieh* case, there has been an exception for state immunity in commercial matters. The existence of commercial exception to state immunity is a creation of globalisation. [203]

Another example is the case of *Philippine Admiral v William Shipping (Hong Kong)*.[204] The Philippine Admiral was a ship owned by the Philippine government due to the Japanese reparation settlement after the Second World War. The operation of the vessel was under the liberation steamship company charter, and it aimed to carry freight till the 1972. Consequently, it was docked in Hong Kong for repair, where a dispute appeared including the cost payment

[200] Joyner, '*International Law in the 21st Century: Rules for Global Governance'* (n192)
[201] The Charkieh (6200) [1873] L.R. 4 A. & E.59 at p.75 (Sir Robert Phillimore). 23. Id. at. 84. 24. Id. at 86. 25
[202] ibid
[203] Nagan and Root, 'The Emerging Restrictions on Sovereign Immunity' (n 128)
[204] *Philippine Admiral v William Shipping (Hong Kong) Ltd and another* (1976) 2 WLR 214

between the brokerage firm, shipping agents and LBS. The writs in rem were issued against the ship for its recovery expenses, and it was arrested. The Philippine government failed to take any measures to return the vessel till the supreme court of Hong Kong ordered its sale and proceed of sale to be paid to the court. Hence, the state of Philippines raised the claim of sovereign immunity to stop this legal action. The United Kingdom (UK) courts applied the restrictive immunity theory. The court's decision was that this was a purely commercial issue; thus, the state of Philippines was not allowed to use its sovereign authority under the international law.[205]

Another example demonstrated that restrictive theory is widely accepted is the *Condor and Filvem v Minister of Justice* case, the constitutional court noted that the restrictive immunity theory had been accepted for the last thirty years. The court held that immunity will not be applied in commercial activities.[206]Also, the restriction of state immunity is seen in the case of *Trendtex Trading Corporation v Central Bank of Nigeria.*[207] The defendant bank, a separate legal body from the Nigerian government, had issued a letter of credit in favour of the Swiss company Trendtex with the approval of the previous government. Nonetheless, the new government cancelled this approval and ordered the bank to not pay for the cement. As a result, Trendtex sued the bank, demanding payment. The bank applied to set aside the writ on the legal ground that the bank is part of the state and thus immune from suit under the sovereign immunity doctrine. Its rejection to pay was a sovereign government act that was not subject to the English courts. Consequently, the Court of Appeal had to determine the applicability of the sovereign immunity doctrine to the Central Bank of Nigeria.

However, the English Court of Appeal did not permit the bank's argument on sovereign immunity to succeed. It was said that the bank was not allowed to sovereign immunity. This is because the state established it under statute as a separate legal entity. Thus, the bank could not be immune from suit.[208] The *Trendtex* case was a confirmation that international law had changed. It dealt with the relationship between international law and the United Kingdom's domestic law. For the first time, the English Court had applied restrictions on the law of

[205] ibid

[207] *Trendtex Trading Corporation v Central Bank of Nigeria,* [1977] 64 ILR 111

[208] ibid

sovereign immunity. This provides that doctrine of restrictive immunity is used only when the state is involved in commercial matters. However, the definition of commercial transaction is unclear. For example, the classical exposition of this principle was stated by Lord Denning in the *Trendtex* case[209] when he stated that:

> "If a government goes into the market places of the world and buys boots or cements- as a commercial transaction- that government department should be subject to all the rules of the market place. The seller is not concerned with the purpose to which the purchaser intends to put the goods."

Also, it is significant to note that under principles of restricted immunity, state immunity is not allowed if the state acts contrary to the foreign investor's interest or the agreement terms. Nevertheless, if a host state's actions are related to public interest, then the state will be allowed to use its immunity power. Thus, distinguishing between commercial acts and sovereign acts is important for the tribunals to decide whether a state will be liable or not. Although *Trendtex* case is one of the essential court decisions on sovereign immunity. It makes restrictive approach to be applied widely. However, it does not clearly determine what constitutes a commercial transaction. Also, because of different jurisdiction, national laws define commercial transactions differently. There is a lack of consensus on whether the court should look at the nature of the transaction or the purpose of the transaction.[210] Accordingly, broad laws blur the line between illegal and legal. Adjudicators might over or under-enforce the law because they are trying to square the law with the facts of the case to render their own notion of justice.

This makes scholars such as Schmitthoff attempted to clarify what constitutes a commercial transaction. Schmitthoff presented the denial of state immunity by citing Sir Hersch Lauterpacht, limiting the state immunity is based on uniform and it became unworkable. Thus, it should depend on the nature of the state act and not the purpose of the state act.[211] This is reflected in some of domestic laws on immunity; the judicial attitude in the United States, for instance, appears to follow this nature of transaction test as well.[212] In addition to the recent

[209] *Trendtex Trading Corporation v Central Bank of Nigeria* (n207)
[210] ibid
[211] Clive M Schmitthoff, 'The Claim of Sovereign Immunity in the Law of International Trade' (July 1958) 7(3) The International and Comparative Law Quarterly 452
[212] ibid

United Nations convention of 2004 on jurisdictional Immunities of States and their property (UNCSI) attempts to clarify what constitutes a commercial transaction [213] This UN convention was adopted by resolution 53/38 of 16 December 2004 by the UNGA. UNCSI attempts to unify the distinguish test. It displays a preference for the nature test but still it considers the purpose test as stated in Article 2(2) as follows:

> "In determining whether a contract or transaction is a 'commercial transaction' under paragraph 1 (c), reference should be made primarily to the nature of the contract or transaction, but its purpose should also be taken into account if the parties to the contract or transaction have so agreed, or if, in the practice of the State of the forum, that purpose is relevant to determining the non-commercial character of the contract or transaction."[214]

Accordingly, it appears that UNCSI did not provide clarity on whether the adjudicators should look at the nature of the transaction or the purpose of the transaction in defining commercial transaction. This can invite selective interpretation. Adjudicators might over or under-enforce the law because they are trying to square the law with the facts of the case to render their notion of justice. This is seen in the Argentina's bond case.[215] Argentina's sovereign debt restructuring measures to cope with its financial crisis negatively affected its Italian investor's benefits. This made these investors to take proceedings in a different jurisdiction under their state of origin. Italian investors found that the Italian court did not accept the jurisdiction as it had accepted Argentina's request of sovereign immunity under the principles of international law approved by the Court of Cassation, citing the "public purpose [...] of protecting the primary need of economic survival of the population in a historical context of very serious national emergency"[216]

[213] United Nations Convention on Jurisdictional Immunities of States and their Property of 2004, (16 December 2004). UN Doc Supp. No.22 (A/59/22),

[214] UNGA, Res/59/38 (2 December 2004) adopted by the United Nations General Assembly, 59th Session, [hereinafter U.N. Convention], Part 1, Art. 2(2). FSIA 1603(d) which states that "The commercial character of an activity shall be determined by reference to the nature of the course of conduct or particular transaction or act, rather than by reference to its purpose."

[215] The claim is based on the 1991 Argentina–Italy treaty on economic cooperation

[216] Decision No. 11225, reproduced in Rivista di diritto internazionale privato e processuale (2005), at 1094.

In contrary to another similar case that was raised in another jurisdiction. In the *Republic of Argentina v Weltover, Inc* case,[217] it was dispute raised from the crisis faced by South American countries and adjudicated by the US Supreme Court. The claim was about the issuance of bonds by the government of Argentina to secure foreign capital investment and stabilise its national economy. The American company Weltover Inc.'s interests suffered because of this plan. It insisted on claiming full repayment following the default in the federal district court of New York. At the same time, Argentina claimed sovereign state immunity, thereby a lack of jurisdiction, on the subject issue. The court applied the restrictive theory of sovereign immunity allowing the state to be sued in commercial matters. The court considered that raising money is a commercial activity despite its purpose was to help the plans of the government. Hence, the court did not accept the Argentine claim for sovereign immunity, and accepted the dispute jurisdiction.[218]

As a result, distinguishing test between commercial acts and sovereign acts is important for to decide whether a state will be liable or not. However, the state practice reveals that distinguishing test can reach a different outcome; hence, a clear criterion is needed to determine whether it is a sovereign act or not. Although UNCSI still need to provide clarity on what constitutes a commercial transaction. The UNCSI seems to be the most effective attempt to codify the state immunity law and harmonise state practice to the international level.[219] It aims to formalise a reliable approach to jurisdictional immunity. It provides a common source of law and unifies many of the competing areas in the international law to achieve uniformity. However, the convention illustrated that the customary international law rule will continue to manage issues that are not regulated by the current convention.[220]

The UNCSI cannot be considered a treaty law because it was not enforced due to lack of state ratification. Like this, the state immunity will continue to acquire its legal power from the customary international law until this convention comes into force. Also, the ICJ confirmed that the immunity of the state had been adopted as "a general rule of customary

[217] *Republic of Argentina v Weltover Inc.* United States Supreme Court, 504 U.S. 607 (1992) para 607–608.
[218] ibid
[219] Hazel Fox, *The Law of State Immunity* (Oxford university press 2002).
[220]UN Convention on Jurisdictional Immunities of States and their Properties of 2004 (n 213)

international."[221] Accordingly, it appears the law of state immunity invites selective enforcement due to nature of customary international law is open for many interpretations

Nevertheless, nowadays most of codifications of the law of state immunity are based on the theory of state restrictive immunity. Starting from the 1970s, many jurisdictions applied the doctrine of restrictive immunity by the national court's decision. This created the national legislations of the UK State Immunity Act (SIA) and the US Foreign Sovereign Immunities Act 1976 (FSIA). Moreover, many other efforts to codify the sovereign immunity law, which is found in non-governmental drafts such as the Institut de Droit International in 1954, Harvard Research Project the Draft convention III in 1932[222], Montreal Convention of the International Law Association in 1982[223] and American Law Institute's Restatement of Foreign Relations Law in 1965.[224] Also, the international community tried to codify sovereign immunity by international conventions.[225] This includes the Brussels convention of 1926 related to the immunity of State Owned Vessels and the European convention on State Immunity. [226]

It is also vital to note that in order to apply the restrictive theory, state immunity must be waived. It is important to note that whenever there is lack of implicit or explicit waiver, state immunity is an influential tool available to the state to stop litigation before it begins. Thus, the investor has to negotiate the state immunity waiver with the host state party before the project implementation.[227] This sheds light on the significance of understanding the concept of the waiver of state immunity and its effect on disputes.

[221] Fox, *The Law of State Immunity* (n 219)
[222] Harvard Research's Draft on the Competence of Courts in regard to Foreign States of 1932
[223] Draft Montreal Convention of the International Law Association of 1982
[224] American Law Institute's Restatement of Foreign Relations Law of 1965
[225] David Gaukrodger, 'Foreign State Immunity and Foreign Government Controlled Investors' (2010) OECD Working Papers on International Investment 2/2010, OECD Publishing 10
[226] Only eight states are party to the Convention <http://conventions.coe.int/Treaty/Commun/ChercheSig.asp?NT=074&CM=8&DF=&CL=ENG> accessed 1 December 2014
[227] Schmitthoff, 'The Claim of Sovereign Immunity in the Law of International Trade'(n211)

3.6 Waiver of state immunity

The idea of waiving the state immunity is based on government's entrance into the market. As a result, the government is subject to the market place rules. The unequal relationship between private individuals and the judicial sovereign is hence converted into a relationship in which both the parties have the same legal duties and rights. In turn, an arbitration that arises from such a relationship is considered private because its authority comes from the disputing parties' consent. Usually, the individual's claims against the state come from the state's power to pass legislation, issue judicial decisions or adopt compulsory regulations.[228] This immunity waiver is accepted in customary international law and can be made before or after the dispute.[229] However, there are two types of state immunity waivers under international law. The first type is waiving the state immunity from adjudication. The second type is waiving the state immunity from enforcement.

3.6.1 State waiver of immunity from adjudication

Once a state waives its immunity, a foreign investor is allowed to sue the state under international law. A state may waive its immunity from international adjudication/ jurisdiction over disputes either in the BIT provision or the investment contract by stipulating an arbitration clause with another party. Immunity waiver can be either explicit or implicit. The host state has the choice of settling disputes through arbitration, which is explicit wavier, or state involvement in the commercial transaction with a foreign investor, which is implicit wavier. This includes state enterprises as a part of the state by law.[230] A state's entry into an arbitration agreement means that this state will be treated exactly as a private party and will be required to fulfil the agreement obligations or be subject to adjudication.[231] Compromising the interests

[228] Van Harten, 'The Public-Private Distinction in The International Arbitration of Individual Claims Against The State' (n 107)
[229] The ILC addressed the consequences of entering an arbitration agreement as shown in Article 17.
[230] ibid
[231] Fox, *The Law of State Immunity* (n 219)

of a foreign investor for the sovereignty interest was part of customary expectations. However, the establishment of the investment treaty balanced the relationship between host state and foreign investors.[232] It is expected for the interstate BIT to include a clause that permits foreign investors to make a claim to the international tribunal and overcome the sovereign immunity matter.[233]

Investment treaties provide arbitrators a jurisdiction to resolve a wide class of disputes that arise from the state sovereign acts.[234] This is because the protection of foreign investments requires the host state to provide recompense for its regulatory actions that adversely affect the project.[235] Hence, when a state conducted written agreement with a foreign investor to submit to arbitration in the event of a dispute relating to commercial transaction, the state will not be able to use the immunity defence.[236]

A scholar such as Fox asserts that "the plea of sovereign immunity in the sense of a procedural bar to jurisdiction based on the personal capacity of the litigant, has little immediate relevance in arbitration proceedings."[237] This is because the arbitration proceedings are established on the agreement of both parties in the arbitration agreement. The fact that the state enters into an arbitration agreement means that it has accepted the arbitral tribunal's jurisdiction and waived its immunity from jurisdiction. Also, Crawford demonstrated, "subject to the doctrine of non-justifiability, no fundamental principle prohibits the exercise of jurisdiction, and immunity may be waived by the state concerned either expressly or by conduct."[238]

Generally, international law develops a restriction framework for state immunity in arbitration. There is an international law principle that is reflected in Article 12 of the 1972 European

[232] Dolzer Rudolf, 'The Impact of International Investment Treaties on Domestic Administrative Law' (n26) ILP 953
[233] ibid
[234] Van Harten, "The Public-Private Distinction in The International Arbitration of Individual Claims Against The State" (n 107)
[235] Charles Brower and Stephen Schill, 'Is Arbitration a Threat or a Boom to the Legitimacy of International Investment Law Symposium: International Judges' (2008-09) 9(2) Chicago Journal of International Law 471, 483
[236] Katherine Reece Thomas, 'Enforcing Against State Assets: The Case for Restricting Private Creditor Enforcement and How Judges in England Have Used 'Context' When Applying the 'Commercial Purposes' Test' (2015) 2(1) Journal International and Comparative Law
[237] Hazel Fox, 'Sovereign Immunity and Arbitration' in J.D. Lew (ed), *Contemporary Problems in International Arbitration* (Centre of Commercial Studies, Queen Mary College, London 1986) 323.
[238] James Crawford, *Brownlie's Principles of Public International Law* (8th edn Oxford University Press 2012) 501

Convention on State Immunity (ECSI). It mentions that in the case of a contracting state's written acceptance of the arbitration clause in the event of a commercial or civil dispute, this state will not be allowed to use the immunity claim from the court jurisdiction.[239] Likewise, in Article 17 of the UNCSI 2004, notes that if the state accepts arbitration in any commercial disputes, it will not be permitted to use the immunity claim.[240]

An example that demonstrates the international customary law application regarding the waiver of state immunity is the *Anglo-Iranian Oil* case (1952) where the ICJ noted that the state's rejection of the arbitration is "a grave violation of international law".[241] Thus, a state's acceptance of the clause of arbitration is a waiver to the state immunity claim in international law. Moreover, there are national legislative provisions that clarify how the acceptance of arbitration can be applied. [242] For example, the FSIA, as interpreted in the tribunal of *Libyan American Oil Company (LIAMCO) v Socialist People's Libyan Arab Jamahiriya* case,[243] illustrated that the state's acceptance of arbitration is considered an immunity waiver from the US court's jurisdiction. Section 1605(a) (6) of the FSIA states that:

> "Enforcement of an award will be activated in three circumstances: where the arbitration occurs in the US; where there is an applicable treaty or international agreement concerning recognition and enforcement of the award; or if the underlying claim could have been brought in the US but for the presence of the arbitration agreement."

Libya's claim of sovereign immunity from the national court of the foreign investor was refused because this defence was waived by its clear agreement to the arbitration provisions and choice of law clause in the contract.[244] There is a similar example to the FSIA in different jurisdictions. Section 9 of the UK SIA (1978) notes that the state's acceptance of arbitration in the event of commercial disputes means that the state cannot use the immunity claim from courts in the UK.[245]

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[239] European Convention on State Immunity (ECSI) 1972, art 2
[240] UN Convention on Jurisdictional Immunities of States and their Property of 2004 (n 188)
[241] *Anglo-Iranian Oil Co. Case (United Kingdom v Iran)* Preliminary Objection Judgment of July 22nd, 1952
[242] The Foreign Sovereign Immunities Act (FSIA) of 1976 is a US law, codified it develops the limitation on what extent a foreign sovereign nation can be sued in the courts of the US. In international law, the government immunity is known as state immunity while in the national law it is known as sovereign immunity.
[243] *LIAMCO v Government of the Libyan Arab Republic* (n 156)
[244] ibid
[245] s 9UK State Immunity Act 1978

Another example in the arbitration context is *Soleh Boneh Intl Ltd (Israel) and Water Resource Development Intl (Israel) v The Republic of Uganda and National Housing and Construction Corp of Uganda* case.[246] The dispute occurred due to the contract execution with the foreign investors in Uganda, which was guaranteed by the government of the host state. The proceedings for arbitration took place in Sweden where Uganda claimed sovereign immunity. Nevertheless, Uganda found that it had waived its immunity by accepting the arbitration clause in the previous agreement. [247] This case provides that state's acceptance of the arbitration clause is considered a state immunity waiver. Consequently, it will not be allowed to use the immunity defence and will be subject to international adjunction. However, arbitration clause can be interpreted differently which can result to inconsistent decisions.

3.6.1.1 Inconsistent decisions on immunity wavier

State practice demonstrated the inconsistent views regarding the application of the state immunity waiver from the jurisdiction. A case that demonstrates this point is the *Southern Pacific Properties (Middle East) Limited (SPP) v Arab Republic of Egypt* case.[248] It was an agreement between the Hong Kong and the Egyptian General Organization for Tourism and Hotels (EGOTH), a private company that had formerly been in public ownership. The competed Minister of Tourism had attached his approval signature to the first agreement but not in the part of the document that stated that the state was a part of the contract. This document did not include the arbitration clause in the event of a dispute. However, this omission was corrected in the supplemental agreement signed by the EGOTH on a separate page of the second document. The project cancellation caused a huge loss to the *SPP*, which required compensation by arbitration against the host state and EGOTH.[249]

It was debated that by approving and signing the agreement, the representative minister was not part of the subject or contract to any obligations. It was decided that the arbitration clause that was added in the supplementary document was not a waiver of state sovereign immunity

[246] *Soleh Boneh International Ltd v Government of the Republic of Uganda and National Housing Corporation* (1976) ICC Award No. 2321 (4 July 1974) I Yearbook of Commercial Arbitration
[247] ibid
[248] *Southern Pacific Properties (Middle East) Limited v Arab Republic of Egypt*, ICSID ARB/84/3 Award on Merits 20 May 1992, ICC 3493 (1983)
[249] ibid

from suit. The first ICC arbitral tribunal in 1983 disagreed, noting that the supplemental agreement was evidence that Egypt had agreed to arbitration for resolving disputes. Thus, jurisdiction was developed and immunity was not a matter. After a year, Egypt raised an appeal in the Paris Court of Appeal, which decided that the comments and signature added in the supplemental agreement that included the arbitration clause were only an expression of the state's supervisory power over its territory. It found that the minister did not have the intention to make the state join the agreement or handle any obligations. Therefore, the award was annulled. The French Court of Cassation (*Cour de Cassation)*, upon hearing an appeal from *SPP* in January 1987, held that lack of evidence existed to show the state participation intention.[250]

Hence, it is important to distinguish between these roles using the individual case facts to determine if the state immunity has been waived or not. Nevertheless, state supervision does not lead to loss of sovereignty. This case demonstrated the inconsistent views of the ICC Arbitral Tribunal and the Paris Court of Appeal regarding the matter of state immunity waiver. Generally, over-enforcement theory provides that over-enforcement to the law can occur when adjudicators are interpreting the law in expansive manner. This is reflected in the decision of ICC tribunal where tribunal applied extensive interpretation to the law. On the other hand, Paris court of Appeal applied less restrictive interpretation. It appears that over or under-enforcement generally reflects adjudicator's opinion in defining rules that may be over-enforced or under-enforced. Both over- and under-enforcement theories can explain that inconsistent decision between ICC tribunal and French Court of Cassation resulted because of analytical reasons. Adjudicators are trying to square the law with the facts of the case to render their own notion of justice

Another similar example that demonstrated the inconsistency decisions on use of the state immunity waiver from international jurisdiction is the *Creighton v Qatar* case.[251] Where the French Supreme Court has accepted the theory of implicit waiver of immunity from jurisdiction by virtue of adherence to an ICC arbitration clause.[252] In contrast, the final Court of Appeal of

[250] ibid
[251] Creighton Limited v Minister of Finance of Qatar and Minister of Municipal Affairs and Agriculture of Qatar, Appeal judgment, Case No 98-19068, (2000) 207 Bulletin civil I, 135, ILDC 772 (FR 2000)
[252] ibid

Hong Kong in *DRC v FG Hemisphere* (2011)[253] held that the agreement to arbitrate under the rules of the ICC is not enough *per se* to apply a waiver of immunity from jurisdiction. It appears that Adjudicators might over or under-enforce the law because they are trying to square the law with the facts of the case to render their own notion of justice.

Also, the case of *Tekno-Pharma AB v Iran*[254] highly demonstrates the confusion regarding the waiver of state immunity. In this example there was an arbitration clause in the agreement. Iran illustrated that the place of arbitration was Sweden and the governing law Swedish, but it argued that it did not mean the waiver of state immunity. The Swedish Court of Appeal's decision, which was confirmed by the Supreme Court later, held that the arbitration agreement is not enough for the court to consider that there is a waiver of state immunity. However, this judgment is not consistent with the general trend of restrictive immunity; implicit immunity waiver is valid by the arbitration agreement.[255] It appears that the Swedish court in *Tecno-Pharma* case under-enforced the general trend of restrictive immunity. The court tried to square the law with the facts of the case to render their own notion of justice on the other hand, the same court (Swedish Court of Appeal) in the case of *Libyan American Oil Company v Libya* concluded that Libya's insertion an arbitration clause into the concession agreement can be considered as a waiver of its immunity.[256]

Accordingly, state practice demonstrates that there is inconsistency regarding the concept of waiver of state immunity. It appears that there are various interpretations on immunity wavier and arbitration clauses. This might be because of analytical reasons where in some instances the law is either over or under-enforced. Adjudicators are trying to square the law with the facts of the case to render their own notion of justice. This results to inconsistent decisions

Consequently, states practice provides that state cannot claim immunity once it is involved in a commercial activity, but the tribunals have to figure out if the state's act is sovereign or commercial. A legitimate sovereign state act must be grounded on public interest while

[253] *Democratic Republic of the Congo and Others v FG Hemisphere Associates LLC* (Final appeal nos 5, 6 and 7 OF 2010 (Civil) (8 June 2011)
[254] *Tekno-Pharma AB of Stockholm v State of Iran*, Judgment of 21 December 1972 of Supreme Court (*Högsta domstolen*) <http://www.coe.int/t/dlapil/cahdi/Source/state_immunities/Cahdi%20_2005_%206%20bil%20PartII%20SWEDEN.pdf>
[255] Dhisadee Chamlongrasdr, *Foreign State Immunity and Arbitration* (Cameron 2007)
[256] *Libyan American Oil Company v State of Libya*, Judgment of 18 June 1980 of Court of Appeal (*Svea hovrätt*)

commercial acts must be based on an agreement between the investors and state administrative public authority. On one hand, state public authority is entitled to full compensation if its commercial acts have negatively affected the contractor which was unexpected when the contract was created. On the other hand, the state has the inherent right to terminate a contract with investors for public interest, which can negatively affect a foreign investor's interests without compensation.[257]

Nevertheless, it is significant to note that although there are inconsistent decisions on immunity wavier but still the general consensus is states will not be immune from international adjunction once they were involved in commercial matters. However, the state will always invoke the sovereign argument. When a state's claims for jurisdictional immunity fail, there is still the possibility of a plea of immunity from any following award enforcement. This raises the question of whether such state waiver of immunity from adjunction extends to enforcement.

3.6.2 Waiver of immunity from enforcement

Enforcement is the judgment against state's property for the international law violation. There are two ways to enforce arbitral award – either through the International Centre for Settlement of Investment Disputes (ICSID) Convention or the New York Convention.

3.6.2.1 International Centre for Settlement of Investment Disputes (ICSID) Convention

ICISD is created by the World Bank, this convention is limited to the treaty claims between states and foreign nationals.[258] It was enforced in 1966. [259] The main objective of the ICSID Convention is to "promote private foreign investment by improving the investment climate for investors and host states."[260] Thus, the ICSID mechanism provides foreign investment

[257] The Supreme Administrative Court (Egyptian Council d'Etat) – Judgment No. 1562-10 and 67-11 (11/5/1968 – 13/117/874); Egyptian Council d'Etat (1996) 424 (as cited in Al-Adba N, Tarawneh)
[258] See Sornarajah, *The Settlement of Foreign Investment Disputes* (n141)
[259] ICSID, List of states and other signatories of the Convention (as of 11 April 2014), ICSID Doc.No. ICSID/3. ICSID Convention, Regulations and Rules
[260] Aron Broches, 'Awards Rendered Pursuant to the ICSID Convention: Binding Force, Finality, Recognition, Enforcement, Execution' (1987) 2 ICSID Review 287, 329

protection from hostile state acts. Walde contended that "investment arbitration is one of the most powerful instruments available to foreign investors to counteract political risk at least to the extent such risk is within the control of the host state."[261] It intended to balance between the interests of the host states and investors.[262] Also, ICSID allows investors to claim against states without dependence on the home states of the investors, which takes away diplomatic protection.[263]

ICSID prevents reviewing the arbitral award; it is an automatic enforcement. It is isolated from the national law. Other instruments governing arbitration, on the other hand, leave the enforcement stage to be interpreted by the national laws or applicable treaties.[264] The recognition, enforcement and execution of the arbitral awards are reflected in Articles from 53–55. Article 53 (1) requires "the parties" to an arbitration, the investor and the state, to accept by and comply with the arbitral award. Article 54(1) states that (1) "The award shall be binding on the parties and shall not be subject to any appeal or to any other remedy except those provided for in this Convention." Article 55 states that although member states must recognise and enforce the award, each state's laws interrelated to sovereign immunity from execution continue to apply.[265] Also, scholars such as Broches clarified:

> "as Article 53 affirmed the absolute binding force of the award on the international law level, Article 54 affirms its external finality, i.e., vis-à-vis domestic court. The award is *res judicata* in each and every contracting state."[266]

Seemingly, the effectiveness of the execution measures depends on the national law on sovereign immunity in the state where execution is required. This is because the ICSID Convention does not supersede or alter the rules on immunity from execution applicable in the contracting states under their domestic law. As a result, arbitral awards are treated differently in the contracting states.[267] The reason for this issue is explained in the Report of the Executive Directors to the ICSID Convention:

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[261] Thomas Walde, 'Investment Arbitration under the Energy Charter Treaty – From Dispute Settlement to Treaty Interpretation' (1996)12 Arb Intl 429, 432.
[262] See "Report of the Executive Directors on the Convention on the Settlement of Investment Disputes between States and Nationals of Other States" (18 March 1965) in *ICSID Convention, Regulations and Rules* (ICSID 2006) 35, 40
[263] Sornarajah, *The International Law on Foreign Investment* (n1)
[264] Aron Broches, Selected Essays: World Bank, ICSID, and Other Subjects of Public and Private International Law' (1995) 19 Fordham Int'l L.J. 818
[265] ICSID Convention, art 53 and 54
[266] A Broches, 'Awards Rendered Pursuant to the ICSID Convention: Binding Force, Finality, Recognition, Enforcement, Execution' (n260)
[267] ibid

> "...Because of the different legal techniques followed in common law and civil law Jurisdictions and the different judicial systems found in unitary and federal or other non-unitary States, Article 54 does not prescribe any particular method to be followed in its domestic implementation but requires each contracting state to meet the requirements of the Article in accordance with its own legal system."[268]

However, this explanation ensures that the enforcing state is not only allowed to review the arbitral award but also to serve as a procedural bar. Schreuer argued on this point that "the impossibility to enforce an ICSID award as a consequence of the law concerning the execution of judgments in one or several states in no way affects the obligation of the party to the ICSID arbitration to abide by and comply with the award in accordance with Art.53(1)."[269] Therefore, the failure of the state party to enforce the award would be considered as a violation of a treaty obligation, which can raise state responsibility issues including diplomatic protection.[270] The ICSID award has advantages over other types of arbitral awards. For example, public policy matters do not cause a problem as in other arbitral awards. This is because Article 52 under ICSID provides lawful grounds for an annulment, which might fall under international public policy such as serious departure from fundamental procedural rule and corruption charges on a tribunal member but again those grounds cannot be challenged under the domestic courts.[271]

This is reflected in case of *SOBAI v Republic of Senegal*,[272] which was a dispute regarding low-income housing project construction in Dakar. The tribunal conducted an award in favour of SOABI in February 1998. This made Senegal appeal to the *Cour d'appel.* Senegal raised a public policy matter and the decision of the *Cour d'appel* which held that the award execution was contrary to public policy because it was a breach of the principle of immunity. The under-enforcement theory can explain that *Cour d'appel* underenforce Article 53 and 54 of ICISD convention. However, the decision of the *Cour d'appel* was annulled by the *Cour de cassation*, which concluded that under the ICSID Convention a foreign state must accept the award. Article 53 and 54 established autonomous regimes for recognition and execution. It appears

[268] ibid
[269] Christoph Schreuer, *The ICSID Convention: A Commentary* (Cambridge University Press 2009).
[270] ibid
[271] ICSID Convention, art 52; *Interim Report on Public Policy as a Bar to Enforcement of International Arbitral Awards,* Committee on International Commercial Arbitration, International Law Association, London Conference (2000) 9
[272]"Recognition and Enforcement of ICSID Awards: The Decision of the French Courde Cassation Soabi v. Senegal" 2 (3) ARIA 1991; *Société Ouest Africaine des Bétons Industriels* (*SOABI*) *v Senegal,* ICSID Case No ARB/82/1, Award of 25 Feb 1988

that the French courts under-enforced the law due to analytical reasons, they were not aware of the lack of authority in the review of ICSID awards.[273]

This confusion was also seen in the case of *LETCO v Liberia*.[274] The district court of US that had recognised and executed the arbitral award referred to the obligations under Article 54.[275] The court was in conflict with Article 54, the automatic recognition of the arbitral award, which states that the sovereignty that has been waived by consent goes to the ICSID arbitration. Conversely, Article 55 of the ICSID Convention permits the domestic court to decide the domestic law on sovereign immunity only in the execution stage and not in the recognition stage. Although, such confusion should not occur because the ICSID Convention is clear enough that its award is final and does not require judicial review. However, it is vital to note that arbitral awards are either enforced under ICSID convention or New York convention.

3.6.2.2 New York Convention

It was adopted by the UN and enforced on 7 June 1959.[276] Its objective to enable the recognition and enforcement of arbitral awards between parties. It is also known for contractual claims.[277] However, the problem is that the New York Convention is not clear on the issue of state sovereignty. This is because its award cannot be considered a final award.[278] It is obligatory for all contracting states to enable the recognition and enforcement of arbitral awards between parties. In accordance with the procedural rules provided in Article III. This provides:

> "Each Contracting State shall recognize arbitral awards as binding and enforce them in accordance with the rules of procedure of the territory where the award is relied upon, under the conditions laid down in the following articles. There shall not be imposed substantially more onerous conditions or higher fees or charges on the

[273] ibid
[274] *LETCO v Liberia*, United States District Court, Southern District of New York, Judgment, 12 December1986, 2 ICSID Reports 367/8
[275] ibid
[276] See The New York Arbitration Convention of 1958, http://www.newyorkconvention.org/
[277] Albert Jan van den Berg, *The New York Arbitration Convention of 1958: Towards Uniform Judicial Interpretation*, (Kluwer Law International 1981)
[278] New York Convention, art I(1) states:
"This Convention shall apply to the recognition and enforcement of arbitral awards made in the territory of a State other than the State where the recognition and enforcement of such awards are sought, and arising out of differences between persons, whether physical or legal. It shall also apply to arbitral awards not considered as domestic awards in the State where their recognition and enforcement are sought."

recognition or enforcement of arbitral awards to which this Convention applies than are imposed on the recognition or enforcement of domestic arbitral awards."[279]

Thus, the New York Convention permits the domestic court to decide the domestic law on sovereign immunity in both recognition and execution stages. It is different from the ICSID Convention, which permits the domestic court to decide the domestic law on sovereign immunity in the execution stage only.

This provides that the New York Convention award is not automatically recognised in the domestic courts. It also provides a list of grounds on which the recognition and enforcement might be rejected. The grounds can be categorised into two groups.[280] It can be rejected on the ground that the competent authority in the enforcing state finds that (a) "The subject matter of the difference is not capable of settlement by arbitration under the law of that country; or (b) The recognition or enforcement of the award would be contrary to the public policy of that country."[281] For example, the US case of *Parsons & Whittemore Overseas Co. v Societe Generale de I'Industrie du Papier,* the court concluded that public policy is a ground for rejecting to enforce arbitral awards "only where enforcement would violate the forum state's

[279] New York Convention, art III
Enforcing Arbitral Awards Against Sovereign States
[280] Grounds for refusing enforcement under Article V:
"1. Recognition and enforcement of the award may be refused, at the request of the party against whom it is invoked, only if that party furnishes to the competent authority where the recognition and enforcement is sought, proof that:
(a) The parties to the agreement referred to in article II were, under the law applicable to them, under some incapacity, or the said agreement is not valid under the law to which the parties have subjected it or, failing any indication thereon, under the law of the country where the award was made; or
(b) The party against whom the award is invoked was not given proper notice of the appointment of the arbitrator or of the arbitration proceedings or was otherwise unable to present his case; or
(c) The award deals with a difference not contemplated by or not falling within the terms of the submission to arbitration, or it contains decisions on matters beyond the scope of the submission to arbitration, provided that, if the decisions on matters submitted to arbitration can be separated from those not so submitted, that part of the award which contains decisions on matters submitted to arbitration may be recognised and enforced; or
(d) The composition of the arbitral authority or the arbitral procedure was not in accordance with the agreement of the parties, or, failing such agreement, was not in accordance with the law of the country where the arbitration took place; or
(e) The award has not yet become binding on the parties, or has been set aside or suspended by a competent authority of the country in which, or under the law of which, that award was made."
[281] V (2) – Article V(2)(a) – Provisions – NYCG 1958

most basic notions of morality and justice."[282] Thus, under-enforcement theory can explain that in some instances the arbitral award is underenforced due to institutional reasons where national courts refuse to enforce the arbitral awards.

However, the public policy defence has restrictions. For example, in the *Methanex Corporation v United States of America* case,[283] the tribunal held that the state's commitments should follow the general principles of international law. Regulations for public policy must be based on non-discriminatory principles. The foreign investors should not be subject to expropriation and compensation for public interests. Apart from the public policy issues, the state is required to compensate foreign investors for any unlawful act.[284]

The problem is that public policy is a controversial topic the domestic court can refuse the arbitral award" by public policy grounds. The definition of public policy is unclear; hence, it is important to assess the range of public policy and how international conventions define and use it in enforcing arbitral awards. The problem is, it is hard to provide a uniform standard for public policy that reflects the political, legal, religious and economic changes over time. Both over and under-enforcement theories can explain that broad criteria such as Public policy blur the line between illegal and legal. It opens to many different interpretations that depend on the judge's opinions rather than actual culpability and legislative definition. Judges can easily over or under enforce the law based on their discretion. This made scholars such as Choi to argue that Article III of the New York Convention can allow uniformity in the interpretation of judicial processes or legislation.[285]

Generally, as previously discussed ICSID overcomes this challenge by leaving no room for defence of public policy. Conversely, the New York Convention permits domestic courts to raise exceptions to international public policy to reject the recognition and enforcement of

[282] *Parsons & Whittemore Overseas Co. v Societe Generale de I'Industrie du Papier*, 508 F.2d 971 (2d Cir. 1974), at. 973.
[283] Methanex v United States, Final Award on Jurisdiction and Merits (3 August 2005) 44 ILM 1345; United Nations Commission on International Trade Law, Arbitration Rules, part 4, chap D.
[284] ibid
[285] Susan Choi, 'Judicial Enforcement of Arbitration Awards under the ICSID and New York Conventions' (1995-1996) 28 New York University Journal of international & Politics175 197

foreign arbitral awards on both procedural and substantive grounds.[286] This makes scholars such as Draguiev to debate that the New York Convention should have the same status as a final national judgment since ICSID award is executed by its own without the need of special procedures.[287] Therefore, the international community should encourage contracting parties to modify New York convention to have the same ICISID status as a final national judgment.

Also, states can attempt to integrate their national laws with public policy defence to avoid international state liability. Another similar case is *ATA v Kingdom of Jordan*. The Turkish construction company ATA claimed that it had entered into a contract with the Jordanian state-controlled entity APC for dike construction, a part which collapsed. This raised a dispute between the parties that was referred to the arbitration.[288] The tribunal dismissed the claim of the APC and ruled in favour of the ATA. The ATA requested the national court of Jordan to execute the award but both the Court of Appeal and the Court of Cassation applied the national arbitration law and annulled the award. Therefore, the ATA made another claim under the same arbitration clause in the contract. The tribunal had temporal jurisdiction and found that the national courts of Jordan had applied the arbitration law of Jordan wrongfully. This is because the law was found incompatible with Article II of the New York Convention or otherwise Jordan would breach its international obligations by relying on its national legislation.[289] Thus, we can infer that interaction between the international law and national law is causing confusions. Nevertheless, there are other constraints in the enforcement stage under both conventions the ICISD and New York.

