The Investment Treaty Arbitration Review

Third Edition

Editor
Barton Legum

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THE INVESTMENT TREATY ARBITRATION REVIEW

THIRD EDITION

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PREFACE

The past year has confirmed the usefulness of *The Investment Treaty Arbitration Review*'s contribution to its field. The biggest challenge for practitioners and clients over the past year has been to keep up with the flow of new developments and jurisprudence in the field. There was a significant increase in the number of investment treaty arbitrations registered in the first years of this decade. These cases have come or are now coming to their conclusions. The result today is more and more awards and decisions being published, making it hard for practitioners to keep up.

Many useful treatises on investment treaty arbitration have been written. The relentless rate of change in the field rapidly leaves them out of date.

In this environment, therefore, *The Investment Treaty Arbitration Review* fulfils an essential function. Updated every year, it provides a current perspective on a quickly evolving topic. Organised by topic rather than by jurisdiction, it allows readers to access rapidly not only the most recent developments on a given subject, but also the debate that led to and the context behind those developments.

This third edition adds new topics to the *Review*, increasing its scope and utility to practitioners. It represents an important achievement in the field of investment treaty arbitration. I thank the contributors for their fine work in developing the content for this volume.

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Part VII

Multilateral Treaties

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Chapter 30

THE TRANS-PACIFIC PARTNERSHIP

Andrew Stephenson and Lee Carroll[1]

I 2018 UPDATE – ISDS UNDER THE PROPOSED CPTPP

Following the United States' presidential election in November 2016 and President-elect Donald Trump's decision not to participate in the Trans-Pacific Partnership, representatives of the remaining 11 states (Australia, Brunei, Canada, Chile, Japan, Malaysia, Mexico, New Zealand, Peru, Singapore and Vietnam) convened with the intention of bringing the TPP into force, albeit in an amended form. Those 11 states, reportedly led by Japan, Australia and New Zealand, sought publicly to reaffirm the strategic and economic significance of the TPP.

In November 2017, ministers of the 11 states announced that their efforts had culminated in an agreement on the core elements of a re-named Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP). The parties reportedly concluded negotiations in Tokyo in early 2018. The text of the CPTPP has not yet been released, but it is understood that the states have agreed to incorporate the provisions of the TPP with the exception of a limited set of provisions (numbering 22) that are to be suspended.

As regards the TPP's Investment Chapter (Chapter 9), the CPTPP will suspend application of the investor–state dispute settlement (ISDS) arbitration mechanism to claims for a breach of an investment agreement or investment authorisation (i.e., where an investor has a specific contract or authorisation with the government).[2] This means that under the CPTPP, only claims that relate to a breach of the substantive obligations contained in Section A of the Investment Chapter can be submitted to ISDS. Claims cannot be sought

1 Andrew Stephenson is a partner and Lee Carroll is a special counsel at Corrs Chambers Westgarth.

2 It does this by suspending:
(i) the definitions of "investment agreement" and "investment authorisation";
(ii) the application of Article 9.19, which provides for the submission of claims to arbitration, as it applies to investment agreements and investment authorisations;
(iii) Article 9.22.5 which provides for the appointment of arbitrators for claims submitted in respect of investment agreements and investment authorisations;
(iv) Article 9.25.2 which provides for the applicable law as it applies to claims submitted in respect of investment agreements and investment authorisations; and
(v) Annex 9-L which provides for Investment Agreements.

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for breaches of investment agreements[3] or investment authorisations.[4] By 'suspension', it is understood that the provisions are merely dormant, ready for re-inclusion if and when a new post-Trump administration decides to participate (and the 11 remaining states agree). However, the suspension, while it lasts, will limit the scope of the investment provisions that a claim may relate to.

The extent to which ISDS will be impacted (reducing the risk of claims against states) may depend, in part, on each state's domestic laws as to the circumstances in which a foreign investor can invest in the state without governmental approval (and therefore, without an 'investment authorisation').

Australia, for example, has a foreign investment approval regime that regulates certain types of acquisitions by 'foreign persons' of equity securities in Australian companies and trusts, and of Australian businesses and Australian real property assets.[5] Under that regime, an entity is a 'foreign person' if a foreign holder (which may be an individual who is not ordinarily resident in Australia, a foreign government or a foreign corporation) holds a substantial interest in the entity of at least 20 per cent. In the case of two or more unrelated holders, they must hold an aggregate substantial interest of at least 40 per cent. Generally speaking, foreign investment approval is required where a foreign person acquires a 10 per cent interest in an agribusiness, a 20 per cent interest in an Australian entity or any interest in land. The application of monetary threshold requirements varies depending on whether the acquisition is of a land or non-land interest, and the type of entity obtaining the interest.

