Constitutional Law and the Settlement of Investor-State Disputes: Some Interplays

BOISSON DE CHAZOURNES, Laurence, MCGARRY, Brian

CHAPTER 14

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Laurence Boisson de Chazournes and Brian McGarry

1 Introduction

The State's role in the international legal order is a thread that can be traced throughout Judge Koroma's scholarship. In particular, his contributions to dialogues on the international judicial law-making function as well as emerging themes in international law, such as solidarity and multiculturalism, demonstrate a reflective approach to questions of normative harmony and conflict. It is in this spirit that the authors present the following brief observation on the synergies between domestic and international legal regimes which may appear in the context of investor-State claims and defenses. While issues of constitutional law may arise directly in the ratification process of investment treaties and the execution of arbitral awards, well-established hurdles to the application of domestic law in transnational fora substantially limit the degree to which such issues factor into the merits of investor-State disputes. Nevertheless, they may gain prominence through informal paths. Rather than directly applying constitutional law per se, tribunals may utilize other paths such as deferring to domestic interpretations of constitutional principles, or to constitutional procedures that appear, for example, to protect fair and equitable treatment.

From the outset, we may note that links between international and domestic spheres can play a role in rooting arbitral awards in what the WTO Appellate Body in the EC – Hormones case described in memorably stark terms: “the real world where people live, work and die.” The following year, an ad hoc tribunal in the Himpurna California Energy case echoed this sentiment in an investment context. As to the applicable norms in a case involving corruption, that tribunal declared that it “do[es] not live in an ivory tower [...] [n]or does [it]


view the arbitral process as one which operates in a vacuum, divorced from reality."³ The year thereafter, the S.D. Myers tribunal introduced this view into dispute settlement under the North American Free Trade Agreement (NAFTA).⁴ Moreover, it stressed its approach as deferential to democratic processes. In its evaluation of minimum standards of treatment, the tribunal stated that it "does not have an open-ended mandate to second-guess government decision-making,"⁵ finding instead that "[t]he ordinary remedy [...] for errors in modern governments is through internal political and legal processes."⁶

In terms of tribunals’ analysis and consideration of domestic constitutions during the course of arbitrations, we can draw attention to two broad paths. The first concerns informal comity toward constitutional principles and idiosyncrasies that may lie at the heart of an investment dispute. The second is the extent to which a host-State may formally rely upon constitutional guarantees to its people as a defense to a claim, particularly in the context of a domestic crisis.

2 Informal Deference to Constitutional Expertise

A general theme that emerges with respect to the former is tribunals’ willingness or reluctance to ‘second-guess’ domestic courts’ interpretations of their own constitutional safeguards and domestic legal complexities.⁷ The extent to which tribunals have regarded host-State constitutions should not be viewed as a measure of the legal force of constitutional provisions against international law. Rather, we may see deference to national interpretations of principles enshrined in both domestic law and international law. Foremost among these principles is that of fair and equitable treatment. This is a fundamental principle of most domestic laws and the basis for a pervasive claim in investment dispute settlement.

³ Ibid., paras 219–220.
⁵ Ibid., para. 261.
⁶ Ibid.
It is possible for a treaty to refer directly to constitutional State norms, as is the case in the CARICOM-Cuba investment treaty. This treaty incorporates by reference the fair and equitable treatment standards found in the domestic legislation of the host-State. However, such direct formulations are unique for straightforward reasons. If the meaning of fair and equitable is defined exclusively by the legal framework of the host-State, tribunals may arguably lack interpretative norms for gauging State compliance.

Yet the difference between purely domestic versus international conceptions of fair and equitable treatment is not as distinct as it may seem. An examination of the element of 'proportionality' illuminates this point. In a purely domestic sense, this concept primarily serves to limit the involvement of public authorities within the private sphere. From these State-based origins, proportionality tests have increasingly penetrated transnational legal systems. Most notably, the adoption of such a test in the jurisprudence of the Court of Justice of the European Union (CJEU) has diffused this concept into

