Environmental concerns have amplified dramatically in the past decades. Global threats to the environment such as climate change or declining biodiversity have emerged and become an essential part of the world’s social challenges. The investment landscape is also changing. Traditionally, the home and host State role was clearly divided between North and South, with the members of the Organisation for Economic Co-operation and Development (OECD) as the capital exporting countries. Nowadays, however, developing economies have become increasingly large investors themselves. Furthermore, transnational corporations (TNCs) have become an important player within the investment system fuelling the discussion on how to include investors’ obligations into international investment agreements (IIAs). Others are concerned with the perceived imbalance between investor protection and the host State’s right to regulate. These concerns arose largely in response to the increasing number of investor-State disputes touching on delicate public policy issues and often leading to unexpected interpretations and/or heavy charges on [...]
INCLUDING ENVIRONMENTAL PROTECTION IN INTERNATIONAL INVESTMENT AGREEMENTS

Chiara Nyfeler
Fröschbach 55
8117 Fällanden

30 April 2015
University of Geneva
Faculty of Law
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## ABBREVIATIONS

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<th>Abbreviation</th>
<th>Description</th>
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<tbody>
<tr>
<td>BIT</td>
<td>Bilateral investment treaty</td>
</tr>
<tr>
<td>CAFTA</td>
<td>Central America–Dominican Republic–United States Free Trade Agreement</td>
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<tr>
<td>CETA</td>
<td>Comprehensive Economic and Trade Agreement</td>
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<td>COMESA</td>
<td>Common Market for Eastern and Southern Africa</td>
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<td>CSR</td>
<td>Corporate social responsibility</td>
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<td>ECT</td>
<td>Energy Charter Treaty</td>
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<td>ECtHR</td>
<td>European Court of Human Rights ed.</td>
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<td>EPA</td>
<td>Economic partnership agreement</td>
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<td>EU</td>
<td>European Union</td>
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<tr>
<td>FDI</td>
<td>Foreign direct investment</td>
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<tr>
<td>FET</td>
<td>Fair and equitable treatment</td>
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<tr>
<td>FIPA</td>
<td>Foreign Investment Promotion and Protection Agreements fn.</td>
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<tr>
<td>FTA</td>
<td>Free trade agreement</td>
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<tr>
<td>GATS</td>
<td>General Agreement on Trade in Services</td>
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<tr>
<td>GATT</td>
<td>General Agreement on Tariffs and Trade</td>
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<tr>
<td>ICSID</td>
<td>International Centre for Settlement of Investment Disputes</td>
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<tr>
<td>ICSID Convention</td>
<td>Convention on the Settlement of Investment Disputes between States and Nationals of other States; also called Washington Convention</td>
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<tr>
<td>IEL</td>
<td>International environmental law</td>
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<td>IIAs</td>
<td>International investment agreements</td>
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<td>IIL</td>
<td>International investment law</td>
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<td>IIISD</td>
<td>International Institute for Sustainable Development</td>
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<td>IPAs</td>
<td>Investment promotion agencies</td>
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<td>IPFSD</td>
<td>Investment Policy Framework for Sustainable Development</td>
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<td>ISDS</td>
<td>Investor-State Dispute Settlement</td>
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<td>MAI</td>
<td>Multilateral Agreement on Investment</td>
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<tr>
<td>MEAs</td>
<td>Multilateral Environmental Agreements</td>
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<tr>
<td>MIGA</td>
<td>Convention Establishing the Multilateral Investment Guarantee Agency</td>
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<tr>
<td>NAFTA</td>
<td>North American Free Trade Agreement</td>
</tr>
<tr>
<td>OECD</td>
<td>Organisation for Economic Co-operation and Development</td>
</tr>
<tr>
<td>PCB</td>
<td>Polychlorinated biphenyls</td>
</tr>
<tr>
<td>RCEP</td>
<td>Regional Comprehensive Economic Partnership</td>
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<tr>
<td>SADC</td>
<td>Southern African Development Community</td>
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<tr>
<td>TNCs</td>
<td>Transnational corporations</td>
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<tr>
<td>TTIP</td>
<td>Transatlantic Trade and Investment Partnership</td>
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<tr>
<td>UK</td>
<td>United Kingdom</td>
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<tr>
<td>UNCTAD</td>
<td>United Nations Conference on Trade and Development</td>
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<tr>
<td>USA</td>
<td>United States of America</td>
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<tr>
<td>Vol.</td>
<td>Volume</td>
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<td>WCED</td>
<td>World Commission on Environment and Development</td>
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INTRODUCTION