[286] Fifi Junita, 'Public Policy Exception in International Commercial Arbitration- Promoting Uniform Model Norms' (2012) 5(1) Contemp. Asia Arb. J 45
[287] Deyan Draguiev, 'State Responsibility for Non-Enforcement of Arbitral Awards' (2014) 8 World Arbitration and Mediation Review
[288] *ATA Construction, Industrial and Trading Company v the Hashemite Kingdom of Jordan* ICSID ARB/08/2 Award of 18 May 2010
[289] ibid

3.6.2.3 Immunity enforcement constraints in international investment law

A. Sovereign property**:**

Sovereign properties are always used by a state for diplomatic or sovereign functions.[290] They cause constrains in the enforcement of arbitral awards because they are always immune from execution regardless of the commercial activity exception. On the contrary, other foreign state properties used for sovereign purposes can be subject to execution whenever the foreign state has either implicitly or explicitly waived a sovereign immunity from execution.[291] For example,in the case of *Sedelmayer* who held German nationality and made huge investment through the stock acquisition of a Russian company. From 1994 to 1996, his investment in Russia was expropriated with a lack of compensation. Hence, Sedelmayer use the Germany-Soviet BIT in the Stockholm Chamber of Commerce (SCC) arbitration proceeding and acquired a favourable arbitral award. Sedelmayer tried to execute the award in Germany but was not successful. First, Sedelmayer attempted to execute against the VAT funds of the Russian diplomatic staff transactions in Germany. Then he tried to execute against the pecuniary rights held by Russia for fare payment for passage through its air space. In both cases, the national German courts ruled that the assets had sovereign function, which could not be executed against sovereign property according to general international law. Also, Sedelmayer complained to the European Court of Human Rights (ECtHR). [292]

The ECtHR confirmed that the award was enforceable under "possession" in Article 1, Protocol 1 of the European Convention on Human Rights (ECHR). Nonetheless, the court ruled that the case was inadmissible as ECHR would not be breached if the state followed the principles of international law and the rules on state immunity against execution.[293] The under-enforcement theory can explain that the law is under-enforced in the case of *Sedelmayer* because of institutional reasons rather than analytical reasons.

[290] See UN Convention on State Immunity, art 21; Sovereign property includes military property, diplomatic property, cultural heritage property and the central bank.
[291] Cedric Ryngaert, 'Embassy Bank Accounts and State Immunity from Execution: Doing Justice to Financial Interests of Creditors' (2013) 26 Leiden Journal of international law 73
[292] Franz J. Sedelmayer v Germany, Applications No. 30190/06 and No. 30216/06, Judgment, 10 November 2009 [hereinafter "Sedelmayer"].

[293] Convention for the Protection of Human Rights and Fundamental Freedoms (adopted 4 November 1950, entered into force 3 September 1953) 213 UNTS 221 (ECHR)

In general, protection of sovereign properties is seen in state practice. An example of this is the case of *LETCO v Liberia*.[294] The US District Court, Southern District of New York deliberated the effect of the Article 54 of the ICSID Convention in detail, confirming that:

> "Liberia, as a signatory to the Convention, waived its sovereign immunity in the United States with respect to the enforcement of any arbitration award entered into pursuant to the Convention. When it entered into the concession contract with LETCO, with its special provision that any dispute thereunder be settled under the rules of ICSID and its enforcement provision thereunder, it invoked the provision contained in Article 54 of the Convention which requires enforcement of such an award by Contracting States."

However, the court held Liberia's immunity from execution according to Article 55 since the US law provides "exceptions to the immunity of a foreign state from execution upon a judgment entered by a Court of the United States if the property is or was 'used in commercial activity in the United States." In its decision, the court demonstrated that the assets in question – the taxes and the fees – were sovereign assets rather than commercial assets. The claimant failed in executing the arbitral award because the US law on sovereign immunity was applied.[295]

The under-enforcement theory can explain that the law is under-enforced in the case of *LETCO v Liberia* due to institutional reasons rather than analytical reasons. We can conclude from the case of *LETCO v Liberia* is that despite the fact that consent to the arbitration agreement is a waiver of sovereign immunity from jurisdiction and enforcement, when it comes to foreign property a separate waiver is required. Also, this makes scholars such as van den Berg argue that despite the shift in the doctrine of sovereign immunity to a restricted approach from jurisdiction in many states, a sovereign immunity from execution is still absolute.[296] Thus, the under-enforcement theory can explain that the restrictive state immunity is under-enforcement in some instances in the enforcement phase for institutional reasons.

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[294] *Liberian Eastern Timber Corporation* (*LETCO*) *v Republic of Liberia*, ICSID ARB/83/2, Award of 31 Mar 1986

[295] ibid

[296] Albert Jan van den Berg, *Some Recent Problems in the Practice of Enforcement under the New York and ICSID Conventions* (Cambridge University Press 1993)

Another similar example related to execution against diplomatic property (sovereign property) is the case of *Noga v Russian Federation.* A Swiss company named *Noga* made a loan agreement with the Russian Federation to ensure the sale of petroleum products. In pursuing the matter between both parties,[297] the 1991 and 1992 contract showed that the Russian Federation did not merely sign the arbitration clause but also expressed that it had waived its immunity from suit, execution and attachment permitted by the principles of customary international law and international conventions.[298] The French court in this case interpreted the waiver of sovereign immunity from execution clause in a narrow and strict way. The over-enforcement theory can explain that the French court did extensive interpretation to the law. This is because *Noga* had attached the Russian embassy bank, which was considered diplomatic property in necessity of special protection with reference to the diplomatic immunity law.[299] Although the Russian Federation had expressed waiver from all immunities involving diplomatic immunity, the Paris Court of Appeal stated that:

> "…such a waiver did not extend to the diplomatic immunities from execution guaranteed by the 1961 Vienna Convention and by customary international law, which are governed by specific rules distinct from those applicable to foreign States."

The determination of the waiver of diplomatic immunity must be referred to the Preamble 77 and Article 3 (78) of the Vienna Convention according to which it "reserves immunities and privileges of diplomatic and protection of all diplomatic functions facilities. Although the Paris Court of Appeal accepted that the Vienna Convention does not specifically refer to a bank account of diplomatic mission, the Court relied on Article 25 of the said Convention"

The *Noga* case is consistent with the UNCSI convention that excludes a bank account used or intended for use in the diplomatic mission of state except when a foreign state has expressed its consent on waiving its immunity from execution.[300] This case demonstrated that civil law

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[297] *Embassy of the Russian Federation et.al v Compagnie NOGA d'importation et d'exportation (NOGA),* Paris Court of Appeal (1st Ch. A), 2000/14157

[298] Nancy B Turck, 'French and US Courts Define Limits of Sovereign Immunity in Execution and Enforcement of Arbitral Awards' (2001) 17(3) ARB. INT'L 327, 332

[299] Chamlongrasdr, '*Foreign State Immunity and Arbitration'*(n255)

[300] See UN Convention, art 21(1)(a); See UN Convention, art 19(a) and (b), which reads:
"No post-judgment measures of constraint, such as attachment, arrest or execution, against property of a State may be taken in connection with a proceeding before a court of another State unless and except to the extent that:
(a) the State has expressly consented to the taking of such measures as indicated:

countries such as France have limitations regarding execution against embassy bank accounts. Accordingly, enforcement is limited to commercial purposes and not sovereign purposes. Thus, the claimant must prove that the assets were used for commercial purposes. Chamlongrasdr debated that it is not always clear what assets can be attached for non-governmental purposes. It is vague which state assets can be considered for "commercial purposes." In general, national courts want to protect the state's assets and interpret legislation accordingly.[301]

Generally, under-enforcement legal theory explain that under-enforcement of law reflects adjudicators opinion of its own institutional ability to define rules that may be over-enforced or under-enforced at different times depending on circumstances. Hence, national courts will seek to under-enforce the arbitral awards to protect the state's assets. This raised the question of whether the mixed purposes of embassy banks could be attached. Although bank account is provided in the UN convention, it does obviously specify the mixed purpose of embassies.

B. Mixed purposes property:

Mixed purpose properties cause more constraints than pure sovereign properties in the enforcement of arbitral awards. Their assessment is difficult in the diplomatic context where it creates more complexity in properties such as embassy banks with mixed purposes. It remains unclear as it varies from state to state. There is lack of actual case law dealing with embassy bank accounts for mixed purposes in the investment environment.[302] Recent codifications such as under section 13 (5) of the UK SIA attempted to provide a solution, which is to permit the head of the sovereign state's diplomatic mission to issue a certificate as evidence to confirm whether such a property is in usage or planned for use in a sovereign purpose.[303] Generally, under-enforcement reflects adjudicator's opinion of its own institutional ability to define rules that may be over-enforced or under-enforced at different times depending on circumstances. Hence, under-enforcement theory can explain that state's diplomatic mission will always seek

(i) by international agreement"
[301] Chamlongrasdr, *'Foreign State Immunity and Arbitration*' (n255)
[302] Ryngaert, 'Embassy Bank Accounts and State Immunity from Execution: Doing Justice to Financial Interests of Creditors' (n291)
[303] See s13(5) UK Sovereign Immunity Act 1978

to under-enforce arbitral award. It appears that state's diplomatic mission will always argue that the property is used for sovereign purpose in order to protect state's assets.

This reflected in the case of *Alcom Ltd. v Republic of Colombia*. The Colombian Ambassador submitted a certificate to the lower court to confirm that funds were not used for commercial purposes. The funds were used for the daily expenses in the running of the embassy. However, the UK Court of Appeal looked at the nature of the transactions and refused a certificate on the grounds that it was not accepted as definite evidence and the regular expenses of operating the embassy could not be considered as protected property. Contrarily, the House of Lords did not agree with the Court of Appeal on looking at the nature of the transaction instead of its purpose. [304] Seemingly the House of Lords and the Court of Appeal have different views on whether to apply nature or purpose test in order to execute against state property of mixed purposes. This can attribute to the problems of under-defined rules where broad rules invite selective enforcement. Adjudicators might over or under-enforce the rules because they are trying to square the law with the facts of the case to render their own notion of justice.

It seems that existing overlap between diplomatic law and sovereign law is because most of the domestic laws on sovereign immunity and the Vienna Convention do not mention mixed purposes properties. Also, the UNCSI is silent on it. Hence, arbitral awards enforcement against mixed purposes properties depend on the interpretation of the domestic law.[305] Also, most of the domestic laws on sovereign immunity are silent regarding mixed purposes and only refer to the types of property that enjoy the special protection of sovereign immunity from execution.[306] This can attribute to the problems of under-defined law where broad law invites selective interpretation. These vague laws allow enforcement authorities to select from many potential offenders behind the scope of the statute.

Nevertheless, adjudicators can avoid the overlap between the diplomatic law and the sovereign law. This is because the rule of customary international law, the privileges and immunities of diplomats and their properties are protected by the Vienna Convention on Diplomatic Relations

[304] ibid
[305] Vienna Convention, art 25; *Embassy of the Russian Federation et.al v Compagnie NOGA d'importation et d'exportation (NOGA),* Paris Court of Appeal (10 August 2000), reported in (2001) XXVI Yearbook of Commercial Arbitration 273, at 275
[306] See US FSIA, s 13(5); UK SIA, ss 14(4) and 16(1); Australian FSIA, ss 31(4) and 32(3)(a); Canadian SIA, ss 12(3) and (4), and UN Convention, art 21.

of 1961.[307] In this matter, such immunities and privileges will not be affected by national law provisions on sovereign immunity for the purpose of execution. Although, Vienna Convention does not precisely refer to an embassy bank account, we can refer to Article 3 and Article 25 of the Vienna Convention,[308] which respects the full facilities for the performance of the diplomatic function, considered to be a customary international law of diplomatic immunity. Accordingly, Sovereign properties are causing constraints in the enforcement stage. Also, the role of national laws in permitting enforcement against the state's property can cause inconsistent decisions on enforcement against states properties.

C. National laws and inconsistent decisions on enforcement.

In general, ICSID Convention and New York Convention permit the domestic court to decide the domestic law on sovereign immunity in the enforcement stage. This raises many constraints because state immunity laws vary among different jurisdictions, which can result in different outcomes regarding the waiver of immunity for property. For example, the US district court in the *Birch Shipping Corp v Embassy of the United Republic of Tanzania* case applied an approach different from the *Alcom* case in addressing the purpose test of an embassy account. In this example, the court considered if the property was for sovereign or commercial purpose. The court made its decision based on the purpose test instead of nature test.[309] Hence, there is a difference between English and American courts regarding "commercial purpose" as an

[307] Vienna Convention on Diplomatic Relations of 1961
[308] Vienna Convention, art 3 reads:
"1. The functions of a diplomatic mission consist inter alia in:
(a) representing the sending State in the receiving State;
(b) protecting in the receiving State the interests of the sending State and of its nationals, within the limits permitted by international law;
(c) negotiating with the Government of the receiving State;
(d) ascertaining by all lawful means conditions and developments in the receiving State, and reporting thereon to the Government of the sending State;
(e) promoting friendly relations between the sending State and the receiving State, and developing their economic, cultural and scientific relations.
2. Nothing in the present Convention shall be construed as preventing the performance of consular functions by a diplomatic mission." See also Vienna Convention, art 25.
[309] *Birch Shipping Corp v Embassy of the United Republic of Tanzania,* 507 F.Supp. 311 (D.D.C. 1980)

exception of sovereign immunity. The UK state immunity act does not refer to the purpose of the transaction unlike US courts that look at the nature of transaction to define the acts.[310]

It seems that national laws cause inconsistent judgement regarding such distinguishing tests on state immunity. As a result, The UNCSI attempted to provide a solution to such an issue in Article 2(2):

> "In determining whether a contract or transaction is a 'commercial transaction' under paragraph 1(c), reference should be made primarily to the nature of the contract or transaction, but its purpose should also be taken into account if the parties to the contract or transaction have so agreed, or if, in the practice of the State of the forum, that purpose is relevant to determining the non-commercial character of the contract or transaction."[311]

However, as previously mentioned, UNCSI did not provide clarity on whether the adjudicators should look at the nature of the transaction or the purpose of the transaction in defining commercial transaction. Another problem that culminated from the various national laws on state immunity that cause uniformity on executing against state properties is that some codifications have no nexus requirement between the property to execute and the underlying claim.[312] For example, the Canadian and the Australian SIA applied the same approach with no nexus requirement.[313] These laws under-enforce nexus requirement. These laws appear less restrictive. Conversely, there are some other codifications where national laws on state

[310] Sornarajah, *The International Law on Foreign Investment* (n 1)
[311] UNGA Res/59/38 (n75)

[312] s13(4) UK Sovereign Immunity Act 1978

[313] Australian SIA, s 32(3)(a) reads:
"(3) For the purposes of this section:
(a) commercial property is property, other than diplomatic property or military property, that is in use by the foreign State concerned substantially for commercial
purposes; and"
See Canadian SIA, s 12(1)(b) reads:
"(1) Subject to subsections (2) and (3), property of a foreign state that is located in Canada is immune from attachment and execution and, in the case of an action *in rem,* from arrest, detention, seizure and forfeiture except where
(b) the property is used or is intended to be used for a commercial activity or, if
the foreign state is set out on the list referred to in subsection 6.2(2), is used or is intended to be used by it to support terrorism or engage in terrorist activity;"

immunity that are established in over-enforced manner. Whilst the nexus requirement is significant condition to be fulfilled.[314]

For example, in the cases of *LIAMCO* and *Ipitrade* in Switzerland, the court "declined to exercise jurisdiction and refused to permit execution against the assets of Libya located in Switzerland on the ground that the underlying transaction…bore no contact with Switzerland other than the fact that the sole arbitrator had elected to locate the seat of arbitration in Geneva."[315] Thus, the Swiss Court exercise weighted its decision on the important link with the Swiss territory.[316]

Accordingly, the nexus requirement can cause complexity in the enforcement stage. The over-enforcement theory can explain that nexus requirement is highly restrictive condition. It is hard in defining or establishing a connection between a property and the underlying claim. Hence, states use different approaches in dealing with the nexus requirement in their domestic law, which can result in different outcomes.

Likewise, nexus requirement is seen as having a negative impact of the effectiveness of arbitration because it leaves the private party without compensation. According to Chamlongrasdr, "by imposing the requirement of the connection between the property and the underlying claim, not only does it cause difficulties for courts in determining the attachable property, but also private parties seeking execution against the property of a foreign state have to face with unnecessary burdens."[317] Thus, this provision limits the availability of attachable property because not all commercial properties of a foreign state located in a certain state are used for commercial activity and have a link with the underlying claim. Consequently, the UNCSI provided a practical solution that reduced requirement of underlying claim.[318] The

[314] See before 1988 Amendment of the US FSIA, s 1610(a)(6)
[315] *Socialist Libyan Arab Popular-Jamahiriya v Libyan American Oil Company (LIAMCO)*, Swiss Federal Tribunal (19 June 1980), 62 ILR 228, at 234–236.
[316] Jean-Flavien Lalive, 'Swiss Law and Practice in Relation to Measures of Execution against the Property of a Foreign State' (1979) 10 Netherlands Yearbook of International Law153
[317] Chamlongrasdr, '*Foreign State Immunity and Arbitration'* (n 255)
[318] See UN Convention on Jurisdictional Immunities of States and their Property of 2004 (n 188), art 18(1)(c); 30 ILM 1563 (1991), it reads:
"1. No measures of constraint, such as attachment, arrest and execution, against property of a State may be taken in connection with a proceeding before a court of another State unless and except to the extent that:
(c) the property is specifically in use or intended for use by the State for other than government non- commercial purposes and is in the territory of the State of the forum

UNCSI changed the link criteria between property and underlying claim.[319] Therefore, the UNCSI allows execution against all commercial properties of the entity engaged in the proceedings and is not narrowed to the execution of commercial property, which has a link with the subject-matter of the claim.

In addition, national laws are also causing uniformity regarding the waiver of pre-judgment and post-judgment. There are some national laws on state immunity that are established in over-enforcement manner that do not include waiver regarding pre-judgment attachment. For example, the rules of sovereign immunity from execution regarding central bank funds vary in each jurisdiction. For example, under subsection 1611(b)(1) of the US FSIA, which does not include waiver regarding pre-judgment attachment. This provides that a foreign central bank could express sovereign immunity from execution for its fund or property in its own account only for a post-judgment.[320] This restriction is less preventive in case the property is under the commercial activity exception under Section 1610 (d), which allows pre-judgment attachment.[321] This situation might be changed for a post-judgment attachment, which allows the foreign state to waive "its immunity from attachment in aid of execution or from execution either explicitly or by implication."[322]

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and has a connection with the claim which is the object of the proceeding or with the agency or instrumentality against which the proceeding was directed."

[319] UN Convention on Jurisdictional Immunities of States and their Property of 2004 (n 188)
According to art 19(c), "a post-judgment measure of constraint is possible in the case only of an execution against the commercial property of a foreign state in connection with the entity against which proceedings refer". The Annex to the Convention provides that the "entity" under art 19 means "the State as an independent legal personality, a constituent unit of a federal State, a subdivision of a State, an agency or instrumentality of a State or other entity, which enjoys independent legal personality".

[320] *Weston Compagnie de Finance et d'Investissement, S.A. v La Republica del Ecuador, 823 F. Supp. 1106 (S.D.N.Y. 1993*); Andrew Dickinson, *State Immunity: Selected Materials and Commentary*, (Oxford University Press 2004) 326.

[321] US Foreign Sovereign Immunities Act (FSIA) 1976, s 1610 (d) reads:

"d) The property of a foreign state, as defined in section 1603 (a) of this chapter, used for a commercial activity in the United States, shall not be immune from attachment prior to the entry of judgment in any action brought in a court of the United States or of a State, or prior to the elapse of the period of time provided in subsection (c) of this section, if—
(1) the foreign state has explicitly waived its immunity from attachment prior to judgment, notwithstanding any withdrawal of the waiver the foreign state may purport to effect except in accordance with the terms of the waiver, and
(2) the purpose of the attachment is to secure satisfaction of a judgment that has been or may ultimately be entered against the foreign state, and not to obtain jurisdiction."

[322] Section 1610 (a)(1) US Foreign Sovereign Immunities Act (FSIA) 1976

Conversely, other domestic laws on state immunity under-enforce the requirement of post-judgment only and it allows the pre-judgment. Whilst pre-judgment attachment for a central bank's property is permitted under Section 13(3) of the UK SIA, but only with express consent of the Central Bank.[323] It is exactly the same under Article 18 of the UN Convention.[324]Therefore, international codifications and some domestic laws on sovereign immunity are flexible in allowing pre-judgments with the requirement of express consent by the foreign state.[325] In this situation, such pre-judgment measures are easier to use when dealing with the commercial property of a foreign state and not a sovereign property or central bank, which evokes sensitivity regarding international relations between states.[326]

As a result, the law on state immunity is fragmented because it is governed by various national laws with diverse scopes of immunity. This provides different levels of protection to the state's assets. Accordingly, some decisions can be seen as investor-friendly and others as more protective of the state's assets to be subject from execution. It depends on jurisdiction and the national law on state immunity. This makes scholars to attempt to clarify reasons for such fragmentation.

3.7 Reasoning of fragmentation on laws of state immunity

Scholars such as Anne van Aaken argued that this fragmentation is caused because of conflict of laws between the treaty obligations under the international investment law and the national

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[323] s 13(2)(a) and 13(3) UK Sovereign Immunity Act 1978

[324] UN Convention on Jurisdictional Immunities of States and their Property of 2004 (n 188)
UN Convention, art 18 reads:
"No pre-judgment measures of constraint, such as attachment or arrest, against property of a State may be taken in connection with a proceeding before a court of another State unless and except to the extent that:
(a) the State has expressly consented to the taking of such measures as indicated:
(i) by international agreement;
(ii) by an arbitration agreement or in a written contract; or
(iii) by a declaration before the court or by a written communication after a dispute between the parties has arisen; or
(b) the State has allocated or earmarked property for the satisfaction of the claim which is the object of that proceeding."

[325] s 1610(d), US Foreign Sovereign Immunities Act (FSIA) 1976; s 13(2)(a), UK Sovereign Immunity Act 1978 and 13(3); Canadian Sovereign Immunity Act, s 10(1); European Convention, art 23 and UN Convention, art 18

[326] See Christoph Schreuer, *State immunity: Some recent developments* (Grotius Publication 1988) 162; G.R

state sovereign laws.[327] Accordingly, both foreign investors and the host state can suffer from the fact that in certain cases there might be a conflict between state obligations under the domestic law and the international law.[328] This shed the light on the question of bridging the gap between international investment law and domestic sovereign immunity to provide a fair balance between the investor's and the state's sovereign interest should be addressed.[329] Also, Koskenniemei illustrated that this fragmentation comes from different tribunals or courts interpreting the same law differently.[330] Similarly, Schill argued that fragmentation of international investment law results from various legal sources, proceedings and inconsistent interpretations.[331] This can be seen in the investment arbitration where the foreign investor is subject to both international law and national law. Hence, there are inconsistencies in the arbitral award. It appears that literature effectively explain root causes of such fragmentation in international investment law. Also, existing literature support findings of both over- and under-enforcement theories.

However, both over- and under-enforcement theories provide deeper analysis on how rules of state immunity are applied in international investment law. Both theories provide that such fragmentation due to analytical and institutional reasons. The laws of state immunity are interpreted differently. Adjudicators interpret the law either narrowly or broadly to render their own notion of justice. In addition to the shared responsibility between the national law and international law in enforcing the arbitral awards. This attribute the problem of such fragmentation. However, some scholars see fragmentation as opportunity. For Pauwelyn, fragmentation is not always a bad thing because of regulatory competition that might increase efficiency and lead to the development of new legal tools. It can also lead to competition among the best interpretations in case there is a tension between treaties.[332]

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[327] Anne Van Aaken, 'Fragmentation of International Law: The Case of International Investment Protection'(2008) University of St. Gallen Law School, Law and Economics Research Papers Series 1/2008, 2
[328] Ibid
[329] Khanpoj Joemrith, "Enforcing Arbitral Awards against Sovereign States: The Validity of Sovereign Immunity Defence in Investor -State Arbitration" (PhD Thesis, SOAS, University of London) <http://eprints.soas.ac.uk/22784>
[330] *Fragmentation of International Law: Difficulties Arising from the Diversification and Expansion of International Law* – Finalised by Martti Koskenniemi (A/CN.4/L.682), 13 April 2006, para 24.
[331] Stephan Schill, 'Investment Treaties: Instruments of Bilateralism or Elements of an Evolving Multilateral System?' (2008) Paper for the 4th Global Administrative law Seminar
[332] Joost Pauwelyn, 'Bridging Fragmentation and Unity: International Law as a Universe of Inter-Connected Islands' (2004) 25 Mich. J. Int'l L 903

Similarly, Benvenisti and Downs argued that fragmentation can result in competition between organisations, courts, regimes and other institutions, which can permit the correction of faults, improve creativity and lead to overall improved performance to better law-making and law-application.[333] Competition will propel systems to improve accountability as an example. For example, the ECtHR jurisprudence mentions the "overriding importance" of *jus cogens*. This has made the ICJ refer to these norms after a lot of reluctance. Thus, fragmentation can also improve the legitimacy and effectiveness of international law and its application.[334]

Generally, the unity and fragmentation of international law should work together in enforcing law and conflicting rules should be avoided. However, since different branches of international law overlap, careful examination of such interactions, such as commercial questions de-linked with human rights or environmental protection, is required. These interactions require the development of a unitary framework of international law; thus, there is a need of harmony and a coherent set of disciplines, which is not necessarily applied universally among all states but at least coherent. Generally, fragmentation cannot totally be avoided because often two judges from the same legal system can apply the same law differently and reach different outcomes.[335]

Although Koskenniemi argued that fragmentation is not inevitable and interpretative formalism is the only practicable way to diminish incoherence and conflicts, Koskenniem's analysis and writings demonstrate that fragmentation does not threaten international law as a whole system and the tensions require the use of formal interpretation as a bridge between competing institutional and political issues.[336] Moreover, Broude presented Koskenniemi's argument as the problem of "susceptibility of a fragmented system to be captured by unaccountable governance networks."[337] Moreover, Kennedy presented the argument of Koskenniemei that there is absent unified theory of international law and that the formal unity of international law is impossible.[338] Accordingly, fragmentation cannot be totally avoided, but

[333] Eyal Benvenisti and George W Downs, 'The Empire's New Clothes: Political Economy and the Fragmentation of International Law' (2007) 60 Stanford Law Review 595
[334] Anne Peters, 'The Refinement of International Law: From Fragmentation to Regime Interaction and Politicization' (2017) 15(3) International Journal of Constitutional law 671
[335] Pauwelyn, Bridging Fragmentation and Unity' (n 308)
[336] *Fragmentation of International Law: Difficulties Arising from the Diversification and Expansion of International Law* – Finalized by Martti Koskenniemi (A/CN.4/L.682), 13 April 2006, para 24.
[337] Tomer Broude Keep Calm and Carry On: Martti Koskenniemi and the Fragmentation of International Law (2013). 27 TEMPLE International & Comparative Law Journal 279
[338] David Kennedy, 'The Last Treatise: Project and Person (Reflections on Martti Koskenniemi's From Apology to Utopia' (2006) 7 German Law Journal 982, 985

we need to harmonise state practice at the very least. Hence, the current situation demonstrated the fragmentation of international investment law. As the state immunity waiver is applied separately between jurisdiction and enforcement, there should be a complete sovereign immunity waiver that involves both jurisdiction and enforcement. Thus, it is important to review the different scholars' recommendation on this issue.

3.8 Recommendations to harmonise the state practice

Some scholars recommended the amendment of investment treaties and international conventions. Paulsson proposed that the New York and the ICSID conventions should be amended to establish a friendly atmosphere by providing a substantial degree of arbitral award enforceability.[339] Bjorklund added that the sovereignty waiver should be written to determine the range and attachable property involved including the diplomatic mission's property and the sovereign property once a dispute has started.[340] Moreover, Justin recommended a review of the UNCSI. For example, this convention agreed on a common definition of "commercial transaction", stressing on the nature test over the purpose test and listing certain examples to clarify the definition. It looks into its nature but also its purposes. Thus, it provides a vague definition of "commercial transaction" to the states.[341] The states are left to decide what constitutes a commercial transaction for the purpose of commercial-transaction immunity. This creates inconsistent practices and a struggle to use the nature/purpose test.[342]

Justin added that the UNCSI provides immunity to state agencies and instrumentalities "to the extent that they are entitled to perform and are actually performing acts in the exercise of sovereign authority of the State."[343] This provision leaves the decision on whether a state agency qualifies for immunity to several states whose state agencies vary in scope and size because of differing economic and political systems. This increases the chance that the

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[339] Jan Paulsson, 'ICSID's Achievements and Prospects' (1991) 6(2) ICSID Review 380
[340] Andrea K. Bjorklund, 'Sovereign Immunity as a Barrier to the Enforcement of Investor-State Arbitral Awards: The re-politicization of International Investment Disputes' (2010) 21 American Review of International Arbitration 211, 230
[341] Justin Donoho, 'Minimalist Interpretation of the Jurisdictional Immunities Convention' (2009) 9(2) Chicago Journal International Law article 12
[342] ibid
[343] Jurisdictional Immunities Convention, art 2(1)(b)(3)

agency's state and the forum state will disagree about whether such agency qualifies for immunity.[344] This issue is problematic in the law of state immunity. According to Collier and Lowe, "the extent to which immunity should be enjoyed by agencies, connected to the State but not so closely as to constitute central organs of government, remains a perennial problem in the law of State immunity."[345] Feldman also proposed to narrow and specify the list of non-commercial immune properties that are not subject to an execution. Most codifications in this area do not present a clear list of the types of property, including military property and diplomatic central banks that are immune from execution and the possibility of the waiver of state property. The UNCSI has listed specially protected property under Article 21 but is silent on properties with mixed purposes such as bank accounts.[346] Hence, these recommends can be valid and the UNCSI should consider them before ratification.

However, Damrosch debated that the UNCSI could not harmonise state practice because the non-parties to the treaty will not be bound to it.[347] This makes other scholars to propose that instead of focusing only on amending the international conventions or creating a uniform regime on sovereign immunity rules, the creation of a *lex specialis* set of soft laws could be a realistic solution. For instance, Fox proposed the creation of rules related to the attachment of state property in arbitral award enforcement through an UNCITRAL Model law.[348] Therefore, a state could use a model law in their domestic law with a *lex specialis* status within the international investment law regime. This could additional supplement the principles and rules that are provided in the UNCSI and support the development of the current domestic law on sovereign immunity. The amendment to the international treaties or international conventions might be not reachable in a particular jurisdiction and might be subject to certain restrictions under domestic law. Thus, it is important to have a parallel alteration of the domestic law concerning sovereign immunity in each state to secure the arbitral award execution before the domestic court and support the international convention applicability. This requires the model law to be stipulated in the same manner as the international convention.[349]

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[344] Donoho, 'Minimalist Interpretation of the Jurisdictional Immunities Convention'(n 341)
[345] John Collier and Vaughan Lowe, *The Settlement of Disputes in International Law: Institutions and Procedures* (Oxford University Press 1999) 272
[346] Mark B Feldman, 'Amending the Foreign Sovereign Immunities Act: The ABA Position' 20 (1986) 20 INT'L & CoMP. LAW Q. 288
[347] Lori Fisler Damrosch, 'Changing the International Law of Sovereign Immunity Through National Decisions' (2011) 44 VANDERBILT JOURNAL OF TRANSNATIONAL LAW 1185, 1189–1191
[348] Hazel Fox, 'State Immunity and Enforcement of Arbitral Awards: Do We Need an UNCITAL Model Law Mark II for Execution Against State Property?' (1996) 12 Arbitration International 89, 93
[349] ibid

Also, Fox's suggestion that "The law of state immunity that it is at the point of intersection of international law and national procedural law."[350] Generally, it could be a logical argument that the domestic law and the international law should work parallelly to achieve harmonising state practice on state immunity but integrating the model law into the domestic law might be difficult to implement because every state has its own polices based on its socio-economic factors. According to Bjorklund, the law on sovereign immunity in each state reflects its own culture and tradition; thus, it will bring different interpretations and make it difficult to achieve uniformity in the sovereign immunity interpretation approaches.[351]

However, there can be general agreement regarding state immunity where national laws can implement it without touching state policies. Bjorklund clarified that it is important for the amendment of sovereign immunity execution laws to reach harmonisation at the national law level.[352] For example, there are national laws, such as the UK SIA and the US FSIA, where foreign investors are obligatory to prove that the property in question is applied for a commercial or sovereign purpose.[353] It is suggested that by shifting the burden of proof to the state, the state will be able to safeguard the inviolability of particular properties. This recommendation is especially needed in the case of mixed purpose properties. As Fox suggests, "it might go so far, as does Swiss law, to reverse the burden of proof where the party seeking enforcement has a valid award against a state so as to require the state to prove that the property sought to be attached is not governmental in nature or that it is in non-commercial use."[354]

Nevertheless, scholars such as Kuipers debate that many solutions have been recommended such as changes in the domestic sovereign immunity laws, changes in the international laws or amending international agreements regarding the waiver of execution immunity. This solution is unrealistic because it requires political willingness which is absent in the international community.[355] As Henkin observed, nations comply with international law based on their

[350] Hazel Fox, *The Law of State Immunity* (n219)
[351] Bjorklund, 'Sovereign Immunity as a Barrier to the Enforcement of Investor-State Arbitral Awards' (n319)
[352] ibid
[353]Hazel Fox, 'Enforcement Jurisdiction, Foreign State Property and Diplomatic Immunity' (1985) 34(1) The international and comparative law quarterly115
[354] ibid
[355] Jacob A Kuipers, 'Too Big to Nail: How Investor-State Arbitration Lacks an Appropriate Execution Mechanism for the Largest Awards' (2016) Int'l & Comp. L. Rev. 417

interest and the calculated advantage over cost; thus, it's important to examine how they calculate such a formula and why they observe the law as a part of their foreign policy.[356]

It is also recommended to balance between public and private interests. As Delaume illustrated, the problem is that modern codifications do not elaborate on the investors' entitlements and the state's duties when the state is incapable of complying with the arbitral award.[357] Therefore, there is a need to balance between state obligations and investor rights. Bowett illustrated that there could be tension between the sovereign immunity law and the international investment law. Thus a balance must be struck between public and investor interests for the arbitral award enforcement.[358] Aaken recommends that balancing between public and private interests should be "a good faith interpretation of substantive provisions of investment law may lead to a reading and application of investment law more consistent with other special areas of international law."[359] Conversely, Schill recommends balancing between the public-private interests by viewing the ECtHR's jurisprudence as it has dealt with the protection of investor rights and sovereign immunity in the human rights law context. Nevertheless, it can be applied as a guideline in dealing with the relationship between sovereign immunity law and international investment law to decide whether the state-raised sovereign immunity defence to avoid enforcing the arbitral award can be considered a violation of the investment treaty obligations.[360]

In the ECtHR jurisprudence, most of the cases depend on Article 1 of the Protocol[361]regarding the right to property and Article 6(1) of the ECHR regarding a fair trial in order. As Kingsbury and Schill demonstrated, court interpretation referred to other rules of international law

[356] Louis Henkin, *How Nations Behave* (1st edn Cambridge University Press 1968)
[357] Georges R Delaume, 'Enforcement of State Contract Awards: Jurisdictional Pitfalls and Remedies'(1993) 8 ICSID Review 29, 29.
[358] Derek W Bowett, 'Contemporary Developments in Legal Techniques in the Settlement of Disputes' (1983) 180 The Hague Academy of International Law.169, 220
[359] Anne Van Aaken, 'Fragmentation of International Law: The Case of International Investment Protection' (n303)
[360] Stephan W Schill, 'Cross-Regime Harmonization through Proportionality Analysis: The Case of International Investment Law, the Law of State Immunity and Human Rights' (2012) 27 ICSID Review - Foreign Investment Law Journal
[361] Protocol of ECHR, art1 reads as follows: "Every natural or legal person is entitled to the peaceful enjoyment of his possessions. No one shall be deprived of his possessions except in the public interest and subject to the conditions provided for by law and by the general principles of international law. The preceding provisions shall not, however, in any way impair the right of a State to enforce such laws as it deems necessary to control the use of property in accordance with the general interest or to secure the payment of taxes or other contributions or penalties."

involving general principles of law provided in Article 31(3)(c) of the Vienna Convention on the Law of Treaties (VCLT) and the customary international law. Thus, it can support the harmonisation of the conflict between the competing interests of the state and the foreign investors.[362] Accordingly, it is a valid suggestion to find different ways to arrive at a proper interpretation and to refer to different jurisprudences such as the ECtHR to address the immunity problem in the context of international investment law.

Furthermore, diplomatic pressure is recommended by other scholars such as Rosenberg who illustrated that the foreign investor's domicile state can apply diplomatic pressure for compliance and enforcement. This is unofficial lobbying by officials from the state of the investor using any political leverage they might hold in the international arena.[363] For example, in the case of *Petrobart v The Kyrgyz Republic*, the host state tried to evade compliance with the European Court of Justice (ECJ) arbitral award in favour of the Cypriot energy trader Petrobart Limited. Diplomatic intervention came from the Stockholm Chamber of Commerce in Sweden. Consequently, the Kyrgyz Republic agreed to pay.[364] However, Rosenberg debated that the success of diplomatic pressure depends on the international status of the state.[365] Kuipers added that the problem is that the home state is confronted with a domestic political matter regarding to what extent advocating the claim of the investor will affect the political environment of the home state.[366] It is logical that diplomatic pressure is not a good strategy because it depends on the state's status, which might worsen the current situation.