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8 Agreement on Reciprocal Promotion and Protection of Investments [between the Caribbean Community (CARICOM) and the Republic of Cuba] (1990).
9 Ibid., Art. 4 ("Each Party shall ensure fair and equitable treatment of Investments of Investors of the other Party under and subject to national laws and regulations").
11 Similarly, other guarantees against investor discrimination such as the national treatment standard are common to federal constitutions (such as the U.S.), supranational entities (such as the EU), and, in particular, the WTO. In an investment context, most treaties take a minimalist approach to national treatment guarantees that results in a comparatively amorphous and complex study of trends. For an excellent analysis of the state of jurisprudence on this particular issue, see J. Kurtz, 'The Merits and Limits of Comparativism: National Treatment in International Investment Law and the WTO', in S.W. Schill (ed.), International Investment Law and Comparative Public Law (Oxford: Oxford University Press, 2010), pp. 243–278.
12 R. Kläger, op. cit., pp. 236–237. This function of proportionality may have originated in the administrative law of Germany. The concept has since developed into a doctrinal element of constitutional law in that State.
the legal systems of States across Europe. This has paved two-way streets between domestic and international interpretations of fair and equitable treatment. A similar influence may be ascribed to the jurisprudence of the European Court of Human Rights (ECtHR). With respect to the latter, proportionality is firmly established as an important tool to restrict the discretion left to State authorities, and to scrutinize the legitimacy of their measures. The concept is also well-known in WTO law. In this area, analysis under Article XX of the General Agreement on Tariffs and Trade (GATT) has utilized a sort of proportionality test.

For the purposes of our review, however, it may suffice to narrow the focus toward those claims that specifically allege a denial of justice. Foreign investor claims that question the legal effectiveness of host-State administrative procedures may informally trigger issues of comity. This is due to a true distinction between the aforementioned institutions and investment tribunals. Such tribunals are not constituted to serve as appellate courts reviewing domestic judicial decisions, much less very fine points of national law. To that extent, Jan Paulsson has submitted that even "gross or notorious injustice [...] is not a denial of justice merely because the conclusion appears to be demonstrably wrong in substance; it must impel the adjudicator to conclude that it could not have been reached by an impartial judicial body worthy of that name." Denial of justice allegations do not direct arbitrators to gauge the substantive accuracy of a State's application of its own laws. We must therefore consider fair and equitable treatment in this regard as a principle related to procedural fairness. With this in mind, we may turn to some recent NAFTA

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17 It is in this light that some commentators have posited that the unifying theory behind the fair and equitable treatment standard is the concept of legality. Such a view concludes
arbitrations that have raised related and complex constitutional issues. We can now more concretely appreciate how a tribunal – by emphasizing the procedural character of its FET analysis – may therefore draw inspiration from domestic interpretations of this principle.

For example, the tribunal in the Glamis Gold case dealt with a U.S. agency’s “lengthy, reasoned legal opinion” of constitutional law. The namesake Canadian corporation in this case was engaged in the exploration and extraction of precious metals throughout the continent. In 1994, Glamis Gold acquired mining rights for a proposed open-pit gold mine on U.S. federal lands, in the California desert lands known as Imperial Valley. Given the potential ecological damages associated with the firm’s proposed mining practices, permission to commence exploration hinged on a thorough environmental review. This review considered, inter alia, the rights of indigenous populations in the area. In 2001, after years of study, the relevant federal agency formally denied the Glamis Gold project.

This rejection was based in large part on an apparent conflict between the longstanding U.S. mining statute liberalizing mining rights in the American west, and the religious freedoms guaranteed under the State’s federal constitution. Noting that a local tribe’s religion required it to worship in a pathway traversing the proposed mining area – and analogizing U.S. Supreme Court precedents addressing other natural resource agencies – the executive order found that the federal government was bound to “preserve[e] the physical integrity of the sites unless such a choice [was] impracticable, forbidden by law, or clearly inconsistent with essential agency functions.”

However, following a change in presidential administrations the same year, this opinion was reversed and the Imperial Valley Project was approved. In response to this federal turnaround, California adopted an emergency regulation implementing onerous remediation requirements designed to preserve lands near tribal sacred sites. This example of dual regulatory sovereignty results from a constitutionally enshrined federalism that surfaces somewhat fre-

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18 Glamis Gold v. United States of America, Award, NAFTA/UNCITRAL (16 May 2009), para. 761.
19 Constitution of the United States of America, amend. 1.
20 Glamis Gold, op. cit., para. 142.
quently in NAFTA Chapter 11 claims, which are what Glamis Gold brought next. The firm filed NAFTA claims alleging regulatory expropriation under Article 1101 and a violation of fair and equitable treatment under Article 1105, stemming from both the initial federal ruling and the eventual state measures.

The latter claim serves as our focal point, as it required the tribunal to review what it called "[the U.S. agency's] complicated legal opinion on an issue of first impression that changed a [...] century-old regime upon which Claimant had based reasonable expectations." The question, therefore, was whether this administrative interpretation of constitutional law violated NAFTA's incorporation of customary international standards of fair and equitable treatment by altering the investor's legitimate expectations. The tribunal's response cast NAFTA Article 1105 as deferential to the due process interpretations of domestic constitutional courts. The tribunal stated that it would not 'second-guess' the original federal opinion or California measures relying upon it unless such decisions had appeared "blatantly unfair or evidently discriminatory" or "evidence[d] a complete lack of process." In so doing, the tribunal left the claimant's only potential recourse at the courthouse steps.