Where approval under the Australian foreign investment approval regime is required and given, we would suggest that such approval would meet the definition of 'investment authorisation' under the CPTPP. That approval is, in effect, the issue of a 'no objection notification', which is a permission to proceed with the proposed action (or investment). However, it is difficult to see how the Australian government could breach such an approval (unless perhaps it retracts its permission to proceed), which means the suspension of ISDS as it

3 'Investment agreement' is defined to mean:

'a written agreement that is concluded and takes effect after the date of entry into force of this Agreement between an authority at the central level of government of a Party and a covered investment or an investor of another Party that creates an exchange of rights and obligations, binding on both parties under the law applicable under Article 9.25.2, on which the covered investment or the investor relies in establishing or acquiring a covered investment other than the written agreement itself, and that grants rights to the covered investment or investor:

a with respect to natural resources that a national authority controls, such as oil, natural gas, rare earth minerals, timber, gold, iron ore and other similar resources, including for their exploration, extraction, refining, transportation, distribution or sale;

b to supply services on behalf of the Party for consumption by the general public for: power generation or distribution, water treatment or distribution, telecommunications, or other similar services supplied on behalf of the Party for consumption by the general public; or

c to undertake infrastructure projects, such as the construction of roads, bridges, canals, dams or pipelines or other similar projects; provided, however, that the infrastructure is not for the exclusive or predominant use and benefit of the government.' [Footnotes omitted.]

4 'Investment authorisation' is defined as 'an authorisation that the foreign investment authority of a Party grants to a covered investment or an investor of another Party '. [Footnotes omitted.]

5 The regime is set out in the following legislation: Foreign Acquisitions and Takeovers Act 1975 (Cth); Foreign Acquisitions and Takeovers Regulation 2015 (Cth); Register of Foreign Ownership of Water or Agricultural Land Act 2015 (Cth) and its accompanying regulations; and Foreign Acquisitions and Takeovers Fees Imposition Act 2015 (Cth) and its accompanying regulations.

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applies to investment authorisations may have limited impact in Australia. Notwithstanding, it remains to be said that the suspension of ISDS to claims for a breach of an investment authorisation does not preclude companies that wish to avail themselves of ISDS from considering corporate structuring with a view to obtaining this protection. For example, a company may consider a restructure that would bring it outside the definition of 'foreign investor'.

As at the time of writing, the CPTPP is forecast to be signed in Chile on 8 March 2018. Thereafter, each member country will need the approval of its own legislative body to bring the treaty into force domestically.

Notwithstanding the partial suspension of the ISDS mechanism, the TPP, in its current CPTPP form, remains a recent consensus[6] in respect of the rights that states are prepared to afford foreign investors and the extent to which those rights can be enforced through ISDS. It is, therefore, a reference for the latest thinking on ISDS. In this context, the analysis of the ISDS chapter in the TPP that was published in the previous edition of this publication remains important reading. The full text of the original chapter is reproduced below.

II THE TRANS-PACIFIC PARTNERSHIP: DOES IT ACHIEVE THE NECESSARY BALANCE BETWEEN INVESTMENT PROTECTION AND REGULATORY DISCRETION?

i Introduction

The inclusion of investor–state dispute settlement provisions in international investment agreements, including the recently disclosed Trans-Pacific Partnership, has become contentious around the world. In Australia, at least, the concern intensified after Philip Morris Asia sued the Australian government in 2011 under the Hong Kong–Australia BIT challenging Australia's tobacco plain-packaging legislation. Critics believe the inclusion of ISDS in international investment agreements compromises a government's sovereignty by enabling foreign corporations to sue a government for passing new laws or implementing new policies – effectively, domestic regulation in the public interest.

The authors consider that there is a real issue to be addressed, but, properly understood, it is not ISDS clauses that give rise to this issue, but rather the vague nature of the substantive rights created by treaties that contain ISDS clauses. Those rights are intended to promote investment and, therefore, growth for the states entering into the treaties. If the advantage of growth through investment is real and the price of that investment is the creation of substantive rights stipulated in the treaties, then there must be a way for an investor to enforce those rights. In the absence of a proper mechanism for enforcement, the rights granted are hollow and will be unlikely to promote the investment sought.

The vague nature of the rights created by old treaties has been directly considered in the TPP. The TPP is part of a new generation of international investment agreements that, by its terms, better achieves the balance between investment protection and regulatory discretion. In our view, the TPP is unlikely to restrict a government of a member state from legitimately regulating in the public interest. We discuss below the key provisions of the TPP's 'Investment Chapter' (Chapter 9), which, we say, supports our argument. We concentrate

6 Note also that the Peru-Australia FTA concluded 10 November 2017 contains an ISDS arbitration mechanism and an ISDS arbitration mechanism is being negotiated in the Regional Comprehensive Economic Partnership (between Australia, China, India, Japan, Korea and New Zealand).

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on the expropriation protection in Article 9.8 primarily because it is this standard that has engendered particular concern about the potential to limit a state's right to regulate in pursuit of non-investment policy objectives.

The protections afforded to investors in the Investment Chapter are typical protections (such as fair and equitable treatment), which, as drafted, appear to be derived from US investment treaty practice, and can be found in similar terms in many of Australia's modern free trade agreements. However, the TPP incorporates language that clarifies the protections, particularly the protection against expropriation. It thereby instructs the arbitrators to conduct a balancing exercise between investment protection and regulatory discretion, rather than leaving the protections open to different interpretations by different arbitrators. The TPP also enlarges the ambit of the exceptions to the protections. That is, it allows a state to be exempt from the obligations of the treaty in certain listed situations in which compliance would be incompatible with key policy objectives.

