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# DEDUCING AN INVESTOR'S FET EXPECTATION IN INTERNATIONAL INVESTMENT LAW

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## ABSTRACT

*The 'fair and equal treatment' provision is prevalent in the great majority of bilateral investment agreements. In recent years, the FET standard has been the subject of several significant research. The idea of justifiable expectations has a limited relationship to the occurrence of regulatory changes enacted by governments that may harm foreign investment. Scholars are becoming more interested in this subject. The debate remains as to whether the notion achieves a fair balance between the interests at issue in investment treaty arbitration, or does it offer an unfair advantage for one side over the other? After more than 10 years of intense usage, do we truly understand what the theory of "legitimate expectations" stands for and what it aims to accomplish? These conventional risks give investors' interests disproportionate weight at the expense of public interests and a State's regulatory authority. In addition, while considering whether expectations are "fair," the level of development of the host country must be considered with additional care. This article examines the origins and history of the word "legitimate expectations," analyses how it has been employed by arbitral tribunals deciding investment claims over the last ten to fifteen years and defines "Legitimate Expectations."*

## INTRODUCTION

The need that a foreign investment be provided "fair and equitable treatment" (FET) has become the central criterion in investment treaty law, safeguarding foreign investors from harm caused by arbitrary, discriminatory, or abusive governmental conduct. The norm is reflected in the great majority of international investment agreements (IIAs), bilateral trade agreements (BITs), and free trade agreements (FTAs) that govern foreign investment between nations, such as the North American Free Trade Agreement (NAFTA). As a result of the exponential increase

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in the number of investment disputes covered by investment treaty law throughout the latter half of the 2000s, FET under investment treaty law has become the most disputed and debated part of this corpus of international law.[2]

Additionally, it has garnered the most unfavourable attention.[3] FET is inherently a nebulous term and is often expressed in minimum wording in IIAs.[4] This allows a great deal of leeway for ad hoc courts using the norm to assign meaning to the text, and some have not hesitated to take an expansive stance. The fact that these tribunals are not susceptible to effective appellate review increases the likelihood of inconsistency in interpretation. Indeed, the system has been accused of exceeding its power in limiting regulatory autonomy and for delivering uneven outcomes.[5]

This article explores the FET criterion that has been articulated as "transparency and protection of legitimate expectations." The regulatory framework impacting investments must be easily discernible, and choices affecting investments must be traceable to this framework. When state regulatory activity changes counter to the reasonable expectations of the investor, therefore having a detrimental impact on the investment, this may violate FET requirements. This idea is basically an arbitral creation, since it is not mentioned in any IIA rules. These standard risks giving the interests of investors undue weight at the cost of public interests and a State's legal power to regulate. In addition, while using such a concept, extra care must be taken to consider the degree of development of the host nation when evaluating whether expectations may be "reasonable."

According to the Organisation for Economic Co-operation and Development (OECD), the requirement of transparency is a "relatively new concept not generally considered a customary

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[2] U.N. Conf. Trade & Dev., *World Investment Report 2010: Investing in a Low- carbon Economy* 84 (U.N. Conf. Trade & Dev. 2010). *See also*, Stephen Fietta, *Expropriation and the 'Fair and Equitable' Standard: The Developing Role of Investors Expectations' in International Investment Arbitration*, 23 J. Intl. Arb. 375–99, 376 (2006).

[3] Anthony De Palma, *Nafta's Powerful Little Secret; Obscure Tribunals Settle Disputes but Go Too Far Critics Say*, N.Y. TIMES (Mar. 11, 2001), HTTPS://WWW.NYTIMES.COM/2001/03/11/BUSINESS/NAFTA-S-POWERFUL-LITTLE-SECRET-OBSCURE-TRIBUNALS-SETTLE-DISPUTES-BUT-GO-TOO-FAR.HTML.

[4] Matthew Porterfield, *An international common law of investor rights*? 27 U. Pa. J. Intl. Econ. L . 79–113, 88 (2006).

[5] Susan D. Franck, *Empiricism and International Law: Insights for Investment Treaty Dispute Resolution*, 48 Va. J. Intl. L. 767, 768 (2007–2008).

international law standard."[6] However, according to Dolzer and Schreuer, "[b]oth the requirement of transparency and the protection of legitimate expectations are by now firmly rooted in arbitral practice."[7] This article asserts that this should not be the case.

This article is divided into five sections. Section 1 introduces the subject and sets the scope for the rest of the paper. Section 2 analyses the background and purpose behind FET provisions in investment treaties. Section 3 analyses the protection of legitimate expectations of investors. Section 4 delves into the legal status of protection which investors can expect from legitimate expectations provisions in investment treaties. Finally, section 5 sums up the article and concludes.

## TRACING THE ORIGIN OF THE FET OBLIGATION

In investment treaty law, the FET obligation is a non-contingent norm. In other words, it is an absolute criterion that must be applied to nations without regard to situation or other 'relative' elements, such as those included in 'national treatment' or 'most-favored country' provisions. The objective of a non-contingent standard, according to Fatouros, is that "the treatment they prescribe is determined beforehand and thus, presumably, does not fall below a minimum standard"; however, the disadvantage of such a standard is clear: "the generality and abstraction of these standards remains an important drawback." It is often difficult to evaluate whether a certain metric is "just," "reasonable," or "fair."[8]

There is no unanimity among courts or academics over the precise substance of FET. While parts and specific needs of the standard have been elucidated, the precise liability level for how destructive a state's acts must be in order to violate the norm has remained elusive. In this regard, Schill remarks:

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[6] Org. Econ. Co-operation & Dev., *Fair and Equitable Treatment Standard in International Investment Law*, in *International Investment Law: A Changing Landscape: A Companion Volume to International Investment Perspectives*, 118 Org. Econ. Co-operation & Dev. Publg. (2006), HTTPS://DOI.ORG/10.1787/9789264011656-EN.