In this manner, the tribunal implied a notable give-and-take in Chapter 11 disputes. Foreign investors may be inclined to select arbitration over domestic U.S. litigation, as NAFTA tribunals may construe expropriation more broadly.

21 NAFTA Chapter 11 is a notable prism through which we can view international and domestic legal interplay. One reason for this is that the basic constitutional tensions at play in federalist States are particularly visible in investment dispute settlement. NAFTA's States Parties vest substantial constitutional authority in sub-federal sovereigns, governing economic and environmental matters alike. In Canada, for example, the federal government in 2010 settled a Chapter 11 claim brought by U.S. investor AbitibiBowater, arising from an expropriation by the province of Newfoundland and Labrador. Canada's constitution, however, does not include any mechanism whereby Ottawa can recoup its C$130 million settlement - the largest in NAFTA history at the time - from its province through legal action. See L.L. Herman, 'Federalism and international investment disputes', IISD Investment Treaty News (12 July 2011), available at: http://www.iisd.org/itn/zon/12/federalism-and-international-investment-disputes/. Similar issues abound in the U.S. constitutional model, and are easily capable of yielding the opposite imbalance. For example, following the Methanex arbitration, Washington was able to recoup its arbitral costs from the unsuccessful Canadian claimant. However, California has no direct avenue in U.S. constitutional law to claim from this sum its considerable expenses in preparing to defend the water health regulation at issue. See M. Bottari & L. Wallach, 'Federalism and Global Governance', Public Citizen Global Trade Watch (2008), available at: http://www.citizen.org/documents/federalism.pdf.

22 Glamis Gold, op. cit., para. 761.

23 Ibid., para. 24.
under Article 1105 than federal courts would construe the term under the U.S. constitution. Yet when it comes to Article 1105 claims concerning fair and equitable treatment, investor-State tribunals – such as in the *Glamis Gold* case – may demonstrate more reluctance than their domestic judicial counterparts to review administrative decisions and constitutional interpretations.

The *Grand River* case was a subsequent NAFTA dispute with facts even more intertwined with domestic federalism issues and informal issues of ‘second-guessing’ domestic institutions. In this case, the investor, a Canadian cigarette distributor, arranged a business strategy that would mitigate its financial obligations under the contemporary tobacco laws in many U.S. states. Such obligations required tobacco distributors to place large sums into escrow accounts in order to settle claims related to the damaging health effects of cigarettes.

However, *Grand River* attempted to circumvent these state requirements by distributing its product primarily through the quasi-sovereign ‘Indian territories’ occupied by federally recognized tribes. The major question for the tribunal in the eventual NAFTA case, therefore, was whether U.S. constitutional law and federalism granted U.S. states the regulatory authority to impose their escrow laws on commerce in tribal reservations within a state’s territory.

Striking a deferential note similar to *Glamis Gold*, the tribunal stated that “U.S. federal Indian law is a complex and not altogether consistent mixture of constitutional provisions, federal statutes, and judicial decisions by the U.S. Supreme Court [...].” Finding that “U.S. domestic law is currently far from conclusive about the question raised here of the extent of permissible state regulation,” the *Grand River* tribunal cautiously noted that “[d]etermining the contents of that law ... often calls for necessarily uncertain predictions of how future courts will apply past decisions involving different [state regulations].”

From this context, the tribunal forcefully returned to the themes of the *Glamis Gold* tribunal’s treatment of claims based on NAFTA Article 1105 fair and equitable treatment, stating that it “is loath to purport to address ... delicate

24 U.S. Constitution, amend. v.
26 Ibid., para. 132.
27 Ibid., para. 137.
28 Ibid., para. 138. The tribunal in a more recent NAFTA arbitration was similarly reluctant to make determinations regarding the division of federal and provincial competences under Canada’s constitution. *Bilcon of Delaware et al v. Government of Canada*, Award, NAFTA/UNCITRAL, PCA Case No. 2009-04 (17 Mar. 2015), para. 526 (“The Tribunal recognizes that constitutional doctrine can be complex, controversial and shifting [...]").
and complex questions of U.S. constitutional law." 29 Dismissing Grand River's claims in full, the tribunal asserted its reluctance to address delicate matters of federal law, finding instead that such "issues of national law belong in national courts, not in an international tribunal." 30 In other words, because U.S. authorities' determination on the matter had not presented a *prima facie* case of denial of justice cognizable at the high threshold of customary international law under NAFTA Article 1105, the tribunal in *Grand River* refused to 'second-guess' domestic constitutional interpretations.