What we can infer from reviewing the pros and cons of the scholars' recommendation on the dilemma of lack of certainty of waiver of state immunity. In addition to the analysis of state practice through both over- and under-enforcement theories. It seems that UNCSI should bring practical solutions that could harmonise the state practice on immunity waiver to a certain extent. However, before recommend the state to ratify it, it is important to overcome the

[362] Benedict Kingsbury and Stephan Schill, *Public Law Concepts to Balance Investor's Rights with State Regulatory Actions in the Public Interest- The Concept of Proportionality* (Oxford University Press 2010)
[363] Charles B Rosenberg, 'The Intersection of International Trade and International Arbitration: The Use of Trade Benefits to Secure Compliance with Arbitral Awards' (2014) 44 Georgetown Journal of International Law
[364] Jarrod Hepburn & Luke E Peterson, *As New Arbitral Claim is brought against Kyrgyzstan, an ICSID Award Remains Unpaid* (29 September 2011)
[365] Rosenberg, 'The Intersection of International Trade and International Arbitration: The Use of Trade Benefits to Secure Compliance with Arbitral Awards' (n363)
[366] Kuipers, 'Too Big to Nail' (n 355)

shortages highlighted in this chapter regarding clarification of what constitutes a commercial transaction and the treatment of state agencies. The challenge of mixed purpose state properties must also be addressed. This goes along with considering scholars recommendation on the good faith interpretation approach and the ECtHR jurisprudence. Although the UNCSI could help to overcome debatable issues that cause inconstancy in applying the waiver of immunity in the investment, it is not enough. Furthermore, the international community should provide incentives through international financial institutions such as the IMF or World Bank on the best state practice regarding the enforcement of arbitral awards.

3.9 Concluding Remarks

It appears that transitional governments is obliged under international law to fulfil the obligations of the previous regime. Otherwise, it has to pay compensation for foreign investors. Going back to the chapter's main question, the question of Are unconstitutional transitional governments immune under international law for measures they take against foreign investments? Answering the main chapter question will take us back the previously discussed challenges of the state immunity defence. There is no obvious answer to this question. This is because of the fragmented and uncoordinated development of the many sub-disciplines of international law, protection of foreign investments from hostile host state's governmental measures remain moot and unpredictable. Although there is was a significant effort in the nineteenth century to shift from absolute immunity to restrictive sovereign immunity. The state practice is fragmented between absolute and restrictive theories of sovereign immunity.

It seems that literature effectively explain root causes of such fragmentation in international investment law. However, both theories over-enforcement and under-enforcement provide deeper analysis on how rules of state immunity are applied in international investment law. The theories explained that such fragmentation due to analytical and institutional reasons. It appears that some tribunals under-enforce the rules of State waiver of immunity from adjudication because of analytical reasons due to their interpretation to law. Adjudicators might over or under-enforce the law because they are trying to square the law with the facts of the

case to render their own notion of justice. The textual analysis is as a tool to free adjudicators from constraints. However, drawbacks in justifying interpretation will increase indeterminacy.

Likewise, rules of State waiver of immunity from enforcement in some instance is under-enforced some of because institutional reasons. The shared responsibility in enforcing the arbitral awards with national courts. Also, effectiveness of the enforcing arbitral awards relies on the national law on sovereign immunity in the state where execution is required. There are various jurisdictions where the rules of state immunity are over-enforced while in other jurisdiction the rules of state immunity are less restrictive. This is attributes to the problem of fragmentation between absolute and restrictive theories of sovereign immunity.

The current situation appears that there is gap between the domestic sovereign immunity and international investment law to provide a fair balance between investor and state's sovereign interest that should be addressed. The interaction between national law and international law on state immunity requires the development of a unitary framework of international law. Thus, UNCSI should bring practical solutions. However, before we recommend the state to ratify it, it is important to overcome the shortages highlighted in this chapter regarding clarification of what constitutes a commercial transaction and the treatment of state agencies. It should address the challenge of mixed purpose state properties. Instead of leaving the states to struggle with such issues and provide inconsistent practices, which will undermine the objective of the whole convention. This convention can offer a practical solution to overcome the discussed challenges. The problem is that the convention will be interpreted differently by the different national courts. Thus, the UNCSI should provide guidance in this annex.

Nevertheless, it is not enough to recommend the development of the UNCSI because it cannot alone harmonise state practices. This is because the non-parties to the treaty are not compelled by it. Accordingly, this chapter recommends that the international community should establish incentives to encourage states to comply with the large awards rendered against them by involving multinational organisations such as the World Bank and the IMF to put pressure on states through financial incentives. Also, international community should use the advantage of fragmentation in the international investment law. As scholars argue, it can bring competition

among the different jurisdictions, which can increase efficiency and lead to the development of new legal tools in this area.

Accordingly, this chapter concludes the state immunity waiver is applied separately between jurisdiction and enforcement; there should be a complete sovereign immunity waiver that involves both jurisdiction and enforcement. This chapter recommends an effective mechanism to enforce arbitral awards without exception to prompt, adequate and fair compensation in all cases where foreign investments are impounded by hostile states. Finally, sovereign defences can lead to the necessity defence to figure out the extent to which the state has valid purposes for breaching its international obligations. Accordingly, necessity defence will be examined in the coming chapter.

Chapter 4: Whether transitional governments allowed to use the law of state responsibility to accommodate changes for measures they take against foreign investments?

4.1Introduction

The law of state responsibility defines the international obligations of state and what establishes a violation of such obligations and the consequences of that breach. It gives the state the right to react in certain circumstances thus providing a permissible means for that reaction.[367] The United Nations General Assembly (UNGA) did a great effort to codify the rules of state responsibility. UNGA established the International Law Commission (ILC) codify the rules of customary international law on state responsibility.[368] Nevertheless, the question is how arbitral tribunals interpret articles of state responsibility in the light of changing needs and circumstances of the international community.[369] More specifically, how arbitral tribunals interpret articles of state responsibility during emergency times. Generally, transitional or revolution times can be considered as an emergency crisis where economic, political and social forces are beyond the state's control. In emergency times, state will always argue that the circumstances were out of its control. Conversely, investors will argue that the state's participation in the crisis is because the state's acts of mismanagement.[370] In all cases the emergency times can cause instability in the state, which can lead to negative consequences to among others foreign investment protection.

However, international law recognises different state defences.[371] The relevant ones that the state can use in its emergency crisis to avoid international obligations towards foreign investment protection are the state of necessity defence and the force majeure defence.[372]

[367] Text adopted by the Commission at its fifty-third session in 2001 and submitted to the General Assembly as a part of the Commission's report covering the work of that session. The report, which also contains commentaries on the draft articles, appears in Official Records of the General Assembly, Fifty-sixth Session, and Supplement No. 10 (A/56/10). The text has been reproduced as it appears in the annex to General Assembly resolution 56/83 of 12 December 2001.

[368] See Article 13, paragraph (1)(a), of the Charter of the United Nations, http://legal.un.org/cod/

[369] Caron, 'The ILC Articles on State Responsibility' (n27)

[370]Elizabeth A Martinez, 'Understanding the Debate Over Necessity: Unanswered Questions and Future Implications of Annulments in the Argentine Gas Cases' (2012) 23 Duke Journal of Comparative and International Law149.

[371] Defences of consent, self-defence, countermeasures, force majeure distress and state of necessity.

[372] The ILC incorporated 'necessity' as art25 (formerly art 33), and 'force majeure' as art 23 in Chapter V (Circumstances Precluding Wrongfulness).

Therefore, it is important to examine whether unconstitutional transitional governments that came to power due to revolution can invoke these defences to avoid its international obligations towards foreign investment protection.

Subsequently, the transitional or revolution time represents emergency crisis where economic, political and social forces are beyond the state's control. This requires not being limited to examine revolutionary cases but to examine other cases that involve the emergency times. Both doctrines of necessity and force majeure under the law of state responsibility in context of international investment law will be examined. In order to conduct deeper analysis, this chapter uses both under-enforcement and over-enforcement theories as interpretative tools to assess how the law of state responsibility is enforced in context of international investment law.

4.2Doctrine of state necessity

The doctrine of necessity operates under the law of state responsibility to preclude the legal wrongfulness of an act.[373] Generally, tribunals interpret necessity as a source of exception to preclude wrongful acts by the state in times of emergency.[374] Herein lays the importance of understanding the concept of necessity. Sloane demonstrated the concept of necessity by referring to the early scholars who wrote about the law of nations such as Gentili, Hugo Grotius and Alberico, these scholars considered the right of necessity defence. However, it is important to understand the concept of necessity; otherwise, all states will never obey its international obligations.[375]

Early scholars such as Grotius explained that many internal laws of different countries considered the right to self-preservation, clarifying that the Jewish and Roman laws act upon the same principle that does not allow us to kill anybody who has taken our belongings except for protecting our survives.[376] Also, Cheng explained that necessity means a state has the right to take any measures for self-preservation whether lawful or not. A state had failed in trying all

[373] Myanna Dellinger,' Rethinking Force Majeure in Public International Law' (2017) 37 Pace Law Review 2
[374] Chester Brown and Kate Miles, *Evolution in Investment Treaty Law and Arbitration* (Cambridge University Press 2011)
[375] Sloane, 'On the Use and Abuse of Necessity in the Law of State Responsibility' (n27)
[376] Hugo Grotius, The Rights of War and Peace (2005 ed.) vol. 1 (Book I) [1625]

legal means of self-preservation and its very existence is in danger. In addition, there is no other way to overcome the danger.[377] Also, Ago, who developed the concept of state necessity, illustrated that the essential interests of the state should cover political and economic survival.[378] Accordingly, necessity situation covers all emergency times regardless of nature of crisis.

In addition to the classical scholars' attempts to narrowly define the concept of necessity, as the nature of the state's right and that each state is given the right to take necessary actions to sustain its existence. Sloane cited classical scholars such as Thomas Hobbes who portrayed the concept of necessity as the natural right of man to use his power to maintain his existence. Other classical scholars cited by Sloane such as Vattel described the necessity defence in terms of an earth designed to feed all its inhabitants, which does not allow starvation because the properties are invested in others. Therefore, a nation can force its neighbours who acquire more for themselves to give back a fair share at a fair price and can obtain it by force if they refuse to do so.[379] The classical concept of state necessity considers these unlawful acts as lawful on a temporarily basis. It was based on the natural rights of states to maintain their existence. However, the concept of necessity narrowed down in the last decade of the twentieth century. The state could be exempted from its international obligations only under grave circumstances. There is uncertain whether these scholars view necessity as an excuse or a justification.[380]

Accordingly, scholars such as Hill explained that the concept of the state necessity defence should be interpreted as a justification instead of an excuse; thus, there should be an exemption clause for breaching obligations.[381] In contrast, Johnstone argued that if the International Centre for Settlement of Investment Disputes (ICSID) tribunals visualised the state necessity defence as a justification for breaching its obligations instead of an excuse, the state can accept

[377] Bin Cheng, General Principles of Law as Applied by International Courts and Tribunals (Cambridge University Press 1987)
[378] Robert Ago, *Addendum to the Eighth Report on State Responsibility* (Document A/CN. 4/318/ADD.5-7) (1980)
[379] ibid
[380] Sloane, 'On the Use and Abuse of Necessity in the Law of State Responsibility' (n 27)
[381] Sarah Hill 'The 'Necessity Defense' and the Emerging Arbitral Conflict in its Application to the U.S.-Argentina Bilateral Investment Treaty' (2007) 13 Law & Business Law Review of Americas 547

its responsibility but reject that its acts were evil, so it will have the opportunity to avoid such responsibility.[382]

Also, Paddeu debated considering the state necessity defence as a justification in raising the concern that such a state excuse could weaken the rule of law. This is because a state necessity defence means an excuse for violating the international law. States can abuse the necessity defence under normal circumstances. As a result, many scholars attempted to explain the concept of the state necessity defence, but it appears that the state necessity defence is debatable.[383] Therefore, in order to prevent such a debate, the necessity defence is codified in Article 25 by the 2001 Articles on Responsibility of States for Internationally Wrongful Acts (ARSIWA).[384] It aimed to codify the existing customary international law.[385]

Article 25 Necessity:

> "1.Necessity may not be invoked by a State as a ground for precluding the wrongfulness of an act not in conformity with an international obligation of that State unless the act: (a) Is the only way for the State to safeguard an essential interest against a grave and imminent peril; and (b) Does not seriously impair an essential interest of the State or States towards which the obligation exists, or of the international community as a whole. 2. In any case, necessity may not be invoked by a State as a ground for precluding wrongfulness if: (a) The international obligation in question excludes the possibility of invoking necessity; or (b) The State has contributed to the situation of necessity."

The over-enforcement theory can explain that the criteria of necessity are stipulated in restrictive manner. It seems hard to fulfil. The justification of creating stricter rules might be to support political processes to minimizing the use of necessity defence. Also, it is important note that despite these articles are general in coverage, they do not essentially adopt in all cases, specifically in the treaty regimes. Contracting states have the right to draft the BITs to involve

[382] Robert Martinson, 'New Findings, New Views: A Note of Caution Regarding Sentencing Reform' (1979) 2 Harvard Law Review 7
[383] Federica Paddeu, 'The Impact of Investment Arbitration on The Development of State Responsibility Defences' (2017) University of Cambridge Faculty of Law Legal Studies Research Paper
[384] *Articles on State Responsibility*, art. 25.
[385] Kelley Chubb, 'The 'State of Necessity' Defense: A Burden, Not A Blessing to The International Investment Arbitration System' (2013) 14 Cardozo Journal of Conflict Resolution 531

a provision that permits the use of the state necessity defence to defend wrongful state acts.[386] Many BITs include certain provisions for the protection of security interests, where a state can use it as a defence to justify its wrong actions.[387] Also, many international investment agreements provide exceptions but are limited to certain circumstances such as armed conflict, war and other emergencies. Generally, in the investment context, arbitral tribunals usually refer to two sources of authority when analysing the state necessity defence validity: 1) investment treaty provisions and 2) customary international law.[388]

Moreover, state necessity defence in the international investment arbitration for breaching the investment treaty may include many different defences such as public policy, environmental, humanitarian and economic /political necessity. Thus, it is relevant to examine the cases that involve the emergency crisis regardless of the nature of emergency crisis. Generally, under customary international law, the state of necessity and other circumstances precluding wrongfulness does not terminate or annul the international responsibility. It only gives an excuse or justification for non-performance while the circumstance in question subsists.[389] This is seen in the state practice

4.3State practice

An early case of necessity defence was negotiated by Permanent Court of International Justice (PCIJ) in 1929. This is the case of the *Brazil loans*, where Brazil paper francs suffered a critical depreciation. Accordingly, Brazil raised the necessity defence that it had suffered from a war; hence, it should be exempted from its obligations. The PCIJ refused Brazil's argument and held that "the economic dislocation caused by the Great War [World War I] has not, in legal principle, released the Brazilian Government from its obligations."[390]

[386] ibid
[387] Yannaca-Small, "International Investment Perspectives: Freedom of Investment in a Changing World" (n27)
[388] ibid
[389] ILC Commentary to Chapter V of Part I, paras 2–4
[390] Payment in Gold of Brazilian Federal Loans Contracted in France (Fr. v. Braz.), Judgment, 1929 P.C.I.J. (ser. A)

Another early case of the necessity defence in the investment context is the "*Societe Commerciale De Belgique" Belgium v Greece*, which shows the confusion of such a defence. In this case, the main case question was whether the Greek government could mitigate, defer or avoid its debt by using the state necessity defence. The PCIJ rejected the state necessity defence and ordered the Greek government to pay its debt to the French railway company.[391] Regardless the Greek government's weak financial situation, the court emphasised on the need to balance all the interests. The court stated that "the legitimate interests of the company, the ability of Greece to pay and the traditional friendship between the two countries" should be balanced.[392] Nevertheless, the court eventually held that the obligation to meet treaty obligations outweighed the severity of high national debt. It appears that there is restriction in using the necessity that before the ILC articles formulated the restricted criteria of using the necessity plea, the international tribunals restricted the use the necessity plea.

Also, in the case of Gab`eikovo-Nagymaros Project ("GN-Project"), the ICJ acknowledged the legitimacy of the state necessity defence and stated that such a defence is an extremely narrow issue. It also clarified that the necessity defence does not stop the treaty but avoids state responsibility in severe circumstances. The ICJ added that the state necessity defence seized the state to comply with the treaty obligations. The standard for using the state necessity defence is based on the degree of danger that threatens the state's essential interests. A state's essential interests can be, to maintain its internal peace, the ecological preservation of some or all of its territory and the survival of a part of its population. The ICJ is stricter in circumstances that involve grave danger to the state's economic or political stability.[393] This reflects the restricted criteria of using the necessity defence.[394] It is also seen in the modern era of necessity.

The most recent ICISD recent case is *Unión Fenosa Gas, S.A. v. Arab Republic of Egypt* where the dispute resulted from the Egyptian revolution in 2011. In this case there was no necessity provision in the treaty.[395] Thus, Egypt raised the necessity defence under customary

[391] Arbitral Tribunal of Permanent Court of International Justice.
[392] Societe Commerciale de Belgique (Belg. v. Greece), Judgment, 1939 P.C.I.J. (ser. AlB) No. 78
[393] Gabcikovo-Nagumaros Project (Hung. v. Slovk.), 1997 I.C.J. 3 (Order of Feb. 5)
para. 52
[394] Article 33 of state necessity that is adopted by first reading of ILC
[395] *Unión Fenosa Gas, S.A. v. Arab Republic of Egypt* (n 135)

international law. It referred to the conditions of Article 25 of necessity.[396] The respondent argued that the national electricity prioritisation was the "only way" to safeguard essential interests of Egypt from a grave and imminent peril. The tribunal held that respondent has the burden to prove all elements and claimant has to disprove them. Tribunal examined the "only way" element in Article 25(1) (a) of the ILC Articles. It found that the non-supply of gas to the plant was not attributable to the social unrest and Egyptian revolution. Also, the tribunal examined the Article 25(1) (b) of the ILC Articles "essential interest" against a grave and imminent peril. It found that the issue is not related to public safety, it is related but to the gas shortage in Egypt. The inequity between demand and supply was not caused by Egyptian revolution. [397]

Also, tribunal examined "Contribution to the situation of necessity" Article 25(1) (b) of the ILC Articles. It found that the state had not contributed to the revolution. However, the tribunal viewed that it was unnecessary to refer to the contribution element as there were other elements of necessity defence were met. Thus, the plea of necessity was rejected.[398]

Accordingly, we can see that there is a lack of understanding of how the criteria of necessity defence works. The necessity defence was rejected although the condition of Article 25 (2)(b) of the ILC Articles "Contribution to the situation of necessity" was not met. This raised the question of why the tribunal did not give importance to the contribution condition although it is listed in the criteria of necessity. This raise the question of whether conditions to meet the necessity can be considered separately or all together. It appears that there is no guidance on whether all the conditions should be fulfilled or not. This can attribute to the problems of under-defined law where broad law that invites selective enforcement. This vagueness made tribunal to decide to under-enforce the condition of "Contribution to the situation of necessity" Article 25(1) (b) of the ILC Articles.

Both over and under-enforcement theories can explain why tribunal put more important to certain conditions than other conditions. It might be because tribunal of *Unión Fenosa Gas* was

[396] Egypt argued that such a defence has been recognized in the case of Continental Casualty v. Argentina (2008) and Gab kovo-Nagymaros (1997).
[397] ibid
[398] *Unión Fenosa Gas, S.A. v. Arab Republic of Egypt* (n 135)

trying to square the law with the facts of the case to render its own notion of justice. Hence, the tribunal narrowed the necessity defence and protecting more the investors' interests.[399] The over-enforcement theory can explain that in some cases adjudicators can over enforced the rules by not considering the state's irregular situation.

Generally, the right of states to take necessity action is not limited to war and military action. It includes other emergency situations such as economy crisis where it qualifies under doctrine of necessity.[400] This is reflected in modern era of the necessity defence the Argentina's investment arbitration cases resulted from its fiscal and economic crisis in the late 90s.[401] To stop economic recession, changes in the political leadership (new government) and social unrest took place. Moreover, the government presented a legislation that enabled contract renegotiation with the public services providers who were foreign investors, reformed the exchange system for the foreign currency, which led to severe losses for the foreign investors and limited the transfers out of the country territory. The economic crisis and other social issues forced the government to change the concessions provided to the foreign investors. Also, this crisis affected the rule of law and order in the state.[402]

As a result, Argentina used the state necessity defence to be exempted from its international obligations during its economic crisis. Argentina debated that its emergency measures did not establish a breach of its obligations under the treaty. Even if they did breach its international obligations, the state should be exempted from its liability since "... the very existence of the Argentine State was threatened by the events that began to unfold in 2000."[403] From the point of view of Argentina, the state's acts were to maintain financial, economic and social stability.

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[399] ibid

[400] Subedi, *International Investment Law Reconciling Policy and Principle* (n745)

[401] *CMS Gas Transmission Company v Argentina*, ICSID ARB/01/8, Award of 12 May 2005; *Enron Corporation and Ponderosa Assets, L.P. v Argentina*, ICSID 01/3, Award of 22 May 2007; *LG&E Energy Corporation et al. v Argentina*, ICSID ARB/02/1 Award of 25 Jul ,2006; *Sempra Energy International v. Argentina*, ICSID Case No ARB/02/16, Award of 28 September 2007 ; *Continental Casualty v Argentina*, ICSID Case No ARB/03/9,Award of 5 Sep 2008; *El Paso Energy International Company v Argentina*, ICSID ARB/03/15, Award of 31 Oct 2011; *BG Group v Argentina*, *ad hoc* arbitration pursuant to UNCITRAL Rules, Award of 24 Dec 2007; *National Grid v Argentina*, *ad hoc* arbitration pursuant to UNCITRAL Rules, Award of 3 Nov 2008

[402] Ibid.

[403] *CMS Gas Transmission Company v Argentina*., paras. 304−305 (n401)

Scholarly writing paid great attention to whether the necessity defence could be used in the investment arbitration.

Despite the fact that all arbitral tribunals on Argentina agreed on the required conditions in order to invoke Article XI.[404] In addition, all the disputes were raised from the same facts and most of them were based on the Argentina-US BIT.[405] Nevertheless, the tribunals reached different conclusions on the necessity application. Some tribunals justified the use of the necessity defence while other tribunals refused to consider financial crisis as an excuse to allow states to be exempted from their obligations.[406] This makes scholars to argue that the state practice of the necessity defence creates a questionable foundation of confusion and inconsistency. [407] Accordingly, it is important to examine root causes of inconsistent decisions. This requires examining how the arbitral tribunals in the Argentina cases used the criteria of state necessity under customary international law into treaty law.[408]

4.4 Criteria of state necessity in Argentina case

4.4.1 Essential security

It is debatable who decides if the state's essential interests are at stake or not. Many multilateral agreements give this role to the state, but some BITs do not include clear language of self-judging.[409] Consequently, some tribunals rejected the clauses of essential security due to the lack of clear language on self-judging.[410] This is reflected in the Argentine case in which all tribunals agreed that Article XI is not a self-judging provision due to lack of clear language.

[404] ARTICLE XI: This Treaty shall not preclude the application by either Party of measures necessary for the maintenance of public order, the fulfilment of its obligations with respect to the maintenance or restoration of international peace or security, or the Protection of its own essential security interests; also see Tarcisio Gazzini, 'Foreign Investment and Measures Adopted on Grounds of Necessity: Towards a Common Understanding' (2010) 7(1) Transnational Dispute Management

[405] Treaty Between the United States of America and the Argentine Republic Concerning the Reciprocal Encouragement and Protection of Investment (signed 14 November 1991, entered into force 20 October 1994) (US–Argentina Treaty).

[406] Catherine H Gibson, 'Article Beyond Self-Judgment: Exceptions Clauses in Us Bits' (2015) 38 Fordham Int'l L.J. 1

[407] Brown and Miles, *Evolution in Investment Treaty Law and Arbitration* (n374)

[408] Generally, there was a coordination of Draft Article 25 and Article XI (treaty provision).

[409] 'Self-judging clause' means the state will be the sole arbiter to determine its essential interests. It is a way to exempt the state from the international obligations from the unilateral acts.

[410] Yannaca-Small, 'International Investment Perspectives: Freedom of Investment in a Changing World' (n27)

The *CMS* tribunal stated that "when States intend to create for themselves a right to determine unilaterally the legitimacy of extraordinary measures importing non-compliance with obligations assumed in a treaty, they do so expressly."[411] Along these lines, the *Enron* tribunal stated that "truly exceptional and extraordinary clauses such as a self-judging provision normally must be expressly drafted to reflect that intent, as otherwise there can be a presumption about not having that meaning in view of its exceptional nature."[412] The *LG&E* tribunal reached a similar the same decision, stating that the provision is not self-judging.[413] Thereby, the vagueness of Article XI made tribunals in the Argentine case reject considering Article XI as an NPM clause.[414] This can contribute to the problems of under-defined law in which broad law invites selective enforcement.

It is also important to answer the question of whether economic emergency can be considered an essential security interest. The answer is shown in these four cases, *CMS v Argentine Republic*, *LG&E v Argentine Republic* ، *Continental Casualty v Argentina*, *Sempra v Argentine Republic* and *Enron v Argentine Republic*[415], which occurred due to the economic crisis that Argentina faced in 2000. The state of Argentina contended that it should be excused from its international responsibility on the legal ground of a state emergency or necessity. Although the tribunals of these cases agreed that economic interest is to be applied to essential security provisions, the arbitral tribunals reached dissimilar conclusions regarding the concept of state necessity. Accordingly, there was disagreement amongst the arbitral tribunals about the liability issue. The tribunals reached the same decision in the *Enron*, *Sempra* and *CMS* cases[416], but in the *LG&E* and *Continental Casualty* cases, the tribunals arrived at a different conclusion[417], despite the fact that it was the same government with similar facts in which the tribunals interpreted the same treaty.[418] These tribunals arrived at dissimilar conclusions on

[411] *CMS Gas Transmission Company v Argentina Enron Corporation. v Argentina; Sempra Energy International v. Argentina* (n401).
[412] *Enron Corporation v. Argentina* (n401)
[413] *LG&E Energy Corporation et al. v.Argentina* (n401)
[414] *LG&E*, Decision on Liability of 3 October 2006, para. 255; *Enron*, Award of 22 May 2007, para. 333-334; *Sempra*, Award of 28 September 2007, paras. 374-375.
[415]*CMS Gas Transmission Company v Argentina Enron Corporation. v Argentina; Sempra Energy International v. Argentina* (n401)
[416] ibid
[417] *LG&E Energy Corporation et al. v. Argentina; Casualty v Argentina*; (n401)
[418] All tribunals interpreted the same treaty provisions in the BIT between the US and Argentina, including Article XI of the BIT, which provides: 'This Treaty shall not preclude the application by either Party of measures necessary for the maintenance of public order, the fulfilment of its obligations with respect to the maintenance or restoration of international peace or security or the protection of its own essential security interests'.

this criterion.[419]These tribunals examined essential security with grave and imminent peril requirements. The disagreement between tribunals was the degree of the economic crisis.

4.4.2 Grave and imminent peril requirements

To be successful, the necessity invocation requires the state to show that it was facing grave and imminent peril. The circumstances should be endangering to the state's essential interest. However, as previously discussed there was disagreement on the degree of crisis gravity. In the *Enron, Sempra* and *CMS* cases, the tribunals noted that Article XI of the treaty did not precisely define the conditions of its use, so customary law rules had to be used as a subsidiary source of law. Therefore, these tribunals applied requirements of Grave and imminent peril under Draft Article 25 as expression of customary international law for the state necessity defence into the Article XI. Accordingly, *Enron, Sempra* and *CMS* tribunals concluded that although there was a severe crisis faced by Argentina, it did not cause total social and economic collapse. Thus, state was not exempted for its liability and had to pay compensation.[420]

Consequently, over-enforcement theory can explain *CMS, Enron and Sempra* tribunals' view on seeing justice by over-enforcing the requirement of essential security and narrowing the state policy in response to the emergency crisis. These tribunals protected the investor's interest more than the state's interest. A state will be liable to foreign investors for any damages resulting from its essential policy response to an emergency crisis.

In contrast, the *LG&E* tribunal reflected Article XI of the BIT and the state necessity defence in the customary international law separately; it did not look at the requirements of customary international law. These tribunals, referred to the treaty provision standalone (Article XI). *LG&E* tribunal noted that Article XI is enough to exempt Argentina from its international liability. The *LG&E* tribunal considered the crisis severe enough to threaten "total collapse of the Government and the Argentine State' and stated that, 'from 1 December 2001 until 26 April

[419] Andrea Bjorklund, '*Emergency Exceptions'* in Peter Muchlinski, Federico Ortino and Christoph Schreuer (eds), *The Oxford Handbook of International Investment Law* (Oxford University Press 2008).
[420] *CMS Gas Transmission Company v Argentina Enron Corporation. v Argentina; Sempra Energy International v. Argentina* (n401)

2003, Argentina was in a period of crisis during which it was necessary to enact measures to maintain public order and protect its essential security interests." [421]

The *LG&E* tribunal found that the state should not be liable for damages to foreign investors during the emergency times. It appears that the *LG&E* tribunal determined justice by under-enforcing the state's obligations towards investors during the crisis times. Thus, a state should not be accountable for damages to foreign investors during emergencies. The tribunal has clarified that the purpose of the clause is not to excuse states from liability, but to give them the freedom to take the necessary measures to maintain public order during emergencies.[422] The under-enforcement theory can provide that *LG&E* tribunal attempted to balance between both the rights of the host state and foreign investors by under-enforcing the state's international obligation during the crisis times only. *Continental Casualty* tribunal reached similar conclusion to the *LG&E* tribunal.[423]

Nevertheless, it is essential to highlight that despite the guidance provided by ICJ judgment on the *Gabčikovo-Nagymaros* case while evaluating the gravity and imminence of a peril, the tribunals of the Argentine cases did not rely on it. They were not willing to conduct a substantiated and methodological assessment of the extent of the economic crisis. Some tribunals even completely stopped from figuring out whether this condition was satisfied as they had already found that the other more easily demonstrable components of necessity were not established.[424]

We can infer that the outcome of necessity rules interpretations is not the same among different tribunals. This might be because tribunals interpret the textual language based on their views of the meaning of words. This might be because of absence of guidance on using treaty law and customary international law to assess legality of necessity defence. It appears that requirements of Grave and imminent peril under international customary law are established in rigid manner. On the other hand, it appears that the requirements of necessity defence in general under the treaty provision are established in lenient manner. Therefore, tribunals select the source of law that fit their own notion of justice. This can attribute to the problems of broad

[421] *LG&E Energy Corporation et al. v. Argentina* (n401)
[422] *LG&E Energy Corporation et al. v. Argentina* (n401)
[423] *Continental Casualty v Argentina,* (n401)
[424] *National Grid PLC* v Argentina (n401)

law that invites selective interpretation. Thus, theories of over-enforcement and under-enforcement can explain the lack of guidelines on how applicable a source of law is. This invites selective interpretation. Accordingly, the question of state's liability during the emergency times depends on the applicable law. This caused the tribunals' decisions to be divided into two groups concerning the matter of graveness and imminence of the peril.

4.4.4 The "only way" requirement

This criterion of the state necessity defence appears that it will not be applied once there are other available means even if they are less convenient or costlier.[425] As a result, *CMS*, *Enron* and *Sempra* tribunals interpret the rigid requirement of "only way" Draft Article 25 as expression of customary international law. The *CMS*, *Enron* and *Sempra* tribunals found that Argentina would not be excused from its obligations since the requirements of state necessity had not been met.[426] *Enron* tribunal illustrated that arbitration should not substitute the government's economic choice but only assess whether such a choice was the only available one.[427]

Generally, it is debatable if it is the only available way or not and whether the requirements of state wrongfulness have been met or not. One can argue that such a standard would fail to be tested under Article 25 simply because there will always be a debate on other alternatives. It appears that Article 25 stipulate rigid rules. However, there should be permit a lenient interpretation to the "only way" requirement for the purpose of allowing the practical application of the concept of necessity in economic emergencies cases; otherwise, it will be rarely available to use due to the strictness of the interpretation. Accordingly, the over-enforcement theory can explain that *CMS*, *Enron* and *Sempra* tribunals see justice through applying rigid rules of customary international law and narrowing the application of state necessity. This makes scholars such as Brown and Miles to argue that tribunals had applied

[425] This is as per the rules of state necessity which is codified in Article 25(2)(a) ILC Articles on State Responsibility; also see August Reinisch, *Netherlands Yearbook of International Law: Necessity Across International Law* (Cambridge University Press 2010)
[426] CMS Gas Transmission Company v Argentina Enron Corporation. v Argentina; Sempra Energy International v. Argentina (n401).
[427] *Enron v Argentina* para. 309 (n401)

this criterion without considering the state pressure, informational limitations and severe time constraints. [428]

In contrast, other tribunal, such as the *LG&E*, reached a different conclusion; the tribunal did not evaluate whether the state measures were the merely ways to deal with the crisis. Instead it noted that any economic recovery package was essential to address the crisis. Furthermore, the tribunal noted that any other economic policy would not place the claimant in a better position. [429] The under-enforcement theory can explain that *LG&E* tribunal refused to enforce the legal rules where the legislature intended to enact and considered the state's irregular situation to provide more justice. The *LG&E* tribunal relied on Article XI of the US-Argentina BIT. The tribunal noted that Argentina did not violate its duties under the BIT. [430] Also, *Continental Casualty* tribunal reached similar conclusion to the *LG&E* tribunal.[431]

Accordingly, tribunals' decisions can be divided into two groups regarding the matter of "only way" requirement. This might be because rules of necessity are stricter under customary international law than treaty law. At the same time, there is a lack of guidelines on how applicable a source of law is. This invites selective interpretation.

4.4.5 Non-contribution to necessity

This criterion of necessity requires the state to prove that it has not contributed to the crisis.[432] The tribunals disagreed about the principle of state contribution to a state of necessity. The *LG&E* tribunal interpreted requirements of non-contribution to necessity under treaty provision (Article XI). The *LG&E* tribunal held that there was absence of solid evidence to prove that Argentina had contributed to the crisis.[433] Accordingly, it found that Argentina was justified.[434]

It is also significant to mention that *Continental Casualty* tribunal did not assess whether Argentina's policies contributed to the crisis but whether these policies were reasonable at the

[428] Brown and Miles, *Evolution in Investment Treaty Law and Arbitration* (n374)
[429] *LG&E Energy Corporation et al. v Argentina* (n401)
[430] *Casualty v Argentina* (n401)
[431] *Continental Casualty v Argentina,* (n401)
[432] This is as per the rules of state necessity which is codified in Article 25(2)(b) ILC Articles on State Responsibility.
[433] *LG&E Energy Corporation et al. v Argentina* (n401)
[434] Ibid.

time.[435] The under-enforcement theory can explain that *Continental Casualty* tribunal see justice through under-enforcing the rigid rules of the "non-contribution to necessity" under Article 25. The *Continental Casualty* tribunal attempts to provide more justice by making its decision on assessing the reasonability of taken policies. Also, as the tribunal of *Continental Casualty* justified the Argentina's economic policy. It mentioned that the former financial policies of Argentina were recognised by the international financial community as a beneficial economic policy especially those policies recommended by the IMF.[436] So how was Argentina mistaken in revising such policies? Should modifying successful policies be counted as wrong action?

On the contrary, the *CMS* tribunal found that there was a shortage of governmental policies that contributed to the crisis significantly. The tribunal of *CMS* relied on the rigid rules of Art.25 of the ARISWA. [437] The tribunal stated that "the government policies and their shortcomings significantly contributed to the crisis and the emergency and while exogenous factors did fuel additional difficulties, they do not exempt the Respondent from its responsibility in the matter"[438] The same approach was adopted by the *Sempra* and *Enron* tribunals.[439]

Accordingly, both theories of over-enforcement and under-enforcement can explain that the requirement of "non-contribution to necessity" under customary international law resulted to restrictive interpretation. This is reflected in the decisions of *CMS, Sempra* and *Enron* tribunals, in contrast to the necessity rules under treaty law. It applies less restrictive interpretation which is reflected in the decision of *LG&E* tribunal. Accordingly, the question of state's liability during the emergency times depends on the applicable law. The Tribunals' decisions have been divided into two groups on matters relating to the crisis. We can infer that there is a lack of guidelines on how applicable a source of law is. This invites selective interpretation. Adjudicators can select the source of law that renders their own notion of justice.

[435] *Continental Casualty v Argentina*, (n401)
[436] ibid
[437] *CMS Gas Transmission Company v Argentina* (n401).
[438] Similar conclusions were reached in *Enron*, Award of 22 May 2007, paras. 311−312; *Sempra*, Award of 28 September 2007, paras. 353−354.
[439] *Sempra Energy International v Argentina and Enron Corporation v Argentina* (n401).

Also, Brown and Miles explained that the *CMS* and *Enron* tribunals confirmed that "contribution does not necessarily have to be made by the current administration and may be attributed to former administration." Over-enforcement theory can explain that that *CMS* and *Enron* tribunals over enforced the rules of necessity. On the other hand, the *LG&E* tribunal reviewed the current administration alone and under-enforced the past administration policies.[440] Therefore, assessing the actions and policies of the former and current administration and the effects domestic and international causes had on the crisis creation or whether it was permissible to invoke the state to change such policies remains vague. [441] This might be because adjudicators might over or under-enforce the law because they are trying to square the law with the facts of the case to render their own notion of justice.

Finally, the Article 25(2) (a) criteria of international obligation in question excludes the possibility of invoking necessity; or Article 25 (1) (b) does not seriously impair an essential interest of the state or states towards which the obligation exists or of the international community as a whole. These factors did not take the attention of the tribunals, these conditions were unenforced. It appears that that they agreed that Argentina's acts did not endanger the international community interests and other states.[442]

Also, the compensation issue is vague. BITs only address compensation for losses suffered under particular circumstances. They do not require payment of provide guidelines for measuring compensation.[443] This seen in the clause is contained in the Argentina-US BIT.[444]

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[440] Brown and Miles, *Evolution in Investment Treaty Law and Arbitration* (n374)

[441] ibid

[442] *CMS*, Award of 12 May 2005, para. 325; *LG&E*, Decision on Liability of 3 October 2006, para. 257; *Enron*, Award of 22 May 2007, para. 310; *Sempra*, Award of 28 September 2007, para. 352.(n 401)

[443] Note, however, that some provisions of this kind, particularly in the BITs concluded by the UK, include a second part that requires adequate compensation for certain types of losses. For example, Article 4(2) of the Bahrain-UK BIT (1991) provides:

> (2) Without prejudice to paragraph (1) of this Article, nationals or companies of one Contracting Party who in any of the situations referred to in that paragraph suffer losses in the territory of the other Contracting Party resulting from:
> (a) requisitioning of their property by its forces of authorities, or
> (b) destruction of their property by its forces or authorities, which was not caused in combat action or was not required by the necessity of the situation,
> shall be accorded restitution or adequate compensation. Resulting payments shall be freely transferable.