[7] RUDOLPH DOLZER & CHRISTOPHER SCHREUER, PRINCIPLES OF INTERNATIONAL INVESTMENT LAW 134 (Oxford U. Press 2008).

[8] ARGHYRIOS A FATOUROS, GOVERNMENT GUARANTEES TO FOREIGN INVESTORS 135–141 (Columbia U. Press 1962).

*"Fair and equitable treatment does not have a consolidated and conventional core meaning as such nor is there a definition of the standard that can be applied easily. So far it is only settled that fair and equitable treatment constitutes a standard that is independent from national legal order and is not limited to restricting bad faith conduct of host States. Apart from this very minimal concept, however, its exact normative content is contested, hardly substantiated by State practice, and impossible to narrow down by traditional means of interpretative syllogism."*[9]

Further, Muchlinski declares:

*"The concept of fair and equitable treatment is not precisely defined. It is, therefore, a concept that depends on the interpretation of specific facts for its content. At most, it can be said that the concept connotes the principle of non-discrimination and proportionality in the treatment of foreign investors."*[10]

Moreover, nations have given little thought to the legal duties that their IIAs may imply, indicating that they did not think that the standards they were agreeing to would be so stringent.

In the vast majority of instances, FET obligations in BITs are among the treaty terms that have not been adequately drafted. These lead to nations not expecting the obligation which they have signed up for. Schneur described this in his oral testimony as:

*"[M]any times, in fact in the majority of times, BITs are among clauses of treaties that are not properly negotiated. BITs are very often pulled out of a drawer, often on the basis of some sort of model, and are put forward on the occasion of state visits when the heads of states need something to sign and the typical two candidates in a situation like that are Bilateral Investment Treaties, and treaties for cultural cooperation. In other words, they are very often not negotiated at all, they are just being put on the table, and I have heard several representatives who have actually*

[9] STEPHAN SCHILL, THE MULTILATERALIZATION OF INTERNATIONAL INVESTMENT LAW 263 (Cambridge U. Press 2009).
[10] PETER MUCHLINKSKI, MULTINATIONAL ENTERPRISES AND THE LAW 625 (Oxford Intl. 1995).

> *been active in this Treaty-making process, if you can call it that, say that, 'We had no idea that this would have real consequences in the real world'."*[11]

Consequently, the FET norm has evolved into the twenty-first century's version of John Selden's equity, with its measure varying on the size of the Chancellor's foot.[12] Given the varying formulations of FET in different IIAs, the generally vague wording, and the disagreement over the exact relationship between the international FET standards, in a system without a coherent appellate mechanism or system of binding precedent, it is surprising that arbitral tribunals have displayed such coherence in identifying and applying the principles encompassed by the fair and equitable standards.[13] It is customary for arbitral courts to cite past verdicts, so reaffirming lines of reasoning in investment treaty law that have become commonplace.

## PROTECTING LEGITIMATE EXPECTATIONS IN INTERNATIONAL ARBITRATION

### *Customary International Law: The NAFTA Experience*

#### *1. Introducing Transparency Obligations*

*Metalclad v. Mexico* is the first lawsuit brought under NAFTA concerning transparency and legitimate expectations, as well as the first case in which a claimant was victorious under Article 1105.[14] The complaint had obtained federal building and operating licenses to construct and run a landfill. It relied on assurances from federal authorities that it had the necessary authorizations. The local government ultimately denied a development permission.

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[11] Prof. Christopher Schreuer, oral testimony on behalf of the Claimant, Wintershall Aktiengesellschaft v. Argentina, ICSID Case No. ARB/04/14, Award (8 Dec. 2008), at 85.
[12] J. Selden, *Table Talk*, from EVANS AND JACK, SOURCES OF ENGLISH LEGAL AND CONSTITUTIONAL HISTORY 223–224 (Butterworths 1984).
[13] Dolzer & Schreuer, *supra* note 7, at 133–147. *See also* U.N. Conf. Trade & Dev., *Series on Issues in International Investment Agreements II*, at xvi and 61–83; Roland Kläger, *Fair and equitable treatment: A look at the theoretical underpinnings of legitimacy and fairness*, 11 J. World Inv. & Trade 435, 443 (2010).
[14] Metalclad Corp. v. Mexico, Award, 30 Aug. 2000, 5 ICSID Rep. 209.

Article 1105(1) of the North American Free Trade Agreement states that "each Party must grant to investments of investors of the other Party treatment consistent with international law, including fair and equitable treatment and complete protection and security."

The tribunal determined that Metalclad had the right to rely on the testimony of federal authorities,[15] and ruled that the actions of the state and municipality violated Article 1105's FET obligation. The tribunal ruled that:

> *"Prominent in the statement of principles and rules that introduces the Agreement is the reference to 'transparency' (NAFTA Article 102(1)). The Tribunal understands this to include the idea that all relevant legal requirements for the purpose of initiating, completing and successfully operating investments made, or intended to be made, under the Agreement should be capable of being readily known to all affected investors of another Party. There should be no room for doubt or uncertainty on such matters. Once the authorities of the central government of any Party (whose international responsibility in such matters has been identified in the preceding section) become aware of any scope for misunderstanding or confusion in this connection, it is their duty to ensure that the correct position is promptly determined and clearly stated so that investors can proceed with all appropriate expedition in the confident belief that they are acting in accordance with all relevant laws."*[16]

This paragraph merits additional examination. The first need is a clear regulatory structure. However, the regulatory structure was clear at the time of investing. When deciding to continue with an investment, the investor is cognizant of the regulatory structure. Unless NAFTA requires a reform of the regulatory structure to enhance openness upon joining the FTA, this is of little relevance to the argument at hand. Even then, this would be a commitment owed by Mexico to its NAFTA free trade partners; it would be a stretch to extend this obligation to a foreign investor that entered Mexico lawfully.