This comity toward executive opinions on 'complex' questions of constitutional law is particularly noteworthy because claimant Grand River argued that U.S. authorities had violated one of the State's international human rights obligations: the duty to consult with indigenous peoples prior to making important regulatory decisions affecting their interests. 31 As this legal duty arguably formed part of the claimant's reasonable expectations at the time of contracting, the *Grand River* tribunal essentially deferred to domestic treatment of federalism questions in lieu of its own competence to counterbalance legitimate investor expectations. 32

On this point, we may return to our earlier discussion of the role of constitutional law in instances where an international treaty does not address relevant fundamental rights. Under NAFTA, a tribunal "shall decide the issues in dispute in accordance with this Agreement and applicable rules of international law." 33 This mandate does not refer expressly to constitutional or any State law, and yet we have seen NAFTA tribunals in *Glamis Gold* and *Grand River* find cause to show informal deference to domestic law. Concerning the legal interests of local populations that are intertwined in these cases, one may begin to discern a certain tendency in investor-State arbitration to recognize a

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29 Ibid., para. 234.
30 Ibid.
31 Ibid., paras 180–181.
32 Another NAFTA Chapter 11 arbitration recently initiated by a Canadian investor against the U.S. followed on the heels of a separate, ongoing arbitration between the parties concerning the relative authority of investment tribunals to affirm or refute domestic judiciaries' treatment of their own constitutions. Canadian pharmaceutical company Apotex argued unsuccessfully that U.S. courts misapplied statutory and constitutional law in multiple decisions, in what amounts to a violation of NAFTA commitments concerning national treatment, fair and equitable treatment, and expropriation. Apotex Holdings Inc. and Apotex Inc. v. United States of America, Award, ICSID Case No. ARB(AF)/12/1 (25 Aug. 2015).
33 NAFTA, Art. 1131.
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rather broad margin for governments to make their own choices in ensuring the respect of constitutional norms within their jurisdictions.\textsuperscript{34}

3  Formal Application of Constitutional Obligations

The right of compensation in case of expropriation, like the guarantee of fair and equitable treatment, is a fundamental principle common to a majority of domestic legal systems, and many of these States codify this right at the constitutional level (including Croatia, Denmark, Germany and Italy).\textsuperscript{35} U.S. jurisprudence has explained that State's constitutional permission of compensated takings on the basis of States' implicit police powers: exercises of a government's sovereign right to protect its people's lives, health, morals, comfort and general welfare, at a level paramount to any rights under contracts between individuals.\textsuperscript{36} In more recent decades, the U.S. Supreme Court extended this reasoning to contracts between individuals and the entities of the states.\textsuperscript{37}

Like the constitutional courts of these domestic legal systems, those of transnational jurisdiction broadly support the principle that States may terminate or otherwise modify contracts with private parties in the event of superseding public interests. This authority is indeed so uncontroversial that it is generally read as an implied exception to investment treaty umbrella clauses.\textsuperscript{38}

However, despite overlaps between domestic and international legal principles in this context, direct reference to constitutional law as a host-State defense against foreign investors' claims has proven problematic in practice. This is because it is a formal path to applying domestic law. As such, it may be examined in contrast with the informal paths we have just seen in the context of fair and equitable treatment claims.

For example, if proof of a taking is established in an investment arbitration, constitutional law may inform the fact of whether sufficient justification exists


\textsuperscript{35} F. Lenzerini, 'Property Protection and Protection of Cultural Heritage', in S.W. Schill (ed.), op. cit., p. 566.


\textsuperscript{38} S.W. Schill, 'Umbrella Clauses as Public Law Concepts in Comparative Perspective', in S.W. Schill (ed.), op. cit., p. 340.
to excuse the host-State from any required and outstanding compensation. However, domestic constitutions vary widely on this point and may not provide substantive clarity to the tribunal concerning a government's conformity or non-conformity with its own laws defining states of emergency. For example, France's 1958 constitution vests broad discretion and powers in the President when "the proper functioning of the constitutional public authorities is interrupted." The U.S. not only similarly lacks any clear constitutional discussion of economic emergencies, but also lacks any constitutional provision on emergency authorities beyond the rudimentary suspension of "habeeas corpus "when in cases of rebellion or invasion the public safety may require it." 