Environmental concerns have amplified dramatically in the past decades. Global threats to the environment such as climate change, declining biodiversity, deforestation, and pollution of the oceans or depletion of the ozone layer have emerged and become an essential part of the world’s social challenges. The investment landscape is also changing. Traditionally, the home and host State role was clearly divided between North and South, with the members of the Organisation for Economic Co-operation and Development (OECD) as the capital exporting countries. Nowadays, however, developing economies have become increasingly large investors themselves. Furthermore, transnational corporations (TNCs) have become an important player within the investment system fuelling the discussion on how to include investors’ obligations into international investment agreements (IIAs).

Others are concerned with the perceived imbalance between investor protection and the host State’s right to regulate. These concerns arose largely in response to the increasing number of investor-State disputes touching on delicate public policy issues and often leading to unexpected interpretations and/or heavy charges on States’ budgets. Notably, the complexity of the investment system has evolved, pressuring for more comprehensive agreements.

These changes and deficiencies reveal the need to address wider public policy objectives, such as the protection of the environment or sustainable development goals, in the international investment regime. These developments are leading to a new generation of IIAs. The time is opportune: 1300 bilateral investment treaties (BITs), that is almost half of the existing BITs, expire in the near future. This offers a unique opportunity to address irregularities within the agreements and ultimately to revisit the whole international investment regime. However, environmental protection is a marginal target in current strategies of investment promotion agencies (IPAs), despite the importance in national and global policy agendas.

Hence, the purpose of this paper is to contribute to a better understanding on how to include environmental protection into international investment agreements. Stocktaking of the current treaty practices and highlighting the most important investment arbitration decisions, it is thus a critical analysis of the models available at the moment and what could be the de lege ferenda. The paper opts for the viewpoint of the treaty negotiator. The focus is therefore less on the interpretation of environmental friendly clauses by arbitral tribunals.

This paper is divided into three parts. In Part I the basics of the international investment system are set out and the question on why to include environmental

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2 The term IIAs refers to BITs, bilateral and regional FTAs that include provisions on foreign investment and to sectoral agreements, like the ECT.
3 UNCTAD, *Towards a new generation of international investment policies: UNCTAD’s fresh approach to multilateral investment policy-making*, above 1, p. 5.
protection into IIAs is answered. It starts with a historical analysis of the international investment regime, examines the evolution of environmental protection and considers the much-discussed concept of the right to regulate. In Part II the question on how to include environmental protection into IIAs is analysed. It sets out the different types of recurring clauses in IIAs regarding the environment and provides a critical analysis of each individual clause. Finally, in Part III the apparent problems that could occur when including environmental language in IIAs are considered. Furthermore, the potential impact of the inclusion of environmental protection in IIAs is addressed.

PART I

1. Historical background of IIAs

Until the mid-20th century, international investment was not perceived as a stand-alone field; rather it was intertwined with trade. However, its roots go back to the 17th century when nation-States started tax-exempting nationals from the other contracting party. In the first half of the 20th century, some attempts to a multilateral approach to investment protection were made, but they all failed. At that time, investment protection was mainly diplomatic, that is the home State assuming the investor’s claim, or the protection was assured through specialized claims commissions.5

International investment activity increased importantly in the period after World War II when new States joined the international parquet. Investment in the newly independent countries became a major issue in the multilateral fora. Inflow of capital was aimed at increasing the standard of living and the general development of these countries. At the same time, international investors were concerned about the effective protection of their investment against interference by the host State.6 According to the foreign investors and their governments, applicable international law failed to include contemporary investment practices, the existing principles were vague and “the content of the existing international legal framework was subject to sharp disagreement between industrialized countries and newly decolonized developing nations.”7 In fact, with the demise of colonization, the emerging States attacked increasingly the legitimacy and content of the traditional principles of the protection of foreign investment. They argued that western countries had exclusively shaped customary international law and that the international law (at that time) was an obstacle to their economic advancement.8 The newly independent countries claimed sovereignty over their natural resources and successive waivers of nationalization followed.9