[444] Article IV(3) of the Argentina-US BIT, a provision that is representative of the clauses of this type, was invoked by the respondent in the Argentinean cases. Article IV(3) states: 'Nationals or companies of either Party whose investments suffer losses in the territory of the other Party owing to war or other armed conflict, revolution, state of national emergency, insurrection, civil disturbance or other similar events shall be accorded treatment by such other Party no less favorable than that accorded to its own nationals or companies or to

The BITs are concerned with compensation for losses experienced in the event of riots, armed conflicts, insurrections and 'state of national circumstances. [445]However, they only determine the foreign investor's right to non-discriminatory treatment. Thus, the substantive question is left unanswered.[446] This can contribute to the problems of under-defined law when broad law invites selective enforcement.[447] On the other hand, the customary law does not provide clarity on such matters. For instance, ILC Article 27 determines the consequences of successful invocation of the necessity defence and other circumstances precluding wrongfulness.[448] However, the problem is Article 27 does not provide clarity on the requirement to provide compensation in all circumstances. This is reflected in the *LG&E* award, in which the tribunal noted that Article 27 does not determine whether any compensation was payable to the party affected by losses, what kind of losses could be compensated for and in what circumstances the compensation should be payable.[449] This can also contribute to the problems of under-defined law when broad law invites selective enforcement and result to inconsistent decisions

Therefore, both over and under-enforcement theories can explain that due ambiguity of laws. The criteria of necessity under customary international law are subjective and open to different interpretations. Arbitrators will make their decisions on what they perceive as reasonable and equitable in the situations of a certain case. This can result that arbitrators can choose to over- or under-enforce the law based on their discretion. There is increased likelihood that dispute outcomes will be balanced, but it will be difficult to predict the outcome. Also, the different sources of law in the treaty provisions and customary international law are causing confusion. There is a lack of guidelines on how applicable a source of law is. Some tribunals noted that Article XI of the treaty did not precisely determine the conditions of its use, so customary law rules had to be applied as a subsidiary source of law. On the other hand, other tribunals under-

nationals or companies of any third country, whichever is the more favorable treatment, as regards any measures it adopts in relation to such losses' (emphasis added).

[445] This last circumstance makes such provisions relevant to economic turmoil such as Argentina's circumstances in the early 2000s.

[446] See Sergey Ripinsky, 'State of Necessity: Effect on Compensation' (2007) Research Fellow in International Law, British Institute of International and Comparative Law. <http://ssrn.com/abstract=1546991>. [2007]

[447] See Article 15 of the (2002) BIT between Austria and Libya contains such an extended war clause; also see Article 5 Compensation for Losses in (1980) BIT between Sri Lanka and the United Kingdom

[448] ILC Article 27 provides: 'Consequences of invoking a circumstance precluding wrongfulness. The invocation of a circumstance precluding wrongfulness in accordance with this chapter is without prejudice to: [...]
(b) The question of compensation for any material loss caused by the act in question' (emphasis added).

[449] *LG&E et al v Argentina.* (n401).

enforced the customary law rules and relied on treaty law. Accordingly, there is laws ambiguity that creates selective enforcement that result to inconsistent decisions.

4.5 Effects of conflicting jurisprudence

The phenomena of conflicting arbitral decisions can affect the legitimacy of the whole system. A real dilemma is realised in the way different arbitral tribunals addressed the Argentina case. Despite the mutual understanding of these tribunals on the conditions that constitute the ground of necessity, each of them applied the emergency clause in an incoherent and inconsistent manner. Argentina's crisis raised controversial questions about the nature, existence and permissibility of the state necessity defence.[450] Argentina's case demonstrated the degree to which a new government is allowed to take necessity measures in response to an emergency or crisis. However, it does not provide clear answer because of the conflicting awards.

This makes scholars such as Martinez argue that these conflicting opinions of the tribunals regarding the use of state necessity had a negative impact on foreign investors. It further undermines the confidence in the investment arbitral tribunal. [451] This uncertainty can weaken the authority of the international investment arbitration, which might discourage parties from referring to the international arbitration institutions.[452] Burke-White demonstrated that countries such as Bolivia exit the ICSID system because of these reasons. Therefore, the investor-state arbitration system could be in a crisis of losing its confidence. If states and investors lose confidence in the system, they will not consent to it.[453]

Thus, Franck explained that such uncertainty in the investment treaty system hurts the legitimate expectations of both sovereign states and investors. Eventually, this will negatively affect the existence of international investment treaties and the international legal order. The application of the rule of law has to be clear and consistent otherwise its legitimacy will be in

[450] Sloane, 'On the Use and Abuse of Necessity in the Law of State Responsibility' (n 27)
[451] Martinez, 'Understanding the Debate Over Necessity' (n370)
[452] Franck Thomas, *The Power of Legitimacy Among Nations* (Oxford University Press 1990)
[453] ibid

a crisis. Therefore, it is important to understand the elements that affect the legitimacy of the system.[454]

The concept of legitimacy depends on different factors such as coherence and determinacy. This results in reliability and predictability and other concepts such as justice, accountability, fairness and representation. The absence of these concepts prevents investors and governments from understanding how to obey the law. Consequently, it will undermine its legitimacy. The concept of determinacy is the way in which the rules are transparent and clear in the international arbitration system. In reality, the current arbitration system has many rules that are undetermined and hard to predict. This makes it easy to justify noncompliance. The concept of coherence is another factor of legitimacy. It necessitates the interpretation and use of rules to be consistent in order to promote justice and fairness.[455]

Accordingly, Thomas argued that the concept of inconsistency requires the rules to be applied in a uniform manner in each case. Consequently, dissimilar application of the same rule is undermining the legitimacy of the whole system. Therefore, the lack of the concepts of determinacy and coherence in investment treaty arbitration has created a legitimacy crisis.[456] However, according to the Koskenniemi argument, fragmentation cannot be inevitable.[457] Thus, at least we need to have more harmonised arbitral awards. This is raising the questions of how could this happen? Therefore, it is important to examine how scholars attempt to address fragmentation problem. Some scholars tried to define reasons behind such fragmentation. Other scholars presented different suggestions to harmonised arbitral decisions.

4.6 Addressing fragmentation of the international investment law

Scholars highlighted that the conflicting decisions on necessity result from the criteria of necessity. Subramanian clarified that one of the conditions for a successful necessity defence

[454] Franck, 'The Legitimacy Crisis in Investment Treaty Arbitration' (n 342)
[455] ibid
[456] Thomas, *The Power of Legitimacy Among Nations* (n427)
[457] *Fragmentation of International Law: Difficulties Arising from the Diversification and Expansion of International Law* – Finalized by Martti Koskenniemi (A/CN.4/L.682), 13 April 2006, para 24

under customary rule is to prove that the state has not contributed to the necessity situation, this is very controversial. It causes confusion because identifying the extent of state contribution to the crisis has been applied differently among arbitral tribunals. For example, the *CMS* tribunal found that Argentina contributed to the crisis in a significant manner, while the *LG&E* tribunal reached a different decision. [458] Also, Sloane clarified that the ILC articles on state necessity are unclear and defined in a negative manner because of its broad textured language, it is difficult to identify which article assists more than another. It leads to many different interpretations.[459] There is uncertainty in Article 25 regarding whether foreign investors or the state should bear the loss.[460]

Unfortunately, arbitrators do not start the reconstruction task of what the ILC work should look like. This might be because simplifying the work of the ILC is complex job.[461] Thus, lack of clear secondary rules (international customary law) is causing dilemma. As Hart clarified, the absence of a secondary rules system provides a lack of understanding on how primary rules are made, interpreted and then applied.[462]

Furthermore, Sornarajah, one of the leading scholars in international investment law, criticised the criteria of necessity such as contribution to the situation of necessity on the ground that no state will adopt policies with the intention of contributing to its crisis.[463] Sornarajah argued that the high requirements for successful necessity application could potentially ruin the necessity defence of the treaty.[464] It is unreasonable for states to rely on the criteria of state necessity defence because it has to prove that there were no other available options regardless of the fact that these other options could be less convenient and more costly.[465] This makes scholars such as Caron to argue that codifying the ILC is at risk, and there is a need for a better approach in providing more clarity and guidance. Caron illustrated the argument of other scholars such as Crawford that there is a need for a sustained legal development process and flexibility rather than controversial and uncertain features of the texts.[466]

[458] Subramanian, 'Too Similar or Too Different' (n27)
[459] Sloane, 'On the Use and Abuse of Necessity in the Law of State Responsibility', (n 27)
[460] ibid
[461] Caron, 'The ILC Articles on State Responsibility' (n 27)
[462] Herbert Lionel Hart, *The Concept of Law* (Oxford University Press 1961) viii, 263, 21s
[463] Sornarajah, *The International Law on Foreign Investment* (n 1)
[464] ibid

[466] Caron, 'The ILC Articles on State Responsibility' (n 27)

Also, Reinisch supported Subramanian's argument that the criteria of state necessity defence are complex. The Argentina case demonstrated that the criteria of state necessity defence is difficult to apply. This means that there is always a little chance of the non-fulfilment under the obligations of BITs.[467] However, it is debatable that the reason of this rigid criteria of necessity in the ILC Drafted Articles is to make the state necessity defence rarely used as an excuse of non-performance of an international obligation and to be limited in a strict manner to the safeguards against any abuse. [468]

Martinez clarified that the ILC set restrictions for the admissibility of necessity in order to avoid possible abuse of necessity.[469] However, these restrictions are not enough there should be certain standards in order to prevent the misuse of the ILC in the use of the state necessity defence. The necessity should only be used to protect many of the state's interests to safeguard the environment and preserve the safety of civilians in a public emergency. [470] Also, Yannaca-Small expressed concern for the states misusing of the ILC Drafted Articles on the state responsibility. Thus, Yannaca-Small cited the Crawford argument that states should avoid the misuse of state necessity defence. A state must use the necessity defence only when they have complete knowledge of the actualities and have consciously chosen a way that does not breach international obligations.[471]

Other scholars argued that various source of law is seen as the reason behind inconsistency of the necessity application. Amerasinghe demonstrated that international investment law is derived from classical international law. This includes the provisions of public international law, rules of state responsibility under the ILC's articles on state responsibility, and the rules under investment arbitration.[472] This explains that the interpretation and use of international

[467] August Reinisch, *Necessity in Investment Arbitration* (Cambridge University Press 2011)
[468] ibid
[469] Martinez, 'Understanding the Debate Over Necessity" (n346)
[470] ibid
[471] Yannaca-Small, "International Investment Perspectives: Freedom of Investment in a Changing World" (n27)
[472]Chittharanjan Felix Amerasinghe, *Local Remedies in International Law* (2nd edn, Cambridge University Press 2004); also, see Vienna Convention on the Law of Treaties, 1155 UNTS. 331; 8 ILM. 679 (1969), International Law Commission, *Draft Articles on Responsibility of States for Internationally Wrongful Acts*, November 2001, Suppl No. 10 (A/56/10), chp.IV.E.1

investment law are integrated with other areas of international law.[473] Such integration causes inconsistency in interpretation, which makes arbitral awards unpredictable. Also, there is strict limitation where arbitral tribunal always refers to investment treaty provisions and customary international law to examine the validity of the state necessity defence. [474] However, the problem is that the ILC Drafted Articles do not command the status of a treaty but are accepted as an authoritative statement. This invites selective enforcement.[475]

Other scholars found that conflicting decisions on necessity result from the textual language of the BITs and the general features of the system of investment arbitration. Subramanian highlighted the arguments of other legal scholars such as Ripinsky and Williams who argued that many of the current investment agreements define the provisions of the necessity defence scope in a similar way but in a different language. This has resulted in different interpretations and caused the problem of fragmentation in international investment law. Furthermore, the definition of essential security interests differs from one treaty to another and sometimes from one treaty to another of the same state.[476]

This makes scholars such as Franck to recommend changing the texts of investment treaties and listing the substantive rights of the investors.[477] However, Subramanian highlighted the problem of renegotiating the text of the treaty to revise the emergency commitments. The complexity is because of the numerous BITs between several countries, which mean that it might take several years to implement such a recommendation. In addition to the clarification of all the possible future matters of the necessity clause, interpretation might not be feasible. This is because the relationship between the treaty and customary international law will be useful in settlement matters.

Other scholars such as Subramanian argued that the problem of conflicting decisions results from a lack of appeal, reviewing system and binding precedents system.[478] However, due to

[473] Philippe Sands, 'Custom, Treaty, Cross-Fertilisation of International Law' (1998) 1 Yale Human Rights & Development Law Journal 3
[474] Susan D Franck, 'The Legitimacy Crisis in Investment Treaty Arbitration: Privatizing Public International Law Through Inconsistent Decisions' (2005) 73 Fordham Law Review 1521
[475] Roman Boed, 'State of Necessity as a Justification for Internationally Wrongful Conduct' (2000) 3 Yale Human Rights & Development Law Journal 1
[476] Subramanian, "Too Similar or Too Different" (n27)
[477] Franck, 'The Legitimacy Crisis in Investment Treaty Arbitration' (n 449)
[478] Subramanian, 'Too Similar or Too Different'(n27)

the absence of a precedents system and the shortage of annulment procedures, there is doubt on whether there will be consistency in interpretation in the future. Hence, Cubb recommended establishing an appellate body for the international investment arbitration system, such as the world trade organization (WTO) appellate system, which could enhance the stability and clarity of state necessity defence. [479]

This is similar to Frank's recommendations on the existence of an appellate mechanism in order to avoid the inconsistency in tribunal decisions on the state necessity defence. The use of such a system will not be realised until the establishment of a permanent appellate court, which will allow the legal fault to be corrected. It is important for scholars to fulfil this gap by harmonising public international law. The concept of arbitration can achieve its purpose on justice-promoting and assist the law to be established in an equitable and harmonised manner.[480] Also, Kohler demonstrated that the absence of a binding system of precedent raises the question of how arbitrators refer to the earlier cases and gain guidance to reach their decisions. Implementing the precedents system in the ICSID will benefit both parties and encourage foreign investments.[481] Furthermore, Schreuer argued that there is a necessity for a coherent case law as it will improve the predictability of arbitral tribunal decisions. The inconsistency of the ICSID arbitral decisions illustrated that the ICSID system needs reform. There must be a binding precedent system to ensure that the doctrine of necessity will used by arbitral tribunals in a uniform manner. It will help equilibrium the rights of investors against the powers of the state.[482]

Moreover, Bart recommended that to avoid such inconsistencies in arbitral tribunal decisions on the state necessity defence, there must be a system of law instead of a set of arbitrary decisions. Bart pointed that the ICSID Convention needs to clarify what constitutes a valid necessity argument; therefore, there is a need for amendments in the ICSID Convention.[483] Furthermore, Bart demonstrated that the current investment arbitration system is polarised with non-hierarchical, conflicting and disagreeing decisions. This requires a common understanding

[479] Chubb, 'The 'State of Necessity' Defense' (n 385)
[480] Franck, 'The Legitimacy Crisis in Investment Treaty Arbitration' (n474)
[481] Gabrielle Kaufmann-Kohler, 'Arbitral Precedent: Dream, Necessity or Excuse?'(2007) 23 Artificial Intelligence and Law 357
[482] Christoph Schreuer, 'Diversity and Harmonization of Treaty Interpretation in Investment Arbitration by' (2006) 3 Transnational Dispute Management
[483] Bart MJ Szewczyk,'Application of the International Convention on the Elimination of All Forms of Racial Discrimination' (2011) 105 American Journal of International Law 547.

of the rules; thus, state parties and law makers should clarify the applicable law for the substantive scope of necessity under BITs. This is because the inconsistent application of the state necessity defence under the customary international law and BITs have raised a concern on major policy issues.[484] Further, it requires the interpretation of necessary measures.[485]

Also, Nolan and Sourgens demonstrated the role of the self-judging clause in balancing the state right to regulate its public order and the treaty clauses.[486] The problem is one tribunal can read this clause means that the state is the only arbiter of applying the necessity measures. Another tribunal can read the clause that each party is the sole arbiter in emergency times.[487] Furthermore, Bart illustrated that the difficulty in defining essential arbitral standards resulted in the inconsistency of the arbitral decisions. It is left for the arbitral tribunals to decide the state's essential interest standards.[488] Consequently, there are various self-judging clauses in the BITs; thus, it is unclear to what extent these clauses can allow the state to be the sole arbiter and to what extent it will be excused from its obligations. Thus, there should be mechanisms that help in assessing essential interests where it should be measured by good faith and a margin of appreciation standards. The ICJ noted that the self-judging clause is subject to good faith obligations, which are codified in Article 26 of the 1969 VCLT. [489] Therefore, Binder recommended establishing institutionalised mechanisms that have the competence to decide the application of necessity.[490]

Also, Claussen recommended the proper use of the source of law regarding the state necessity defence to determine the necessity measures for security interests. The ICSID arbitral tribunals refer to different sources to determine what constitutes a state necessity defence.[491] This makes scholar such as Kurtz to recommend coherence among different sources of law on the use of the state necessity defence. Kurtz explained that treaty and customary defence work differently.

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[484] ibid
[485] ibid
[486] Michael D Nolan and Frédéric G Sourgens, 'The Limits of Discretion? Self-Judging Emergency Clauses in International Investment Agreements' (2011) Yearbook on International Investment Law & Policy 303, 362
[487] ibid
[488] Szewczyk, 'Application of the International Convention on the Elimination of All Forms of Racial Discrimination' (n458)
[489] Nolan and Sourgens, 'The Limits of Discretion' (n 486)
[490] Christina Binder, 'Stability and Change in Times of Fragmentation: The Limits of Pacta Sunt Servanda Revisited' (2012) 25 Leiden Journal of international law 909
[491] Kathleen Claussen, "The Casualty of Investor Protection in Times of Economic Crisis" (2009) 7 YLJ 118

It is hard to say that all the custom elements are placed in the new treaty as there is an obligation towards fair and equitable treatment in a treaty. This means that we have to refer to the customary international law to identify the meaning of rules. However, the problem is that there is a lack of defined textual links to the customary international law in the treaty exception. This is seen in the case of Nicaragua where the ICJ had to rely on the difference between the customary and treaty standards and where it noted that there is an overlap between the two legal sources of law.[492]

Thus, there is a necessity for future arbitrators to develop a defensible and robust method to the relation between customary plea and treaty exception. Further, Kurtz argued that it is more convincing for arbitrators to interpret the treaty defence alone without transplanting it from the customary law.[493] Accordingly, Cubb argued that clarifying the source of law is the first step to reduce the confusion in the usage of the state necessity defence. The international investment system should establish a hierarchical legal system.[494] Multilateral agreements should create procedures that explicitly define the use of the state necessity defence.[495]

Other scholars such as Subramanian recommended looking for a new interpretative methodology that can bring some gains on the usage of the state necessity defence.[496] It is similar to Koskenniemi's argument that fragmentation cannot be inevitable and that interpretative formalism is the only practicable way to diminish incoherence and conflicts.[497] As a result, other scholars such as Cheng found that there should be a balance test to determine the state right to use the state necessity defence.[498] Also, Kingsbury and Schill recommended the use of the proportionality approach to define the proper use of state necessity defence. For Kingsbury and Schill, it is simply a legal interpretation method used in the conflicts between legitimate public policy purposes and different legal principles.[499]

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[492] Jürgen Kurtz, 'Adjudging the Exceptional at International Investment Law: Security, Public Order and Financial Crisis' (2010) 59 International and Comparative law Quarterly l.
[493] ibid
[494] For instance, the US courts model helps differentiate between the primary and secondary sources.
[495] Chubb, 'The 'State of Necessity' Defense' (n 385)
[496] Subramanian, 'Too Similar or Too Different' (n27)
[497] *Fragmentation of International Law: Difficulties Arising from the Diversification and Expansion of International Law* – Finalized by Martti Koskenniemi (A/CN.4/L.682), 13 April 2006, para 24.
[498] Cheng, 'General Principles of Law as Applied by International Courts and Tribunals' (n353)
[499] Benedict Kingsbury and Stephan Schill, *Public Law Concepts to Balance Investors' Rights with State Regulatory Actions in the Public Interest the Concept of Proportionality* (Oxford University Press 2010)

Moreover, Kingsbury and Schill recommended proportionality analysis. It can provide criteria to make tribunals consider the relevant interests under the applicable principle and balance them in a developed framework. It can provide clear assessment and make the tribunals more accountable.[500] Thus, Kingsbury and Schill clarified the structure of the proportionality analysis. It is based on addressing the relationship between the government acts and the tools used to reach the end. The first step is to analyse whether the state measures served legitimate government objectives. The second step is to examine whether it was the less invasive tool available to reach the stated objectives. The third step is proportionality which requires the consideration of all relevant factors. For instance, to do the cost-benefit analysis is to consider all the alternative policies that can provide better optimisation of the conflicting rights. Also, Kingsbury and Schill noted that regardless of the criticism that it provides more power to the arbitrators, it is still the better method to deal with the difficult assessments that exist in the international investment law. It can be considered to be a standard technique; thus, it can improve the legitimacy of international investment law.[501]

Similarly, Reinisch recommended the use of the proportionality approach to determine whether the state measures can be considered the only means to safeguard state interests. Similarly, it can support the valuation of the state contribution element by requiring that it be substantial.[502] However, the proportionally analysis is not recommended to substitute the rules of treaty interpretation under the VCLT. It is an interpretation treaty exercise to solve the dilemma of competing rights. Its core advantage is that it helps tribunals to balance between open ended concepts. It has played a role in public international law in solving conflicts between equal sovereigns. For example, in the *Gabčíkovo-Nagymaros* case, proportionality analysis was a legal factor in considering the use of force as a right to self-defence. The ICJ noted that according to customary international law, self-defence will only be permitted if it is proportional to the armed attack and if it was necessary to respond.[503]

[500] ibid
[501] ibid
[502] Reinisch, 'Necessity Across International Law' (n 467)
[503]Gabcikovo-Nagumaros Project (n393)

Nevertheless, Federico criticised the use of proportionality approach to strike a balance between public policies and private rights.[504] Federico argued that any effort to balance public policy wide values and investors' interests will ultimately fail. The international tribunals will not be able to achieve such a balance whenever there is a dispute. This is because the current system only focuses on foreign investment protection with an absence of the legitimate balance of various interests, values and policies.[505] Moreover, Federico illustrated the legal debate about the future of investment law. Policy makers have realised that the role of investment treaties was not only to promote foreign investments but also to ensure environmental protection, economic growth and social equity. Thus, investments treaties should work parallel so as to protect foreign investments and maintain the state's authority to regulate its public interests.[506] In the future, international investment law should create clear standards of investment protection that should include strict balancing.[507]

Therefore, what we can infer from the existing literature and case law that the main reasons of inconsistent arbitral awards on necessity might be because there is lack of guidelines on how applicable a source of law is. In addition to vagueness of texts and rigid subjective criteria of necessity under customary international law. Both over- and under-enforcement theories deeply explain that the problems of under-defined law where broad law that invites selective interpretation. Adjudicators might over or under-enforce the law because they are trying to square the law with the facts of the case to render their own notion of justice.

This is seen in scholar's argument. Caron recommended that decision makers should avoid reading the articles and consulting commentaries on each article. The ILC Articles should aim to develop and codify the law of state responsibility for international wrongful acts. They should not be an obstacle to the changing circumstances of the international community. The decision makers should apply the articles of state responsibility in a verbatim manner instead of considering them as an evidence of rule. These articles should be examined rigorously

[504] Federico Ortino, 'Investment Treaties, Sustainable Development and Reasonableness Review: A Case Against Strict Proportionality Balancing' (2017) 30 Leiden Journal of international law 71.
[505] ibid
[506] ibid
[507] ibid

together with their related history and context in weighting whether they provide the right outcome.[508]

Consequently, after reviewing the pros and cons of the scholars' recommendation on the dilemma of lack of uncertainty of state necessity defence in international investment law: in addition; to analysing case law through both over- and under-enforcement theories. It appears the interaction between customary international law and treaty law on state responsibility is problematic. It requires the development of a unitary framework of international law. Also, rigid subjective criteria of necessity in the customary international law need to be addressed. Article 25 of the ILC should provide guidance to the tribunals on how to apply the case with the criteria rather than leaving it for each tribunal to apply it without having the knowhow. Furthermore, there is a need to establish a persuasive precedent system that can provide a degree of uniformity in the decisions. However, it is important to note that there is a similar defence that can be used by the host state in an emergency or crisis –the force majeure.

4.7 Doctrine of force majeure

Under the law of state responsibility, there is a similar defence to the doctrine of necessity, which operates to preclude the legal wrongfulness of a state act in the international investment law context when force majeure-type circumstances arise.[509] Force majeure can be described as international or internal conflicts or abnormal events that affect the rights and interests of foreigners with a notion that the states affected by abnormal events can avoid their international obligations.[510] The emergency of unforeseeable and extraordinary events has provided legal grounds for parties to request to terminate contract.[511] The force majeure defence can be

[508] Caron, 'The ILC Articles on State Responsibility' (n 27)
[509] Dellinger, Rethinking Force Majeure in Public International Law (n373) http://digitalcommons.pace.edu/plr?utm_source=digitalcommons.pace.edu%2Fplr%2Fvol37%2Fiss2%2F2&utm_medium=PDF&utm_campaign=PDFCoverPages
[510] Federica I Paddeu, 'A Genealogy of Force Majeure in International Law', in *The British Yearbook of International Law The Author* (Oxford University Press 2012)
[511] Subedi, *International Investment Law Reconciling Policy and Principle* (n772)

presented in changes in weather, governmental actions, labour strikes and economic events; however, economic hardship or financial difficulty does not excuse performance.[512]

For example, in previously mentioned case, *Mobil Oil Iran Inc. v Government of the Islamic Republic of Iran* case,[513] the tribunal was created to figure out the investors' claim for compensation as these investors refused to consider that Iran was acting on force majeure. On the other hand, new Iranian regime claimed that its decision was a practice of state sovereignty "in a force majeure event and it should be exempted from its international liability. Although tribunal recognised the revolution as a force majeure situation, the situation cannot be considered terminated or frustrated for cause of force majeure. This is because a new revolutionary Islamic Government had already been established. Thus, the tribunal held rejected the force majeure defence. The tribunal held that Iran had to pay fair compensations.[514]

Moreover, codification of the force majeure defence started in the UN era. Force majeure is applied when a state is in a situation where it is impossible for it to conduct its international obligations following the occurrence of unforeseeable and unforeseen event.[515] The 'force majeure' article adopted by the Commission in the second reading eventually became Article 23 of ARSIWA.[516]

The Article 23 of ARSIWA, states:

> "1. The wrongfulness of an act of a State not in conformity with an international obligation of that State is precluded if the act is due to force majeure, that is the occurrence of an irresistible force or an unforeseen event, beyond the control of the State, making it materially impossible in the circumstances to perform the obligation.
>
> 2. Paragraph 1 does not apply if:

[512] Jay D Kelley 'So What's Your Excuse? An Analysis of Force Majeure Claims' (12 February 2006) Texas Journal of Oil, Gas, and Energy Law 2

[513] *Mobil Oil Iran Inc. and Others v Government of the Islamic Republic of Iran*(n151)

[514] ibid

[515] Paddeu 'A Genealogy of Force Majeure in International Law' (n 510)

[516] International Law Commission, 'Draft Articles on the Responsibility of States for Internationally Wrongful Acts with Commentaries', UN GAOR, 56th Sess., Supp. 10, Ch. 4, (2001) UN Doc A/56/10 (ARS), Article 23.

A. the situation of force majeure is due, either alone or in combination with other factors, to the conduct of the State invoking it;

B. the State has assumed the risk of that situation occurring."[517]

Over-enforcement theory can explain that criteria of Art. 23 are hard to fulfil. It might be to support political processes to minimize the abuse of force majeure defence.
Generally, Art. 23 represent the customary international law. It provides that the force majeure defence includes a situation where a state is forced to act against its international obligations. External forces beyond the state's control that have made it impossible for it to fulfil its obligations.[518] It precludes the state from performing the obligations under the treaty whenever there is an unforeseen event or an irresistible force outside the state's control makes the state performance impossible. The state act must not include the element of free choice.[519] However, Article 23 does not cover situations that make state obligations burdensome and involve state neglect even if the violation of the treaty was unintended or accidental by the state.[520]

The ILC Articles on force majeure had been recognised by international tribunals. For example is *Libyan Arab Foreign Investment Company (LAFICO) v Burundi* is another case that clarified the force majeure defence.[521] The republic of Burundi and the Libyan Arab Republic concluded an agreement in 1975 which established the Holding company (HALB).[522] The objective of HALB was to invest in companies working in particular areas of the Burundi economy. In 1978, HALB began its investment program. Investments were either held straightforwardly by HALB or by its two subsidiaries. In 1981, Libya shifted its shareholding in HALB to the Libyan Arab Foreign investment Company (LAFICO). However, on April 5, 1989, Burundi cut off diplomatic relations with Libya. Brunel expelled all Libyan nationals residing in Burundi and banned all Libyan people from entering Burundi.[523]

[517] ibid
[518] Ioana Tudor, *The Fair and Equitable Treatment Standard in The International Law of Foreign Investment* (2008)
[519] ibid
[520] ILC Articles. ILC Commentary, art 23(2)(b)
[521] *Libyan Arab Foreign Investment Company (LAFICO) v Burundi* (1991) 96 ILR 279
[522] This agreement provided that "the assets of the Company [HALB] shall not be the subjects of nationalisation, confiscation, sequestration nor any other measure capable of infringing the rights of the shareholders or limiting the ability of the Company to achieve its objects (Article 15, paragraph 1).
[523] *LAFICO v Burundi* (n521)

Consequently, the Director-General of ACC and the Director-General of HALB, who were Libyan citizens, were required to leave the country. This made Burundi and LAFICO raise a claim in international arbitration. The government of Burundi justified its action by stating: "For some time the diplomatic personnel of the Peoples' Bureau in particular, and all Libyan nationals' resident in Burundi in general, have been participating in activities of destabilisation, putting the peace and internal and external security of the Republic of Burundi in danger."[524]

Therefore, the Government of Burundi concluded that the measures it took were meant to maintain its public interest against danger to internal peace and security. The tribunal had to question whether the expulsion action was a breach in a rule of customary international law. The first thing the tribunal recognized was the right of every state to expel a foreigner who endangered its security. However, there was a question of whether Burundi's act could be justified by Article 31 of ILC (now Article 23). Burundi relied on "material impossibility" to excuse or justify its action. The state claimed that it should be exempt from international obligations because there was a threat to internal and external peace and security.[525] However, the arbitral tribunal declined the plea of force majeure due to Burundi's control of the situation.[526]

However, the issue of determining the situation of impossibility is based on a subjective criterion. This is because any government can have other options than breaching its international obligations with foreign investors. This raises the question of the costs of such options, assessed not in monetary but more importantly in humanitarian and security terms. For instance, in the case of *Autopista v Venezuela*.[527] In this case, the foreign investor raised an investment arbitration claim because Venezuela did not comply with the concession agreement.[528] On the other hand, Venezuela had debated that there was a force majeure

[524] ibid
[525] ILC in its 1996 Draft Articles on State Responsibility ([1996] GAOR 51st Session Supp 10, 125) DRAFT ARTICLES ON STATE RESPONSIBILITY WITH COMMENTARIES THERETO ADOPTED BY THE INTERNATIONAL LAW COMMISSION ON FIRST READING January 1997, Article 31's changed reference to material impossibility has been changed to Article 23.
[526] *LAFICO v Burundi* (n521)
[527] *Autopista Concesionada de Venezuela CA v Bolivarian Republic of Venezuela*, ICSID ARB/00/5, Award (14 July 1987) Claims Tribunal Award No. 311-74/76/81/150-3

[528] Autopista Concesionada de Venezuela, C.A. ('Aucoven') is under the foreign control of a US national and Venezuela agreed to ICSID jurisdiction based on such fictional foreign control.

situation (violent reaction and civil unrest) that led to the state's non-compliance with its international obligations under the concession agreement. The government could have met its international obligations by using military force against protestors. This negatively affected the security of the state and increased death. However, Autopista tribunal did not accept the claim of force majeure defence under international law. [529]

It seems that the conditions of force majeure are strict and subjective. It is also seen in the criteria of unforeseeability that it is causing confusion. It is seen in the *Autopista* case, the tribunal did not recognise Venezuela's defence. This is because in 1989 Venezuela had experienced similar events that resulted in many deaths in response to an increase in gasoline prices. Consequently, the tribunal decided that the effect of civil conflict on the Venezuelan community, which had occurred eight years earlier, was evident because the 1997 riots could have been foreseen during the negotiation of the concession agreement. The tribunal rejected the plea of force majeure on the ground that the civil unrest was not wholly unforeseeable because of similar events took place after the petrol prices were raised.[530] It seems that the tribunal set the bar high for foreseeability. The tribunal interpreted the event to be foreseeable by the possibility that it was to occur. The tribunal used the Venezuelan previous record of conflict as a benchmark for the foreseeability, despite the fact that it had been a decade since the last similar upheaval event.

However, another similar ICISD case was the *RSM Production Corporation v Central African Republic*.[531] The tribunal used a different approach in determining the term of foreseeability. RSM and the Central African Republic entered into a contract in which a foreign investor obtained a four-year license for oil exploration. However, due to political turmoil in the Central African Republic, the foreign investor invoked a force majeure clause to be exempted from contractual liability. Despite the fact that in this case, the force majeure was based in the contract, the tribunal that inspected the elements was the same as those under international law.[532] Although the country had experienced outbreaks of violence and was politically

[529] The tribunal supported its opinion by referring to Draft Articles on state responsibility.
[530] *Autopista Concesionada de Venezuela CA v Bolivarian Republic of Venezuela* (n522)
[531] *RSM Production Corp v Central African Republic*, ICSID Case No. ARB/07/02 (Decision on Jurisdiction and Liability, 7 December 2010).
[532] The contract defined *force majeure* as 'Unforeseen events, irresistible and beyond the control of the party invoking such as earthquake, strike, riot, insurrection, civil commotion, sabotage, acts of war or conditions attributable at war'.

unstable, the tribunal held that the conflict was not foreseeable. In contrast to the *Autopista* tribunal, the *RSM* tribunal did assess the country's past record of violence, and instead it assessed the 'foreseeability' condition in relation to other conditions and certainly its effect on the performance of the obligation.[533]

This raises the question of why there was flexible interpretation in the *RSM* decision inconsistent with the strict interpretation of the *Autopista* decision. In the former case, the foreign investor invoked the force majeure defence, while in the latter case, the state invoked the force majeure defence. This raises the question of whether the unforeseeability should be evaluated differently depending on whether the party invoking force majeure is an investor or the state. This is problematic since there is a lack of tangible criteria to assess foreseeability. Also, the decision of the *Autopista* tribunal will make the force majeure useless if any state has previously experienced riots and protests. Both over and under-enforcement theories can explain that criteria of Art. 23 are subjective. It can invite selective interpretation; tribunals can either over or under-enforce it to render their own notion of justice.

Generally, force majeure situation will exempt the state from responsibility, and at the same time the state should be exempt from responsibility in the case of damage which could not be avoided. Thus, the force majeure criterion is coordinated with the due diligence rule.[534] This is reflected in the most recent case of a revolutionary government using the force majeure defence is the *Ampal* case. On May 23, 2012, the *Ampal-American Israel Corporation* ("Ampal") filed a Notice of Arbitration at ICSID against Egypt. The US Company Ampal had invested in an Egyptian company named the *East Mediterranean Gas Company SAE* ("EMG"). In 2005, the *EMG* concluded an agreement with two Egyptian state-owned companies, the Egyptian Natural Gas Holding Company ("EGAS") and the Egyptian General Petroleum Corporation ("EGPC"), to transport gas from Egypt to Israel. On the 25th of January, the Egyptian revolution occurred. Ampal complained about a total of 13 attacks on the pipeline between Egypt and Israel that transported natural gas from Egypt to Israel, the subject of the investment.[535] As a result, Ampal

[533] ibid

[534] René Provost (ed), *State Responsibility in International Law* (Ashgate 2002).

[535] *EAST MEDITERRANEAN GAS S.A.E. v EGYPTIAN GENERAL PETROLEUM CORPORATION (Egypt) EGYPTIAN NATURAL GAS HOLDING COMPANY, ISRAEL ELECTRIC CORPORATION LTD,* ICC Case 18215/GZ/MHM, Award of 4 December 2015

claimed that Egypt had breached its obligations under the US-Egypt BIT[536] on several occasions, which included the Egyptian government's failure to protect and secure the pipeline against military attacks during the revolution.[537]

However, investment tribunal relied on the due diligence standard in order to determine applicability of the force majeure defence. According to the *Ampal* tribunal, the subsequent attacks on the pipeline created a pattern of delayed measures or a failure to implement measures to safeguard the security and safety of the pipeline, and hence the investor's investment in the violation of its due diligence obligation. There is also a lack of evidence that the EGAS applied any security measures after the first attack or that it performed a risk valuation. Therefore, the *Ampal* tribunal dismissed the force majeure defence and did not consider the extraordinary circumstances the country was facing, its limited resources and the revolution.[538] Therefore, due diligence plays an important role as a threshold in determining the applicability of the force majeure defence under international law. The role of due diligence is also seen in the old case of *Gould Marketing*, the tribunal stated:

> By force majeure, we mean social and economic forces beyond the power of the state to control through the exercise of due diligence. Injuries caused by the operation of such forces are therefore not attributable to the state for the purposes of its responding for damages.[539]

Consequently, we can infer that if an event occurs within the state's control but fails to take appropriate measures of control, the state's responsibility will be decided by using the due diligence standard. On the other hand, if the event is outside the state power to control, then the force majeure defence would come into play. The due diligence rule excludes the state's responsibility for injury in such a case.