With one exception, the investment protections can be enforced directly by TPP investors through ISDS. The one exception is that ISDS will not apply between Australia and New Zealand (by side letter). This is not a new scenario.[7] There was a similar bilateral carveout under the ASEAN-Australia-New Zealand Free Trade Agreement; a recognition that each country has strong mutual trust and understanding of each other's court system, demonstrated also by the trans-Tasman treaty on enforcing court judgments.[8]

The ISDS mechanism in the TPP is also fairly typical of modern international investment agreements, but it includes additional procedural safeguards that protect governments from unmeritorious claims, ensure transparency and allow TPP member states (rather than the arbitral tribunal) to maintain control over the TPP's interpretation.

Critics who argue that there should be no ISDS at all in the TPP and other international investment agreements risk rendering investment protections virtually unenforceable. By relying solely on interstate dispute resolution measures, the affected investor must persuade its state to pursue a claim. It is also important to remember the historical justification for ISDS, which was to protect businesses that invested in foreign jurisdictions where there may not have been robust democracies, rule of law or effective enforcement systems. Although most of the TPP member countries are developed nations, concerns continue, because even in developed countries, states can, consistent with their own laws, breach the acceptable standards enshrined in treaties. Given that the treaties are designed to promote investment by providing clear statements of principle, it is appropriate that the final determination of whether that principle has been violated should be truly independent of the state that is the defendant. It would also be unsaleable for a treaty to stipulate that an investor from a developing country can only have recourse to the host state's courts, while an investor from a developed country can prosecute its claim by independent arbitration. The agreement evidenced by the TPP is most unlikely, unless it is enforceable by investors from all countries in the same manner. That is, there must be reciprocity.

7 In fact, it is interesting that there were not more exclusions of ISDS by side letter particularly as between the United States and Australia, who excluded ISDS from the Australia–US FTA (2005) reportedly on the basis that the countries had strong trust in each other's legal systems.

8 Australia and New Zealand have agreed to recognise and enforce judgments of the other's courts in its territory pursuant to the Agreement between the Government of Australia and the Government of New Zealand on Trans-Tasman Court Proceedings and Regulatory Enforcement (2008).

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A blanket exclusion of ISDS in all international investment agreements is not the answer to concerns about a government's right to regulate in the public interest. The answer lies in the drafting of the investment protections themselves and, we submit, the text of the TPP goes some way to achieving the necessary balance between investment protection and regulatory discretion.

III THE TRANS-PACIFIC PARTNERSHIP

i Introduction

The TPP is the world's largest regional free trade agreement, between 12 countries who represent approximately 40 per cent of the global economy – Australia, Brunei, Canada, Chile, Japan, Malaysia, Mexico, New Zealand, Peru, Singapore, the United States and Vietnam.[9] The text of the TPP, negotiated for about seven years, was agreed on 5 October 2015.

It is not known how soon it will enter into force (or if at all, being at the whim of each country's domestic politics).[10] It will enter into force when (or if) at least six of the original signatories, who must account for at least 85 per cent of the combined GDP of the original signatories in 2013, have ratified the agreement.[11] This means that the TPP cannot enter into force unless both Japan and the United States ratify it.

There are many extant agreements between TPP member countries. Australia, for example, already has an investment agreement with every TPP member country except Canada.[12] Although Australia's existing agreements with Mexico, Peru and Vietnam will terminate on entry into force of the TPP, by side letter, the remainder of Australia's investment agreements (and indeed, it seems all of the extant agreements between other TPP member countries) will remain in effect. This may mean that a foreign investor has a choice between suing under an existing investment agreement and suing under the TPP and, if it has that choice, will no doubt choose the agreement that provides to it the best protection. However, as discussed below, the curtailed scope of the application of the most favoured nation (MFN) clause in the TPP means that an investor is unlikely to be able to sue under the TPP and rely on better terms in an existing agreement (or the absence of carveouts from investment protection in that existing agreement as found in the TPP). This is because the MFN clause in the TPP is limited in its application to future international investment agreements only.

9 The TPP is open to accession by other countries: Article 30.4 of the TPP. Indonesia's president, for example, has declared that Indonesia intends to join the TPP.

10 Australia formally signed the TPP in New Zealand on 4 February 2016.

11 TPP, Article 30.5.

12 See: the ASEAN-Australia-New Zealand Free Trade Agreement (2009) (the ASEAN countries are Brunei, Myanmar, Cambodia, Indonesia, Laos, Malaysia, the Philippines, Singapore, Thailand and Vietnam); the Australia-Chile Free Trade Agreement (2009); the Agreement between Australia and Japan for an Economic Partnership (2014); the Malaysia-Australia Free Trade Agreement (2012); the Agreement between the Government of Australia and the Government of the United Mexican States on the Promotion and Reciprocal Protection of Investments (2007); the Agreement between Australia and the Government of the Republic of Peru on the Promotion and Protection of Investments (1997); the Singapore-Australia Free Trade Agreement (2003); the Australia-United States Free Trade Agreement (2005).