Hence, a legal framework that would guarantee stability and predictability had to be developed. But again, a broad multilateral approach to investment protection

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7 Ibid., p. 330.
8 Ibid., p. 324.
Countries such as Germany and Switzerland, lacking colonial ties, or an informal network in developing countries, saw their investments threatened and therefore started pursuing the bilateral approach. The first BIT between Germany and Pakistan was concluded in 1959. Those early BITs safeguarded exclusively the investors’ interests in the host States. Likewise, the first generation of BITs was only concluded between developed and developing countries.

In 1966 the Convention on the Settlement of Investment Disputes between States and Nationals of other States (ICSID Convention) entered into force, providing for direct investor-State arbitration, a singular dispute settlement mechanism in international law, provoking the second generation of BITs. The number of BITs concluded rose rapidly in the 1980s when developing countries started concluding BITs among themselves.

There were nearly 3000 BITs in 2013; free trade agreements (FTAs) and regional instruments added the number of IIAs exceeds 3000. Hence, an immense network of bilateral and regional treaties exists, but there is no multilateral treaty granting substantive rights. The two multilateral conventions that exist contain only procedural – the ICSID Convention – or functional rights – the Convention Establishing the Multilateral Investment Guarantee Agency (MIGA).

### 2. Evolution of environmental protection

Both international investment law (IIL) and international environmental law (IEL) are young fields of law. Even if environmental concerns have existed for a long time and their roots can be found in Roman law, the international framework for the protection of the environment has been developed primarily since the late 1960s. Especially the Stockholm Conference in 1972 marked a clear milestone in giving priority to environmental protection even at the detriment of economic development.

However, the famous Brundtland Report and the Rio Conference in 1992, promoted the reconciliation of environmental protection and economic development, now known as sustainable development. At the turning of the millennium, a new strategy aiming at the inclusion of the private sector for the achievement of environmental goals (public-private partnerships) and notions such as corporate social responsibility (CSR) appeared in the international panorama.

Again in 2012, the international policy with regard to environmental protection changed with the Rio+20 Conference, which affirms the shift towards a green

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10 Ibid., pp. 8-9.
13 M. Jacob, ‘Investments, Bilateral Treaties’, above 5, § 73.
economy. Behind the green economy approach lies the idea of a fundamental transformation of the economy (including abandoning certain forms of production and looking for new ones), which is based on the presumption that economic activity that relies on environmental considerations is indeed profitable.  

3. Interaction between international investment and environmental protection

3.1. Policy shift towards including environmental objectives

As mentioned above, traditionally, BITs pursue the exclusive goal to protect the investors’ businesses abroad. Only recently, BITs are beginning to reflect policy shifts by including other objectives, such as national security, public health and environmental protection. In a similar effort, States search to include more regulatory freedom concerning human rights and labour standards or to combat corruption. Free trade agreements (FTAs) are more extensive agreements pursuing various objectives, among them the establishment of closer trade and investment relations. They contain usually a specific chapter on investment, including, generally speaking, the same rules on promotion and protection of investment as incorporated in BITs. The gradual paradigm shift can also be found in FTAs with the inclusion of specific chapters on environmental protection.

3.2. Why including environmental language into IIAs

Historically, IIL and IEL have developed independently. Until recently, instruments dealing with international investment have made little if any reference to instruments relevant to the environment and vice versa. The concept of fragmentation was often advanced in this context. It means “not only specialisation but also mutual ignorance or, at least, mutual disinterest.” However, as noted, the relation between IIL and IEL is changing towards a positive integration which affects as well the normative development of these two branches and which might eventually overcome fragmentation.