[15] *Id.* at p. 89.
[16] *Id.* at p. 76.

If this is not a NAFTA requirement, the investor must accept the regulatory environment at the time the transaction was made. A claimant is not permitted to later assert that the legal system they encountered when they decided to invest was insufficiently transparent if the system has not undergone significant change. Later, in *GAMI v. Mexico*, it was established unequivocally that NAFTA arbitrators do not have the authority to review rules and regulations that precede a foreign investor's investment choice.[17] In *S.D. Myers v. Canada*, the tribunal reaffirmed that parties must operate in accordance with the law as it existed at the time of the investment.[18] Outside of NAFTA, it is clear that investors must not only analyze the regulation as it exists, but also the degree of development of the host nation, in order to determine what expectations may be reasonable. Thus, in *Genin v. Estonia*, the panel found no violation of the criterion of fairness and equity and deemed it relevant that the claimant had agreed to invest in:

> *"a renascent independent state, coming rapidly to grips with the reality of modern financial, commercial and banking practices and the emergence of state institutions responsible for overseeing and regulating areas of activity perhaps previously unknown."*[19]

Metalclad recognized the regulatory system in Mexico as it existed at the time of its investment, presumably after obtaining legal counsel on the relevant legislation influencing its investment. The statements made by the tribunal on the level of openness needed by the "relevant legal requirements" were clearly flawed. This is not to say that a State may keep legal requirements secret or introduce new requirements arbitrarily affecting the value of a foreign investment; rather, a claimant cannot establish that they were not accorded fair and equitable treatment because the legal system they found and accepted when they made the investment was not sufficiently transparent. The second part of the above-quoted case passage imposes on governments of host states a 'duty' to ensure that they clearly state the correct legal position regarding an investment, not just when they become aware of a misunderstanding or confusion, but whenever there is any 'scope' for such a misunderstanding or confusion. This is a considerable load, especially for a developing nation.[20] Furthermore, it is difficult to imagine any commercial or economic connection in which one party is obligated to function as legal

[17] GAMI v. Mexico, Award, 15 Nov. 2004 (2005) 44 I.L.M. p. 93.
[18] S.D. Myers v. Canada, Second Partial Award, 21 Oct. 2002.
[19] Genin v. Estonia, ICSID Case No. ARB/99/2, Award, 25 Jun. 2001, p. 348.
[20] International Monetary Fund, *Growth Resuming Danger Remains*, World Economic Outlook (April 2012).

counsel for the other, and it is much more difficult to see a court or tribunal encouraging one party to depend only on legal advice from the other. It is implausible for the court to assert the existence of such a burden. At no time did the court imply that Metalclad may have deemed it advisable to retain independent counsel.

"Metalclad was led to believe, and did believe, that the federal and state permits allowed for the construction and operation of the landfill."[21] This fact was cited by the tribunal while providing its rationale for its ruling in Metalclad's favor. This image inspired Metalclad to continue with its construction in the manner that it did. This fact does suggest unfair treatment; however, the tribunal provided no legal authority for the proposition that Metalclad was entitled to rely on these representations, nor did it question whether independent counsel would have clarified the misunderstanding or whether Metalclad had sought such counsel.

In its conclusion regarding the FET criterion under NAFTA Article 1105[22] the tribunal made no reference to any legal source other than Article 1105(1),[23] and the use of the phrase "transparency" in Article 102(1). Despite the clear reference to "international law" in Article 1105(1), the tribunal did not explain what this meant for the fair and equitable criteria under NAFTA. The award was later overturned by the Supreme Court of British Colombia.[24]

### *2. Response under NAFTA and Clarification of the International Customary Standard*

Shortly after the wide interpretation of Article 1105(1) in *Metalclad*, the case of *Pope & Talbot v. Canada* was decided.[25] In this case, the tribunal rejected Canada's claim that a violation of the FET norm requires "egregious" behavior.[26] The court proceeded by stating that Article 1105 requires "that covered investors and investments receive the benefits of the fairness elements under ordinary standards applied in the NAFTA countries."[27] The NAFTA Free Trade

[21] Metalclad Corp. v. Mexico, *supra* note 14, at p. 85.
[22] *Id.* at p. 74-101.
[23] *Id.* at p. 74.
[24] *Metalclad Corp. v. Mexico*, Review by British Columbia Supreme Court, 2 May 2001, 5 ICSID Rep. 238, paras 57–76.
[25] *Pope & Talbot Inc. v. Government of Canada (Merits, Phase 2),* 13 World Trade & Arbitration Materials 61 (10 Apr. 2001).
[26] *Id.* at p. 108.
[27] *Id.* at p. 118.