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ii The TPP – its terms

Preamble

Non-investment policy objectives rarely appear in the preamble of older international investment agreements (such as the Hong Kong–Australia BIT). As a result, tribunals resolving disputes under those agreements have interpreted the standards therein (and any exceptions) in light of the narrow stated object and purpose of the treaty (i.e., investment protection and promotion). The preamble is an aid to the interpretation of a treaty[13] and is commonly used by arbitral tribunals to identify the treaty's object and purpose and to construe its terms.[14]

By contrast, some modern agreements contain language in the preamble that lists other non-investment policy objectives (such as the promotion of sustainable development). The preamble to the TPP does this; it expressly recognises a state's 'inherent right to regulate'. It also states that the TPP member countries resolve to:

> *preserve the flexibility of the Parties to set legislative and regulatory priorities, safeguard public welfare, and protect legitimate public welfare objectives, such as public health, safety, the environment, the conservation of living or non-living exhaustible natural resources, the integrity and stability of the financial system and public morals.*

This preamble should go some way to identifying areas that will be legitimate areas of regulation, even if that regulation adversely affects an investment of an entity from another TPP member state. However, it is unlikely that the preamble amounts to carte blanche for regulation in the specified areas. Presumably regulation must otherwise be consistent with the terms of the TPP; for example, it must not be discriminatory (i.e., discriminate in favour of domestic investments) and it must be reasonable (interpreted widely) to meet a legitimate policy.

Investor and investment

The definitions of 'investor' and 'investment' are important to the scope of application of the rights and obligations of an international investment agreement. This is subject to the terms of the 'denial of benefits' clause, which permits the exclusion of certain investors from protection.

Other than a state party, there are two types of investors under the TPP: a national or an enterprise of a party.[15]

A national is a natural person who has the nationality of a party according to Annex 1-A or a permanent resident of a party.[16] Annex 1-A provides for party-specific definitions of nationality. As with most investment treaties, the TPP bases nationality exclusively on the laws of the state of the claimed national. In Australia, a natural person who is an Australian citizen, as defined in the Australian Citizenship Act 2007, has Australian nationality.

13 Vienna Convention on the Law of Treaties (1969), Article 31.

14 See, e.g., *Siemens AG v. The Argentine Republic*, ICSID Case No. ARB/02/8, Decision on Jurisdiction, [81].

15 TPP, Article 9.1.

16 TPP, Article 1.3.

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An enterprise of a party is an enterprise constituted or organised under the law of a party or a branch located in the territory of a party that also carries out business activities there.[17] In respect of the inclusion of a branch, an enterprise of a party need not be an enterprise constituted or organised under the law of a party. It may be constituted and organised under the law of any state (including a non-state party). However, in that case what is critical is that the entity carries out 'business activities' in a state that is a party to the TPP.

However, this definition needs to be read with Article 9.14, a denial of benefits clause, which permits the exclusion of certain investors. Such a clause is not uncommon in modern treaties. It enables a TPP member country to deny the protections in the Investment Chapter to:

a an investor, who is owned or controlled[18] by a (natural or legal) person of a non-state party or the denying state party, who has no substantial business activities in the territory of any state party other than the denying state party;

b an investor, who is owned or controlled by a (natural or legal) person of a non-party and the denying state party has in place measures with respect to that non-party (or a person of the non-party) that prohibits transactions with the investor or that would be breached if the benefits of the Investment Chapter were accorded to the investor.

The first carveout gives TPP member countries the authority to carve out from the definition of 'investor' shell companies owned by persons of a third country that do not have substantial business activities in the territory of a state party. Its purpose is to stop treaty shopping. Unlike earlier treaties, it will not be possible for investors from non-party states to structure their investment to take advantage of the treaty. While the principle of 'abuse of right' prevented the late adoption of a nationality for the purpose of a treaty, that general principle of international law is much narrower than the denial of benefits clause in the TPP.

The second carveout relates to an entity that has a substantial business in a TPP member state but the state, which might otherwise have been the subject of a claim, has regulations in place that prohibit transactions with the investor. An example of such a regulation is the long-standing US embargo[19] on almost all trade and investment involving Iran, prohibiting US persons[20] from engaging in transactions or dealings with Iran. On 16 January 2016, the United States lifted the nuclear-related 'secondary sanctions' (directed towards non-US persons for conduct involving Iran that occurs outside the United States) but the domestic trade embargo remains in place.

Article 9.14 will not operate automatically. The right to deny will need to be exercised through positive action by the TPP member country in question (such as an exchange of letters with the relevant investor).[21]

'Investment' is defined widely and is again based on US investment treaties (including the Australia–US FTA).[22] The definition sets out numerous specific (but non-exhaustive)

17 TPP, Article 9.1.

18 Some agreements, such as the Agreement between Australia and Japan for an Economic Partnership (2014), give definition to 'owned' and 'controlled'. The TPP does not do so expressly.

19 Governed by the US Treasury Department's Iranian Transactions and Sanctions Regulations.

20 Defined broadly to include citizens, permanent residents, US entities and their foreign branches, and foreign persons while in the United States.

21 *Plama Consortium Limited v. Republic of Bulgaria*, ICSID Case No. ARB/03/24, Decision on Jurisdiction, 8 February 2005.

22 TPP, Article 9.1.

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examples of an investment including intellectual property rights, equity participation in an enterprise and construction contracts and other similar contracts. The definition of 'investment' expressly excludes 'an order or judgment in a judicial or administrative action'. In addition, the TPP also requires that the asset has the 'characteristics of an investment' such as the commitment of capital, the expectation of gain or profit, or the assumption of risk. This is not a new test.[23] It is, however, an additional hurdle for an investor to meet when bringing a claim.