It appears that the due diligence standard plays a significant role in both old and modern international investment law (*Gould Marketing* and *Ampal* cases). Thus, it is essential to explain the concept of due diligence. The host state's obligation under the due diligence standard is not to prevent every injury or risk; instead, the state is required to take reasonable

[536] Treaty between the United States of America and The Arab Republic of Egypt Concerning the Reciprocal Encouragement and Protection of Investments. Signed March 11, 1986 (modified); Entered into Force June 27, 1992.
[537] *Ampal-American Israel Corp. v Egypt,* (n138).
[538] ibid
[539] *Gould Marketing, Inc v Iran et al.* U.S. Court of Appeals, Ninth Circuit, 23 October 1989

actions, within its capacity, to prevent risk. This is revealed in the tribunal of *AAPL v Sri Lanka*, where *Freeman's* definition of due diligence was applied: "nothing more nor less than the reasonable measures of prevention which a well-administered government could be expected to exercise under similar circumstances."[540]

Accordingly, a state is required to practice due diligence in respect of foreign investments which are present on its territory.[541] This is also seen in international conventions.[542] The problem with due diligence is that there is a lack of understanding regarding whether the state is requisite to respect the minimum international standard of diligence or is only bound to exercise due diligence according to its national affairs. This made scholars such as Provost to argue that a due diligence obligation depends on the situation; thus, this flexibility does not allow more precise rules. Generally, due diligence is assessed via the average general standard of a well-organised state or the behaviour of a civilised state. Nevertheless, in certain areas, the due diligence standard must not be based on average standard but good or even excellent standard, for example, in terms of state protection relating to ultra-hazardous activities that harm the environment, a state must exercise a high level of diligence as standard.[543]

It is debatable if due diligence became more specific it would lose its characteristic of denoting general and flexible norms of behaviour.[544] On the other hand, others can see it differently; indeed, there should be limits to the flexibility of due diligence as a norm. The more precise the obligation content that diligence requires, the more precise of what is expected by the state in terms of acting. Predictability will take place once flexibility and generality are reduced.[545]

Moreover, state practice attempted to provide objective standards for due diligence. The first standard is related to the degree of a state's effectiveness in controlling particular areas within its territory. The second standard is related to the significance of the interest being protected. Lastly, the third standard is the degree of predictability of the harm.[546] These objective

[540] *Asian Agri Prods Ltd v Sri Lanka*, ICSID Case No ARB/87/3, Final Award, 3 (27 June 1990)
[541] Iona Tudor, *The Fair and Equitable Treatment Standard in the International Law of Foreign Investment* (Oxford University Press 2008).
[542] Art 10 of the Harvard Law School Draft proclaims that a 'state is responsible if an injury to an alien results from its failure to exercise due diligence to prevent the injury', while Article 1 of the OECD Draft Convention on the Protection of Foreign Property states that: 'most constant protection and security must be accorded in the territory of each Party to the property of nationals of the other Parties [...] the rule indicates the obligation of each Party to exercise due diligence as regards actions by public authorities as well as others in relation to such property'
[543] Provost, *State Responsibility in International Law* (n 534).
[544] ibid.
[545] ibid.
[546] ibid.

standards can provide guidance, but still there is a lack of clarity in terms of defining the due diligence standard. This attribute to the problems of under-defined law where broad law that invites selective interpretation. This sheds light on the necessity for any further tribunals to define due diligence standard parameters in both extraordinary and ordinary circumstances.

Additionally, it is important to mention that the idea of force majeure comes from civilian legal systems and is meant to preclude their responsibility for breaching the contract.[547] This makes it important to note that the force majeure defence is in the international law of responsibility and is codified in Article 23. It must be differentiated from force majeure clauses in that it is contained in an investment contract administered by international commercial law and national law. However, the force majeure clauses have been more frequently invoked than force majeure in international law to excuse the non-performance due to a conflict situation.

This is seen in the case of the *Himpurna California Energy Ltd (Bermuda) v PT. (Persero)* in the Indonesian political and economic crisis that followed the overthrow of the Suharto regime in Indonesia in 1998. The government of Indonesia took IMF's advice to suspend many project contracts that were made with foreign investors, but the plea of force majeure was rejected due to contract clause anticipating such an event and the requirement that such a risk would be carried by the state.[548] This is demonstrates the importance of the force majeure clause in determining the consequences of such an event. Also, breaching investment contracts can be brought to investor-state arbitration because the parties have explicitly provided that the contractual breach is raised to the breach of the investment treaty by means of an umbrella clause or that contractual breaches are so essential that they establish a violation of an investment treaty standard.[549]

It seems that tribunals address force majeure claims under the rules of customary international law. This might be because treaty clauses such as the force majeure clauses are undefined, and there are no standards to use these clauses. Also, there are various versions of force majeure clauses or war clauses which made it hard to identify its scope, implications and remedy.[550] For example, some treaties contain an extended war clause, and this clause provides the right

[547] Sornarajah, *International Law on Foreign Investment* (n 1)
[548] *Himpurna California Energy Ltd. v PT. (Persero) Perusahaan Listruik Negara*, UNCITRAL Ad Hoc-Award of 4 May 1999, YCA XXV (2000), 13 et seq
[549] Jure Zrilič,' Armed Conflict as Force Majeure in International Investment Law' (2019) 16 Manchester Journal of International Economic Law
[550] Aleksandra Vonica, 'International arbitration agreements and their adjustment clauses: are they in a state of evolution? '(n26)

for foreign investors to ask for compensation during times of conflict broadly without providing details. Therefore, the substantive question is left unanswered.[551] Accordingly, the tribunal tends to interpret the force majeure under Article 23 of ARSIWA. However, it appears that there is vagueness on the meaning of force majeure in international law. Particularly the problem is seen in defining the subjective terms of impossibility and unforeseeability. This result in inconsistent interpretation in state practice as previously discussed.

As a result, over-enforcement theory explains that the criteria of Article 23 are established in over-enforced ways that make it rare for the state to fulfil its requirements. Thus, the under-enforcement theory provides that in some instances the under-enforcement of a law can results in more justice. This way, some tribunals can attempt under-enforce rigid rules of force majeure in some instances can provide more justice. The textual analysis is as a tool to free adjudicators from constraints. However, drawbacks in justifying interpretation will increase indeterminacy. Also, it is important to note that there is little attention among scholars in addressing the force majeure defence under international investment law. However, the recent investment claims resulting from Arab spring events in 2011 made such examinations important. The Arab spring events shed light on the importance of examining state defences. This is raising the question of what we can conclude from both defences regarding necessity and the force majeure.

4.8 Necessity defence v Force majeure defence

The state necessity defence applies if the Article 25 requirements are met. It could then provide an excuse or justify invoking the state act to maintain its public interest before the damage becomes unavoidable and materialises. In turn, the force majeure defence applies; if the requirements of Article 23 are fulfilled, the state act could also be excused.[552] Although the main common feature between them is that both of them are used by states under extraordinary circumstances. Additionally, the application of both the defences is limited to a particular time, which shows the temporary effect. However, the difference is that the force majeure defence is used as a response against a current occurrence or a past event. It cannot adapt any future

[551] Article 12 of the Energy Charter Treaty
[552] Paddeu 'A Genealogy of Force Majeure in International Law' (n 510)

events, and it is not about avoiding the damage. It is about reacting to the damage done. Conversely, in the plea of state necessity, the reason of defence is based on future expectation of a future damage caused by a future or past event. Also, under force majeure defence, the state is deprived of acting in free choice. In contrast to state necessity, the state deliberately decides measures to ensure the protection of its public interests versus its international obligations. However, using each state defence depends on the content and the character of the obligation itself.

For example, when observing economic data, states are capable to predict the probability of a financial crisis. In this case, the states cannot take recourse to force majeure as a justification when faced with difficult financial circumstances or serious economic crises instead they should use the necessity defence to justify the acts applied to address the financial crisis.[553]
Finally, all of these defences may be excuses or justifications for the non-fulfilment of conventional and customary obligation. In all cases, the proof burden falls on the invoking state.[554] Generally, both necessity and force majeure exceptions allow the state to be exempt from its obligations but in a restrictive and over enforced manner. The over-enforcement theory can justify restrictive criteria as ILC view might to make the necessity and force majeure defences the last option to stabilise the treaty so it gives a little room for the state to change. Nevertheless, the contradictory awards by the investment tribunals created a tension between foreign investment protection and the legitimate state measures in critical circumstances.[555] However, these state defences can also be raised under the law of treaties. This is raising the question of what is the difference between the law of treaties and law of state responsibility.

4.9 Law of treaties v Law of state responsibility

It is essential to note that the defences of force majeure and necessity can be used under both the law of treaties and law of state responsibility. Generally, law of treaties is a set of national

[553] Alberto Alvarez-Jimenez, 'The Great Recession and the New Frontiers of International Investment Law: The Economics of Early Warning Models and the Law of Necessity'(2014) 17 Journal of International Economic Law 517
[554] Paddeu 'A Genealogy of Force Majeure in International Law'' (n 510)
[555] ibid

and international rules that govern the life of the treaties from their formation to termination. The most important convention on the law of treaties was established between states in Vienna on 23 May 1969 (VCLT). It covers interstate relations excluding issues such as international responsibility for noncompliance.[556] It is important to determine which set of rules applies to these contact points. This is because there is a functional separation between the fields of the law of treaties and that of state responsibility. Under law of treaties, Article 61 acknowledged a ground for the treaty termination or suspension on the basis of impossibility of performance.[557] Article 62 permitted the state to withdraw or terminate a treaty in the event of major circumstantial or unforeseen changes.[558] Also, article 62 of the VCLT is limited to the cases of permanent destruction or disappearance of an essential object in the treaty execution.[559]

Under the law of state responsibility, there are Article 23 of the force majeure and Article 25 of state necessity. The defence of force majeure and necessity in the ILC Articles do not affect the continuation of state obligations. Its rules are like the circumstances precluding wrongfulness does not suspend the primary rule operation. The ILC considered that the circumstances precluding wrongfulness should work by stopping the affected obligations, the defences only excusing or justifying non-performance for the time being.[560] They are not the same as the state defence under VCLT because Article 61 and Article 62 bring modifications to the primary rules. The VCLT provisions concern the treaty's existence and obligations.[561]

[556] Vienna Convention on the Law of Treaties Concluded at Vienna on 23 May 1969

[557] VCLT, art 62 states: "1. A fundamental change of circumstances which has occurred with regard to those existing at the time of the conclusion of a treaty, and which was not foreseen by the parties, may not be invoked as ground for terminating or withdrawing from the treaty unless: (a) the existence of those circumstances constituted an essential basis of the consent of the parties to be bound by the treaty; and (b) the effect of the change is radically to transform the extent of obligations still to be performed under the treaty. 2. A fundamental change of circumstances may not be invoked as a ground for terminating or withdrawing from a treaty: (a) if the treaty establishes a boundary; or (b) if the fundamental change is the result of a breach by the party invoking it either of an obligation under the treaty or of any other international obligation owed to any other party to the treaty. 3. If, under the foregoing paragraphs, a party may invoke a fundamental change of circumstances as a ground for terminating or withdrawing from a treaty it may also invoke the change as a ground for suspending the operation of the treaty"

[558] There are certain conditions that have to be met as "essential basis of the consent of the parties to be bound by the treaty" and "the effect of the change [in those circumstances] is to transform the extent of obligations still to be performed under the treaty."

[559] Paddeu 'A Genealogy of Force Majeure in International Law' (n 510)

[560] ILC, art 23 and 25

[561] Vienna Convention on the Law of Treaties Concluded at Vienna (n556)

For example, in the *Rainbow Warrior* case, New Zealand argued that the provisions on treaty suspension and termination of the VCLT had superseded the law of state responsibility. A similar argument was made by Slovakia in *Gabcˇı´kovo-Nagymaros*. Both states argued that the VCLT regime replaced the use of the law of state responsibility with respect to treaty breaches. However, in both cases, the tribunals declined their arguments and demonstrated that the VCLT provisions were narrowed to the question of the continued existence of treaty. Hence, referring to the law of treaty or state responsibility depends on the circumstances of each case. For example, immediate reaction to an unforeseen situation may not be easily dealt with under the lengthy procedures for termination of treaties in the VCLT. It may be better addressed under the state responsibility defence of force majeure.[562] For instance, in the case of *Gabcikovo-Nagymaros*, Hungary was transitioning from communism to democracy, so, the government had to terminate a treaty with Slovakia regarding the construction of a dam.[563]

The ICJ did not accept Hungary's defence. The reason behind this is that the court viewed that these political changes in Hungary should not change its international obligations. This is the same situation under the investment treaty as it is hard to debate that such international obligations could be changed by the new government.[564] Thus, the necessity defence is a prominent and restricted concept. It does not terminate a treaty but exempts state responsibility under tough circumstances. Also, the legal consequences of successful reliance on Articles 25 or 23 of the ILC are different from the law of treaties. This is because the successful use of necessity or force majeure does not lastingly affect the treaty. It is only excusing the non-performance on the temporary basis.[565] Thus, the compensation matters are left open.[566]

4.10 Concluding Remarks

Going back to the main question of the chapter; whether transitional governments allowed to use the law of state responsibility to accommodate changes for measures they take against

[562] Paddeu 'A Genealogy of Force Majeure in International Law' (n 510)
[563] Gabcikovo-Nagumaros Project (n373)
[564] Bonnitcha, 'Investment Treaties and Transition from Authoritarian Rule' (n15).
[565] Binder, 'Stability and Change in Times of Fragmentation' (n 465)
[566] ibid

foreign investments? It is unclear when it is acceptable for the host state to use the state defences. This is because of conflicting arbitral decisions. There is fragmentation in the international investment law which can affect the legitimacy of the whole system. This made it important to examine root causes of such fragmentation. Thus, analysing the texts and case law through over- and under-enforcement theories.

These theories provide that problem of fragmentation on necessity defence might be due to analytical reasons. Arbitral tribunals decision depend on how the tribunal interprets the treaty provision and the criteria of necessity under international customary law. It seems that the law is applied based on discretion where is there are no guidelines on how applicable a source of law is. Tribunals select the source of law that renders their own notion of justice. Generally, few criteria make law enforcement subjective and open to many different interpretations that depend on the arbiter's opinions rather than actual legislative definition. Thus, tribunals might over or under-enforce the law because they are trying to square the law with the facts of the case to render their own notion of justice. This results to conflicting awards.

This makes it is problematic to predict the tribunal's decisions on necessity. States do not know when to use the state necessity defence under the international investment law. Thus, the treaty parties cannot forecast how the provisions of the treaty will be interpreted. This will increase opportunity that dispute outcomes will be balanced, but it will be difficult to predict the outcome.

Likewise, the analysis of force majeure defence is causing confusion as state necessity defence. There is vagueness on what the meaning of force majeure in international law. The problem can be seen in defining criteria of force majeure; particularly, subjective terms of impossibility and unforeseeability. This attribute to the problems of under-defined law where broad law that invites selective interpretation. Tribunals might over or under-enforce the law because they are trying to square the law with the facts of the case to render their own notion of justice. This problem also exists in defining due diligence standard as a threshold in determining the applicability of the force majeure defence under international law. It seems that there is lack in defining parameters of due diligence. This attribute to the problems of under-defined law where broad law that creates selective interpretation. The more precise the obligation content that

diligence requires, the more precise of what is expected by the state in terms of acting. This sheds light on the necessity for any further tribunals to define due diligence standard parameters in both exceptional and ordinary circumstances.

Also, over-enforcement theory can explain that criteria of necessity and force majeure under customary international law are hard to fulfil. It made the success and use of such defences rare. The over-enforcement theory can justify such restrictive criteria to minimize the use of state defences. The purpose might be to promote foreign investments protection and at the same time to avoid abusing use of state defences. Therefore, there is a lack of understanding on how the high requirement criteria of state defences can be successful within the investment context. Thus, under-enforcement theory can explain that in some cases tribunals can attempt to under-enforce rigid criteria of state defences under customary international law to render their own notion of justice. On the other hand, other tribunals can see justice by fully enforcing such rigid criteria. Generally, textual analysis is as a tool to free adjudicators from constraints. However, drawbacks in justifying interpretation will increase indeterminacy. Also, the criteria of necessity and force majeure under customary international law are subjective and open to different interpretations. Tribunals might over or under-enforce the law due to analytical reasons. This created a vagueness regarding the application of state defences towards foreign investments during emergency.

Accordingly, we can infer that there are tensions between foreign investment protection and legitimate state measures in crisis circumstances. Their future directions within investment disputes remains unclear. The protection of foreign investment from state defences during emergency times remains uncertain. We need to have guidance and predictable arbitral awards on the state defences under laws of state responsibility in international investment law context. States and investors have to be guided to determine the use of state defences through the ILC Drafted Articles on State Responsibility and the available ICSID decisions on the state defences.

Therefore, this chapter recommends international efforts to harmonise the interpretation of legitimate state defence during emergency times. The interaction between treaty law and customary international law on state responsibility require the establishment of a unitary

framework of international law. Accordingly, this chapter recommends establishment of new convention that can unify different sources of law. Also, this new convention should provide guidance on subjective criteria of necessity and force majeure under customary international law. Finally, this chapter recommends the establishment of a precedent system that can provide a degree of uniformity in the decisions. Hence, Host states' responsibilities under international investment law need to be examined. The subsequent chapter will examine whether unconstitutional transitional governments responsible under international law for protection and measures against foreign investments.

Chapter 5: Whether transitional governments responsible under international law for protection and measures against foreign investments?

5.1Introduction

Under the law of state responsibility, a state is liable for foreign investment protection. The state responsibility comes into play when a sovereign breach the right of foreign investors either under investment treaties or customary international law. The state is required to make up for the damages and the violations it has have caused. Accordingly, it is significant to examine the limits of a state's responsibility in respect of foreign investment during periods of upheaval and indeed, after revolution. To achieve this, it is essential to examine two phases – the state's responsibility during the course of a revolution and those relevant after such a time. The question regarding the first phase is to what extent are revolutionary governments responsible for protecting foreign investment during revolution? In order to answer this question, we have to examine what constitutes state responsibility for internationally wrongful acts. Additionally, we have to examining the degree to which the state is responsible for the foreign investment protection. The question relating to the second phase is, to what extent is the state allowed to take measures against foreign investments for public interests during post-revolutionary times? This chapter uses both over- and under-enforcement theories as interpretative tools to assess how the law of state responsibility is enforced in context of international investment law.

5.2 Phase One

5.2.1 Doctrine of state responsibility

State responsibility means that the host state has to accept the consequences of its acts and decisions. This provides that the state is responsible for its internationally wrongful acts under international law. This principle of responsibility begs the question of the right of foreign investors of protection. State responsibility is regulated under public international law, and this involves many issues. Firstly, it limits the defences and justifications on which a state might rely to avoid its international obligations for a wrongful act.[567] Secondly, it covers the consequences of the state's act in breaching its international obligation; particularly, the state's obligation to end its wrongful act and to make full reparation.[568]

As previously mentioned an effort has been made to codify the laws regarding state responsibility through ARSIWA, adopted by the ILC in 2001. These articles are known as secondary rules that aim to identify the main concepts covered by state responsibility.[569] Ago clarified that the ILC Articles on state responsibility define rules that place obligations on states to determine whether said obligations have been violated and the consequences of such violations.[570] Moreover, Crawford[571] demonstrated that the ILC articles on state responsibility aimed to restate most of the substantive international law and customary law.[572] However, they do not explain the content of the international obligations that give rise to that responsibility.[573] It is important to note that prior to the final adoption of the ILC's articles on state responsibility, many works aimed to provide a complete overview of state responsibility, although none of these are completed. For example, Brownie's work, although it is an early work, still has

[567] Michael Feit, 'Responsibility of the State under International Law for the Breach of Contract Committed by a State-Owned Entity' (2010) 28(1) Berkeley Journal of International Law 142, 176.
[568] Sabine Lowe, 'Responsibility and Liability in General Public International Law and in the Law of Outer Space' (LLM thesis, Institute of Air and Space Law McGill University Montreal 1991) 4–5.
[569] Borzu Sabahi, *Compensation and Restitution in Investor-State Arbitration: Principles and Practice* (Oxford University Press 2011).
[570] ILC 'State Responsibility' (1970) II Yearbook of the International Law Commission 1, 306 para 66 (c).
[571] Crawford is the leading monograph on state responsibility and the ILC's last Special Rapporteur on state responsibility.
[572] James Crawford, *The International Law Commission's Articles on State Responsibility: Introduction, Texts and Commentary* (Cambridge University Press 2002) 74.
[573] Robert Ago, who was responsible for establishing the basic structure and orientation of the ILC project, saw the articles.

substantial value in current times and should be read in light of the ILC articles.[574] Also, there are other scholars, such as Provost and Ragazzi, who provided academic writings on state responsibility after the final adoption of ILC articles.[575]

Generally, it can be seen that the ILC articles on state responsibility reflect international customary rules, and aim to assist in the interpretation of the primary rules of state responsibility under international investment law. These primary rules can be seen in investment treaties where they define the content of international obligations and breaches of state responsibility.[576] Therefore, the law of state responsibility can be seen as the union of the primary and secondary rules since, according to Hart, the union of primary and secondary rules is essential when it comes to establishing an effective legal system.[577]

Nevertheless, the perception of state responsibility raises the question of whether the state is exempt from a responsibility to protect foreign investments during times of conflict, such as when a revolution occurs. This issue is addressed in the many clauses in investment treaties which deal with violent situations. These treaty provisions are interpreted and applied by arbitral tribunals; they maintain the investor's interests in times of conflict.[578] This is also reflected in the recent ILC related work: the draft articles on the effects of armed conflicts on treaties.[579] These articles provide that international obligations and the rights of the state remain applicable in times of conflict.[580] Consequently, as a rule, treaties which deal with the foreign investment protection will continue to be applied after the occurrence of conflicts.[581]

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[574] Ian Brownlie, *System of the Law of Nations, State Responsibility, Part I* (Oxford University Press 1983).
[575] René Provost (ed), *State Responsibility in International Law* (Ashgate 2002); Maurizio Ragazzi (ed), *International Responsibility Today: Essays in Memory of Oscar Schachter* (Martinus Nijhoff Publishers 2005).
[576] Crawford, *The International Law Commission's Articles on State Responsibility* (n 572)
[577] Hart, *The Concept of Law* (n462)
[578] Christoph Schreuer, *The Protection of Investments in Armed Conflicts* (Cambridge University Press 2013).
[579] ILC, 'Draft Articles on the Effects of Armed Conflicts on Treaties, with Commentaries' (2011).
[580] ibid; see Article 3: Absence of *ipso facto* termination or suspension the outbreak of an armed conflict does not *ipso facto* terminate or suspend the operation of treaties a s: (a) Between States parties to the treaty that are also parties to the conflict; b) Between a State party to the treaty that is also a party to the conflict and a State that is a third State in relation to the conflict. See also Article 5: The operation of treaties on the basis of implication from their subject matter [1.] In the case of treaties, the subject matter of which involves the implication that they continue in operation, in whole or in part, during armed conflict, the incidence of an armed conflict will not as such affect their operation.
[581] See NAFTA art 1105(2), which also contains the obligation to non-discriminatory treatment with respect to measures adopted relating to losses suffered owing to armed conflict or civil strife.

There are two types of responsibility which must be honored by the host state: contractual liability and international responsibility.[582] The criterion that distinguishes between them is whether the state acts in its sovereign capacity or in a commercial role as a party to a contract. The ILC asserts that international law held that host state's conduct violation relating to breach of contract will not raise international state's responsibility. The international state responsibility will only be raised in contractual liability context when other factors arise that attract international scrutiny; for example, when justice has been denied.[583] Also, in the *Shufeldt Claim*, arbitrator held that the revocation of a concession contract through the practicing of public authority is thereby raised to the status of an international claim.[584] Accordingly, it appears that the state's international responsibility exists whenever the state exercises its public authority.

Generally, any irregularities in the acts of a state acts can prompt the application of the principle of responsibility. This principle is defined by the ILC draft articles on the Responsibility of States for Internationally Wrongful Acts. Article 1 provides that "every internationally wrongful act of a State entails the international responsibility of that State."[585] This is clarified in Article 2 as "an internationally wrongful act of a State when the conduct consisting of an action or omission: (a) is attributable to the State under international law; and (b) constitutes a breach of an international obligation of that State." [586]

It seems that this Article 1 defines the basic principle, whereby every internationally wrongful state act raises the question of its international obligations, while Article 2 states the criteria used to establish the existence of internationally wrongful acts of the state. Moreover, a state is responsible for its state organs and entities which act in a way that harms investments.[587] The elements of the states' Attribution Under the ILC Articles are defined in Article 4, which refers to the 'Conduct of organs of a State.'[588] Article 5 refers to the 'Conduct of persons or entities

[582] Feit, 'Responsibility of the State under International Law for the Breach of Contract Committed by a State-Owned Entity' (n 567)
[583] ILC, 'Draft Articles on Responsibility of States for Internationally Wrongful Acts, with Commentaries' (2001) art 2 para (3) (ILC Draft Articles).
[584] *Shufeldt Claim (Guatemala v USA)* (1930) 2 RIAA 1079.
[585] ILC Draft Articles (n 17).
[586] ibid.
[587] *Asian Agri Prods Ltd v Sri Lanka* (n513)
[588] ILC Draft Articles (n 17) art 4. It explains, 1. 'The conduct of any State organ shall be considered an act of that State under international law, whether the organ exercises legislative, executive, judicial or any other functions, whatever position it holds in the organization of the State, and whatever its character as an organ of the central Government or of a territorial unit of the State. 2. An organ includes any person or entity which has that status in accordance with the internal law of the State.' The commentary to the Draft explains that (1) para 1 of art 4 includes an organ of any territorial governmental entity within the State on the same basis as the central

exercising elements of governmental authority.'[589] This latter includes a discussion of harms that are perpetrated by government authorities,[590] courts,[591] military,[592] and employees of state entities.[593] Article 8 refers to 'Conduct directed or controlled by a State.'[594]

Articles 4, 5 and 8 each set forth a basis for attribution to the state. Nevertheless, they do not identify in which cases a wrongful act can be attributed to the state and the consequences of responsibility. These articles also do not have a general rule regarding those issues. The said rules differ from one context to another for reasons that fundamentally relate to the purposes and objects of the treaty provisions or other rules that give rise to the primary obligations.[595] The use of said rules was reflected in a recent case, that previously mentioned *Ampal-American Israel Corp. and others v Arab Republic of Egypt*.[596] As previously said, claimant claimed that Egypt had breached the United States–Egypt BIT.[597]

The claimant was a group of US-incorporated companies along with shareholders of a tax-free zone company called the East Mediterranean Gas Company (EMG) incorporated in Egypt. The main purpose of EMG is to purchase natural gas from Egypt and to export it to Israel through a pipeline. EMG, as well as the Egyptian General Petroleum Company (EGPC), the latter being a state-owned company, signed a preliminary agreement for the sale of natural gas in 2000.

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governmental organs of that State: this is made clear by the final phrase. Art 4 covers organs, whether they exercise 'legislative, executive, judicial or any other functions.'

[589] ILC Draft Articles (n 17) art 5 explains that 'The conduct of a person or entity which is not an organ of the State under Article 4 but which is empowered by the law of that State to exercise elements of the governmental authority shall be considered an act of the State under international law, provided the person or entity is acting in that capacity in the particular instance.' According to the ILC commentary, art 5 deals with the attribution to the State of conduct of bodies which are not State organs in the sense of art 4, but which are nonetheless authorised to exercise governmental authority.

[590] *MNSS BV v Montenegro*, ICSID Case No ARB(AF)/12/8, Award (2016); also see *Venezuela, C.A. v Bolivarian Republic of Venezuela*, ICSID Case No ARB/12/21 (2012).

[591] *Frontier Petroleum Serv Ltd v The Czech Republic*, UNCITRAL Case No. 2008-09, Award of 12 November 2010

[592] *American Manufacturing & Trading, Inc. v Republic of Zaire*, ICSID Case No. ARB/93/1 (1997).

[593] *Wena Hotels Ltd v Egypt*, ICSID Case No ARB/98/4, 84 (2000).

[594] ILC Draft Articles (n 17) art 8 explains that 'The conduct of a person or group of persons shall be considered an act of a State under international law if the person or group of persons is in fact acting on the instructions of, or under the direction or control of, that State in carrying out the conduct.' According to ILC commentary (1), as a general principle, the conduct of private persons or entities is not attributable to the state under international law. Circumstances may arise, however, where such conduct is nevertheless attributable to the state because there exists a specific factual relationship between the person or entity engaging in the conduct and the state. Art 8 deals with two such circumstances.

[595] ILC Draft Articles (n 17) art 2 para (3).

[596] Ampal-American Israel Corp. et al (n 138).

[597] Treaty between the United States of America and The Arab Republic of Egypt Concerning the Reciprocal Encouragement and Protection of Investments Signed March 11, 1986 (modified); Entered into Force June 27, 1992

EGPC and EMG further entered into a Tripartite Agreement and a Source Gas Sale Purchase Agreement (GSPA) in 2005, together with the Egyptian Natural Gas Holding Company (EGAS), which is a state-owned company.

The issue is that, after the Egyptian revolution, Egypt terminated the GSPA in order to discontinue all exports to Israel. Therefore, the claimant raised a claim against Egypt for breaching the BIT. The claimant argued that EGPC/EGAS' conduct was attributable to Egypt by virtue of Articles 4, 5, 6, 8 and 11 of the ILC Draft Articles on State Responsibility (the ILC Articles).[598]

The arbitral tribunal assessed the issue of attribution and agreed with the claimant, finding that under Article 4 of the ILC Articles, EGPC/EGAS are state organs. The tribunal made its decisions by referring to Egyptian law, which stated that EGPC is a public authority that is supervised by the Ministry of Petroleum. EGAS was in the same position since it is completely owned by EGPC and also supervised by the Minister of Petroleum. Moreover, the tribunal found that under Article 8 of the ILC Articles, the acts of EGPC/EGAS were attributable to Egypt, since both entities acted at all times under the state of Egypt's direction and control. The tribunal finally held that under Article 11 of the ILC Articles, Egypt acknowledged EGPC/EGAS' acts because it ratified the termination of the GSPA.[599] Accordingly, *Ampal* case explains how tribunals assess state responsibility for internationally wrongful acts. However, this begs the question of the degree to which revolutionary governments are responsible for its failure in protecting foreign investment during times of upheaval: i.e., during the revolution which brought them to power?

5.2.2 State Responsibility for Failure to Protect a Foreign Investment

Under international law, the host state is responsible for any failure to provide full protection and security ("FPS") to foreign investors. The FPS standard is one of the "non-absolute" treatment standards. It does not depend on the host state's treatment of other investors or investments. This standard obliges the state to adopt protective measures to protect investors

[598] *Ampal-American Israel Corp v Egypt* (n 138).
[599] ILC Draft Articles (n 17) art 11: '*Conduct acknowledged and adopted by a State as its own* Conduct which is not attributable to a State under the preceding articles shall nevertheless be considered an act of that State under international law if and to the extent that the State acknowledges and adopts the conduct in question as its own'.

and investments from physical harm.[600] The state obligation is to provide protection and facilitation to foreign investments on its territory; this is expressed in customary international law and in treaties between individual investors and nations. It is found in most BITs as the 'most constant protection and security' provision (also expressed as 'full protection and security'); for example, Article 2(2) of the United Kingdom–Vietnam BIT reflects this common formulation, stating:

"Investments of nationals or companies of each Contracting Party shall at all times be accorded fair and equitable treatment and shall enjoy full protection and security in the territory of the other Contracting Party."[601]

Generally, standards of protection and security work as guarantees against physical violence.[602] The host state is responsible for violence by its organs. This was reflected in the *Biwater Gauff* v *Tanzania* case, where the tribunal held that the "full security" standard is not limited to a state's failure to prevent actions by third parties, but also extends to actions by organs and representatives of the state itself. At the same time, the state is responsible for protecting the investor against private violence.[603] This is reflected in the case of *El Paso Energy Co. v Argentina*, which found that the FPS standard "is a residual obligation provided for those cases in which the acts challenged may not in themselves be attributed to the Government, but to a third party."[604]

A good example of private violence occurring where the state held responsibility for foreign investment protection is given in the case of *AAPL* v *Sri Lanka*, where investments had been devastated in the counter-insurgency operation carried out by the security forces of security forces.[605] The applicable treaty provided that foreign investments "shall enjoy full protection and security."[606] The tribunal held that there is no evidence on whether the destruction had been caused by the security forces of the state or by the insurgents. However, the tribunal held

[600] Nartnirun Junngam, 'The Full Protection and Security Standard in International Investment Law: What and Who Is Investment Fully [?] Protected and Secured From?' (2018) 7(1) American University Business Law Review 1
[601] Agreement Between the Government of the United Kingdom of Great Britain and Northern Ireland and the Government of the Social Republic of Vietnam for the Promotion and Protection of Investments(2002)
[602] Roland Klager, *Fair and Equitable Treatment in International Investment Law* (Cambridge University Press 2012).
[603] Such as demonstrators and unpaid employees.
[604] *El Paso Energy Int'l Co v The Argentine Repub*, ICSID Case No ARB/03/15, Award of 31 October 2011)
[605] *AAPL* v *Sri Lanka*, 4 ICSID Reports 246, Award of 21 June 1990.
[606] Agreement Between the Government of the United Kingdom of Great Britain and Northern Ireland and the Government of the Democratic Socialist Republic of Sri Lanka for the Promotion and Protection of Investments.

that although in principle a state is not responsible for the insurgent's actions, it has a protection duty which implies that it does not matter whether the damaging acts originated from the government's forces or insurgents.

Another example is seen in the case of *American Manufacturing and Trading Inc. (AMT) v Zaire*, where there was domestic unrest in the host state; the tribunal held that Zaire did not take any action to protect the property of the claimant during the riots that took place.[607] The tribunal also held that there was no evidence regarding whether Zairian armed forces had committed illegal acts, but Zaire had responsibility and an 'obligation of vigilance' was established in relation to the failure to provide full protection and security and for the losses caused by the riots.[608]

Consequently, over-enforcement theory can explain that FPS standard is extensive interpreted among different arbitral tribunals where it extends to the state's duty to protect against private violent actions. This raises the question of whether tribunals should consider the ability of the state to protect foreign investment during times of conflict. This is reflected in case of *Pantechniki v Albania* – a dispute raised because of the overrunning of the investor's road work site in Albania during the civil disturbances of 1997. The claimant alleged that the government had failed to provide full security and protection to investments, because of the civil disturbances.[609] In this case, the sole arbitrator, Paulson, made a distinction between the refusal of the host state to provide protection and its inability to do so. Paulsson found that the authorities of Albania were "powerless in the face of social unrest of its magnitude" and dismissed the claim. The *Pantechniki* tribunal wisely opined: "[a]n investor investing in an area with endemic civil strife and poor governance cannot have the same expectation of physical security as one investing in London, New York or Tokyo."[610]

Another similar situation is found in *LESI*; the tribunal assessed the standard of due diligence taken by measuring the degree of protection granted by the host state to its nationals as opposed to nationals of third party states.[611] The *LESI* tribunal found that Algeria was not liable under

[607] *AMT v Zaire*, ICSID Case No ARB/93/1, Award of Feb 1997
[608] See Congo, Democratic Republic of the - United States of America BIT (1984).
[609] See Agreement Between the Government of the Hellenic Republic and the Government of the Republic of Albania for the Encouragement and Reciprocal Protection of Investment.
[610] *P Pantechniki SA Contractors & Engineers v Repub of Albania*, ICSID Case No ARB/07/21, Award of 20 July 2009.
[611] Claims due to Algeria's civil unrest during the 1990s affected a public tender awarded to the claimant for the construction of a dam that would provide drinking water to the city of Algiers.

FPS, because it was not less favorable inclined to protect foreign investors than it was to protect its own nationals.[612] Accordingly, using the under-enforcement theory as analytical tool can explain that *Pantechniki* and *LESI* tribunals under-enforced the host state liability under FPS based on justification the limited ability of the state to protect foreign investment during civil disturbances. Thus, under-enforcement theory can reflect the tribunal view on protecting state's interests above investor's interests.

On the other hand, the *Ampal* tribunal is the latest case by today date to have addressed a state's responsibility to protect foreign investment in the course of a revolution. As mentioned earlier, the dispute happened because of a pipeline that was operated by the Egyptian company Eastern Mediterranean Gas (EMG), where majority-owned by the Ampal-American Israel Corp. The purpose of the pipeline is to deliver natural gas provided by the Egyptian Natural Gas Holding Company (EGAS) to Israel.

The claimant raised the claim that Egypt had violated the clause of full protection and security under BIT by not taking necessary measures to avoid attack. From February 2011 to April 2012, the pipeline was attacked 13 times by terrorists. Claimant complained that due to the Egyptian revolution, Egypt "failed to take reasonable precautionary, preventive, and remedial measures" to protect the pipeline's physical security from attacks and that this was in breach of Egypt's FPS obligations under the US-Egypt BIT. The *Ampal* tribunal confirmed that "Egypt was under no absolute obligation or strict liability but had to comply with a standard of due diligence, which had to be assessed against the particular circumstances in which the damage occurs." The tribunal placed emphasis on how the host state responded to the harm.[613]

[612] *Consortium Groupement L.E.S.I.- DIPENTA v. République algérienne démocratique et populaire,* , ICSID Case No ARB/03/8, Award of 10 June 2005.

[613] The *Ampal* tribunal stated that 'The duty imposed by the international standard is one that rests upon the State. However, since it concerns an obligation of diligence, the Tribunal is of the view that the operation of the standard does not depend upon whether the acts that give rise to the damage to the Claimants' investment are committed by agents of State (which are thus directly attributable to the State) or by third parties. Rather the focus is on the acts or omissions of the State in addressing the unrest that gives rise to the damage'.

The *Ampal* tribunal relied on the case of *Pantechniki*, noting that a government should not be internationally responsible "for failure to plan for unprecedented trouble of unprecedented magnitude in unprecedented places." The *Ampal* tribunal thus concluded that because of "political instability, security deterioration and general lawlessness [in the region], the first attack did not violate the FPS standard."[614] According to the *Ampal* tribunal, "the subsequent attacks on the pipeline created a pattern of delayed measures or a failure to implement measures to guarantee the safety and security of the pipeline and hence the investor's investment in violation of its due diligence obligation."[615]

The over-enforcement theory can explain that although the *Ampal* case tribunal referred to the *Pantechniki* tribunal, but it did not consider the exceptional circumstances of the state and its limited resources. It seems that the *Ampal* tribunal ignored the complex political transition which took place in Egypt and focused only on pipeline protection. Although some attacks were not entirely unforeseen, still there was radical political change taking place. This made the role of the armed forces to provide all possible protection was impossible to entirely fulfil. This is because the Egyptian military was subject to an absence of internal security and also had huge political responsibilities. Indeed, according to Provost, the issue is the state's failure to discharge its responsibility to protect, and its violation of its international obligations, and these issues should be considered without reference to the state's means of enforcement.[616]

However, over-enforcement theory can explain that the *Ampal* tribunal transformed the standard of due diligence from a duty of care to a strict liability unconsciously. The problem with this lies in the fact that this decision of the *Ampal* tribunal is not a development of, but an accurate use of the FPS standard under customary international law. This is because neither ICISD precedents nor customary international law set clear parameters for FPS standard. Thus, both over- and under-enforcement theories can shed the light on the vagueness of texts, arbitral tribunals can easily choose to over or under-enforce the law based on arbitrator's discretion. This can result to inconsistent decisions. Further tribunals need to define parameters of FPS standard in both exceptional and ordinary circumstances.