Commission, which is comprised of officials from the three NAFTA countries, responded immediately to the tendency toward wide interpretation in these decisions. It released a note of interpretation explaining that NAFTA Article 1105 includes the following provisions:

> *"The concepts of 'fair and equitable treatment' and 'full protection and security' do not require treatment in addition to or beyond that which is required by the customary international law minimum standard of treatment of aliens."*[28]

The inference is clear. The minimum bar for FET under NAFTA is customary international law. Clearly, tribunals interpreting these clauses had exceeded the intent of the nations parties to the treaty. The interpretations of the tribunals in *Metalclad* and *Pope & Talbot* should be rejected since they are contrary to the law.

Since then, NAFTA case law seems to have accepted that customary international law has neither responsibility of transperancy or obligation to legitimate expectations under custimary international law. Since *Metalclad*, no tribunal has ruled that a lack of transparency violated NAFTA Article 1105, and that portion of the judgment has been annulled. Under *Glamis Gold v. United States*, the United States said that "all three States Parties to the NAFTA have agreed that there is no general transparency requirement in Article 1105 and have expressly rejected the notion that transparency forms part of customary international law."[29] In *Cargill v. Mexico*, the court held, "the Claimant has not established that a general duty of transparency is included in the customary international law minimum standard of treatment"[30]

Therefore, it seems, based on declarations by NAFTA nations and tribunal judgments, that responsibilities related openness and safeguarding of investor expectations are not part of customary international law. In regards to IIAs that are not directly related to the customary international law norm, the law is less clear. There, the notion that fair and equal treatment necessitates openness and the safeguarding of investor expectations is maintained.

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[28] North American Free Trade Agreement, *Notes of Interpretation of Certain Ch. 11 Provisions, NAFTA Free Trade Commission*, 31 Jul. 2001, HTTP://WWW.SICE.OAS.ORG/TPD/NAFTA/COMMISSION/CH11UNDERSTANDING_E.ASP .

[29] Glamis Gold Ltd. v. United States, UNCITRAL (NAFTA), Award, 8 Jun. 2009, p. 580.

[30] Cargill Inc. v. United Mexican States, ICSID Case No. ARB(AF)/05/2 (NAFTA), Award, 18 Sep. 2009, at 294.

*Experience outside of NAFTA: The Positive Development of Transparency in Arbitration*

*1. Standard for Transparency*

Outside of NAFTA, tribunals may be obliged to apply two forms of FET provisions that are unrelated to the international minimum standard. Firstly, an unqualified FET provision and secondly, FET clauses connected to international law.

Transparency and the safeguarding of reasonable expectations have been consistently cited by courts as fundamental components of the FET obligation. In reality, tribunals have avoided analysis of the many meanings the two kinds of clauses described above may have, or their link to the international minimum standard, and have instead chosen to concentrate on identifying the particular parts forming the standard.[31] Thus, the variation in meaning between different formulations of FET clauses has been disregarded, with the emphasis on the aspects of the standard as applied to various factual contexts providing the sense of content uniformity.

In *Tecmed v. Mexico*, the 'definitive' assertion of the obligation of transparency was made.[32] The tribunal found a violation of FET in the Spain-Mexico BIT, pursuant to Article 4(1) stating that a contracting party is obligated to guarantee FET "pursuant to international law."[33] The tribunal further stated that:

> *"The Arbitral Tribunal considers that this provision of the Agreement, in light of the good faith principle established by international law, requires the Contracting Parties to provide to international investments treatment that does not affect the basic expectations that were taken into account by the foreign investor to make the investment. The foreign investor expects the host State to act in a consistent manner, free from ambiguity and totally transparently in its relations with the foreign investor, so that it may know beforehand any and all rules and regulations that will govern its investments, as well as the goals of the relevant policies and*

[31] UNCTAD, Investor-State Arbitral Practice, at 61.
[32] *Tecmed v. Mexico*, ICSID Case No. ARB (AF)/00/2, Award, 29 May 2003.
[33] Xiuli Han, *The Application of the Principle of Proportionality in Tecmed v. Mexico,* 6 Chinese J. Int'l L. 635, 650 (2007).

*administrative practices or directives, to be able to plan its investment and comply with such regulations."*[34]

The method necessitates that state behaviour be consistent, ambiguity-free, and transparent, ensuring that the investor is aware in advance of the regulatory and administrative framework and policies that will impact it. The Tecmed "standard" is not only burdensome; it has been famously defined as '[a]ctually not a standard at all; it is rather a description of perfect public regulation in a perfect world, to which all states should aspire but very few (if any) will ever attain'.[35]

It is noteworthy that the tribunal arrived at such a high threshold to define FET, and it is more astounding that it did not cite any source to back its conclusion. Douglas goes on to explain that this comment was obiter dictum, as recognized by common law attorneys; it did not form the foundation of the ruling since Mexico had failed to achieve a far lesser bar in this instance.[36] More astonishing is the fact that this line from *Tecmed* has been frequently considered as the canonical source for the FET standard.[37]

Using this strategy, the tribunal in *CMS v. Argentina*, purely relying on the Preamble to the Argentina-United States BIT[38] which stipulated that FET treatment of investment is desirable to maintain a stable framework for investment was able to discern that the FET standard included a requirement to maintain a "stable framework for the investment"[39] despite the unprecedented financial crisis.

Van Harten characterized the CMS court's interpretation as "[f]rankly...nothing short of adventurous."[40] Nonetheless, the tribunal proceeded with courage (without reference to state practice, *opinio juris*, other instances, or scholarly opinion) to conclude that this approach was

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[34] *Tecmed v. Mexico, supra* note. 33, at para. 154.

[35] Zachary Douglas, *Nothing if Not Critical for Investment Treaty Arbitration: Occidental, Eureko and Methanex*, 22 Arb. Intl. 27, 28 (2006).