Article 9.8: expropriation and compensation

The obligation on TPP member countries not to expropriate is described in terms with which we are already familiar. The language used is almost identical to that used in each of the existing investment treaties Australia has with TPP member countries.

Under Article 9.8, a party must not expropriate or nationalise a covered investment, directly or indirectly though measures equivalent to expropriation or nationalisation, except:

a for a public purpose – which is said to be a reference to a concept in customary international law;[24]
b in a non-discriminatory manner;
c on payment of prompt, adequate and effective compensation; and
d in accordance with due process of law.

As discussed below, Article 9.8 is to be interpreted in accordance with Annex 9-B.

By Article 9.8(6), the concept of 'expropriation' is clarified and narrowed. A state's decision not to issue, renew or maintain a subsidy or grant, or to modify a subsidy or grant, in the absence of a legal or contractual commitment to do so, or in accordance with the terms of the subsidy or grant, does not of itself constitute expropriation.

It is worth mentioning that the Hong Kong–Australia BIT, on which Philip Morris Asia relied, uses 'deprivation' language only in its expropriation clause, which is atypical of investment agreements.[25] Article 6(1) of that treaty requires that investors 'shall not be deprived of their investments nor subjected to measures having effect equivalent to such deprivation'. This language, which prohibits the 'deprivation' of an investment, is significantly wider than the language in the TPP, which prohibits expropriation. The term 'expropriation' carries with it the connotation of a 'taking' of a person's property with a view to transferring ownership of that property to another person (such as the state).[26] By contrast, a 'deprivation' can occur without a 'taking'.[27]

23 It appears, for example, in the Australia–US FTA, the Australia–Chile FTA and the Agreement between Australia and Japan.

24 Footnote 17.

25 Although see also Article 5 of the Netherlands–Czech Republic BIT; Article 4 of the Czech and Slovak Federal Republic–Sweden BIT; Article 4 of the Sweden–Republic of South Africa BIT.

26 See, e.g., *S D Myers v. Canada*, Partial Award, 13 November 2000. Andrew Newcombe contends that a state act that does not involve an acquisition should not be regarded as an expropriation: 'The Boundaries of Regulatory Expropriation in International Law', ICSID Review – *Foreign Investment Law Journal* 1.

27 The tribunal in *CME (Netherlands) v. Czech Republic* (Partial Award, 13 September 2001) considered the meaning of 'deprivation' in Article 5 of the Netherlands–Czech Republic BIT and said (at [150] and [151]):
The Treaty's provision regarding 'deprivation' tracks the broadest expropriation provisions in bilateral investment treaties . . . A 'deprivation' . . . occurs . . . whenever a State takes steps 'that effectively neutralize the benefit of

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The meaning and scope of 'public purpose' under customary international law is obviously important. The tribunal in *ADC Affiliate Ltd v. The Republic of Hungary*[28] stated that the treaty requirement of 'public interest'[29] requires some 'genuine interest of the public'. Andrew Newcombe and Lluis Paradell state that, at the very least, there must be some demonstrable public interest or genuine public need and the expropriation must be made in 'good faith'.[30]

It seems clear that the public purpose requirement would be breached if property were seized for the personal use of a dictator or third party, or as a reprisal for another state's conduct.[31] It is theoretically possible that the termination of a contract by a state because of a financial crisis may be a termination for a public purpose (although this has not been established on the facts in cases to date).[32]

Two cases in which the state taking was said not to be in the public interest are *ADC Affiliate Ltd v. The Republic of Hungary*[33] and *Siemens AG v. The Argentine Republic*.[34]

In the former, a 2001 Hungarian decree voided investors' contracts for the operation and management of the Budapest airport. The airport was subsequently taken over by the state in 2002 but then privatised in 2005. The Hungarian government argued its measures were part of the process for Hungary's access to the EU and served the strategic interests of the state. However, the tribunal concluded that the taking was not in the public interest. It said the subsequent privatisation of the airport, which earned Hungary US$2.26 billion, rendered any public interest argument unsustainable.

In the latter case, the tribunal found there was no evidence of a public purpose because the measures in question, which had the effect of terminating a contract for the provision of national identity cards, were taken to reduce the costs to Argentina of the contract, which had been awarded through public competitive bidding, as part of a change of policy by a new government.

Neither decision should fuel a concern that a state's right to regulate for a public purpose is being curtailed.

Indeed, according to Newcombe and Paradell, the jurisprudence suggests that states are afforded a wide margin of appreciation in determining whether an expropriation serves a public purpose. To this extent, the concern that the obligation not to expropriate may curtail a state's right to regulate in the public interest is overstated. However, provided that the relevant state action falls within the more constrained definition of 'expropriation' in

the property for the foreign owner'. Such expropriations may be deemed to have occurred regardless of whether the state 'takes' or transfers legal title to the investment . . . The Treaty avoids any narrow definition of expropriation in part by avoiding the use of that word altogether. The Treaty focuses on the interference in the investor's ownership, rather than any transfer of the investment to the State, by prohibiting 'deprivations' rather than 'takings'.