[614] Technical report provided that *Attack no 3 (April 2011) took* place *exactly a month later after first and second attacks took place.*
[615] *Ampal-American Israel Corp v Egypt* (n 138).
[616] Provost, *State Responsibility in International Law* (n 534).

Moreover, both over and under-enforcement theories can explain that inconsistent decisions on FPS standards results due to analytical reasons to render their own notion of justice. Some tribunals such as *Pantechniki* and *LESI* tribunals under-enforced the host state liability under FPS based justifying the limited ability of the state to protect foreign investment during civil disturbances. On the other hand, other tribunals such as *Ampal* tribunal see justice by doing expensive interpretation to the law in transforming due diligence standard from a duty of care to a strict liability unconsciously. This highlights the need for parameters of due diligence to be defined. This attribute to the problems of under-defined law where broad law that creates selective interpretation. The more precise the obligation content that diligence requires, the more precise of what is expected by the state in terms of act. However, there is another investment treatment standard defined by international investment law that frequently arises whenever there is a dispute between a foreign investor and a host state in the course of a civil disturbance. This is the standard of fair and equitable treatment.

5.2.3 State failure to provide fair and equitable treatment to foreign investors

Under international investment law, a host state may be held responsible for its failure to provide fair and equitable treatment to foreign investors. The term 'fair and equitable treatment' means that foreign investors share advantages and rights which are similar to those enjoyed by state nationals. However, with regard to the term 'fair and equitable treatment', it is unclear whether the said term relies on the state's judgement and/or the individuals' sense of propriety.[617] The term has not been defined within multilateral, regional or bilateral treaties.[618] For example, in the case *of Suez and others v The Argentine Republic*, the ICISD tribunal noted that the word "treatment is not defined in the treaty text. However, the ordinary meaning of that term within the context of investment includes the rights and privileges granted and the obligations and burdens imposed by a Contracting State on investments made by investors covered by the treaty."[619]

[617] *CMS Gas Transmission Co* (n384), where the tribunal observed this treaty 'like most bilateral investment treaties, does not define the standard of fair and equitable treatment'.
[618] Peter Muchlinski, *Multinational Enterprises and the Law* (Oxford University Press 2007) 635.
[619] *Suez, Sociedad General de Aguas de Barcelona SA, and InterAguas Servicios Integrales del Agua SA v The Argentina Repub*, ICSID Case No ARB/03/17, decision on jurisdiction of 3 Aug 2006

Thus, states develop their own levels and norms regarding what they decide are fair and equitable, in relation to their acts and philosophies. These judgments are made in the context of customary international law and precedent case law.[620] Foreign investors mostly expect 'fair and equitable treatment' in terms of enjoying the same minimum standards in international law as other investors in the same sphere of activity.'[621]

Generally, fair and equitable treatment (FET) clause gives investor the right to sue the government in the international arbitration. However, arbitral tribunals have dissimilar views on the extent in which the FET provides protection from legal and policy changes.[622] Some tribunal considered that the FET provision is a kind of guarantees against any major changes in the policies and laws that govern foreign investments. For instance, *Occidental v. Ecuador* case[623], the tribunal viewed that stability is essential component of FET provisions which is the same as the case of *Temced v. Mexico. Temced* tribunal viewed the FET provisions as it should protect the basic expectations of investors.[624]

This is exactly the same as in the case of *Frontier Petroleum v. Czech Republic*. The tribunal viewed that the legitimate expectations of investor is based on the legal stability of host state.[625] On the other hand, other tribunals viewed that there are circumstances that a host state can legitimately change its contractual terms and laws that govern foreign investments. For example, the Tribunal of *EDF v. Romania* case viewed that FET provisions and legitimate expectations that obliged the stability of business and legal framework is not correct. A state that did not succeed to provide stable business and legal environment should be evaluated in the light of its economic and political situation.[626] Thus, tribunals did not agree on the circumstance that can be qualify as a breach to the FET provisions standards.[627]

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[620] See also the recent *Ampal* (n 138) case where claimant alleged Egypt had breached provisions of the bilateral investment treaty, including the FET clause, art II(4) of the US Treaty and customary international law, by engaging in arbitrary and discriminatory measures against the claimant's investment. This is because it was selling natural gas to Israel. The tribunal found that the wrongful termination of the GSPA by the respondent was tantamount to an expropriation. The tribunal did not have to determine whether the termination constituted a breach of the FET standard.

[621] Foreign investors expect 'fair and equitable treatment' in the same minimum standards in international law as other investors in the same sphere of activity. Even if the investor is accorded national treatment, a state may treat the foreign investor abusively. The international minimum standard of treatment in customary international law is designed to safeguard the states that are responsible for damages and injuries caused by arbitrary acts.

[622] ibid.

[623] *Occidental Petroleum Corporation and Occidental Exploration and Production Company v. The Republic of Ecuador,* ICSID Case No. ARB/06/11, Award of 5 October 2012

[624] *Técnicas Medioambientales Tecmed, S.A. v. The United Mexican States*, ICSID Case No. ARB (AF)/00/2, Award of 29 May 2003

[625] *Frontier Petroleum Serv Ltd v The Czech Republic (*n565)

[626] *EDF (Services) Limited v. Romania,* ICSID Case No. ARB/05/13,2009, Award of 8 October 2009

Also, scholars such as Dolzer illustrated the complexity of clause of fair and equitable treatment. As to define it is a complex task, some tribunals interpreted this clause by using the strictly treaty. They do efforts to spell out the meaning of clause. This is not useful in differentiating the explanation of both terms of Fair and Equitable. It seems sensitive to classify on what can be acceptable or unacceptable. [628]

Accordingly, both over and under-enforcement theories explain the inconsistent decisions on application FET standards is due to analytical reasons. There is a lack of defining the circumstance that can be qualify as a breach to the FET provisions standards. Tribunals interpret the textual language based on their views of the meaning of words. There is also an interrelated requirement that is seen in investment treaties, which is to treat foreign investors in a similar way in which resident nationals of a host state are treated.[629]

The "National Treatment" clause means that foreign investors will be treated equally to national investors. There is should be no discriminations between investors but the problem is this clause has a broad interpretation. Also, it is hard to define "National Treatment." This is because broad interpretation will consider the government actions that negatively affect the foreign investor's interests as a violation to this clause. Although, there can be a lack of evidence. On the other hand, a tight interpretation would ask for a discrimination claim to have an evidence to find a breach. Thus, tribunals can over or under-enforce the requirement of treatment in investment treaties based what they see reasonable. This can result to inconsistent decisions. This issue is identical with other clauses that are used in ILA.[630] This makes scholars to argue that Host states and investors found that the ILAs system is difficult because they do not know how the arbitral panels will interpret such as law.[631]

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[628] Rudolf Dolzer, 'Fair and Equitable Treatment: Today's Contours' (2014) 12(1) Santa Clara Journal of International Law 7

[629] A national treatment provision requires that a state accord the investment and investor no less favourable treatment than the state harmonises to its own investors and their investments in like circumstances with respect to the operation, use, management, disposal or enjoyment of investments. The standard is ambiguous and requires more explanation. Moreover, there is similar investment protection provision 'Non-discrimination'.

[630] some investment treaties stipulate the clause of MFN. The purpose of most favoured nation (MFN) clauses in treaties is to guarantee that the relevant parties treat each other in a manner at least as favourable as the manner in which third parties are treated. Generally, the majority of the investment treaties stipulate the standard of FET with the MFN treatment, national treatment or both.

[631]Brown, 'International Investment Agreements: Regulatory Chill in the Face of Litigious Heat?'(n26)

5.2.4 Findings of first phase question

The first phase, here, questions to what extent are transitional governments responsible for protecting foreign investment in the course of a violent revolution. The answer is there is absence of clarity about the degree to which the host state will be responsible for protecting foreign investors during civil disturbance. Accordingly, the first phase, here, question to what extent are transitional governments responsible for protecting foreign investment in the course of a violent revolution. In terms of the answer, this can be summarized that investment tribunals and international customary law have agreed on what constitutes state responsibility for internationally wrongful acts. A state is responsible for the wrongful act of its state organs. The principle of attribution to a state is well defined, but what constitutes a breach of international obligations based on the case facts and the investment treaties in place.

Nevertheless, there is lack of clarity regarding the degree to which a host state will be responsible for protecting foreign investors during civil disturbance. Both over and under-enforcement theories explain that investment protection standards are undefined where it creates selective interpretation. The *Pantechniki* and *LESI* tribunals assessed the host state's liability under FPS by considering the state's limited resources in relation to protecting foreign investment during civil disturbance. On the other hand, the *Ampal* tribunal examined state liability under FPS without considering the limited resources of the state during civil disturbance. It appears that arbitrators can choose to over or under FPS standards based on their discretion. Arbitrators are trying to square the law with the facts of the case to render their own belief of justice. This is similar to the term 'fair and equitable standard,' is not defined in investment treaties. It depends on arbitral tribunal discretion. Thus, arbitrators can choose to over or under-enforce 'fair and equitable standard' based on their discretion. It appears that tribunals interpret the textual language based on their views of the meaning of words. This is

because investment treaties do not create concrete rules, but only abstract standards and open-ended.[632] This result to inconsistent decisions.

Accordingly, there is lack of clarity regarding the degree to which the host state will be responsible for protecting foreign investors during civil disturbance. This raises a question regarding post-revolutionary periods of a state, namely to what extent are revolutionary governments allowed to change their public polices and laws in ways that they may affect the interests of foreign investors for the purpose to meet the demands of public needs. Thus, the second section of this current chapter examines the limitations imposed on transitional governments in relation to regulating their domestic affairs post revolution. This entails an examination of the state's responsibility for foreign investment expropriation.

5.3 Phase Two

Host state's Right to Regulate versus Expropriation

First of all, expropriation denotes the situation whereby a government takes private property for a purpose deemed to be in the public interest. There are two types of expropriation, namely, direct expropriation and indirect expropriation.

5.3.1 Direct Expropriation

It is not difficult to identify cases where a host state has forced the transfer of property from a private party to the state. In the case of *LG&E v Argentina*,[633] the tribunal clarified the meaning

[632] For example, there is diversity in the way the 'fair and equitable treatment' standard is open-ended and abstract. It depends on how arbitral tribunal will interpret it. Also, some BITs clearly define 'fair and equitable treatment' by referring to international law, while others BIT do not make such reference.
[633] Treaty Between the United States of America and the Argentine Republic Concerning the Reciprocal Encouragement and Protection of Investment (signed 14 November 1991, entered into force 20 October 1994) (US–Argentina Treaty).

of direct expropriation by stating that it is 'the forcible appropriation by the state of the tangible or intangible property of individuals by means of administrative or legislative action.'[634] Moreover, the meaning of 'transfer of property' was confirmed in the case of *Enron v Argentina*, as follows: "the tribunal does not believe there can be a direct form of expropriation if at least some essential components of property rights have not been transferred to a different beneficiary, in particular the State."[635]

Nevertheless, modern state practice exhibits that states rarely use direct expropriation. This is because states know the negative international political consequences of such an act.[636] Investors are aware that expropriation by states can occur, but not usually directly.[637]

5.3.2 Indirect Expropriation

It is hard to find indirect expropriation. This occurs when a state interferes with the use, enjoyment or benefit of an investment, or otherwise the state takes effective control of an investment, resulting in the depreciation of its financial value, but without the direct taking of property.[638] The tribunal of the *Santa Elena v Costa Rica* case noted that states' behaviour in depriving foreign investors of their investments is the fundamental issue when it comes to understanding how indirect expropriation functions. The *Santa Elena v Costa Rica* tribunal stated that

"[T]here is a wide spectrum of measures that a state may take in asserting control over property, extending from limited regulation of its use to a complete and formal deprivation of the owner's legal title. Likewise, the period of time involved in the process may vary – from an immediate and comprehensive taking to one that only gradually and by small steps reaches a condition in which it can be said that the owner has truly lost all the attributes of ownership. It is clear, however, that a measure or series of measures can."[639]

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[634] *LG&E Energy Corporation et al. v Argentina* (n401
[635] *Enron Corp Ponderosa Assets, L P v Argentina* (n401)

[636] Krista Nadakavukaren Schefer, *International Investment Law: Texts, Cases and Materials* (Edward Elgar 2013).

[637] Louis Yves Fortier and Stephen L Drymer, 'Indirect Expropriation in the law of International Investment: I Know It When I See It or Caveat Investor?' (2004) 19(2) ICSID Review – Foreign Investment Law Journal 293.
[638]Rudolf Dolzer and Christoph Schreuer, *Principles of International Investment Law* (Oxford University Press 2012).
[639] *Compania del Desarrollo de Santa Elena, SA v Repub of Costa Rica* (2000) 39 ILM 1317, 1329.

Also, the indirect expropriation is seen in *Ampal* case as mentioned earlier, the *Ampal* case is the most recent case by day date to have addressed a dispute between a revolutionary government and foreign investors. Egypt granted, in 2006, a licence to EMG, the majority of which is owned by the Ampal-American Israel Corp, to continue to work under the private tax-free zone regime. In the following year, it extended EMG's tax-exempt status until 2025. Firstly, the issue was that Egypt cancelled EMG's tax-exempt status in 2008 by enacting new legislation. The claimant claimed that Egypt's measures had destroyed their investment. The question was whether the tax-free license revocation constituted an expropriation. According to the BIT wording, the license was an investment.[640]

The *Ampal* tribunal then analysed whether the wrongful termination of the GSPA constituted an unlawful expropriation under the BIT. In this regard, the *Ampal* tribunal first examined whether the rights conferred to the claimant by the GSPA constituted an investment protected under the BIT. Based on the wording of the BIT, the tribunal found that the claimant's property interest in the GSPA was an investment protected under this. The tribunal also found "that the inclusion of EMG within the tax-free zone system in Egypt was a fundamental part of the economic structure of the investment, which the Respondent knew and accepted from the outset at the highest level of Government, and which it confirmed by the issue of the specific license to EMG, conferring tax-free status under the free zones system until 2025."

These facts take the consideration of a change in the tax regime applicable to Claimants' investment in EMG well outside the realm of the ordinary exercise of the State's regulatory power. Therefore, the *Ampal* tribunal held that the revocation of tax exemption was expropriation.[641]

Generally, it is not clear what host state acts might constitute indirect expropriation; indirect expropriation does, however, involve many elements, none of which individually establish an international wrong. These elements contain cancellation, non-payment, non-reimbursement, and inconsistent legal blocks, non-conforming and so forth.[642] Although indirect expropriation

[640] See US–Egypt Treaty (n 511) art 1(c).
[641] *Ampal-American Israel Corp* (n 138).
[642] See *Waste Management Inc v United Mexican States* (2001), 40 ILM 56, 73.

is recognised in both case law[643] and international conventions,[644] there is a lack of clarity on the whole concept, which raises the question of whether an ordinary state's regulatory measures can result in indirect expropriation.[645] This is seen in the expropriation cases against Argentina, where the state took regulatory measures to safeguard itself from an tremendously severe financial crisis. And this problem was acknowledged over 60 years ago. In 1941, Herz noted "that where measures indirectly interfere with property rights it may often be very difficult to decide whether or not ... the limits of usual interference have been reached or transgressed so as to warrant a finding of expropriation."[646]

Likewise, another scholar, Dolzer, argued that what exactly the concept of indirect expropriation is intended to cover remains a matter of considerable contention.[647] This has led scholars to propose diverse ways to identify indirect expropriation. For example, Dolzer and Stevens proposed identifying indirect expropriation as any act that "... leaves the investor's title untouched but deprives him of the possibility of utilizing the investment in a meaningful way."[648] Isakoff proposed an alternative definition: "...the result of a progression of [state] regulatory measures."[649] Isakoff proposed a broad definition of "wealth deprivation."[650]

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[643] The Iran–US Claims Tribunal in *Starrett Housing Corp v Iran* (1983) 4 Iran-USCTR 122 and *Tippetts v TAMS-AFFA Consulting Engineers of Iran* (1986) 6 Iran-USCTR 219 stated the following with regard to indirect expropriation:
'[it] is recognized in international law that measures taken by a state can interfere with property rights to such an extent that these rights are rendered so useless that they must be deemed to have been expropriated, even though the state does not purport to have expropriated them and the legal title to the property formally remains with the original owner'.

[644] See Louis B Sohn and BB Baxter, 'Harvard Draft Convention on the International Responsibility of States for Injuries to Aliens' (1961) 55(3) American Journal of International Law 548. Indirect expropriation is defined as any such unreasonable interference with the use, enjoyment, or disposal of property as to justify an interference that the owner thereof will not be able to use, enjoy, or dispose of the property within a reasonable period of time after the inception of such interference.

[645] See *Toto Costruzioni Generali SpA v The Repub of Lebanon*, ICSID Case No ARB/07/12, Award of 7 June 2007; *Compania del Desarrollo de Santa Elena, S.A. v Republic of Costa Rica*, ICSID Case No. ARB/96/1, Award of February 17, 2000;*Czech Repub BV (The Netherlands) v The Czech Repub and Señor Tza Yap Shum v The Repub of Peru*, ICSID Case No ARB/07/6,Award of 7 July 2011

[646] John Herz, 'Expropriation of Foreign Property' (1941) 35(2) The American Journal of International Law .

[647] Rudolf Dolzer, 'Indirect Expropriations: New Developments?' (2002) 11 New York University Environmental Law Journal 64.

[648] Rudolf Dolzer and Margrete Stevens, *Bilateral Investment Treaties* (Martinus Nijhoff Publishers 1995) 61–62.

[649] Peter D Isakoff, 'Defining the Scope of Indirect Expropriation in International Investments' (2013) 3 Global Business Law Review .

[650] See Burns H Weston, 'Constructive Takings under International Law: A Modest Foray into the Problem of Creeping Expropriation' (1975) 16(1) Virginia Journal of International Law.

Nevertheless, it appears that determining what constitutes an indirect expropriation is problematic.[651] Also, investment treaties are causing confusion because it have codified indirect expropriation in various ways. This has resulted in vagueness of language, and this has led, in turn, to indirect expropriation parameters being controversial. Olynyk clarified that most investment treaties do not provide guidance on indirect expropriation".[652] For example, the Energy Charter Treaty (ECT) provides that:

"Investments of investors of a Contracting Party in the Area of any Contracting Party shall not be nationalised, expropriated or subjected to a measure or measures having effect equivalent to nationalisation or expropriation..."[653]

Accordingly, tribunals consider the customary international law to determine indirect expropriation.[654] The issue is that international law does not prohibit expropriation per se. International law provides every state with the right to regulate property within its own territory. States are free to expropriate property within their territories, to restrict or permit trade with other states, to differentiate in their commerce relations, and to control their own currency.[655] This raises the question of, to what extent is the host state allowed expropriating foreign investment?

5.3.3 Limitations on the State's Right of Expropriation

Over the past years many expropriations have resulted from spontaneous events or from extreme political events. The idea of property was initially considered as an absolute right of state. This matter has been altered. Property as an absolute right has been substituted by a right with conditions, which are reflected in international customary law.[656] However, under modern investment law, a state can exercise its sovereign power to expropriate, but only under certain conditions. International law attempts to balance between the investor's right to be compensated for property taken and the state's right to regulate the property within its territory.

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[651] Ben Mostafa, 'The Sole Effects Doctrine, Police Powers and Indirect Expropriation under International Law' (2008) 15 Australian Journal of International Law 267.
[652]Stephan Olynyk, 'A Balanced Approach to Distinguishing Between Legitimate Regulation and Indirect Expropriation in Investor-State Arbitration' (2012) 15 International Trade & Business Law Review.
[653] Energy Charter Treaty (opened for signature 17 December 1994, entered into force 16 April 1998) 2080 UNTS 95.
[654] Mostafa, 'The Sole Effects Doctrine, Police Powers and Indirect Expropriation under International Law' (n 651).
[655]Prabhash Ranjan and Pushkar Anand, Determination of Indirect Expropriation and Doctrine of Police Power in International Investment Law: A Critical Appraisal' in Leila Choukroune (ed), Judging the State in International Trade and Investment Law (Springer Nature 2016)
[656] Samy Friedman, *Expropriation in International Law* (The London Institute of World Affairs 1953).

The issues of whether a state uses its right of sovereign power to expropriate the foreign investor's property and the limitation to its use such a power is answered in Article 4 of the UNGA resolution on Permanent Sovereignty Over Natural Resources (representing customary international law).

"Nationalisation, expropriation or requisitioning shall be based on grounds or reasons of public utility, security or the national interest, which are recognised as overriding purely individual or private interests, both domestic and foreign. In such cases, the owner shall be paid appropriate compensation in accordance with the rules in force in the state taking such measures in the exercise of its sovereignty and in accordance with international law. In any case, where the question of compensation gives rise to a controversy, the national jurisdiction of the state taking such measures shall be exhausted. However, upon agreement by sovereign states and other parties concerned, settlement of the dispute should be made through arbitration or international adjudication."[657]

It is critical to mention that the concept of nationalisation is different in its scope from the concept of 'expropriation.' The latter is used to describe a situation where a host state acts in individual cases, while "nationalization" is a measure involving larger changes in the social and economic operation of a state. In general, many MITs and BITs do not distinguish between the concepts of expropriation and nationalisation; this is perhaps because, for the foreign investor, they may have the same legal and practical impact. International conventions provide states with the right to nationalise and expropriate foreign assets on their territory, which is a big concern for foreign investors. Nevertheless, the CERDS does not provide clear definitions of either nationalisation or expropriation. The issue is that, many Multilateral Investment Treaties (MITs), (ILG) or BITs refer to CERDS terms in a general way, tending to focus on the conditions which a state must have fulfilled in order to make its act lawful.[658] These

[657] United Nations General Assembly 'Permanent Sovereignty over Natural Resources' (14 December 1962) Res 1803 (XVII).

[658] See Article 5 Expropriation and Compensation of Agreement on Promotion, Encouragement and Reciprocal Protection of Investments Between the Kingdom of the Netherlands and the United Mexican States (1) Neither Contracting Party shall take any measures depriving, directly or indirectly, nationals of the other Contracting Party of their investments, unless:
(a) the measures are taken in the public interest and under due process of law,
(b) the measures are not discriminatory, and
(c) compensation is paid in accordance with paragraphs (2) to (4) of this Article.
Also see Art 4(1) of the Sweden–Mexico BIT states that "neither contracting party shall expropriate or nationalise an investment of an investor of the other contracting party, either directly or indirectly through measures tantamount to expropriation or nationalisation (hereinafter referred to as 'expropriation')": see Art 13 of Canada's model FIPA (2004), AGREEMENT BETWEEN CANADA AND FOR THE PROMOTION AND PROTECTION OF INVESTMENTS; see Art 6.5 of Comprehensive economic co-operation agreement between India and Singapore (2005): Also, see Art 4 of BIT: Chile and the UK (1996)

conditions are shown in Article 3 of the Organization for Economic Co-operation and Development Draft (OECD, 1967), which states that:

"No Party shall take any measures depriving, directly or indirectly, of his property a national of another Party unless the following conditions are complied with: (i) The measures are taken in the public interest and under due process of law; (ii) The measures are not discriminatory or contrary to any undertaking which the former Party may have given; and (iii) The measures are accompanied by provisions for the payment of just compensation."[659]

Article 6 of the US Model BIT provides a definitive example, stipulating that:

"Neither party may expropriate or nationalise a covered investment either directly or indirectly through measures equivalent to expropriation or nationalisation ("expropriation"), except: (a) for a public purpose; (b) in a non-discriminatory manner; (c) on payment of prompt, adequate, and effective compensation; and (d) in accordance with due process of law."[660]

We can infer that the foreign investment expropriated by a host state is not prohibited per se. International law allows expropriation that is based on three limitations: it should be for a public purpose; on a non-discriminatory basis; and compensation must be paid. Each of these principles has developed its own case law.[661] If these conditions are not met then the expropriation can be deemed unlawful and may be subject to state-foreign investor disputes. Thus, these conditions must be described.[662]

5.3.3.1 Expropriation for a Public Purpose

Public purpose is a condition for lawful expropriation which is seen in most BITs.[663] Generally, it is difficult for a tribunal to decide what constitutes the public interest of a host state. Thus, public interest is decided by the host state alone. This is seen in the tribunal in *Goetz and Others v Republic of Burundi*. The tribunal held that "In the absence of an error of fact or law, of an

[659] Art 3 OECD Draft Guidelines for Multinational Enterprises 1976.
[660] Art 6(1) United States Model BIT 2012.
[661] See NAFTA chap 1110, which also deals with similar limitations: No party may directly or indirectly nationalise or expropriate an investment of an investor of another party in its territory or take measures tantamount to the nationalisation or expropriation of such an investment ("expropriation"), except: (a) For a public purpose; (b) On a non-discriminatory basis; (c) In accordance with due process of law.
[662] See Article III(1) of the US Treaty
[663] Panama–UK BIT (1983) art 5(1); Costa Rica–UK BIT (1982) art 5(1); Bolivia–UK (1988) BIT art5.

abuse of power or of a clear misunderstanding of the issue, it is not the Tribunal's role to substitute its own judgment for the discretion of the government of Burundi of what are 'imperatives of public need ...or of national interest."[664]

Although the existence of a public purpose is determined solely by the host state, some arbitral decisions have assessed the policy that has been adopted by states.[665] In all cases, international investments tribunals require the state to provide evidence to justify any acts claimed to be taken for public purposes. This is seen in the recent case of *Veolia v Egypt*, where a French multinational company signed a contract with the Alexandrian governorate to provide management services for 15 years. Egypt changed its labour laws and increased minimum wages to meet public demand after the Egyptian revolution. In 2012 Veolia raised a claim against Egypt for breaching BIT between France and Egypt. [666] Veolia claimed that the change in Egyptian national laws had harmed their investment. There is a lack of available detail concerning the case, but the tribunal awarded in favour of the state. The tribunal held that the government has the right to improve workers' wages even where this works against the rights of a private investor.[667]

This is in contrast with the *Siemens A.G. v Argentina* case, where there was an agreement between the host state and a German corporate investor who provided identification and immigration services. The new government in Argentina suspended the contract in 1999 and the state had to renegotiate the contract within its own financial agenda, which negatively affected Siemens. The ICSID tribunal found that the state's action constituted unlawful expropriation. There was a lack of evidence to the effect that the state's action was based on a public purpose.

Similarly, to case of *Compañia de Aguas del Aconquija S.A. and Vivendi Universal S.A. v Argentine Republic,* a concession contract was breached between the French company and the Argentinian government.[668] The claimant debated that the government of the host state had

[664] *Goetz and Others v Repub of Burundi*, ICSID Case No ARB/95/3, Decision on liability of 2 September 1998).
[665] See *Marvin Roy Feldman Karpa v United Mexican States*, ICSID Case No ARB(AF)/99/1, Award (16 December 2002).
[666] Egypt - France BIT (1974)
[667] *Veolia Propreté v Arab Repub of Egypt*, ICSID Case No ARB/12/15, Award of 25 May 2018
[668] *Compañia de Aguas del Aconquija S.A. and Vivendi Universal S.A v Argentine Republic* ICSID ARB/97/3. Award of 21 November 2000

undermined the project operation and violated the BIT between France and Argentina.[669] The investor claimed that the government used its power to enforce unilaterally amended tariffs, contrary to the concession agreement terms. Argentina claimed that it is a sovereign act for public policy issues. Thus, the tribunal had to determine whether the Argentina acts were commercial acts or the use of sovereign power. The tribunal held that they were commercial acts. Consequently, there was a breach of the BIT fair and equitable treatment standard.[670] A state cannot rely on the contract clause jurisdiction to avoid its unlawful acts under a treaty. Thus, the treaty clause was activated and the case brought to international jurisdiction. The new government should have renegotiated the concession agreement in a non-coercive and transparent manner. It was unfair and unequitable to terminate the clause because evidence proved that it was not a sovereign act. As there was no evidence that there was a health risk from the water project, as provided by the investor, the government's act was an expropriation and the tribunal award was in favour of the investor.[671]

Both over and under-enforcement theories can explain that requirements of public purpose are hard to define. Tribunals can easily choose to over or under-enforced such requirements based on their judgement. Therefore, it is difficult to know whether a public purpose defence will be successful. Koskenniemi clarified that international law develops from a political process wherein states have contradicting interests. Thus, there is no linguistic ambivalence which can represent international law's indeterminacy.[672] In addition, we can see that the public purpose can justify a legal act of the state but not the level of compensation payable.[673]

5.3.3.2 Expropriation Undertaken on a Non-Discriminatory Basis

The purpose of the non-discrimination criteria is to avoid the host state from carrying out expropriation on a foreign policy interest basis. For example, Article 1102(4) of NAFTA[674]

[669] Agreement on the Reciprocal Promotion and Protection of investments (with related letter). France and Argentina Signed in Paris on 3 July 1991 No. 30174
[670] The obligations for host states to provide foreign investors fair and equitable treatment. It is stipulated in most of investment treaties.
[671] *Compañia de Aguas del Aconquija S.A. and Vivendi Universal S.A v Argentine Republic* (n 668)
[672] Martti Koskenniemi, *From Apology to Utopia: The Structure of International Legal Argument (Reissue with New Epilogue)* (Cambridge University Press 2005).
[673] See *Compañia del Desarrollo de Santa Elena* (n 645).
[674] NAFTA article 1102(4) stipulates: No party may: (a) impose on an investor or another party a requirement that a minimum level of equity in an enterprise in the territory of the party be held by its nationals, other than

warns against discriminatory acts by host states.[675] Moreover, scholars such as Foighel have asserted that "The rules of international law against discrimination can be considered to be satisfied when foreigners are given formal equality with the nationals of the country in question in respect of protection in similar situation."[676] Nevertheless, it is less clear what constitutes such conduct. Both over and under-enforcement theories can explain that requirement of non-discrimination criteria is hard to define. Arbitrators can easily choose to over or under-enforced such requirements based on their interpretation. This can result to inconsistent decisions.

Also, Scholars have tried to clarify the idea of discriminatory treatment. For example, Maniruzzaman contended that non-discrimination requires that foreign investors be treated the same as national investors.[677] Moreover, Dolzer and Stevens suggested that, to determine the presence of discrimination: (i) the measure must result in actual injury to the foreign investor; (ii) the act must be done with the intention of harming the aggrieved foreign investor.[678] Generally, an arbitrator or judge must assess all the relevant circumstances relating to the conduct and its context; this is because there is no list or formula that provides guidance on the conduct's acceptability.[679] Therefore, the rules are over or under-enforced based on arbitrators' discretion.

In addition, it can be prudent for a claimant to prove discrimination. This is seen in the case of the *American Independent Oil Company* (*Aminoil*), Kuwait's government granted an oil concession in relation to exploitation by this American company in 1946. However, after a number of years, the state renegotiated the agreement terms before deciding to pursue what was effectively expropriation under Decree Law Number 124 of 1977. *Aminoil* argued that the state's nationalisation act was based on discrimination, because another foreign oil company, the more local *Arabian Oil Company (AOC)*, which operated offshore under a joint concession granted by the governments of Saudi Arabia and Kuwait, had not had its operations nationalised under the Decree.[680]

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nominal qualifying shares for directors or incorporators of corporations; or (b) require an investor of another party, by reason of its nationality, to sell or otherwise dispose of an investment in the territory of the party.

[675] ibid.

[676] Kenneth S Carlston, 'Review of "Nationalization: A Study in the Protection of Alien Property in International Law" by Isi Foighel' (1959) 1959(1) Washington University Law Quarterly 97.

[677] Munir Maniruzzaman, 'Expropriation of Alien Property and the Principle of Non-Discrimination in International Law of Foreign Investment: An Overview' (1998) 8(1) Journal of Transnational Law and Policy .

[678] Dolzer and Stevens, *"Bilateral Investment Treaties"* (n 648).

[679] Maniruzzaman, 'Expropriation of Alien Property and the Principle of Non-Discrimination in International Law of Foreign Investment: An Overview' (n 650).

[680] Kuwait v American Independent Oil Co (Aminoil) (Award), 66 INT'L. L. REPORTS 519 (Mar. 24, 1982).

The ad hoc arbitral tribunal refused any suggestion of discrimination, stating:

"First of all, it has never for a single moment been suggested that it was because of the American nationality of the Company that the Decree Law was applied to the Aminoil's concession. Next, and above all, there were adequate reasons for not nationalising Arabian Oil. *AOC's* high-cost offshore production operations are such as to give it a special position which requires a high degree of expertise. At the same time, it is working within the framework of a concession granted by both Kuwait and Saudi Arabia, so its position is completely different. Any modification of concession must be agreed to by both countries."[681]

5.3.3.3 Expropriation should be Upon Payment of Compensation

The state's sovereign right to expropriate a foreign investor's property is balanced by the foreign investor's right for compensation. This concept is provided in Chapter II of the Charter of Rights and Duties of States (CERDS, 1974), reflecting the following provisions:

"To nationalize, expropriate, or transfer ownership of foreign property, in which case appropriate compensation should be paid by the State adopting such measures, considering its relevant laws and regulations and all circumstances that the State considers pertinent. In any case where the question of compensation gives rise to a controversy, it shall be settled under the domestic law of the nationalizing State and by its tribunals, unless it is freely mutually agreed by all States concerned that other peaceful means be sought on the basis of the sovereign equality of States and in accordance with the principle of free choice of means."[682]

Also, the recompense principle is stipulated in primary sources, such as the BIT of the United States and the Republic of Uruguay, which states that "neither party may expropriate or nationalise a covered investment either directly or indirectly through measures equivalent to expropriation or nationalisation ("expropriation"), except [...](c) on payment of prompt,

[681] ibid.
[682] Chapter 2 of the Charter of Rights and Duties of States (1974).

adequate, and effective compensation."[683] This is also reflected in the ILC Articles on state responsibility.[684]

Generally, lawful expropriation is well recognised under international law; a state must pay compensation for foreign property which has been expropriated, via a "prompt, adequate and effective" compensation formulation.[685] There is a lack of provisions that regulate unlawful takings of property. So, arbitrators must refer to general principles of law or customary international law[686] However, the question of expropriation legality appears to be of lesser importance in investment arbitrations.[687] This is because, under customary international law, regardless of whether the expropriation is lawful or unlawful, compensation must be given.[688] This is reflected in *Phillips Petroleum*, the tribunal established a unlawful/lawful taking distinction that can be found in customary international law, as reflected in the Case Concerning the Factory at *Chorzów*.[689] In the decision in *Chorzów*, which demonstrates that a lawful act does not require less compensation; such compensation should be equal to the property's value on the date that it was taken.[690]

Also, different tribunals did not differentiate between lawful and unlawful act in term of compensation. For instance, the tribunals of *Wena Hotels v. Egypt*[691], *Metalclad v. Mexico*[692],*Unglaube v. Costa Rica,*[693] *Guaracachi v. Bolivia*[694] and *Middle East Cement v.*

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[683] Treaty Between the United States of America and the Oriental Republic of Uruguay Concerning the Encouragement and Reciprocal Protection of Investment, with Annexes and Protocol (4 November 2005) art 6.
[684] Article 36 Compensation of ILC. 1. The State responsible for an internationally wrongful act is under an obligation to compensate for the damage caused thereby, insofar as such damage is not made good by restitution. 2. The compensation shall cover any financially assessable damage including loss of profits insofar as it is established.
[685] This is also known as the 'Hull formula'.
[686] See Jan Paulsson and Zachary Douglas, *Indirect Expropriation in Investment Arbitration' in Norbert Horn (ed), Arbitrating Foreign Investment Disputes* (Kluwer Law International 2004).
[687] Kevin Smith, *The Law of Compensation for Expropriated Companies and the Valuation Methods Used to Achieve the Compensation* (L.&VALUATION 2001)
[688] As noted in the UNGA 'Charter of Economic Rights and Duties of States' (12 December 1974) Res 3281 (XIX), state sovereignty includes the right of expropriation. Every State has the right to nationalise, expropriate, or transfer ownership of foreign property, in which case appropriate compensation should be paid by the State adopting such measures, taking into account its relevant laws and regulations and all circumstances that the State considers pertinent.
[689] *Phillips Petroleum Co v Curtis*, 182 F.2d 122 (10th Cir 1950).

[690]*Factory at Chorzów* Case (*Germany v Poland*) PCIJ, 1925

[691] *Wena Hotels Ltd* (n593)
[692] *Metalclad Corporation v The United Mexican States*, ICSID Case No ARB(AF)/97/1, Award (30 August 2000)
[693] *Marion Unglaube v. Republic of Costa Rica*, ICSID Case No. ARB/08/1, Award of 16 May 2012
[694] *Guaracachi America, Inc. and Rurelec PLC v. The Plurinational State of Bolivia*, UNCITRAL, PCA Case No. 2011-17, Award of 31 January 2014

Egypt[695] agreed that such a difference is not important because the effect of damages is exactly the same.[696]

This is also seen in the previously discussed case the *Ampal* case[697], in 2000 EMG and EGPC signed a source Gas Sale Purchase Agreement (GSPA). In 2008, EMG and EGPC signed a tripartite agreement together with another state-owned company named the Egyptian Natural Holding Company (EGAS). The investment project can be summarised as a pipeline that delivers natural gas provided by EGAS to Israel. Nevertheless, due to the Egyptian revolution, Egypt terminated the GSPA's right to carry out government policy in order to stop all exports to Israel. Thus, the claimant raised a claim against Egypt for breach of BIT provisions. The tribunal assessed the expropriation conditions set forth by the BIT (public purpose, non-discrimination, prompt and adequate compensation).[698]

The *Ampal* tribunal held that requirements of lawful expropriation have fulfilled the requirements of public purpose and non- discrimination, nevertheless, still has not fulfilled the requirement of warranting prompt and adequate compensation. Also, treaty safeguards an investment from expropriation except if it is complemented by "by prompt and adequate compensation." It is shown in Article III. (1).[699] It establishes international state obligation to pay compensation for expropriating investor's property. However, tribunal noted that regard the compensation matter, it does not require to assess whether the expropriation was unlawful or not.[700]

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[695] *Middle East Cement Shipping and Handling Co. S.A. v. Arab Republic of Egypt*, ICSID Case No. ARB/99/6, Award of 12 April 2002

[696] most of the guidelines and provisions for awarding compensation under IIAs today address lawful expropriation and usually do not involve compensation separate standards for unlawful expropriation.