[36] *Id.* at 28.

[37] Eureko B.V. v. Republic of Poland, Partial Award, 19 Aug. 2005, p. 235; Occidental Exploration & Production Co. v. Republic of Ecuador, LCIA Case UN 3467, Final Award, 1 Jul. 2004, p. 185; MTD Equity Sdn. Bhd. & MTD Chile S.A. v. Republic of Chile, ICSID Case ARB/01/7, Award, 25 May 2004, p. 114.

[38] Treaty between United States of America and The Argentine Republic concerning the reciprocal encouragement and protection of investment.

[39] CMS Gas Transmission Co. v. Argentine Republic, ICSID Case No. ARB/01/8, at 274 and 280.

[40] GUS VAN HARTEN, INVESTMENT TREATY ARBITRATION AND PUBLIC LAW 136 (Oxford U. Press 2007).

"not different from the international law minimum standard and its evolution under the customary international law."[41]

The tribunal in *Enron v. Argentina*, adopting a similar line of reasoning, also determined that the investment required a solid framework.[42] Both verdicts were reversed by ICSID Review Committees on different reasons, and the Committees recognized that the tribunals had not plainly exceeded their authority in interpreting FET.[43]

In *Occidental v. Ecuador*, the tribunal linked the FET criterion to a stable and predictable legal and business environment for investment with the international law criteria, holding that Ecuador's reforms to its tax system violated FET by altering the legal and economic foundation for the investment.[44] Further, the United Nations Conference on Trade and Development (UNCTAD) has stated that:

> *"In these cases, tribunals have gone so far as to suggest that any adverse change in the business or legal framework of the host country may give rise to a breach of the FET standard in that the investors' legitimate expectations of predictability and stability are thereby undermined. This approach is unjustified, as it would potentially prevent the host State from introducing any legitimate regulatory change, let alone from undertaking a regulatory reform that may be called for. It ignores the fact that investors should legitimately expect regulations to change over time as an aspect of the normal operation of legal and policy processes of the economy they operate in."*[45]

[41] *Id.* at p. 284.
[42] Enron v. Argentina, ICSID Case No. ARB/01/3, Award, 22 May 2007, p. 259–60.
[43] Enron v. Argentina, Decision on the Application for Annulment, 30 Jul. 2010, p. 298–316; CMS Gas Transmission Co. v. Argentine Republic, Annulment Proceeding, p. 85.
[44] Occidental Exploration & Production Co. v. Republic of Ecuador, *supra* note 37, at p. 190-196.
[45] U.N. Conf. Trade & Dev., *Fair and Equitable Treatment: UNCTAD Series on international investment agreements II* 67 (New York & Geneva 2012).

### *2. Finding the Limitations on the FET Standard*

In the wake of these rulings, several tribunals have articulated eligibility limitations or requirements, therefore slightly reducing the lofty standards of review articulated in the preceding judgements. It was long overdue for tribunals to emphasize that an investor's legitimate expectations must be "legitimate and reasonable" and grounded in the circumstances surrounding the investment, including not only the facts surrounding the investment, but also the political, socio-economic, cultural, and historical conditions of the host state. In addition, such expectations must be based on the terms that the state presented to the investor, and the investor must have relied on them when selecting to invest.[46]

#### *i. Representations*

Limitations on the theory include the necessity that the expectations be drawn from precise representations. This is not a difficult criterion to meet, and courts have concluded that valid expectations might be formed from non-investment-specific policies that attract foreign investment and on which the investor relied;[47] or specific obligations such as a stabilization provision.[48] Courts have concluded that a violation of contractual rights is insufficient to support a claim of FET violation.[49]

#### *ii. Knowledge of the Regulatory Environment*

Investors should be aware of and analyze the regulatory framework and degree of development of the state they have chosen to invest in. For instance, In *Genin v. Estonia*, the panel considered the claimant's decision to intentionally invest in:

> *"a renascent independent state, coming rapidly to grips with the reality of modern financial, commercial and banking practices and the emergence of state*

[46] Duke Energy v. Ecuador, ICSID Case No. ARB/04/19, Award, 18 Aug. 2008, p. 340.
[47] Methanex Corp. v. United States, UNCITRAL (NAFTA), Final Award, 3 Aug. 2005, p. 7.
[48] U.N. Conf. Trade & Dev., *Investor-State Arbitral Practice*, *supra* note 31 at 95.
[49] Parkerings-Compagniet AS v. Lithuania, ICSID Case No. ARB/05/8, Award, 11 Sep. 2007; Hamester v. Ghana, ICSID Case No. ARB/07/24, Award, 18 Jun. 2010.

*institutions responsible for overseeing and regulating areas of activity perhaps previously unknown."*[50]

*iii. Stabilizing the Expectations of Investors and Genuine Regulatory Action*

In *Saluka v. Czech Republic*, it was determined that in order to be protected, legitimate expectations:

> *"must rise to the level of legitimacy and reasonableness in light of the circumstances...No investor may reasonably expect that the circumstances prevailing at the time the investment is made remain totally unchanged. In order to determine whether frustration of the foreign investor's expectations was justified and reasonable, the host State's legitimate right subsequently to regulate domestic matters in the public interest must be taken into consideration as well...The determination of a breach of Article 3.1 by the Czech Republic therefore requires a weighing of the Claimant's legitimate and reasonable expectations on the one hand and the Respondent's legitimate regulatory interests on the other."*[51]

This paragraph recognizes that it is unreasonable for legitimate expectations to completely restrict a state's ability to regulate in the public good.