28 ICSID Case No. ARB/03/16.

29 The claim was brought under the Cyprus–Hungary BIT.

30 Andrew Newcombe and Lluis Paradell, Law and Practice of Investment Treaties: Standards of Treatment (Kluwer Law International, 2009) at [7.32].

31 Ibid.

32 *Siemens AG v. The Argentine Republic*, ICSID Case No. ARB/02/8 at [273] (the context being Argentina's fiscal crisis).

33 ICSID Case No. ARB/03/16.

34 ICSID Case No. ARB/02/8.

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the TPP (as a consequence of Annex 9-B – discussed below), an expropriation that is legal, for a public purpose, and non-discriminatory must still be subject to prompt, adequate and effective compensation.

Annex 9-B

Annex 9-B circumscribes the meaning of 'expropriation'.[35] The form of this Annex originates from the US and Canadian Model BITs, which were revised in 2004.[36]

Annex 9-B expressly provides that whether an action by a party constitutes indirect expropriation requires a case-by-case, fact-based inquiry that includes consideration of the following factors:

a the economic impact of the government action (although an adverse effect on the economic value of an investment is not sufficient of itself – a clear move away from the oft-criticised 'sole effects' doctrine);[37]

b the extent to which the government action interferes with distinct, reasonable investment-backed expectations; and

c the character of the government action.

In respect of the second factor, the TPP expressly clarifies, by footnote,[38] that whether an investor's investment-backed expectations are reasonable depends on factors such as whether the government provided the investor with binding written assurances and the nature and extent of governmental regulation or potential regulation in the relevant sector. We have suggested previously[39] that rights inherent in an investment should be construed to be flexible rights having regard to the natural evolution of the legal framework that existed at the time of the investment. The nature and course of that evolution will obviously differ between countries for cultural reasons. Accordingly, the concept of expropriation should only arise where the change in regulation falls outside the evolution of the law that could reasonably have been contemplated at the time of the investment.

The third factor above – the 'character' of the government action – is not further explained in the TPP. The ASEAN–Australia–New Zealand FTA and the Malaysia–Australia FTA state that the character of government action includes its objective and whether the action is disproportionate to the public purpose. A test of 'proportionality' was endorsed by

35 The Annex is said to constitute 'an integral part' of the TPP: Article 30.1.

36 See Treaty between the Government of the United States of America and the Government of [Country] Concerning the Reciprocal Protection of Investment (US Model BIT), Art 6(1) and Annex B(4), (2004); Agreement between Canada and [Country] for the Promotion and Protection of Investments (Canada Model BIT), Art 13 and Annex B.13(1) (2004). Very similar annexes can also be found in the Australia–United States FTA, the ASEAN–Australia–New Zealand FTA, the Australia–Chile FTA, the Malaysia–Australia FTA and the Korea–Australia FTA.

37 Accepted by the ICSID Tribunal in *Compania del Desarrollo de Santa Elena v. Costa Rica*, ICSID Case No. ARB/96/1 (17 February 2000).

38 TPP, Annex 9-B, footnote 36.

39 Stephenson and Carroll, 'Protecting Foreign Investments by Using Bilateral Investment Treaties' (2011) 30 *Australian Resources and Energy Law Journal* 40.

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the tribunal in *Tecmed v. Mexico*.[40] The tribunal said 'there must be a reasonable relationship of proportionality between the charge or weight imposed to the foreign investor and the aim sought to be realized by any expropriatory measure'.[41]

The above gives some clarity to the meaning of 'indirect expropriation' under the TPP. Further, Paragraph 3(b) of Annex 9-B states:

> *Non-discriminatory regulatory actions by a Party that are designed and applied to protect legitimate public welfare objectives, such as public health, safety and the environment, do not constitute indirect expropriation, except in rare circumstances.*

Regulatory actions to protect public health are said[42] to include measures with respect to the regulation, pricing and supply of, and reimbursement for, pharmaceuticals (including biological products), diagnostics, vaccines, medical devices, gene therapies and technologies, health-related aids and appliances, and blood and blood-related products.

While some suggest the language 'except in rare circumstances' should be removed from Paragraph 3(b), so that non-discriminatory regulation can never be indirect expropriation, to do so would unduly favour the host state and disadvantage the investor, to the detriment of the whole purpose of international investment agreements.

In addition, Article 9.15, entitled 'Investment and Environmental, Health and other Regulatory Objectives', states:

> *Nothing in this Chapter shall be construed to prevent a Party from adopting, maintaining or enforcing any measure otherwise consistent with this Chapter that it considers appropriate to ensure that investment activity in its territory is undertaken in a manner sensitive to environmental, health or other regulatory objectives.*

This language is also found in the Australia–United States FTA; however, in that agreement it is limited to environmental objectives. The TPP is broader in its reach in relation to 'health or other regulatory objectives'. Article 9.15 requires the state to show that it determined that the measure was appropriate with respect to the objective sought. Presumably this requirement will require proof that, prior to the action that is the subject of complaint, the state actually turned its mind to the issue and made the determination. In addition, it seems reasonably arguable that the state must show the decision was made in good faith (i.e., not for a collateral purpose, such as avoiding the operation of the TPP).