In contrast, investment tribunals have incrementally contributed to a more static norm of emergency powers, notably involving defenses based on the human rights elements of State constitutions. For example, in several disputes arising from its financial crisis, Argentina has explicitly referred to resulting threats to its 'constitutional order', in both the societal and legal senses of the term. The intriguing point here is the manner in which conflicts with human rights obligations appear to arise.

In some instances, Argentina has argued that it took measures in response to its financial crisis that were necessary to uphold the basic rights and liberties of the Argentine public, and has at times cited the supremacy of human rights treaty obligations within its Constitution. The first investment tribunal to render an award in such a dispute was the CMS case, which not only rejected Argentina's human rights defense, but deemed that the human rights and investor obligations in question were not in conflict, and therefore led to no issues of constitutional supremacy. Meanwhile, the tribunal in the Sempra case simply concluded on the same facts that no danger of societal collapse existed to have even necessitated the suspension of liberties. In contrast, an ICSID tribunal's award in the Continental Casualty case reached opposite con-

42 Ibid., pp. 8-12.
43 CMS Gas Transmission v. Argentina, Award, ICSID Case No. ARB/01/08 (12 May 2005).
44 Sempra Energy v. Argentina, Award, ICSID Case No. ARB/02/16 (28 Sep. 2007).
clusions on both the effectiveness of Argentina's emergency defense and the preeminence of its human rights obligations. 45 Of particular note to our discussion of constitutional interplay is the tribunal's remark that Argentina's protection of fundamental liberties was a proactive step that removed the necessity of later suspending such liberties to enforce social order. 46

The resulting deference that the *Continental Casualty* tribunal granted to Argentina's crisis management decisions stands in stark contrast to the limited margin of appreciation that had been granted to Argentina under the same circumstances by the tribunal in the *Siemens* case. 47 Indeed, that tribunal had rejected as unformed Argentina's argument that the property rights claimed by Siemens would have forced Argentina to violate its constitutionally preeminent international human rights treaty obligations. 48

In a more recent case arising from the Argentine financial crisis, the tribunal in *SAUR International* acknowledged fundamental human rights, and in particular the right to water, as safeguarded by both the Argentine constitution and general principles of international law. 49 However, the tribunal held that this regulatory concern must be combined with investors' treaty rights to compensation for property. 50

4 Concluding Remarks

As the application of domestic law in international dispute settlement is an exercise in overcoming well-established hurdles – and as investment arbitration today offers an evolving but inherently fragmented body of precedents – it

46 Ibid., paras 180–181, 270. See also *LG&E Energy v. Argentina*, Decision on Liability, ICSID Case No. ARB/01/1 (3 Oct. 2006), para. 234. Argentina's necessity defense was successful in the *LG&E Energy* case, although that tribunal relied upon a different rationale than in the subsequent *Continental Casualty* case. The *LG&E Energy* decision did not expressly refer to Argentina's human rights obligations, but rather emphasized the social and health-related effects of the financial crisis.
47 *Siemens v. Argentina*, Award, ICSID Case No. ARB/02/08 (6 Feb. 2007).
48 Ibid., para. 79.
50 Ibid.
should not surprise that different tribunals have thus exhibited varying degrees of comity toward States' administrative and judicial procedures. The informal paths that we have traced between constitutional law and investment arbitration rely upon such comity. It entails tribunals' reluctance to probe alleged denials of justice when host-State procedures do not appear to contradict principles of due process and the rule of law. Moreover, it may compel those tribunals' deference to domestic interpretations of constitutional complexities. In practice, these paths have more effectively assimilated constitutional law than have more formal approaches, such as we have seen in host-State defenses based on emergency powers.

Yet these faint but clearing paths between the two legal spheres do not tell the end of the story. There may be marked trails as well, such as our earlier mention of investment treaties incorporating host-State norms by reference. Still another portal may be found in the premise of comparative constitutional analysis. This is not a merely theoretical model or a one-sided push to 'domesticate' investor-State dispute settlement through traditional constitutional constraints. It acknowledges that the standards and tests embraced by tribunals are likely to influence both the future conduct of States and the decisions of other tribunals. Moreover, the trend toward viewing investor-State arbitration as part of a global governance structure naturally encourages resort to principles of comparative constitutional law, particularly when assessing the concept of fair and equitable treatment.

In this sense, the content of such treatment standards is poised to evolve further in the coming years of investment arbitration. Despite the general supremacy of international law, tribunals called upon to decide matters of transnational law may well serve the institutional interests of investment arbitration by integrating a mutually supportive understanding of constitutional and international norms. The doorways between these constructs may remain works in progress for the time being, but as tribunals have increasingly implied, no such edifice is an "ivory tower" of limited view or reach. 51