*3. Limitations on the Transparency and Protection of Legitimate Expectations Requirements: Are They Sufficient to Save the Requirement?*

Many, including states, will see the imposition of restrictions on the extent of the requirement as a necessary counterweight to the onerous *Tecmed* norm. In developing countries, where the regulatory framework may not be as evolved as in industrialized nations, the last two constraints described above are of particular significance.

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[50] Genin v. Estonia, *supra* note 18, at p. 348.

[51] Saluka v. Czech Republic, UNCITRAL Rules, Partial Award, 17 Mar. 2006, p. 304. For similar jurisprudence from other tribunals: Parkerings-Compagniet AS v. Lithuania, *supra* note 48; Continental Casualty v. Argentina, ICSID Case No. ARB/03/9, Award, 5 Sep. 2008; EDF v. Romania, ICSID Case No. ARB/05/13, Award, 8 Oct. 2009.

Nevertheless, these restrictions are often noted as limits of the *Tecmed* standard. This requirement is irrational, has no legal basis, and should be abandoned. This standard's subsequent limits offer a veneer of validity, but nothing more. While courts continue to believe that FET includes openness and preservation of reasonable expectations, reiterating this declaration will not make it real unless an acknowledged legal basis for this assumption is provided.

## LEGAL BASIS FOR PROTECTION OF LEGITIMATE EXPECTATIONS AND TRANSPARENCY

### *Identification of the FET Obligation*

While the phrase "fair and equitable treatment" appears in several treaties regulating foreign investment, it is not often expressed. This may be the first challenge in determining the precise meaning of FET. Four basic formulations of FET in investment treaty practice have been recognized by the UNCTAD. First, an absolute responsibility to provide FET. Second, the obligation to provide FET based on international law. Third, the FET responsibility tied to the minimal level of treatment of foreigners under international customary law. Finally, the FET requirement with added subject matter, such as denial of justice.[52]

The fact that the standard is expressed in several ways hinders the development of a clear and consistent set of standards. Various source treaties necessitate that FET tribunals adopt distinct criteria, since they locate the law in different source treaties. The contention that some parts constitute FET is thus immediately problematic, given that an unqualified FET requirement, as defined by arbitral tribunals, differs significantly from the international minimum standard.

### *Interpreting the FET within the International Minimum Standard*

Continually, there is disagreement on whether modern FET is reflected by the international minimum standard, is connected to the international minimum, or is fully independent of customary international law. This is significant because the test for a violation of the norm is

[52] U.N. Conf. Trade & Dev., *Fair and Equitable Treatment: UNCTAD Series on Issues in International Investment Agreements II, United Nations* xiiv–xiv (New York & Geneva 2012).

basically twofold: state activity will be evaluated first against the principles of good governance and then against the threshold of responsibility or the gravity of the state's wrongdoing.[53] Regarding the second, the origin of the FET duty is essential. If it is linked to the global minimum standard or according to customary international law, state action is not held to such a high level.

### *1. FET Connected to the International Minimum Standard*

The FET has its roots in the international minimum standard for the treatment of aliens, wherein historically developed nations held that governments were required to maintain this standard to safeguard foreign citizens regardless of how a state treated its own residents. This international minimum norm evolved over the nineteenth century[54] and is considered to have solidified with the *Neer v. Mexico* declaration that the treatment of a foreigner constitutes an international wrong:

> *"[S]hould amount to an outrage, to bad faith, to wilful neglect of duty, or do an insufficiency of governmental action so far short of international standards that every reasonable and impartial man would readily recognise its insufficiency."*[55]

It is accepted that the international minimum standard does not contain obligations for openness and protection of reasonable expectations. This does not imply that the minimal international standard is as low as it was in *Neer v. Mexico*. It is often claimed that it has undergone some evolution subsequently. In *Mondev*, the court summarized this approach effectively:

> *"To the modern eye, what is unfair or inequitable need not equate with the outrageous or the egregious. In particular, a State may treat foreign investment unfairly and inequitably without necessarily acting in bad faith."*[56]

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[53] W. Micheal Reisman, *Canute Confronts the Tide: States versus Tribunals and the Evolution of the Minimum Standard in Customary International Law*, 30 ICSID Rev. 616, 624 (2015).
[54] 8, MALCOLM SHAW, INTERNATIONAL LAW 823–827 (Cambridge U. Press 2008).
[55] L.F.H. Neer v. United Mexican States (1926) IV RIAA 60 at 65.
[56] Mondev Int'l Ltd. v. United States, ICSID Case No. ARB(AF) 99/2, Award, 11 Oct. 2002, p. 116.

It is believed that Judge Nikken's approach is the most thorough analysis of the link between FET and the international minimum standard:

> *"In my opinion, the most reasonable interpretation on the content of fair and equitable treatment should be to give it the same meaning as the current minimum standard at the time the pertinent BIT was entered into and not in 1926 (Neer). During the twentieth century there was increasingly less tolerance in the face of abuse of power, so that arbitrary treatment need not be hideous, egregious or outrageous to be considered unjust or inequitable...some arbitral tribunals, such as the Saluka Tribunal, have suggested that the theoretical discussion on the relationship between the two standards is, in practice, superfluous, and when applied to the specific facts of a case, may be more apparent than real."*[57]

*2. Unqualified FET Provision*

In a comprehensive examination of FET's historical antecedents, the OECD documents the origins of the standard in several sources of international law.[58] According to the United Nations Centre for Transnational Corporations[59] and a WTO publication for the Working Group on the Relationship of Trade and Investment,[60] the FET obligation is rooted in customary international law.