The tendency to include non-commercial values in IIAs can be attributed to two changes in policy. First, in a globalized world where crossing borders is not an issue anymore and foreign direct investment is growing, the exploitation of natural resources is increasing as well. Aggravated by recent environmental crises the list of

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19 M. Jacob, ‘Investments, Bilateral Treaties’, above 5, § 16.
20 It should not be forgotten to evaluate the scope of such chapters within each FTA. See for example the EFTA-Singapore FTA 2002 which recognises in its preamble the importance of the protection and preservation of the environment. However, it does neither include a specific chapter on the protection of the latter, nor other specific or substantive rules on the environment. The EFTA-Hong Kong FTA 2011 on the other hand, contains a specific chapter on the environment (chapter 8) which applies to the other chapters of the agreement through its article 8.2.
global threats to the environment expands continuously. Yet, these events encourage a powerful civil society, keen on tackling the necessary changes. A high quality of the environment is a necessary component of the prosperity of civilisation and future generations. The growing awareness of global environmental problems may have pushed for an increased use of environmental language in IIAs.\(^{23}\) Second, new markets and environmental opportunities open up with the greening of the economy. Emerging policies recognize the role of investment as a primary driver of economic growth and sustainable development: environmental goals can be achieved through responsible investment.\(^{24}\) Hence, the private sector plays an important role in providing the main part of the environmentally sustainable investment in the future.\(^{25}\)

Much has to be attributed to North American practice, in particular solutions introduced by the North American Free Trade Agreement (NAFTA)\(^{26}\) concluded in 1992 and entered into force in 1994. In the last decade, Mexico, Canada and the USA facing many investor-State disputes, have undertaken substantive changes to their investment strategies by learning from the NAFTA regime.\(^{27}\)

This paper does not challenge the BIT network and more broadly IIAs per se, but it seeks for a necessary change in how these treaties are conceived. Keeping this in mind, it is crucial to address current problems of the international landscape and thus include clauses concerning inter alia environmental protection. Hence, the paper welcomes innovations that address substantive investment and environmental obligations in IIAs.

However, not all efforts to widen the thematic scope have been met with success.\(^{28}\) For example the Norwegian Model BIT of 2007 was abandoned after harsh critic from the public.\(^{29}\) Indeed, it is a difficult task to balance both investment and environmental protection. The concept of the right to regulate is of particular importance when seeking a proper balance between private and public interests and when achieving an inclusion of public concerns, such as the environment, in IIAs.


\(^{24}\) UNCTAD, *Towards a new generation of international investment policies: UNCTAD’s fresh approach to multilateral investment policy-making*, above 1, p. 2-4.


\(^{28}\) M. Jacob, ‘Investments, Bilateral Treaties’, above 5, § 77.

\(^{29}\) From 2005 until 2013 a coalition of the Labour Party, the Socialist Left Party and the Centre Party formed the Norwegian government. The Socialist Left Part and the Centre Party together with non-governmental environmental and development organisations opposed strongly to the new Model BIT because for them it restrained unduly the government’s ability to regulate in the public interest, whereas large parts of the business felt that the proposed Model did not provide investors with enough protection. In fact, the responses were so polarized that the Model BIT was finally abandoned. See D. Vis-Dunbar, ‘Norway shelves its draft model bilateral investment treaty’, in *investment treaty news*, 2009, available at: http://www.iisd.org/itn/2009/06/08/norway-shelves-its-proposed-model-bilateral-investment-treaty/ (accessed on 10 February 2014).
3.3. The concept of the right to regulate

With the conclusion of an IIA the host State confines its policy space in order to grant the foreign investors different rights aimed at protecting their investments. Those guarantees in turn may attract foreign direct investment. For a long time, this approach seemed adequate and was never questioned. However, as national and international policy develop, and especially the case law on investment arbitration evolves to a perceived systemic disequilibrium in favour of the foreign investors, the necessity of a shift towards rebalancing investors’ and host States’ rights and obligations in IIAs becomes apparent.

It was argued that the function of investment protection of the IIA regime restrains unduly the ability of the host States to pursue sustainable development policies. Furthermore, since BITs run traditionally only few pages, the interpretative power of arbitral tribunals has been particularly large. When making use of their interpretative power, arbitral tribunals are very reluctant to take into account defences based on public concerns, such as the environment. For this reason, very often a breach of the host State’s obligations of investor protection is stated and results in an expensive award. Therefore, States are trying to guide or even delimit the interpretative power of arbitral tribunals in order to safeguard their right to pursue public policy objectives.