[697] *Ampal-American Israel Corp v Egypt* (n 138).

[698] US–Egypt Treaty (n 511) art 3(1) protects an investment from expropriation unless, inter alia, it is accompanied '*by prompt and adequate compensation*'. The article goes on to prescribe that such compensation '*shall be equivalent to the fair market value of the expropriated investment on the date of expropriation*'.

[699]US–Egypt Treaty(n511), Art III prescribe compensation "shall be equivalent to the fair market value of the expropriated investment on the date of expropriation.".

[700] *Ampal-American Israel Corp v Egypt* (n 138).

Moreover, the valuation of the assets in relation to a compensation payment is addressed in primary sources. For example, Chapter 1110 of NAFTA[701] and Article 6(2) of US Model Law[702] refer to said valuation specifically as at the 'date of expropriation'. Moreover, Article 5(2) of the French Model BIT 2006 refers to the 'date of dispossession'[703] Thus, compensation under direct expropriation is based on the date on which the decree or legislation which expropriates is enacted by the host state. On the other hand, in the case of indirect expropriation, the applicable date of valuation will be within the discretionary decision-making authority of the arbitral tribunal.[704]

This is problematic, with Schill arguing that the date of governmental interference is determined based on the tribunal's view of when the compensable loss occurred but does not have the specificity of a law or decree. It can be a progressive series of acts lacking a specific date, but this calculation element must remain because the value of the property may easily change from one day to another.[705] In this sense, both over and under-enforcement theories can explain that arbitrators can over or under-enforce the rules of compensation based on what they see reasonable.

As a result, both over and under-enforcement theories can explain that the criteria for lawful expropriation are subjective. It can create selective enforcement that reflects adjudicators opinion in defining rules that may be over-enforced or under-enforced. However, expropriation legality appears to be of lesser significance in investment arbitrations. The vagueness of defining the concepts of indirect expropriation and compensation are the matters that need to be addressed. After examining the concept of expropriation, a question emerged, specifically whether the existence of treaty clause can be a safeguard for foreign investors which prevents a revolutionary government from pursuing any kind of expropriation.

[701]Chapter 1110 of North American Free Trade Agreement (NAFTA).
[702] See art 6(2) treaty Between the Government of the United States of America and the Government of [Country] Concerning the Encouragement and Reciprocal Protection of Investment (2012) US Model Bilateral Investment Treaty
[703] Draft Agreement Between the Government of the Republic of France and the Government of the Republic of (…) on the Reciprocal Promotion and Protection of Investments (2006), it is known as French Model Bilateral Investment Treaty.
[704] See *Compañia del Desarrollo de Santa Elena SA* (n 645).
[705] Stephan Schill, *International Investment Law and Comparative Public Law* (Oxford University Press 2010) 757.

5.3.4 Treaty clauses versus Expropriation:

Some of treaty clauses work as guarantee that host state will not do any unliteral act (expropriation) where it can affect foreign investment. However, interpreting these clauses is problematic. For example, umbrella clause, the purpose of this clause is that any breach between the parties will be considered as a violation to the BIT. Umbrella clause works as a guarantee that host state will respect all the contractual arrangements with the foreign investors. Host state is not allowed to do unilaterally act such as changing the applicable domestic law or any items in the contract. Otherwise, it will raise the state responsibility and open a room for the international dispute settlement. [706] However, scholars such as Potts demonstrated the complexity of using the umbrella clauses in the investment treaties.[707] Potts clarified that despite the umbrella clause was created during the 1950s, it has not interpreted until the 2003 by the arbitral tribunals. This has established two schools of thoughts. Some tribunals used the strict approach in interpreting the umbrella clauses. Other tribunals were expansive in interpreting the umbrella clauses. Such a different interpretation caused inconsistent arbitral decisions regard the same issue.[708]

For example, in the case of the *SGS V. Pakistan*, the umbrella clause interpreted much narrowed.[709] The *SGS* tribunal noted that the effect of umbrella clause could not raise the violations to the BIT. The *SGS* tribunal clarified the reason behind this is not to make investors to have the monopoly power. The under-enforcement theory can explain that *SGS* tribunal in this case used the purpose of umbrella clause to render its own notion of justice.[710] Six months later, the same claimant raised a similar case in Philippines. In the case of *SGS v. Philippines*, the tribunal followed different direction than the tribunal of *SGS v. Pakistan*. It refused the governments' argument that the umbrella clause is limited to the obligations under the

[706] POTTS , 'Stabilizing the Role of Umbrella Clauses in Bilateral Investment Treatie'(n28)
[707] ibid
[708] ibid
[709] See Agreement between the Swiss Confederation and the Islamic Republic of Pakistan on the Promotion and Reciprocal Protection of Investments, signed on 11 July 1995; entered into force on 6 May 1996 (hereinafter, Switzerland-Pakistan).
[710] *SGS Société Générale de Surveillance S.A. v. Islamic Republic of Pakistan*, ICSID Case No. ARB/01/13, Decision on Jurisdiction 9 of Aug. 2003

international law.[711] The arbitrator rejected to use the narrowed interpretation as his colleagues in the case of *SGS v. Pakistan* [712] and noted that the state has breached its commitments under the BIT.[713] Accordingly, both over and under-enforcement theories can explain that different tribunals interpreted the umbrella clause differently. This is because of analytical reasons. Umbrella clause is interpreted either in narrowed or extensive manner among different tribunals. This has resulted to inconsistent decisions. It appears that application of umbrella clauses is unclear.

There are also other treaty clauses that are problematic in its interpretation. For example, the stabilisation clause stabilises the conditions and terms of an investment project; indeed, it covers the non-commercial risks. Such a clause involves the host government's commitment to not change the regulatory framework governing the project through legislation or any other means.[714] Nevertheless, it is debatable that international law allows the host state to change its national law; it has a sovereign right to do so. This is explained in Chapter 2 of the Charter of Rights and Duties of States, the state has the right to change its laws as well as its social and political system in order to reach its economic objective and policies, but such changes should not cause inexcusable harm to the foreign investor. This has led scholars such as Brownlie to argue that stabilisation can be seen as an unlawful clause because it is against principle of permanent sovereignty over natural resources. However, tribunals such as that in the *Aminol* case have confirmed that a stabilisation clause is not prohibited by international law, but that there is a need for careful interpretation of the specific undertaking in question.[715]

Also, scholars such as Frank clarified that there is difference between government risk and political risk. The former refers to breaches of contracts and regulatory changes, which can be protected by these clauses. While the latter, refers to civil wars and terrorism, where it is irrelevant to assume that the stabilisation clause will protect foreign investors.[716]

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[711] *SGS Société Générale de Surveillance S.A. v. Republic of the Philippines*, ICSID Case No. ARB/02/6, Decision on Jurisdiction 29 of Jan. 2004
[712] ibid
[713] Agreement between the Swiss Confederation and the Republic of the Philippines concerning the promotion and reciprocal protection Investments Closed on March 31, 1997 Entered into force by exchange of notes on 23 April 1999 (Status as of February 20, 2001)
[714] Lorenzo Cotula, 'Regulatory Takings, Stabilization Clauses and Sustainable Development' (OECD Global Forum on International Investment, OECD Investment Division, 2008)
[715] Brownlie, *System of the Law of Nation* (n574).
[716] Sotonye Frank, "Stabilisation Clauses and Foreign Direct Investment: Presumptions versus Realities" (2015) 16 JWIT

Going back to the question of whether the host state is allowed to regulate public interest under a stabilisation clause, the answer is seen in the previously discussed case of *the Libyan American Oil Company (LIAMCO) v Government of the Libyan Arab Republic*.[717] The tribunal held there was a breach of obligations because of the stabilisation clause.[718] Thus, the state had to fulfil its obligations and pay compensation. In general, damage determination is according to "the general principles of law," and the level of state responsibility affects the compensation measurement.[719] This is in contrary to the previously discussed case of *Parkerings v Lithuania*. The ICSID tribunal recognised that the expectations of an investor are legitimate if the host state made a promise that was considered by the investor when making the investment. Thus, the tribunal dismissed the claim, asserting that:

"It is each State's undeniable right and privilege to exercise its sovereign legislative power. A State has the right to enact, modify or cancel a law at its own discretion. Save for the existence of an agreement, in the form of a stabilisation clause or otherwise, there is nothing objectionable about the amendment brought to the regulatory framework existing at the time an investor made its investment. As a matter of fact, any businessman or investor knows that laws will evolve over time. What is prohibited however is for a State to act unfairly, unreasonably or inequitably in the exercise of its legislative power."[720]

This is similar to the considerations made in the previously discussed case of *LETCO v Liberia*, where the tribunal stated that "the main purpose of the stabilization clauses was to protect against arbitrary actions of the contracting government and could not totally impair the sovereign power of states."[721] It seems that some arbitral tribunals highly strict in recognizing the right of state to regulate. This is also shown in the tribunal of *Feldman v Mexico* stated that "Governments must be free to act in the broader public interest through protection of the environment, new or modified tax regimes, the granting or withdrawal of government subsidies, reductions or increases in tariff levels, imposition of zoning restrictions and the like. Reasonable governmental regulation of this type cannot be achieved if any business that is adversely affected may seek compensation, and it is safe to say that customary international law recognizes this."[722]

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[717] *Libyan American Oil Company (LIAMCO) v Government of the Libyan Arab Republic,* Ad Hoc Arbitration, Award 12 April 1977

[718] Stabilisation clause means that the state cannot amend its national laws within the time frame of the foreign investments made.

[719] *Libyan American Oil Company (LIAMCO) v Government of the Libyan Arab Republic* (n 690)

[720] *Parkerings-Compagniet AS v Lithuania*, ICSID Case No ARB/05/8, Award of 11 September 2007 para 331

[721] *Liberian Eastern Timber Corporation (LETCO) v Republic of Liberia*, ICSID Case No ARB/83/2, Final Award (31 March 1986) ICSID Reports 2 (1994), 343 (368).

[722] *Marvin Roy Feldman Karpa* (n638) para 103.

Thus, we can infer that there is a lack of certainty of the use of theses stabilization clauses. Both over and under-enforcement theories can explain that adjudicators might over or under-enforce the law because they are trying to square the law with the facts of the case to render their own notion of justice. This resulted to a different interpretation in respect to the regulatory changes and compensation. There is a lack of understanding on how the international investment law deals with the concepts of stabilization versus changes. This is might be because the application of stabilization clause is based on adjudicator's discretion. Accordingly, we can infer that some tribunals read the stabilisation clause, the state is allowed to change its laws and policies, but it will be subject to the paying of compensation. This had led scholars such as Maniruzzaman to reach the conclusion that: "stabilization clauses are not thus a guarantee against lawful nationalization and for that matter lawful expropriation. These stabilization clauses impose on the state an obligation to act in good faith and give rise to an obligation to compensate in case of their breach."[723] This raises a question, specifically, what are the governmental regulations that can be considered non-compensable regulation?

5.3.5 Non-compensable regulations versus compensable regulations

Despite the fact that a particular state action interferes with a foreign investors' rights to their property, there is exception where action may not be considered to be expropriation. This is because such a measure may represent a reasonable practice of the state's authority to regulate issues that fall under its absolute sovereignty: e.g., health, currency, balance of payments, public order and safety. Under customary international law, states have a well-defined right to regulate business and commercial activities on their territory without compensation.[724] Additionally case law has recognised states' right to regulate, which is also stipulated in

[723] Munir Maniruzzaman, 'The Pursuit of Stability in International Energy Investment Contracts: A Critical Appraisal of the Emerging Trends' (2008) 1(2) Journal of World Energy Law & Business 121, 141.
[724] It is reflected in international instruments. The European Convention of Human Rights implies that compensation is not applicable where there is a general regulatory measure. Art 1 of First Additional Protocol states that: 'Every natural or legal person is entitled to the peaceful enjoyment of its possessions. No one should be deprived of his possessions except in the public interest and subject to the conditions provided for by the law and by the general principles of international law.'

investment treaties.[725] This matter is also discussed by scholars such as Brownlie who contend that "State measures, prima facie a lawful exercise of powers of governments, may affect foreign interests considerably without amounting to expropriation."[726]

This is similar to the argument of Sornarajah: "non- discriminatory measures related to anti-trust, consumer protection, securities, environmental protection, land planning are non-compensable takings since they are regarded as essential to the efficient functioning of the state."[727] Newcombe added that "... no right to compensate arises for reasonable necessary regulations passed for the protection of public health, safety, morals or welfare."[728] This is similar to the statement made by Titi, who argued that "...the right to regulate denotes the legal right exceptionally permitting the host state to regulate in derogation of international commitments it has undertaken by mean of an investment agreement without incurring a duty to compensate."[729]

The problem is that there is a lack of clarity regarding what differentiates non-compensable regulation from indirect expropriation. Despite the fact that this is an important issue for both governments and investors.[730] This led to selective enforcement where some arbitrators can choose to sanction investor and leave other investor for the same conduct. This is also debatable among scholars such as Dolzer and Stevens, "To the investor, the line of demarcation between measures for which no compensation is due and actions qualifying as indirect expropriations (that require compensation) may well make the difference between the burden to operate (or abandon) a non-profitable enterprise and the right to receive full compensation (either from the host State or from an insurance contract). For the host State, the definition determines the scope of the State's power to enact legislation that regulates the rights and obligations of owners in instances where compensation may fall due. It may be argued that the State is prevented from taking any such measures where these cannot be covered by public financial resources."[731]

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[725]For example, the Dominican Republic-Central America-United States Free Trade Agreement (CAFTA-DR), Ch. 10 states that "Except in rare circumstances, nondiscriminatory regulatory actions . . . designed and applied to protect legitimate public welfare objectives . . . do not constitute indirect expropriations"

[726] Brownlie, *System of the Law of Natio*n (n574).
[727] Sornarajah, *The International Law on Foreign Investment* (n1)
[728] *Expropriation: UNCTAD Series on Issues in International Investment Agreements II* (1st edn, United Nations Publication 2012)
[729] Aikaterini Titi, *The Right To Regulate In International Investment Law* (1st edn, Nomos 2014) 33.
[730] Sornarajah, *The International Law on Foreign Investment* (n1).
[731] Dolzer and Stevens, *"Bilateral Investment Treaties"* (n 648).

Moreover, Higgins wrote about the taking of property, stating that "the issue can be further refined as the determination of who is to pay the economic cost of attending to the public interest involved in the measure in question. Is it to be the society as a whole, represented by the state, or the owner of the affected property?"[732] It appears that there is a concern in the international community about the potential for indirect expropriation law to interfere with states' rights to regulate. Accordingly, there are competing norms concerning indirect expropriation and, on the other hand, the state's right to regulate. International law exhibits the tension between protecting the property owners from state actions that interfere with their (the owners') ability to enjoy their own property and the competing interest of maintaining the freedom of states to practice regulatory powers. Arbitral tribunal decisions regard differentiating between indirect expropriation claims (compensatory claims) and state's right to regulate (non-compensatory claims) show competing interests. Some tend to favour the foreign property owner's interest (sole effect approach), and others favour the state's regulatory authority (police power approach).[733]

These approaches need to be examined. However, this require to examine the cases that use these approaches notwithstanding if disputes involve revolutionary government or not. For the purpose to examine whether international law provide the right for revolutionary government to regulate its public interests without paying compensation?

5.3.5.1 Sole Effect Doctrine

This doctrine is the dominant approach, where arbitral tribunals establish said doctrine to determine the existence of indirect expropriation.[734] This approach was termed by Dolzer.[735] It focuses only on the effects that the measures of the state had on the investment. Examining this doctrine will return us to the Iran-United States Claims Tribunal. This is because the 'sole

[732] Rosalyn Higgins, 'The Taking of Property by the State: Recent Developments in International Law' in Collected Courses of the Hague Academy of International Law (Volume 176) (Martinus Nijhoff Publishers 1983) 276–77.
[733] Meg Kinnear and others (eds), *Building International Investment Law: The First 50 Years of ICSID* (Kluwer Law International 2015).
[734] Mostafa , 'The Sole Effects Doctrine, Police Powers and Indirect Expropriation under International Law' (n 624).
[735] Rudolf Dolzer, 'Indirect Expropriation of Alien Property' (1986) 1(1) ICSID Review – Foreign Investment Law Journal 41.

effect approach' was employed heavily in the Iranian case. The political turmoil which occurred during the Iranian Islamic Revolution resulted in many disputes between the revolutionary government and foreign investors. It also resulted in the establishment of the Claims Settlement Declaration and the Iran-United States Claims Tribunal. Briefly, Iran's revolution occurred because of opposition to the 'Shah's' governmental regime, which favored western ways of development.[736] This made Iranians fearful that Iran might become a tool of 'American imperialism.'[737] The revolution resulted in a new government coming to power. During that time public measures were adopted in order to take control of western enterprises.[738] Many of expropriation programs were implemented.[739] The new Iranian government passed a new constitution as well as other statutes which discouraged foreign companies from investing in Iran.[740] Responding to the Iranian expropriations, the United States enforced import blocks on oil from Iran and froze 8 billion dollars in Iranian assets held within the US and by American financial institutions placed abroad.[741]

To resolve the dispute between Iran and the US, the Government of Algeria, as broker, brought the two states into negotiation. Through Algeria's good offices, on 19th January, 1981, Iran and the US made an international agreement, known as the 'Claims Settlement Declaration' ('the Declaration').[742] The Declaration states that "[a]n international arbitral tribunal (the Iran-United States Claims Tribunal) is hereby established for the purpose of deciding claims."[743] Consequently, the tribunal is seen as a 'one-stop-shop.'[744]

The tribunal's work has contributed to the development of international investment law. This has made scholars such as Gibson and Drahozal argue that arbitral awards are "an essential

[736] Shiva Balaghi, 'A Brief History of 20th Century Iran' (*Grey Art Gallery*, 2015)
[737] Steven R Swanson, 'Iran-U.S. Claims Tribunal: A Policy Analysis of the Expropriation Cases' (1986) 18(2) Case Western Reserve Journal of International Law 307.
[738] Sebastian Lopez Escarcena, 'Expropriations and Other Measures Affecting Property Rights in the Case Law of the Iran-United States Claims Tribunal' (2013) 31(2) Wisconsin International Law Journal 177, 180.
[739] ibid.
[740] Farshad Ghodoosi, 'Combatting Economic Sanctions: Investment Disputes in Times of Political Hostility, A Case Study of Iran' (2014) 37 Fordham International Law Journal 1731, 1746–49.
[741] Michail Risvas, 'Book Review: "Regionalism in International Investment Law" edited by Leon E. Trakman and Nicola W. Ranieri' (2014) 15(1–2) The Journal of World Investment & Trade 357.
[742] Romesh Weeramantry, *The Law of Indirect Expropriation and the Iran-United States Claims Tribunal's Role in Its Development' in Leon E Trakman and Nicola W Ranieri (eds*), *Regionalism in International Investment Law* (Oxford University Press 2013) 314, 315.
[743] Declaration of Settlement Claims (signed 19 January 1981, entered into force 19 January 1981) 1 Iran-USCTR 13, art 2.
[744] Weeramantry, *The Law of Indirect Expropriation and the Iran-United States Claims Tribunal's Role in Its Development* (n 742)

source for lawyers and parties involved in investor-state disputes."[745] Indeed, said point is seen in regard to the arbitral tribunal of the International Centre for Settlement of Investment Disputes (ICSID), who referred to the awards rendered by the Iran-United States Claims Tribunal (IRUSCT).[746] This made it important to examine the issue of indirect expropriation in the Iran-United States Claims Tribunal jurisprudence and the effect of political unrest on the development of legal doctrine. Swanson clarified the dilemma involved in the Iranian case where the US asked Iran to respect the international minimum standard. On the other hand, Iran argued that, according to the principles of international law, the state is allowed by sovereign right to seize any foreigners' economic enterprises, for the purposes of national interests and internal affairs.[747]

Generally, there were a small number of claims that involved the direct taking of private property through expropriation or formal nationalisation. The main concern was for tribunals to determine when specific acts of governmental interference with foreign property were in violation of international law. The tribunal noted poor development of indirect expropriation principles within customary international law. Thus, the tribunal established a body of jurisprudence aimed at differentiating internationally-accepted exercises of regulatory authority from expropriations. Tribunals have used an effect-based analysis. This analysis focuses on the effect of governmental measures on investments. For example, in *Starrett House Corp v Government of the Islamic Republic of Iran*, the tribunal held that the revolutionary government of Iran was accountable for its interference with private property even though ownership had not been taken away and also that the government was subject to international responsibility with regard to the fact that that the measure was alleged to have interfered with property rights in such a way as to have in a manner rendered property them 'useless'.[748]

After a number of years, a similar concept was applied by the Chamber Two Tribunal in *Tippetts v TAMS-AFFA.*[749] The tribunal found that the state is liable for damage to property

[745] Christopher S Gibson and Christopher R Drahozal, 'Iran-United States Claims Tribunal Precedent in Investor-State Arbitration' (2006) 23(6) Journal of International Arbitration 521, 521.
[746] See *Wena Hotels Ltd v Egypt* (n 593).
[747] Swanson, 'Iran-U.S. Claims Tribunal' (n 737)
[748] Starrett Housing Corporation, Starrett Systems, Inc. and others v. The Government of the Islamic Republic of Iran, Bank Markazi Iran and others IUSCT Case No. 24
[749] Tippetts v TAMS-AFFA (n 643).

rights regardless of the fact that the "legal title to the property is not affected",[750] and that the government does not need to "acquire something of value" from the alleged interference; the *Tippetts* Tribunal stressed that the government's intention is not as significant as the effect upon the investor.[751] Accordingly, both the *Starrett* and *Tippetts* cases were based on an analysis of effect, rather than on an analysis of a state's intentions.

Moreover, in *SEDCO v National Iranian Oil Co*,[752] as in regard to previous awards, the tribunal recognised that the effect of a measure was a more significant consideration than the state's intention, but held that the state is responsible merely if the interference of governmental is "substantial and excessive"[753] this was echoed in *ITT v Iran*.[754] In the latter case, the tribunal clearly asserted that "the intent of the government is less important than the effects of the measures on the owner, and the form of these measures...is less important than the reality of their impact."[755] Moreover, the police power doctrine denial was clarified in the *Phelps Dodge* case, where the tribunal held that a state act which is motivated by social, economic and financial concerns does not give rise to a 'police power' defence to an expropriation claim.[756]

It seems that Iran-United States claims procedures undertaken during the Islamic Revolution applied an effects-based analysis as opposed to the 'police power' doctrine.[757] This is also reflected in recent cases. For example, in *Aguas del Aconquija* (Vivendi II),[758] the tribunal determined the occurrence of indirect expropriation by finding that the measure had a "devastating effect on the economic viability of the concession" and rendered it "valueless".[759]

Despite the fact that the tribunal did use an effects-based doctrine, there are some practical problems with the use of this concept when analysing expropriation. Tribunals face complexity when characterising the property rights that should to be subject to expropriation analysis.[760] In the *Starrett* case, for example, the tribunal deemed that the government actions destroyed

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[750] ibid.
[751] Tippetts v TAMS-AFFA (n 643). Also see Maurizio Brunetti, 'The Iran-United States Claims Tribunal, NAFTA Chapter 11, and the Doctrine of Indirect Expropriation' (2001) 2(1) Chicago Journal of International Law 203, 206
[752] *SEDCO Inc v National Iranian Oil Co* (Award) [1985] 9 Iran-USCTR 248.
[753] ibid.
[754] *ITT Indus Inc v Iran* (1983) 2 Iran-USCTR 348.
[755] ibid.
[756] *Phelps Dodge Corp and Overseas Private Investment Corp v Iran* (Award) [1989] 10 Iran-USCTR 121.
[757] ibid.
[758] Compañía de Aguas del Aconquija S.A. and Vivendi Universal S.A. v. Republic of Argentina, ICSID Case No. ARB/97/3, Award 20 August 2007 (Vivendi II)
[759] ibid.
[760] Swanson, 'Iran-U.S. Claims Tribunal' (n 737).

the whole value of the investment, and thus they (the actions) constituted a compensable expropriation irrespective of the amount of controlling power taken by the foreign investor.[761] In contrast, the tribunal in the *Tippetts* case expressed the idea that regulatory interference could only be considered as compensable expropriation when the government action in question deprived the investor of the core of their rights in the investment.[762] Although both tribunals focused on the effects of government actions on the property of the investor, they provided different criteria with which to determine the emergence of a compensable indirect expropriation. This difference could affect the tribunal's analysis of expropriation and also a state's capability to practice its public authority.

This is also seen under the BIT system, where arbitral tribunals do not provide a clear explanation of what is meant by substantial deprivation: is this 100% deprivation or is more than half enough? Some tribunals noted that where there is permanent and complete deprivation of the control and/or value of an investment, this should be considered equivalent to taking,[763] meaning that the investors have lost their investments completely. On the other hand, in *Metalclad v Mexico*, the arbitral tribunal noted that the deprivation of an important part of an investment may qualify as expropriation.[764] However, there are other cases where the arbitral tribunal did not follow this reasoning. In the *Marvin Feldman v Mexico* case, the arbitral tribunal did not assess percentage of deprivation on the investment itself, but on the negative affect of the state's measures on investment generally.[765]

Similarly, in case of *LG&E v Argentina*, the arbitral tribunal found that there is absence of substantial deprivation of investments. The investor claimed expropriation because of Argentina's measures, which were adopted due to the country's economic crisis. *LG&E* acquired shares of three companies in the gas distribution field under Argentina's privatisation program. Argentina had granted licenses for a long duration and applied many laws that provided various guarantees. Nevertheless, because of the country's economic crisis, Argentina eliminated the guarantees that had been provided earlier, forced contract renegotiation, and

[761] Starrett Housing Corporation, Starrett Systems, Inc. and others v. The Government of the Islamic Republic of Iran (n721) also see Christopher F Dugan and others, *Investor-State Arbitration* (Oxford University Press 2008) 458.
[762] ibid.
[763] *Burlington Resources Inc. v Repub of Ecuador*, ICSID Case No ARB/08/5, Decision on Liability (14 December 2012).
[764] *Metalclad Corporation v The United Mexican States*, (n 692)
[765] Marvin Roy Feldman Karpa v United Mexican States (n 638)

applied new laws.[766] This made investors claim that there had been an indirect expropriation, and regulatory measures taken by the state substantially affected their share values, which fell by more than 90%. On the other hand, Argentina debated that there was the lack of a causal link between the value of the investment and the measures that they had adopted.[767]

Analyses of the deliberations of the arbitral tribunal in terms of the decrease of value claim have looked at the degree to which the measure interfered with the investment, and specifically its economic impact. The arbitral tribunal recognised that Argentina had adopted "severe measures" that in some ways had affected the investment, but that such measures "did not deprive the investors of the right to enjoy their investment."[768] The investment was still present as it had not "ceased to exist"; moreover, the investor had not lost control over his investments. Accordingly, although the measures adopted were harsh and the value of the investment had decreased by more than 90%, this was not the only element that had to be taken into consideration. The tribunal held that the investor still had the ability to enjoy his investments, meaning that there was no total deprivation or anything near to this. The value of the shares fluctuated for some time during the crisis, but this constitutes a normal business risk. Thus, there is a lack of a unified approach regarding this issue, as well as examples of vague language being applied by the arbitral tribunals, which together provide for the possibility of a wide interpretation of the substantial deprivation rule which relies on the view of the particular arbitral tribunal.[769]

It seems that arbitral tribunals depend on certain elements when evaluating deprivation. These elements are described as deprivation in value, or of control. duration of the measure's effects was permanent. The issue is these criteria can be considered separately or all together. In practice such criteria have been applied differently. For example, In *LG&E v Argentina*, the arbitral tribunal examined all these criteria, namely whether the investor suffered deprivation of value, or of control, and whether the duration of the measure's effects was permanent. Despite there being an negative economic effect on the investment, the criteria of duration and

[766] See US–Argentina Treaty (n 606).
[767] *LG&E Energy Corp v Argentina, LG&E Capital Corp v Argentina and LG&E International, Inc v Argentina*, (n377)
[768] ibid.
[769] Dinara Batyrova, 'Regulatory Expropriation in the Jurisprudence of ICSID Arbitral Tribunal' (LLM thesis, Central European University 2017).

loss of control were absent and thus there was considered to be a lack of substantial deprivation and correspondingly there was also considered to be no expropriation.[770] On the other hand, in the *Starrett Housing Corp. v Iran* and *Tippetts* cases, only one element was examined, and this said element was that of a loss of control which was found to be sufficient to amount to an expropriation, despite it not being permanent. Such contradictory and diverse practice by arbitral tribunals does not add to the predictability and clarity regarding indirect expropriation, which is, in itself, a complex matter.[771]

Accordingly, both over and under-enforcement theories can explain that the sole effect doctrine results in unpredictability and uncertainty within the legal framework, which is applicable to host state governments and foreign investors dealing with expropriation disputes. This is because sole effect doctrine considers only the effects that the measure has had on investments and the investors. The threshold used to evaluate the effect of the measure is substantial deprivation of investment value. Arbitral tribunals' practice shows that they depend on certain elements when evaluating deprivation, which were described as deprivation in value loss of control and duration of the measure's effects was permanent.

Both over and under-enforcement theories explain that elements of evaluating deprivation is subjective resulted that different arbitral tribunals practices apply such criteria differently. This can attribute to the problems of under-defined criteria where broad law that invites selective enforcement. It appears that 'sole effect' doctrine is open to many different interpretations that depend on the arbiter's opinions rather than actual culpability. Adjudicators might over or under-enforce the law because they are trying to square the law with the facts of the case to render their own notion of justice. Generally, the sole effect doctrine conflicts with and contradicts then right of state to regulate

[770] *LG&E v Argentina* (n 410)
[771] Starrett Housing Corporation, Starrett Systems, Inc. and others v. The Government of the Islamic Republic of Iran (n721) Tippetts v TAMS-AFFA (n 643). Also see Batyrova, 'Regulatory Expropriation in the Jurisprudence of ICSID Arbitral Tribunal' (n 742).

5.3.5.2 Police Powers Doctrine

This doctrine was established by the arbitral tribunals and is in contrast to the sole effect approach because it examines the state's intention and the purpose of the adopted regulatory measure. A state keeps its sovereignty despite concluding contracts and treaties. A state does not lose its sovereign inherited right to regulate.[772] The principle of the police powers doctrine is that the state's implementation of regulatory measures and its consequent taking of investments are non-compensable if these meet the following criteria: public purpose, non-discriminatory and proportionality.[773]

The police powers doctrine is an accepted principle which is acknowledged by arbitral tribunals, scholars and states themselves. For example, scholars such as Brownlie argued that under the police powers doctrine, foreign assets and their use may be subjected to trade restrictions, taxation involving quotas and licenses, or devaluation measures.[774] Also, the most important pronouncement relating to the police powers rule in international investment law was conducted in the case of *Methanex v United States* in the context of regulatory measures pursuant of public interest objectives. The tribunal held that the ban amounted merely to lawful non-compensable regulation and not to expropriation, following which it stated that:

"As a matter of general international law, a non-discriminatory regulation for a public purpose, which is enacted in accordance with due process and, which affects, inter alia, a foreign investor or investment is not deemed expropriatory and compensable unless specific commitments had been given by the regulating government to the then putative foreign investor contemplating investment that the government would refrain from such regulation."

Thus, according to the *Methanex* tribunal, determining whether a measure qualifies as a lawful non-compensable regulation or an expropriation depends on whether the state's measures were taken for a public purpose and in a non-discriminatory way, through a law enacted by due process. The tribunal depended on the absence of any such commitment as one of the grounds to dismiss the expropriation claim.[775] Moreover, one of the recent cases where the arbitral tribunal has applied the police powers doctrine is that of *Philip Morris v Uruguay*. An award

[772] Surya P Subedi, *International Investment Law Reconciling Policy and Principle* (1st edn, Hart Publishing 2008) 160–61.
[773] Kinnear and others (eds), *Building International Investment Law* (n 733)
[774] Ian Brownlie, *Principles of Public International Law* (Oxford University Press 2008).
[775] Methanex v United States (n 283).

was rendered in 2016.[776] In this case, Uruguay adopted many regulations for the purpose of safeguarding public health. Philip Morris challenged particularly measures "80/80 Regulation" and the "Single Presentation Requirement" (SPR).[777] The arbitral tribunal examined arbitral tribunal practice and scholarly writings regarding the exercise of police powers. It found that:

"Protecting public health has since long been recognized as an essential manifestation of the State's police power, as indicated also by Article 2(1) of the BIT which permits contracting States to refuse to admit investments "for reasons of public security and order, public health and morality."[778]

However, the arbitral tribunal found that the measures applied by Uruguay in relation to public health protection were lawful measures within the state's police power, and thereby they did not constitute expropriation. This case reveals that the approach of police powers has been recognized and proved, despite that the relevant BIT may not include explicit language relating to it. The measures used by Uruguay were hard on tobacco companies; nevertheless, the legitimate public purpose outweighed the losses that the investor might have had to suffer. The fact that the investor was involved in tobacco products, which are dangerous to people's health, justified the state's act of imposing restrictions on them, and the investor should have expected this and borne the risks. [779]

This raises the question of what limits are there to the right of state to regulate its public interest? According to *ADC v Hungary*, the tribunal's "understanding of the basic international law principles that while a sovereign State possesses the inherent right to regulate its domestic affairs, the exercise of such right is not unlimited and must have its boundaries."[780]

Consequently, scholars have attempted to clarify the state's boundaries to use its police power, what regulatory measures fall under the police powers doctrine? Christie clarified that the function of a state's tax laws, modifications in a state's currency values, actions in the interest of public morality or health justify a state's acts fall under the police powers.[781] Newcombe

[776] *Philip Morris Brands Sàrl, Philip Morris Products SA and Abal Hermanos SA v Oriental Repub of Uruguay*, ICSID Case No ARB/10/7, Award of 8 July 2016..
[777] ibid.
[778] See Agreement Between the Swiss Confederation and the Oriental Republic of Uruguay On the Reciprocal Promotion and Protection of Investments (1988)
[779] *Philip Morris Brands Sàrl, Philip Morris Products SA and Abal Hermanos SA v Oriental Repub of Uruguay*(n749)
[780] *ADC Affiliate Ltd and ADC & ADMC Management Ltd v The Repub of Hungary*, ICSID Case No ARB/03/16, Award (2 October 2006).
[781] George C Christie, 'What Constitutes a Taking of Property Under International Law?' (1962) 38 British Year Book of International Law 307–38

also recommended the employment of the police powers doctrine in regard to the safeguard of the environment and human health to justify non-compensation.[782]

Moreover, Brownlie, Newcombe and Paradell suggested that international authorities acknowledge three wide-ranging categories of police powers that might justify non-compensation where there is a deprivation, these being: a) protection of human health and the environment; b) public order and morality; and c) state taxation.[783] It appears that the problem with these scholars' explanation is that it is hard to define the scope of matters such as public morality because this scope in particular can differ from state to state.[784] Furthermore, a wide margin of appreciation[785] is left to states in terms of self-judging their security interests and determining appropriate measures to safeguard those interests.[786] Accordingly, the police powers doctrine is both broad and abstract.[787] Thus, Weiner suggested that customary law and international convention, along with state practice, should define what establishes a legitimate exercise of government regulation or police powers.[788]

Also, the undefined character of the police powers doctrine, which was asserted by the deliberations of the tribunal of *Saluka*. This tribunal held that international law is yet to determine certainly and comprehensibly which regulations are 'permitted' and will be accepted as falling within the state's regulatory power.[789] The *Saluka* tribunal also stressed the necessity of drawing "a bright and easily distinguishable line between non-compensable regulations on the one hand and, on the other, measures that have the effect of depriving foreign investors of their investment and are thus unlawful and compensable in international law." Moreover, the tribunal noted that it falls on the adjudicator to determine where the adopted regulatory measures cross the line that separates regulation from expropriation.[790]

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[782] Andrew Newcombe, 'The Boundaries of Regulatory Expropriation in International Law' (2005) 20(1) ICSID Review – Foreign Investment Law Journal 32.
[783] Andrew Newcombe and Luis L Paradell, *Law and Practice of Investment Treaties* (n7)
[784] ibid.
[785] Methanex v United States (n 283).
[786] Ian Laird, 'The Emergency Exception and the State of Necessity', Federico Ortino and others (eds), *Investment Treaty Law: Current Issues II* (2007) 235, 238 (advocating the use of necessity as a tool for the Canadian government in its dispute before NAFTA regarding the softwood lumber industry).
[787] Simon Baughen, 'Expropriation and Environmental Regulation: The Lessons of NAFTA Chapter 11' (2006) 18(2) Journal of Environmental Law 207–28.
[788]Allen Weiner, 'Indirect Expropriation: The Need for a Taxonomy of "Legitimate" Regulatory Purposes' (2003) 5 International Law Forum 166..
[789] *Saluka Investments BV v The Czech Republic*, Partial Award (17 March 2006) UNCITRAL.
[790] ibid.

Therefore, according to this debate, the arbitral tribunals have the authority to decide whether a regulatory measure falls within the state's police power or not. This provides a great deal of freedom of choice to arbitrators when they are called on to answer complex questions regarding what constitutes a *bonafide* public purpose and what issues are not for the state concerned to decide. This creates selective enforcement where tribunals might over or under-enforce the law because they are trying to square the law with the facts of the case to render their own notion of justice

Hence, some of the up-to-date BIT has begun to indicate the regulatory right of state. For instance, the USA Model BIT, in its Annex B, provides for exceptions relating to indirect expropriation. Specifically, it states that: "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, does not constitute indirect expropriations."[791] Nonetheless, this will depend on how arbitral tribunals interpret the circumstances and facts of a case, and how they interpret such a clause. This can result that tribunals interpret the textual language based on their views of the meaning of words. Arbitrators will base their decisions on what they see as reasonable and equitable in the circumstances of a certain case.