According to Montt, if the historical context is taken seriously, the FET standard could not have originally referred to anything greater than the international minimum standard of care.[61] Despite this, the UNCTAD concludes that 'many arbitral tribunals have decided otherwise and gave the FET standard a life and a source of its own.'[62] Haeri's documentation indicates:

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[57] Separate Opinion of Judge Nikken in AWG Group v. Argentina, UNCITRAL, Decision on Liability, 30 Jul. 2010, p. 18.
[58] Org. Econ. Co-operation & Dev., *Fair and Equitable Treatment Standard in International Investment Law*, *supra* note 5.
[59] U.N. Ctr. Transnatl. Corporations, *Bilateral Investment Treaties* 42 (1988).
[60] World Trade Org., Working Group on the Relationship between Trade and Investment, Non- Discrimination, Most- Favoured-Nation Treatment and National Treatment, Note by the Secretariat, WT/WGTI/W/118 (4 Jun. 2002).
[61] 1 SANTIAGO MONTT, STATE LIABILITY IN INVESTMENT TREATY ARBITRATION 69 (Hart Publg. Oxford 2009).
[62] U.N. Conf. Trade & Dev., *Series on Issues in International Investment Agreements II*, at 6.

> *"Investment treaty jurisprudence suggests that the fair and equitable treatment standard could be interpreted as an autonomous treaty standard that differs from the international minimum standard (despite the fair and equitable treatment standard's apparent origin in the international minimum standard), particularly where treaty language permits."*[63]

This comment from Haeri best exemplifies the current stance,[64] which is that arbitral jurisprudence describing FET as an unaffiliated independent international norm contradicts all other evidence of FET's origin. Consequently, when a tribunal is tasked with interpreting and applying a FET provision, failing to provide any international law sources to support their interpretation, or failing to cite any authority to justify their deviation from international law standards, as in *Tecmed*, is a significant omission. Such decisions are a cause for worry.

*3. Nexus with International Law*

Clauses tying FET to international law seem to necessitate referencing FET as it appears in international law. However, various interpretations have been presented by certain courts, who find no purpose to resort to international law.[65] Tribunals have argued that in such provisions the reference is merely to the principles of international law and not to "the minimum standard under customary international law"; and secondly, that the formulation "minimum international standard" is so well-established in international law that it is reasonable to assume that states parties would have used this formulation specifically if they had intended to apply it.[66]

The second point is immediately contradicted by the experience under NAFTA (Article 1105: 'each Party shall accord to investments of investors of another Party treatment in accordance

[63] Hussein Haeri, *A Tale of Two Standards: 'Fair and Equitable Treatment' and the Minimum Standard in International Law*, 27 Arb. Intl. 27, 45 (2011).
[64] Haeri, *supra* note 62; Montt, *supra* note 60; Stephen Vasciannie, *The Fair and Equitable Treatment Standard in International Investment Lawand Practice*, 70 Brit. Y.B. Intl. L. 99, 99–164 (1999); JC. Thomas, *Reflection on Article 1105 of NAFTA: History, State Practice and the Influence of Commentators,* 17 ICSID Rev.– For. Inv. L.J. 21, 21–101 (2002).
[65] Tecmed v. Mexico, *supra* note 31.
[66] Christopher Schreuer, *Fair and Equitable Treatment in Arbitral Practice*, 6 J. World Inv. & Trade 357, 360 (2005).

with international law'), where the states explicitly stated that this meant the customary international law standard.

In his fiercely stated separate opinion in the case of *AWG v. Argentina*, Judge Nikken argued further:

> *"This has led to the interpretation somewhat a contrario, applied by the Tribunal to this case, according to which that omission would prove that both standards are different, since the concept of minimum standard is well known and well established in international law, so that if the parties had intended to refer to it, it would have been explicitly mentioned...[but] [t]he question of why there is no mention in the BITs of the international minimum standard cannot be answered properly if the historical controversy on the concept of minimum standard is completely ignored as done in this decision."*[67]

Further elaborating on the historical hostility of economically weaker nations to the minimum standard, Nikken casts serious doubt on the legitimacy of the minimum standard as customary international law.[68] He concludes, then, that it cannot be said with such assurance that "the concept of international minimum standard was a well-established concept."[69]

The reasoning behind Judge Nikken's conclusion that the reference to "international law" in these types of FET provisions relates to the customary international law norm is unquestionably superior to those of his tribunal colleagues who disagree. In addition, it is reinforced by governmental expressions of *opinio juris* on the subject, which gives it considerable weight.

*Significance of the Object and Purpose of the Treaty*

Some courts have claimed to give effect to treaty provisions in light of the goal and purpose of the relevant treaty in accordance with Article 31 of the Vienna Convention on the Law of Treaties, with the object and purpose being the maintenance of a stable legal and commercial

[67] Separate Opinion of Judge Nikken in AWG Group v. Argentina, Supra Note 56, at p. 11–12.
[68] *Id.* p. 12. Also see Stephen Vasciannie, *supra* note 63, at 105; Andrew Newcombe & Lluís Paradell, *Lawand Practice of Investment Treaties: Standards of Treatment*, Kluwer L. Intl. 1, 269 (2009).
[69] Separate Opinion of Judge Nikken in AWG Group v. Argentina, *supra* note 57, at p. 14.

framework. Awards have relied on this strategy to support investor-friendly interpretations, such as the establishment of legitimacy criteria and the preservation of genuine expectations.[70] In *MTD v. Chile*, the court determined that FET required:

> *"treatment in an even-handed and just manner conducive to fostering the promotion of foreign investment. Its terms are framed as a pro-active statement 'to promote', 'to create', 'to stimulate' rather than prescriptions for a passive behavior of the State or avoidance of prejudicial conduct to the investors."*[71]

However, a biased view will result from a singular emphasis on investment security. The fundamental objective of IIAs is to foster growth by establishing appropriate conditions for foreign investments (as opposed to investors). This was acknowledged in *Joseph C. Lemire v. Ukraine*:

> *"the object and purpose of the Treaty [Ukraine-United States BIT] is not to protect foreign investments per se, but as an aid to the development of the domestic economy. And local development requires that the preferential treatment of foreigners be balanced against the legitimate right of Ukraine to pass legislation and adopt measures for the protection of what as a sovereign it perceives to be its public interest."*[72]

In any case, the goal and purpose of a treaty cannot introduce a demand that is lacking from the treaty according to its usual meaning. To safeguard an investor, the goal and purpose of a treaty cannot permit the introduction of additional conditions.

### *Analysing State Practise*

While it would be improper to regard a state's assertions supporting a claim as authoritative, outside the framework of tribunal proceedings, states' perspectives on the criteria they meant

[70] Occidental Exploration & Production Co. v. Ecuador, *supra* note 36, at p. 183; Enron v. Argentina, *supra* note 41, at p. 260; Bayindir v. Pakistan, ICSID Case No. ARB/03/29, Decision on Jurisdiction.
[71] MTD v. Chile, Case No. ARB/01/7, 25 May 2004, p. 113.
[72] Joseph C. Lemire v. Ukraine, ICSID Case No. ARB/06/18, Decision on Jurisdiction and Liability, 21 Jan. 2010.

to be governed by, particularly joint declarations, should be given significant weight. It is improbable that nations would seek to be bound by a higher norm than "goof governance." The explanation made by the NAFTA Commission has been mentioned before. Other states have issued explanations of a similar kind.[73] Judge Nikken noted:

> *"[N]o other State has made any statement to the effect of giving fair and equitable treatment a meaning different from the international minimum standard (let alone linking it to the 'legitimate expectations' of investors and the stability of the legal environment for investment)."*[74]

Relevant state practise and *opinio juris* is almost unanimously of the conclusion that FET refers to the international customary law norm.

*Using Arbitral Practise as Precedent*

There is no precedent system in either international law or arbitration practice.[75] Despite this, arbitral tribunals have been increasingly inclined to cite the authority of previous tribunal rulings. However, it is evident that arbitral tribunal rulings neither establish international law nor bind later tribunals.[76] The importance of jurisprudence in arbitration was underlined by Judge Nikken:

> *"I agree, however, with the notion that like cases should be resolved in the same manner or, as stated by a distinguished scholar and member of this Tribunal, although there is no legal obligation to follow decided cases there is indeed a moral obligation to follow decided cases in order to promote a predictable legal environment. However, great caution is needed when identifying cases as alike, especially when dealing with factual issues like*

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[73] Matthew Pountney, *States weigh-in on DRCAFTA claim*, Global Arb. Rev. (23 Feb. 2012), https://globalarbitrationreview.com/article/states-weigh-in-dr-cafta-claim.

[74] Separate Opinion of Judge Nikken in AWG Group v. Argentina, *supra* note 56, at p. 7.

[75] Shaw, *supra* note 53, at 109–112; Zachary Douglas, *Can a Doctrine of Precedent be Justified in Investment Arbitration?* 25 ICSID Rev.– For. Inv. L.J. 104, 104–110 (2010); Gabrielle Kaufmann-Kohler, *Arbitral Precedent: Dream, Necessity or Excuse?* 23 Arb. Intl. 200 (2010); Porterfield, *supra* note 3, at 79; Mark C. Weidemaier, 51, *Toward a theory of precedent in arbitration*, William & Mary L. Rev. 1895, 1895 (2010).

[76] Jeffery P. Commission, *Precedent in Investment Treaty Arbitration: A Citation Analysis of a Developing Jurisprudence*, 24 J. Intl. Arb. 129, 130 (2007).

*fair and equitable treatment and when, moreover, the BITs often contain significant differences despite their similarity. Furthermore, I understand that moral obligation includes looking critically at decided cases, precisely because they are not binding."*[77]

## CONCLUSION

In conclusion, the openness and preservation of reasonable expectations provisions that have made their way into FET in investment treaties should be disavowed. They demand an excessively high standard of governmental behaviour. It is improbable that nations throughout the globe would have voluntarily agreed to the spread of IIAs demanding FET and deliberately committed themselves to a norm so far beyond what good governance would need. In addition, the expectations of foreign investors are an entirely unsuitable criterion for determining whether state action has been fair and equitable. In any case, the ban on evident arbitrariness in FET is adequate without the addition of a brand-new concept.

Not only is the openness and preservation of legitimate expectations requirement inappropriate on this basis, but neither treaty provisions nor international law provide any justifiable ground for it. It's an innovation. Perhaps the corpus of arbitral jurisprudence can provide creative reasoning assistance, but it cannot establish law. The growth of this line of reasoning by arbitral courts is like to constructing a house of cards on an unstable table - it is weakened by the lack of a strong base, a legal foundation; adding more levels will not make the structure secure.

[77] Separate Opinion of Judge Nikken in AWG Group v. Argentina, *supra* note 57, at p. 24.