Investment schedules

The TPP also contains schedules to the Investment Chapter in which each country has listed country-specific measures or sectors that are exempt from particular provisions of the Investment Chapter. The exemptions are not insignificant. But, they do not apply to the expropriation protection in the Investment Chapter. Australia, for example, has listed foreign

40 *Tecnicas Medioambientales Tecmed SA v. The United Mexican States*, Case No. ARB(AF)/00/2, Award 29 May 2003.

41 At [122].

42 TPP, Annex 9-B, footnote 37.

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investment policy decisions including decisions made pursuant to recommendations of the Foreign Investment Review Board, which regulates significant investments into the country. Australia has also reserved the right to adopt or maintain any measure (for example):

a according preferences to indigenous persons;
b with respect to the provision of law enforcement and correctional services;
c with respect to social services established or maintained for a public purpose such as social welfare, public education, childcare, public utilities, public transport or public housing;
d with respect to the creative arts, indigenous cultural expressions and other cultural heritage; and
e with respect to gambling and betting.

iii Does the MFN clause undo all of the work of the TPP protections?

Some commentators have suggested the most favoured nation clause in the TPP undermines the protections therein to the extent that it allows an investor from a TPP member country to (for example) import substantive protections[43] or more favourable definitions[44] or to bypass procedural preconditions to arbitration[45] from another BIT. In our view, it does not do so.

First, although it is unsettled as to whether an investor can use a MFN clause to bypass preconditions to arbitration (such as the requirement to litigate a dispute in the local courts for a certain period before submitting the dispute to arbitration), this issue does not arise under the TPP because the MFN clause (at Article 9.5(3)) expressly excludes dispute resolution from its scope. In any event, the procedural preconditions to arbitration in the TPP are competitive, as discussed below.

Secondly, Australia's Schedule to Annex II to the Investment Chapter expressly excludes past treaties from its scope. It says:

> *Australia reserves the right to adopt or maintain any measure that accords more favourable treatment to any service supplier or investor under any bilateral or multilateral international agreement in force or signed prior to the date of entry into force of this Agreement.*

Indeed, all of the TPP countries appear to have expressed in some form that the MFN clause will not extend to legal protections in treaties that are currently in force; they will extend only to protections in those treaties a host country signs in the future.

43 For example, the Australian claimant in White Industries Australia Ltd v. India (UNCITRAL Award, 30 November 2011) used the MFN clause in the Australia–India clause to import substantive protections from another Indian BIT (the Kuwait–India BIT), guaranteeing the claimant 'effective means of asserting claims and enforcing rights'.

44 For example, in *CME Czech Republic BV v. Czech Republic* (UNCITRAL Award, 14 March 2003) the tribunal allowed the claimant to use the MFN clause in the Czech Republic–Netherlands BIT to import a more favourable definition of 'just compensation' from another Czech BIT (the US–Czech BIT).

45 For example, in *Maffezini v. Spain* (ICSID Case No. ARB/97/7), the claimant sought to avoid submitting the dispute to the Spanish courts for 18 months as mandated by the Argentina–Spain BIT before resorting to international arbitration by importing the dispute settlement provision from the Chile–Spain BIT, which only required the claimant to observe a six-month negotiation period before filing for arbitration.

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This means, for example, an investor cannot argue that Australia should be liable for actions taken under conditions that are exempt from liability that are not exempt under other BITs (for example, a decision of the Australian government not to renew a subsidy or grant that is protected under Article 9.8(6) of the TPP).

iv ISDS mechanism

The TPP permits arbitration not only of claims for breach of the treaty's substantive investment protections, but also for breach of an investment authorisation or investment agreement. It provides for arbitration under the UNCITRAL, ICSID and ICSID Additional Facility rules, as well as under other rules agreed by both parties.

However, the TPP shows some deference to certain forum-selection clauses that might be contained in investment agreements. Annex 9-L prohibits arbitration of claims for breach of an investment agreement's obligations pursuant to the TPP's ISDS mechanism if the investment agreement already provides for arbitration under one of the following prominent arbitral rules – UNCITRAL, ICSID, ICC or LCIA – and the arbitration would take place outside the territory of the respondent and in that of a signatory to the New York Convention. Interestingly, this carve-out would not cover investment agreements that provide for arbitration under other, equally recognisable, arbitral rules, such as the rules of SIAC, AAA, HKIAC and ACICA.

Article 29.5 (tobacco control measures)

Against the backdrop of threatened and actual ISDS following the introduction of tobacco plain-packaging legislation in Australia, the TPP has introduced a special (and unprecedented) clause preventing tobacco companies making use of the TPP's ISDS provisions. This is the first product-specific exclusion of its kind. Under Article 29.5, a party can elect to deny the use of ISDS for claims challenging a tobacco control measure. A tobacco control measure is defined very broadly.[46] The time at which such an election is to be made is effectively at large. If a party has not elected to deny the use of ISDS with respect to such claims by the time a claim to arbitration is made (e.g., by domestic legislation), the party can still elect to do so during the proceedings (even, it seems, after the hearing). By so doing, the claim will be automatically dismissed.