Thus, the right to regulate has become a key component of new generation treaty negotiations. Seeking for a proper balance between investment liberalization and promotion on the one hand and regulating in the public interest on the other hand, the European Union (EU) and the United States (US) have been particularly involved with the promotion of the right to regulate, pushing it into the spotlight of current IIAs negotiation challenges. As a result, a proper balance between private and public interests would also contribute to the legitimacy of the international investment system.

3.4. Definition of the right to regulate

In this section a short definition of the right to regulate should be given. A genuine right to regulate was defined by one author as “the legal right exceptionally permitting

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32 A. Titi, The Right to Regulate in International Investment Law, Nomos and Dike, 2014, p. 19, see as well chapter IV; European Parliament, Investor-State Dispute Settlement (ISDS) provisions in the EU’s international investment agreements, Volume 2 - Studies, above 14, pp. 73-5.
the host State to regulate in derogation of international commitments it has undertaken by means of an investment agreement without incurring a duty to compensate. Defined like this the right to regulate in the investment context has a narrower sense as the right to regulate \textit{lato sensu}, a basic attribute of State sovereignty under international law. The right to regulate \textit{lato sensu} implies the State’s freedom to engage in political, economic, legislative and other regulatory activity which the State considers appropriate. An IIA would precisely impose restrictions on the State’s freedom \textit{lato sensu}.

Three comments seem indispensable with regard to the above definition of the right to regulate. First, it is a legal right, which is safeguarded through conventional law, by general exceptions clauses or explicit right to regulate clauses or even other treaty-based exceptions or through general international law. Hence, it can be independent of its express incorporation in an IIA. \footnote{Ibid., p. 33.} Second, there is no duty to compensate. This is not only important in the expropriation context, its meaning goes further: the right to regulate exempts the host State from the typical compensation requirement \textit{vis-à-vis} an aggrieved investor. Otherwise, if the host State would have to compensate its regulation, the right would be deprived of its meaning, as the duty to compensation would impair the willingness of the host State to make use of its freedom of action. The arbitral tribunal said in \textit{Marvin Feldman v. Mexico} \footnote{Ibid., p. 33.}:

\begin{quote}
103. The Tribunal notes that the ways in which governmental authorities may force a company out of business, or significantly reduce the economic benefits of its business, are many. In the past, confiscatory taxation, denial of access to infrastructure or necessary raw materials, imposition of unreasonable regulatory regimes, among others, have been considered to be expropriatory actions. At the same time, governments must be free to act in the broader public interest through protection of the environment, new or modified tax regimes, the granting or withdrawal of government subsidies, reductions or increases in tariff levels, imposition of zoning restrictions and the like. Reasonable governmental regulation of this type cannot be achieved if any business that is adversely affected may seek compensation, and it is safe to say that customary international law recognizes this (see infra para. 105). \footnote{Ibid., § 103.}
\end{quote}

A recent doctrine proposes to vary the obligation to compensate according to the principle of proportionality borrowed from the European Court of Human Rights (ECtHR). \footnote{Ibid., § 103.} This doctrine does not increase significantly the legal certainty because it leaves the proportionally test to the discretion of the arbitrator; no predictable sphere of regulatory freedom for the host State can thus be foreseen. \footnote{Ibid., § 103.} Third, this paper suggests leaving out the term ‘exceptionally’ in the definition submitted above. In fact, the suitability of including this term depends on one’s point of view. The approach consists either in admitting that the host State has confined its regulatory power by concluding an IIA and thus (general) exceptions have to be introduced in order to list the measures for which the host State keeps its regulator power, or the approach lies in acknowledging that the host State has anyway the right to regulate \textit{lato sensu} (which can be affirmed for example in an explicit right to regulate clause)

\footnote{A. Titi, \textit{The Right to Regulate in International Investment Law}, above 32, p. 33.}

\footnote{Ibid., p. 33.}

\footnote{Marvin Roy Feldman Karpa v. United Mexican States, ICSID Case No. ARB(AF)/99/1, Award, 16 December 2002.}

\footnote{Ibid., § 103.}

\footnote{See for example A. Kulick, \textit{Global Public Interest in International Investment Law}, above 31. See as well with regard to expropriation Técnicas Medioambientales Tecmed, S.A. v. The United Mexican States, ICSID Case No. ARB (AF)/00/2, Award, 29 May 2003, § 122.}

\footnote{A. Titi, \textit{The Right to Regulate in International Investment Law}, above 32, pp. 34-5.}
and special exceptions should be introduced when such right should be exceptionally restricted. Indeed, there are two possibilities of how these two approaches to the concept of the right to regulate can be introduced in an IIA: either through general exceptions clauses or by incorporating an explicit right to regulate clause.