Moreover, international conventions also recognise the state's right to regulate. For instance, the 1961 Harvard Draft Convention on the International Responsibility of States[792] acknowledges a number of classifications of actions whereby non-compensable taking could take place, i.e.: a) taxation; b) general changes in the value of a currency; c) maintenance of public order, health or morality; d) valid exercise of belligerent rights; or e) normal operation of the laws of the state, subject to certain conditions in the draft convention.[793] Furthermore, the arbitral tribunals' practice has defined the police powers doctrine as non-discriminatory, legitimate and protecting public interests, such as protection of public health, the environment, safety, and morals etc.[794]

[791] US Model BIT (n 117) para 4(b), Annex B
[792] Harvard Draft, art 10.5.
[793] The Harvard Draft Convention does not acquire binding power; nevertheless, it has been cited by arbitral tribunals, which are authoritative sources.
[794] *Expropriation: UNCTAD Series on Issues in International Investment Agreements II* (1st edn, United Nation Publication 2012)

This appears to show that one of the criteria which define the scope of the police powers doctrine is that the adopted measure must be for a public purpose. However, the criterion that there is a public purpose is, at the same time, the requirement for lawful (compensable) expropriation. This creates confusion. In addition, arbitral tribunals raise and note this issue of contradiction and confusion. For instance, in the case of *Azurix v Argentina*, the arbitral tribunal said:

"According to it, the BIT would require that investments not be expropriated except for a public purpose and there be compensation if such expropriation takes place and, at the same time, regulatory measures that may be tantamount to expropriation would not give rise to a claim for compensation if taken for a public purpose."[795]

There are also other criteria related to the police powers doctrine that cause confusion: namely the non-discriminatory and proportionate criteria. As seen in the deliberations of the arbitral tribunal in *El Paso v Argentina*, "...in principle, general non-discriminatory regulatory measures, adopted in accordance with the rules of good faith and due process, do not entail a duty of compensation."[796]

The problem with the non-discriminatory measure criterion is that it is exactly the same as the public interest criterion. The non-discriminatory criterion is also a requirement of lawful expropriation, which is also exactly the same as the public purpose requirement, thus creating confusion and contradiction. It seems that this method of deciding which governmental measures fall in the scope of the police power rule creates confusion regarding the state's right to lawfully expropriate foreign investment under both BITs and customary international law.[797]

Likewise, the other criterion is the proportionality measure, whereby the public purpose, the effect, and necessity of the measure are weighed. As the *LG&E v Argentina* arbitral tribunal rightly stated, "to establish whether state measures constitute expropriation ... the Tribunal must balance two competing interests: the degree of the measure's interference with the right of ownership and the power of the State to adopt its policies."[798] Nevertheless, the question of what can be considered a reasonable relationship of proportionality is a difficult one to answer. This is because it is hard to define what is proportionate and reasonable separately. Such a

[795] Azurix Corp. v The Argentine Republic, ICSID Case No. ARB/01/12, Award (14 July 2006).
[796] *El Paso Energy Int'l Co* (n 604).
[797] Also see *AMCO v Indonesia*, ICSID Case No ARB/81/1, Award (1984)
[798] *LG&E* v Argentine (n 410).

requirement is rather broad and vague.[799] Also, this issue raises the question of how arbitral tribunals determine the case: do they first examine the police power or alternatively the substantial deprivation concept? This can attribute to the problems of under-defined rules where broad rules that invites selective enforcement. Adjudicators might over or under-enforce the law because they are trying to square the law with the facts of the case to render their notion of justice

Additionally, state practice provides contradictory evidence on compensatory regulatory measures and non-compensatory measures. For example, in *Methanex v USA*, the state adopted measures which were for environmental and public health protection, and the tribunal did not consider this to be indirect expropriation. On the other hand, in *Santa Elena v Costa Rica* the state adopted measures to protect the environment as well, but the arbitral tribunal considered them to result indirect expropriation.[800] This can attribute to the problems of under-defined criteria where broad law that invites selective enforcement. Law enforcement subjective and open to many different interpretations that depend on the arbiter's opinions rather than actual culpability and legislative definition. Adjudicators might over or under-enforce the law because they are trying to square the law with the facts of the case to render their own notion of justice

Currently, international law does not provide a well-defined division between regulatory measures that can be considered non-compensable and those that must be considered compensable.[801] The arbitral tribunal noted this problem of uncertainty in the case of *Saluka v Czech Republic*:

"International law has yet to identify in a comprehensive and definitive fashion precisely what regulations are considered ... as falling within the police or regulatory power of State and, thus, non-compensable. In other words, it has yet to draw a clear line between non-compensable regulations on the one hand and, on the other, measures that have the effect of depriving foreign investors of their investment and are thus unlawful and compensable in international law."[802]

[799] *Tecnicas Medioambientales Tecmed, SA v United Mexican States*, ICSID Case No ARB(AF)/00/2, Award (29 May 2003).
[800] *Compania del Desarrollo de Santa Elena SA* (n 645)
[801] Kinnear and others (eds), *Building International Investment Law* (n 733)
[802] ibid 461.

Another problem is that although some arbitral tribunals acknowledged the police powers doctrine, other tribunals have not recognised this said doctrine. It appears that some of the arbitral tribunals have under-enforced the police powers doctrine. In certain cases, states put forth an argument based on the police powers doctrine to defend themselves against the claim of indirectly expropriating foreign investment. Nevertheless, the arbitral tribunal under-enforced the state's police power argument and decided by determining whether or not there was substantial deprivation of foreign investment.[803]

In *Sempra v Argentina*, the investor claimed that the state measures which were taken in the course of the country's extreme financial crisis resulted in foreign investment expropriation.[804] On the other hand, Argentina claimed that "the purpose of the measures is relevant to the determination of an expropriation claim, particularly if such measures are adopted under the police power of the State and are proportional to the requirements of public interest."[805] Nevertheless, the tribunal determined the enquiry of expropriation by focusing merely on the effect of the regulatory measures on foreign investments and decided that the measures did not cause substantial deprivation of foreign investment, and thus there was not expropriation.[806]

A comparable situation arose in *Enron v Argentina*, where the investor claimed expropriation. Argentina, in its submissions, made reference to the doctrine of police powers.[807] Nevertheless, the tribunal under-enforced the doctrine of police powers, and determined the case by relying on the 'substantial deprivation' test.[808] In *EDF International and Ors v Argentine Republic*,[809] foreign investors claimed that the measures that had been taken by the government of Argentina, such as per-emergency alterations, tariff measures and the imposition of emergency, were disputed as expropriation. Argentina raised the doctrine of police powers to support its situation that the acts are not expropriation.[810] Nevertheless, the tribunal under-enforced venture into assessing the police powers defence, and rather grounded its decision on the lack of any 'substantial deprivation' of the claimant's investment.[811] Similarly, in the case of *ECE v*

[803] Kevin Winters, 'Indirect and Regulatory Expropriation in International Investment Law: A Critical Review' (LLM thesis, University of Glasgow 2015).
[804] See US–Argentina Treaty (n 606).
[805] *Sempra Energy International* v *Argentina*, (n401).
[806] ibid.
[807] *Enron Corp v Argentina*, ICSID Case No. ARB/01/3, Annulment Proceeding, 30 July 2010.
[808] ibid.
[809] *EDF v Argentine Republic*, ICSID Case No. ARB/03/23, Award of 11 June 2012
[810] ibid.
[811] ibid.

Czech Republic, the police powers doctrine was invoked by the respondent state for the purpose of justifying its acts. Nonetheless, similar to the tribunal in *EDF,* under-enforced the police powers doctrine.[812]

Recently, in *Mamidoil v Albania*[813] Albania referred to the United Nations Conference on Trade and Development (UNCTAD) report on expropriation,[814] claiming that the measures taken were in pursuance of "general welfare, and were implementing the long standing and publicly known decision.....for overriding socio-economic and public safety consideration."*[815]* Albania also relied on *Feldman* to verify its claim for regulatory autonomy to act in the broader public interest, which includes "protection of the environment, new or modified tax regimes, the granting or withdrawal of government subsidies, reductions or increases in tariff levels, imposition of zoning restrictions and the like."[816] Nevertheless, the tribunal under-enforced the doctrine of police powers and applied the 'substantial deprivation' test for the determination of indirect expropriation.[817] A similar approach was followed in *Perenco Ecuador v Ecuador*.[818]

It seems that the tribunals under-enforced the applicability of police power; they decided the expropriation matter on the basis of the 'substantial deprivation' test.[819] Accordingly, the extent to which states can depend on this doctrine to protect and maintain their sovereign regulatory power in regard to international investment law disputes is unclear. It is problematic to attempt to understand the use of the police powers doctrine. It is significant to note that other tribunals have attempted to overcome the shortcomings of each approach, that of the 'sole effect' doctrine, and that of the police powers doctrine, by combining them. An example in this regard can be seen in the *Tecmed* case,[820] where the tribunal combined analyses of both the effects and the purposes of the interference in order to establish its expropriatory character. However, still it can be confusing due to shortages of both approaches.

[812] *ECE v The Czech Republic*, PCA Case No. 2010-5, Award of 19 September 2013
[813] The tribunal considered the Albanian government, such as refusal of renewal of trading licence against the allegation of indirect expropriation and change of land-use plan.
[814] *Mamidoil v Albania,* ICSID Case No. ARB/11/24, Award of 30 March 2015
[815] ibid.
[816] ibid para 531.
[817] ibid. para 539.
[818] *Perenco Ecuador Ltd v The Repub of Ecuador,* ICSID Case No ARB/08/6, Decision on Remaining Issues of Jurisdiction and on Liability 11 August 2015.
[819] ibid.
[820] Técnicas Medioambientales Tecmed, S.A. v. The United Mexican States (n 598).

Moreover, other tribunals have not agreed that a legitimate public policy purpose can justify expropriation without compensation. This is seen in the case of *Metalclad v. Mexico*[821] and *Santa Elena v. Costa Rica.*[822] This sheds light on the question of what approaches future tribunals could and should follow. Nevertheless, current investment arbitration jurisprudence did not succeed to provide a uniform standard by which to judge a host state's actions that have resulted in them being sued for expropriation.[823]

Consequently, it appears that under the police powers doctrine, the state's legitimate regulatory activity is not subject to compensation. Nevertheless, there is a lack of consensus when it comes to defining the doctrine of police powers. It has numerous overlaps with the requirements of lawful expropriation. The police powers doctrine has the same requirements as that of lawful expropriation: the regulatory measures must be for non-discriminatory and public purposes. Under the doctrine of police powers, compensation is not paid; this is because such measures are not considered by it to amount to expropriation. On the other hand, under lawful expropriation compensation must be paid. This has creating confusion and contradictions that make it difficult to distinguish between non-compensatory and compensatory measures. This can attribute to the problems of under-defined law where bro ad law that invites selective enforcement.

Similarly, it appears that some tribunals recognize police power doctrine while other tribunals did not recognize it. We can also infer that the question of what measures are considered compensatory and which are seen as non-compensatory depends on the degree of international acceptance of specific public interests' purposes. This creates selective interpretation. Thus, both over- and under-enforcement theories provide that undefined criteria of police power approach blur the line between illegal and legal. Arbitrators will choose to let many individuals breach the law and sanction others for the same conduct. Discretion is a problem; there are no guidelines, and few criteria make law enforcement subjective and open to many different interpretations that depend on the arbiter's opinions rather than actual culpability and legislative definition.

[821] *Metalclad Corporation v The United Mexican States*, (n 692)
[822] *Compania del Desarrollo de Santa Elena SA* (n 645)
[823] Prabhash Ranjan and Pushkar Anand, 'Determination of Indirect Expropriation and Doctrine of Police Power in International Investment Law' (n 655).

5.3.6 Findings of second phase question:

The second phase question reads as follows: to what extent is the state allowed to take measures against foreign investments for public interests during post-revolutionary times? The answer is that this is unclear. It appears that regulatory expropriation is a broad topic which does not have a clear definition. This has resulted in many interpretations of its status, and this has in turn caused a clash between some states' interests and some investor's interests. The lack of clarity has also raised the question of how can a foreign investor understand the degree to which a host state's actions can be made liable to the provision of compensation? The answer to said question is that some governmental actions will be considered as indirect expropriation, and thus will result in compensation. On the other hand, there are other governmental actions that will not give rise to compensation. However, the problem is that there is a lack of a clear and distinct line between what measures are considered compensatory and which are seen as non-compensatory. This results to inconsistent decisions. There is fragmentation in the international investment law.

Both over and under-enforcement theories can explain that such fragmentation exists due to analytical reasons. There is texts ambiguity. This might be because of absence of a clear checklist or guideline to distinguish between compensatory and non-compensatory measures. This seems to indicate that arbitral tribunals will always need to continue to look at a diversity of factors that have been recognized in scholarly writings and past arbitral decisions. The future development of such jurisprudence depends on the methods that the tribunals apply the relevant rules under the investment law. As one method can highlight the sovereignty of state and favor the state acts in the case of doubts. On the other hand, a different method could be applied by other tribunals that could focus on the purpose of the investment treaty which is to have investment friendly climate. It will favor the investor's interests over the states' interest.

As a result, the present chapter has shed light on the need to international efforts to establish unified interpretative method for analysing expropriation claims. The new interpretative method should overcome the challenges in both approaches the sole effect and police power. For the purpose to harmonize state practice on addressing expropriation claims. However, this issue needs to be addressed because in reality there are many claims that result from new government. For instance, the unilaterally act from the incoming regime to amend or terminate the concession contract.

Although both over and under-enforcement theories provided deeply analysis on examining to what extent is the state allowed to take measures against foreign investments for public interests during post-revolutionary times. However, it is vital to review the literature in order to completely understand what the reasons are for inconsistent arbitral decisions on state responsibility versus foreign investment.

5.3.7 Reasoning of inconsistent decisions on state responsibility versus foreign investment

Many scholars have attempted to understand the reasons behind inconsistent arbitral decisions on state responsibility versus foreign investment. For example, Aaken noted that the inconsistency of arbitral decisions can be due to the vagueness of investment treaty texts.[824] Although open-textual language in an investment treaty can help parties to reach a consensus easily, on the other hand, it can also lead to inconsistent interpretations and undermine the international investment protection regimes.[825] In a similar way to this, Dolzer and Steven argued that most BITs contain a general provision for indirect expropriation that does not address the difference between non-compensable and compensable regulatory acts. For instance, UK treaties stipulate that expropriation includes measures "having effect equivalent to nationalisation or expropriation." Moreover, French treaties refer to "measures of expropriation or nationalisation or any other measures the effect of which would be direct or indirect dispossession." Many of the US treaties focus on these measures: "any other measure or series of measures, direct or indirect, tantamount to expropriation (including the levying of taxation, the compulsory sale of all or part of an investment, or the impairment or deprivation of its management, control of economic value)."[826] These provisions are related to the legal philosophical argument put forth by Hart, who argued that vagueness in the primary rules makes it unclear for individuals to know their obligations, and vagueness in the secondary rules can cause uncertainty. [827]

[824] Anne van Aaken and Tobias A Lehmann, 'Sustainable Development and International Investment Law: A Harmonious View from Economics' in Roberto Echandi and Pierre Sauvé (eds), *Prospects in International Investment Law and Policy* (Cambridge University Press 2013) 317–39.
[825] ibid.
[826] Dolzer and Stevens, 'Bilateral Investment Treaties' (n 648).
[827] Hart, *The Concept of Law* (n462)

Moreover, Jasper argued that inconsistent arbitral decisions arise because of the fact that investment treaties are a source of international law that contains fixed texts that may not be clear. Moreover, customary law is open for debate, and thus international law norms are loose. This creates the situation whereby international law is indeterminate in character.[828] The problem with indeterminacy is that it does not clarify what the law actually is.[829]

Other scholars, such as Schreuer and Weinger, have stated that the incoherence and inconsistency in the legal doctrine regarding indirect expropriation is due to the absence of a precedential system. The nature of non-binding precedent is founded in Article 53(1) of the ICSID Convention.[830] This non-binding nature provides that arbitral tribunals are not obliged to follow previous arbitral award decisions as authoritative statements, and each tribunal is "at liberty to cite or not to cite previous decisions of other tribunals on similar questions of law."[831]

Moreover, Picker noted that incoherent and inconsistent interpretations of expropriation also arise because of non-legal factors. Arbitrators have different ideological and backgrounds that shape their judgements and accordingly their development of investment treaty jurisprudence.[832] This is similar to the opinion of Gus Van Harten, who claimed that "different legal attitudes, economic strategic and institutional factors" affect the arbitrators' performance and the coherence of arbitral decisions."[833] This is similar to the standpoint of Schill, who noted that different arbitral tribunals might have different philosophies and perspectives on the role of the law. Arbitrators' backgrounds reflect on the principles that they rely on, such as commercial law or public international law. [834]

Other scholars have noted that the inconsistencies in arbitral decisions can be due to the lack of a world government and a single treaty. Hobbes argued that a lack of centralised power, as

[828] Jasper E Bergink, 'International Law as a Political Instrument in the Case of Kosovo (1999–2010)' (2010) 2(4) Amsterdam Law Forum 85
[829] Rosalyn Higgins, *Problems and Process. International Law and How We Use It* (Oxford University Press 1994).
[830] Christoph Schreuer and Matthew Weiniger, 'A Doctrine of Precedent?' in Peter Muchlinski and others (eds), *The Oxford Handbook of International Investment Law* (Oxford University P ress2009) 1188.
[831] Subedi, *International Investment Law Reconciling Policy and Principle* (n745)
[832] Colin B Picker, 'International Investment Law: Some Legal Cultural Insights' in Leon E Trakman and Nicola W Ranieri (eds), *Regionalism in International Investment Law* (Oxford University Press 2013).
[833] Gus Van Harten, 'Arbitrator Behaviour in Asymmetrical Adjudication: An Empirical Study of Investment Treaty Arbitration' (2012) 50(1) Osgoode Hall Law Journal 211, 216–19.
[834] Stephan W Schill, 'W(h)ither Fragmentation? On the Literature and Sociology of International Investment Law' (2011) 22(3) European Journal of International Law 875, 888.

well as the diversity of the interests and values of states, makes it impossible to coordinate in legal order.[835]Also, Hart argued that the lack of an international legislative body and compulsory jurisdiction has inspired misgivings.[836] This has resulted in scholars arguing that a global court and legislature should be created in order to govern world affairs.[837] However, it is difficult to establish such an institution; indeed, such an attempt might result in duplications of functions that would make it difficult to reach a level of certainty and consensus.

Moreover, both over and under-enforcement theories can highlight that conflict of norms in international investment law can be one of the major reasons for inconsistent arbitral awards. The conflicting doctrines are 'indirect expropriation' and 'state's right to regulate.' This is related to the philosophical argument by Marmor, who clarified that two legal norms can contradict each other, one requiring the same obligation that the other prohibits.[838]

Also, Dworkin has made the logical argument that tribunal discretion does not constitute the making of a new law but only the determining of the legal principles that are consistent with existing laws.[839] This is attributed to the problem of discretion where there are no guidelines, and few criteria make law enforcement subjective and open to many different interpretations that depend on the arbiter's opinions rather than actual culpability and legislative definition.

Therefore, scholars not agreed on the reasons of inconsistent arbitral awards. However, these scholars provide valuable reasons that are consistent with the findings of both over- and under-enforcement theories However; these theories provide deeper explanation than existing literature for inconsistent arbitral awards on such matter. Both over- and under-enforcement theories provide that the main reason of inconsistent arbitral awards might be because of vagueness of texts and competing norms under customary international law. The different evaluations of facts and laws are made by different tribunals. It appears that the problem of

[835] Thomas Hobbes, *Leviathan* (AR Waller ed, first published 1651, Cambridge University Press 1935).
[836] Hart, *The Concept of Law* (n 462)
[837] Derek Heater, *World Citizenship and Government* (St. Martin's Press 1996).
[838] Andrei Marmor, *Interpretation and Legal Theory* (2nd rev edn, Hart Publishing 2005) 9.
[839] Ronald Dworkin, *The Model of Rules I', reprinted in Taking Rights Seriously* (Harvard University Press 1977).

fragmentation in international investment law is contributed to the problems of under-defined criteria. Broad law that invites selective enforcement open to many different interpretations that depend on the arbiter's opinions rather than actual culpability and legislative definition. Thus, both theories provide such fragmentation is caused due to analytical reasons. Adjudicators might over or under-enforce the law because they are trying to square the law with the facts of the case to render their own notion of justice.

Accordingly, there is a need to build up a coherent body of case law. These finding sheds light on the legitimacy crisis in context of international investment law. Legal theorists such as Franck have clarified that determinacy and coherence are among the core features giving legitimacy to international rules.[840] Thus, inconsistent tribunal decisions can lead to a legitimacy crisis. Moreover, scholars such as Dolzer have argued that "as we all know, the current system of investment arbitration has not been designed in order to promote uniformity or consistency of either rule-making or interpretation, with the sprawling consequences we have seen…."[841]

5.4Concluding Remarks:

Going back to the research main question whether transitional governments responsible under international law for protection and measures against foreign investments? Tribunals have a uniform answer to such a question. There are inconsistent arbitral decisions regarding state responsibility in terms of foreign investments. The issue is ILC articles define internationally wrongful acts that are attributable to the state. Nevertheless, they do not identify in what cases a wrongful act can be attributed to the state and the consequences of responsibility. Thus, it depends on tribunal's discretion on how they interpret the law with facts. This can result to inconsistent decisions.

It appears that the responsibility of transitional governments responsible for protecting foreign investment during revolution is vague. This might be because of the fragmentation in

[840] Thomas, *The Power of Legitimacy Among Nations* (n427)
[841] Dolzer, 'Fair and Equitable Treatment' (n602)

international investment law. Both over- and under-enforcement theories deeply explain the reason for such fragmentation due to analytical reasons. This can be attributed to the text's ambiguity. Investment treaties provide that the obligation of host state to meet investment protection standards towards foreign investments is maintained during times of conflict. However, these investment protection standards are abstract, tribunals can easily over or under-enforce these standards. This is creating inconsistent decisions.

Also, the over-enforcement theory can explain that FPS standard is over enforced among different arbitral tribunals where it extends to the state's duty to protect against private violent actions. With regard to private violence, the responsibility of state does not create strict liability; it merely imposes an obligation on the state to practice due diligence in order to safeguard foreign investment. Also, there is lacking in defining parameters of 'due diligence.' Adjudicators might over or under-enforce the law because they are trying to square the law with the facts of the case to render their own notion of justice. This is creating inconsistent decisions.

Furthermore, the responsibility of transitional governments to take measures against foreign investments for public interests during post-revolutionary times is vague. This is because of the vagueness of texts. It is hard to define indirect expropriation where it can be a progressive series of acts lacking a specific date. This is also causing difficulty because compensation is determined by the date of governmental interference. This is important issue due to value of the property may easily adjust from one day to another. Likewise, the treaty clauses that do not allow expropriation is causing confusion. It appears that there is lack of guidelines in interpreting these clauses resulting that arbitral tribunals addressed the matter differently. Also, there is a lack of clarity when it comes to defining the difference between the indirect expropriation and non-compensable regulatory state measures. The relevant jurisprudence shows that different arbitral tribunals have used different approaches to distinguishing between non-expropriatory and expropriatory regulatory measures.

Some arbitral tribunals have followed the traditional view and adopted the sole effect doctrine. This doctrine prioritises the investor's rights over the state's right. The sole effect doctrine considers only the effects that the measure has had on investments and the investors. The threshold used to evaluate the effect of the measure is substantial deprivation of investment value. However, case law demonstrates that the practice of arbitral tribunals is contradictory

when applying the substantial deprivation threshold. Arbitral tribunals' practice shows that they depend on certain elements when evaluating deprivation, which were described as deprivation in value loss of control and duration. Both over and under-enforcement theories explain that elements of evaluating deprivation is subjective resulted that different arbitral tribunals practices apply such criteria differently. This can attribute to the problems of under-defined law where broad law that invites selective interpretation. Adjudicators might over or under-enforce the law because they are trying to square the law with the facts of the case to render their own notion of justice.

On the other hand, other arbitral tribunals have recognised the right of state to regulate by adopting the police powers doctrine. This is an opposite doctrine to that of the doctrine of sole effect, since it considers the intent of the state and the adopted measure. Under the approach of police powers, the state's legitimate regulatory activity is not subject to compensation. Nevertheless, there is a lack of consensus when it comes to defining the doctrine of police powers. It has numerous overlaps with the requirements of lawful expropriation. The approach of police powers has the same requirements as that of lawful expropriation: the regulatory measures must be for non-discriminatory and public purposes.

Under the doctrine of police powers, compensation is not paid; this is because such measures are not considered by it to amount to expropriation. On the other hand, under lawful expropriation compensation must be paid. This has creating confusion and contradictions that make it difficult to distinguish between non-compensatory and compensatory measures. This can attribute to the problems of under-defined law where broad law that invites selective interpretation. As a result, the present chapter has shed light on the need to international efforts to establish unified interpretative method for analysing expropriation claims. This new unified interpretative method should overcome the challenges of both doctrines the sole effect and police power.

Accordingly, both over- and under-enforcement theories provide that broad laws of state responsibility blur the line between illegal and legal. Arbitrators will choose to let many individuals breach the law and sanction others for the same conduct. Discretion is a problem; there are no guidelines, and few criteria make law enforcement subjective and open to many different interpretations that depend on the arbiter's opinions rather than legislative definition.

Nevertheless, inconsistent decisions cannot be totally eradicated. This is due to the fact that there is a lack of a single treaty and, a world government. However, the inconsistent arbitral decisions which are made regarding state responsibility in relation to foreign investments need to be minimized in order to create more predictability for host states and foreign investors.

Finally, this chapter recommends international efforts to address vagueness of law. A new convention might be needed to unify and clarify the rules of state responsibility in international investment context. The investment protection standards and what measures are considered compensatory and what non-compensatory need to clarified. Finally, this chapter recommends a precedential system for arbitral tribunals to avoid inconsistent decisions.

Chapter 6: Conclusion

We can conclude that there is a tension between legal stability and political change. On one hand, transitional governments face pressure to enact economic reforms to redress the control of the previous regimes. This might cause major changes in general laws such as taxation, labour and the relationship between investors and the business communities in which they operate in. This create inconsistency with assurances granted by the previous regime. This result in a different regulatory environment to that anticipated by investors when they originally invested. In this sense, transitional governments will always argue that under international law, states have sovereign rights in regulating foreign investments. On the other hand, investment treaties require the incoming governments to pay compensation when they are involved in such economic reforms, thus placing a huge strain on stretched budgets.

This raises the question of how arbitral tribunals address the tension between legal stability and political change. Particularly, there is no central authority—the arbitral panel is decentralised and private. This generates the need for an interpretative tool to analyse how these arbitral tribunals interpret customary international law and investment treaties given the tension between legal stability and political change. Therefore, the thesis started with a theoretical exploration of the framework applicable to the study. It brings the idea of under-enforced legal norms into international investment law. Sager, the prominent constitutional law scholar, developed the under-enforcement legal theory. The theory explains how in some instances the law is not fully enforced because of institutional or analytical reasons. It performed an analytical tool in providing better understanding of how the law is interpreted among different tribunals.

Also, the main relevance of using the under-enforcement theory into the study comes from the fact that it is constitutional theory. At the same time, investment arbitration is a type of global constitutional law. This is because both national constitutional law and investment treaties were established to limit states' sovereignty. This theory has been applied in numerous areas of law but not in the area of international investment law, which brings originality to the study. The use of theory is not a call for full enforcement of the law but rather to provide a better understanding on the differences of awards decisions. The under-enforcement theory also leads

to an examination of over-enforcement theory, its contrary theory, in which adjudicators extend statutes beyond their original understanding.

Over-enforcement of the law can also occur when the legal system stipulate rules that exceed normal deterrence to minimize law violation. Like this, both theories are used as analytical tools to assess the law application. However, use of under-enforcement or over-enforcement theory to assess law enforcement requires certain technique. Some rules do have a determinate meaning. In these circumstances, it would be easy to identify whether the provision is over-enforced or under-enforced. Other rules are less determinate; it requires to predicting over-enforcement and under-enforcement arising in situations where we likely reach agreement on the definition of underlying concepts.

Accordingly, as described in the introduction of this thesis, the core research question is what does the international law allows transitional government in respect of foreign investments? This required examining different state defences under the laws of state immunity and state responsibility. Thus, the thesis examined whether transitional governments can invoke the sovereign immunity defence to avoid international state liability. Thus, this thesis studies doctrine of state immunity. It finds that states have the right to choose their means of administration of their social, economic and political system over their territories without the interference of foreign investors. This can result in legal, political and economic challenges for state sovereignty acts. This made it important for foreign investors to understand the limitation of state sovereignty acts towards foreign investments. State immunity will not be allowed if the state acts are different to the interests of the foreign investor or the agreement terms. Nevertheless, if a host state's acts are related to public interest, the state will be allowed to use its immunity power. The other party is the only one that has the right to compensation.

Mainly, it appears that host states always invoke sovereignty arguments to avoid international adjudication. Consequently, this study studied the development of state sovereign immunity. There was a significant effort in the nineteenth century to shift from absolute immunity to restrictive sovereign immunity. However, under the restrictive theory, state immunity must be waived. There are two types of immunity waiver – state immunity waiver from adjudication and state immunity waiver from enforcement.

Under the wavier of state immunity from adjudication, the study revealed that although the general restrictive immunity is clear, there is a lack of consistency in its use. Both over- and under-enforcement theories provided better explanation on such inconsistency. These theories provide that some tribunals under-enforce the rules of state waiver of immunity from adjudication. This is because of analytical reasons due to their interpretation to rules of wavier of state immunity. Adjudicators might over or under-enforce the law because they are trying to square the law with the facts of the case to render their own notion of justice.

Nevertheless, the state will always invoke the sovereign argument. Likewise, rules of state waiver of immunity from enforcement in some cases is under-enforced because of institutional reasons. There is a shared responsibility between national law and international law in enforcing the arbitral awards with national courts.

Accordingly, this study shows that because of the fragmented and uncoordinated development of many sub-disciplines of international law, protection of foreign investments from hostile host state's governmental measures remain moot and unpredictable. This requires the development of a unitary framework of international law. Thus, UNCSI should bring practical solutions. However, before recommending the state to ratify it, the convention need to clarify what constitutes a commercial transaction, the treatment of state agencies and mixed purpose state properties. Also, an effective mechanism is needed to enforce arbitral awards without exception to expedite, adequate and fair compensation in all cases where foreign investments are impounded by hostile state.

Generally, this study finds that sovereign defences can lead to the necessity defence to figure out the extent to which the state has valid purposes for breaching its international obligations. The dilemma is that during an emergency or crisis, the state will always argue that the circumstances were out of its control and it should be excused from its international responsibility. Nonetheless, the investors will argue that the states' involvement in the crisis is because of the state acts; thus, there should be redress. A revolution or transitional times can be considered an emergency times because it causes instability for the state, which can negatively affect foreign investment protection. Therefore, this study aimed to examine whether a revolutionary government can invoke the state defences to avoid its international obligations towards foreign investment protection.

Under the law of state responsibility, the state obligations and the violation of such obligations and its consequences are defined. According to it, the state has the right to react in particular circumstances. Thus, international law recognises some of the state's defences. Also, the UN established the ILC articles on state responsibility to codify customary international law. As a result, the relevant defences for the revolutionary or transitional government used to avoid its international obligations are the necessity and the force majeure defences. Generally, both state defences exempt the state from its obligations but in a restrictive manner. However, the study finds that it is unclear when it is allowable for the host state to use the state defences. This is because of the fragmentation in international investment law.

Both theories over and under-enforcement explained that such fragmentation is because of analytical reasons. The interpretation of the provisions of the treaty under customary international law remains unclear. Arbitral tribunals decision depend on how the tribunal interprets the treaty provision and the criteria of necessity under international customary law. It seems that the law is applied based on discretion where is there are no guidelines on how applicable a source of law is. Tribunals select the source of law that renders their own notion of justice. Generally, few criteria make law enforcement subjective and open to many different interpretations that depend on the arbiter's opinions rather than actual legislative definition. Consequently, tribunals might over or under-enforce the law because they are trying to square the law with the facts of the case to render their own notion of justice.

It also seems that criteria of state defences under customary international law are hard to fulfill. This might be to stabilise the treaty so it gives the state a little room for change. It appears that there is absence of understanding on how the high requirement of state defences can be successful within the investment context. Thus, some tribunal can attempt to under-enforce such rigid criteria of state defences to render their own notion of justice. On the other hand, other tribunals see justice by doing extensive interpretation to such rigid criteria. This happens because the criteria of state defences under customary international law are subjective and open to different interpretations. This can contribute to the problem of inconsistent decisions. The textual analysis is as a tool to free adjudicators from constraints. However, drawbacks in justifying interpretation will increase indeterminacy.

The study concludes that protection of foreign investments from host state's governmental measures remains unpredictable because of the fragmentation in international investment laws. Thus, this study shed the light on the need for united international effort to establish a single set of procedures to unify the source of law for international investment disputes. There should be international effort to harmonise the interpretation of legitimate state defences during emergency.

Accordingly, this study examined the limits of a state's responsibility in respect of foreign investment during periods of upheaval and indeed, after revolution. To achieve this, it has been necessary to examine two phases – the state's responsibility during and after the course of a revolution. The study finds that under the law of state responsibility, treaties that deal with foreign investment protection will continue to be applied after the outbreak of conflict. It appears that a state's international responsibility exists whenever the state exercises its public power. Any irregularities in state acts will prompt the principle of responsibility to be invoked. In the event of private violence, the state is only responsible if it does not prevent harm. Thus, a state is required to exercise standards of due diligence.

However, the study finds there are inconsistent decisions regard the state responsibility to protect foreign investment during revolution times. Both theories the over and under-enforcement deeply explained that such inconsistent decision on state responsibility is because of analytical reasons. There is vagueness of texts. Investment treaties do not define treatment standards. This can attribute to the problems of under-defined criteria where broad criteria result in selective interpretation. Tribunals interpret the textual language based on their views of the meaning of words. Over or under-enforcement generally reflects adjudicators opinion in defining rules that may be over-enforced or under-enforced. This led to inconsistent arbitral decisions and a lack of predictability. Therefore, the parameter of due diligence and investment protection standards need to be defined.

The study also examined extent in which the state is permitted to take measures against foreign investments for public interests during post-revolutionary times. It finds that under international law, a successor government can work with a different political philosophy. Nevertheless, it has to fulfil the duties of the predecessor government or it will be subject to

compensation in the event of nationalisation and expropriation. Despite the change of government during the revolution, state is subject to the international law. This means that a state as an international person cannot be changed. Thus, the new regime is bound by the same international obligations of the state.

Also, the study finds there are inconsistent decisions regard the state responsibility to take measure against foreign investments after revolution times. Both theories the over and under-enforcement deeply explained that such inconsistent decision on state responsibility is because of analytical reasons. There is vagueness of texts. There is vagueness in defining indirect expropriation claims. This is causing difficulty in compensation matter. Likewise, the treaty clauses that do not allow expropriation is causing confusion. There is absence of guidelines on interpreting these clauses resulting in various interpretation among arbitral tribunals.

There is also ambiguity when it comes to distinguishing between compensatory and non-compensatory regulatory measures. Some tribunal used 'sole effect' doctrine while other tribunal used police power doctrine. These doctrines are wholly opposite to those that they adopt in determining the regulatory expropriation claims. The sole effect doctrine aims to evaluate the effects of the measure only, and the economic impact that the investor has suffered. In contrast, the doctrine of police powers aims to evaluate only the purpose of the measure. This situation has resulted to incoherent arbitral jurisprudence and inconsistent legal doctrines being applied by arbitral tribunals. This study sheds light on the need to better clarify what measures are considered compensatory and what are non-compensatory. There is also a need for unifying the interpretation approach used by arbitral tribunals in making their decisions regarding expropriation claims.

Finally, to return to the central question, what does the international law allow transitional government in respect to foreign investments?

The answer is unclear because there is fragmentation in the international investment law. There are inconsistent decisions among arbitral tribunals. This can negatively affect the legitimacy of the whole system. However, both over and under-enforcement theories made significant contributions to deeply analysing the current problem of fragmentation. These theories indicate that such fragmentation of law of state immunity in international investment law context might be because of analytical and institutional reasons. Tribunal's opinion is seen in defining rules

that may be over-enforced or under-enforced. Also, the shared responsibility between national and international law is problematic. It is causing inconsistent decisions on the rules of state immunity in the investment law context.

Likewise, over-enforcement and under-enforcement theories explain that fragmentation of law of state responsibility in international investment law context is due to analytical reasons. Tribunals interpret the law differently because of laws ambiguity. The interaction between customary international law and treaty law is creating vagueness. It seems that the law is applied based on discretion where there are no guidelines on how applicable a source of law is. Also, investment treaties do not create concrete rules, but only abstract standards and open-ended. There is an ambiguity in defining the clauses. At the same time, customary international law, as the secondary rule, is interpreted differently among different arbitrators. Arbitrators have different backgrounds which reflect their interpretations of the law. These arbitrators can over-enforce or under-enforce the law to render their own notion of justice. This is causing inconsistent decisions on the rules of state responsibility in the international investment law context.

Nevertheless, fragmentation cannot be totally avoided because two judges from the same legal system frequently apply the same law differently and reach different outcomes. Particularly, fragmentation cannot be totally avoided in the context of international investment law. This is because it is difficult to have central world legislator. However, there is a need for harmony and a coherent set of disciplines. Therefore, this dissertation recommends the development of a unitary framework of international law. Unifying state immunity rules in international investment law can happen by addressing the shortage of UNCSI and encouraging states to ratify it. The World Bank and IMF should put pressure on states through financial incentives.

Similarly, the rules of state responsibility in the international investment law context need to be unified and clarified. The challenges between treaty law and customary international law need to be addressed. Accordingly, this study recommends the establishment of a new international convention that like the VCLT (1969) codifies and progressively develops international investment law.

This new convention should simplify the interaction between customary international law and treaty law. The conventions should create concrete rules in international investment law. The convention should address the followings: clarify subjective criteria of both defences, the necessity and force majeure. Also, investment protection standards need to be defined. Indirect expropriation claims and its compensation need to well-defined. Treaty clauses that prohibit expropriation need more guidance on how it should be interpreted. Also, the new convention should provide a clear distinguishing feature between compensatory and non-compensatory regulatory measures is necessary. Correspondingly, this study recommends the establishment of a precedent system in order to provide a degree of uniformity in the decisions. Likewise, there is a need to establish a binding institutionalised mechanism that has the competence to clarify the rules and decide their applications.

Finally, it is vital to mention future research areas and limitation of the present thesis. There is a need for a future research on conducting comparative analysis on recent cases that involve revolutionary government versus foreign investment protection, regard the compensation matter. There is a need to conduct comprehensive study on how arbitral tribunals address compensation matter, in the light of the dilemma of legal stability versus political change. The reason that this study did not conduct such analysis is the limited availability of recent revolutionary government's cases.

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