It is important to note that the carve-out is limited to ISDS only; the rights and obligations in the TPP still apply to tobacco. However, a tobacco company would have to rely on the host state's courts to bring proceedings under Chapter 28 for any alleged breach of the TPP in relation to tobacco. Chapter 28 allows one state to pursue a dispute with another. Although this mechanism remains, it will be much harder for a tobacco company to initiate a claim. It is unlikely that a government (including the governments of the TPP member countries) would agree to bring such an action.

46 A tobacco control measure is defined as a measure related to the production or consumption of manufactured tobacco products (including products made or derived from tobacco), their distribution, labelling, packaging, advertising, marketing, promotion, sale, purchase, or use, as well as enforcement measures, such as inspection, record-keeping and reporting requirements. A measure with respect to tobacco leaf that is not in the possession of a manufacturer of tobacco products or that is not part of a manufactured tobacco product is not a tobacco control measure.

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Procedural safeguards

Importantly, the ISDS provisions in the TPP offer 'procedural safeguards', some of which are common to investment agreements, some of which are new. These are summarised below.

Prior to initiating proceedings, the investor must first endeavour to resolve its dispute with the state through consultations and negotiations for at least six months, a period that is typical of consultation periods in investment agreements.[47] The investor must initiate proceedings within three-and-a-half years from the date on which the investor first acquired, or should have first acquired, knowledge of the alleged breach.[48] This limitation period is also typical.[49]

The notice of arbitration must be accompanied by a waiver, by the investor, of any right to initiate the claim before any other domestic or international court or tribunal. This requirement is intended to prevent the investor forum shopping.[50] There is also scope for the tribunal to decide as a preliminary question, on an expedited basis, an objection that a claim is manifestly without legal merit.[51] This provides a mechanism to strike out frivolous or baseless claims. A related mechanism to discourage frivolous claims is the tribunal's ability to award costs against the investor if the tribunal finds in favour of the respondent's objection.[52]

The investor is also expressed to have the burden of proving all elements of its claim.[53] This is unlikely to constitute a change from the position that would have prevailed in the absence of such a provision.

The TPP has improved provisions that ensure both transparency of the arbitral proceedings and that its interpretation is within the control of member states. In respect of the former, the host state is required to provide all of the arbitral documents (including the notice of arbitration, pleadings, transcripts and the award) to the other non-disputing TPP members and to the public,[54] and hearings are open to the public. These requirements are subject to provisions for the protection of appropriate confidential information.

The provisions of the TPP enable parties to maintain some control over its interpretation. A TPP party that is a party to an arbitration can have the question of whether a measure falls

47 See, e.g., the ASEAN-Australia-New Zealand Free Trade Agreement (2009); the Australia-Chile Free Trade Agreement (2009); the Agreement between the Government of Australia and the Government of the United Mexican States on the Promotion and Reciprocal Protection of Investments (2007); the Agreement between Australia and the Government of the Republic of Peru on the Promotion and Protection of Investments (1997); the Singapore-Australia Free Trade Agreement (2003).

48 TPP, Article 9.20(1).

49 Under Australia's existing investment agreements with the TPP member countries, the limitation period ranges from three to four years.

50 TPP, Article 9.20(2). Such a waiver is also required under the ASEAN-Australia-New Zealand Free Trade Agreement (2009); the Agreement between the Government of Australia and the Government of the United Mexican States on the Promotion and Reciprocal Protection of Investments (2007); and the Singapore-Australia Free Trade Agreement (2003).

51 TPP, Article 9.22(4).

52 TPP, Article 9.22(6).

53 TPP, Article 9.22(7).

54 Compare the provisions in the ASEAN-Australia-New Zealand Free Trade Agreement (2009) in which transparency is optional only.

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within one of its exceptions to the TPP (under Annex I or II to Chapter 9) determined jointly by the TPP parties[55] rather than the tribunal, and these interpretations are binding on the tribunal.[56]

Finally, there is a commitment by TPP member states to consider, at a later date, both a code of conduct for arbitrators in ISDS[57] and an appellate review mechanism to correct errors of law.[58]

IV CONCLUSION

The worldwide concern that ISDS provisions allow foreign companies to sue governments in respect of laws and policies aimed at safeguarding the environment, health and other sensitive areas, is misdirected. It is not the ISDS mechanism that should be critiqued. Rather, attention should be directed to the substantive investment protections themselves – the nature of the rights that are created and the consequences of those rights.

The TPP aims to protect public welfare by ensuring that the investment protections, such as the protection against expropriation discussed in this chapter, build in those public welfare considerations. They are relevant to the content of the investment protection itself and not just as a possible exception to its application. To this end, the TPP goes some way to balancing the interests of governments and investors by promoting foreign investment while recognising the inherent right of governments to regulate in the public interest.

It remains the case that unless investment protections are backed by ISDS, the alternative, which would allow an investor to seek redress, is litigation in the courts of the state alleged to have breached the treaty. This would severely reduce the value of the protections on offer, particularly for those states with developing economies who have not yet developed a strong rule of law or institutions capable of applying it, particularly against the state. Accordingly, a blanket exclusion of ISDS in international investment agreements is not the answer to the above-mentioned concern.

55 Specifically, the Trans-Pacific Partnership Commission, which is composed of government representatives of each party.

56 TPP, Article 9.25.

57 TPP, Article 9.21.6.

58 TPP, Article 9.22.11.

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