PART II

Recently concluded IIAs illustrate the growing tendency of the inclusion of environmental language. In Part I, the need for the insertion of public interest clauses, in particular environmental protection clauses, in IIAs has been acknowledged. In Part II, the current panorama of clauses including environmental language found in IIAs is considered and provision samples are provided. Background information is given and problems that may arise during treaty writing are addressed.

1. Including environmental language into IIAs

There are two main ways of integrating environmental protection in IIAs. Host States can either ensure that the inserted clauses are not subject to restrictions that prevent them from achieving public interest issues, especially that they are not restricted in adopting favourable environmental regulations. Or, IIAs can comprehend obligations for the investors themselves to protect the environment. Despite the multitude of BITs and FTAs and differences in drafting, recurring clauses in IIAs related to the environment are crystalizing.

For the purpose of this paper, only the right to regulate in the public interest with regard to the protection of the environment is analysed. There are other types of regulatory interests, such as human rights, essential security interests or public order that are not considered in this paper. A right to regulate clause can be drafted in many different ways and the concept as such influences almost all types of clauses analysed below. In contrast, CSR clauses and clauses which impose environmental

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43 See Part II subsection 2.5 for explicit right to regulate clauses and subsection 2.10 for general exceptions clauses.
44 If not indicated otherwise, all Agreements and Model BITs referred to in Part II and III can be found in UNCTAD’s International Investment Agreements Navigator, available at: http://investmentpolicyhub.unctad.org/IIA (accessed last on 30 April 2015). It should be considered that many of the cited agreements have not entered into force at the time of writing.
46 A. Titi, The Right to Regulate in International Investment Law, above 32, p. 100, for an analysis see chapter V.
47 The concept of the right to regulate can be retrieved from explicit right to regulate clauses, general exception clauses, performance requirements clauses and clarifications on indirect expropriation clauses. If such clauses assure their rationale, that is to secure a genuine right to regulate to the host State, is a different question, which will be analysed for each clause in particular.
obligations on the investors have to be distinguished since their rationale is to insert (soft) obligations for the investors themselves.

2. Types of recurring clauses in IIAs with regards to environmental protection

Twelve types of clauses featuring environmental language commonly found in IIAs can be distinguished.

<table>
<thead>
<tr>
<th>Types of recurring clauses in IIAs with regard to environmental protection</th>
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<tbody>
<tr>
<td>1. General references to environmental concerns in preambles</td>
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<tr>
<td>2. Defining environmental legislation</td>
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<tr>
<td>3. Indirect expropriation - understanding that non-discriminatory environmental regulation does not constitute indirect expropriation</td>
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<tr>
<td>4. Performance requirements</td>
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<tr>
<td>5. Explicit right to regulate clauses - reserving policy space for environmental regulation</td>
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<tr>
<td>6. Not lowering environmental standards - discourage the loosening of environmental regulation in order to attract foreign investment</td>
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<tr>
<td>7. Encourage progress of environmental protection and cooperation</td>
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<tr>
<td>8. Reference to and coordination with international environmental instruments</td>
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<td>9. Promotion of Corporate social responsibility and investors’ environmental obligations</td>
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<tr>
<td>10. General exceptions</td>
</tr>
<tr>
<td>11. Limiting access to ISDS - excluding the application of the treaty’s dispute settlement mechanisms for the provisions regarding the environmental concerns</td>
</tr>
<tr>
<td>12. Recourse to environmental experts by arbitration tribunals</td>
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</tbody>
</table>

Negotiators opt for different mechanisms when incorporating environmental objectives in IIAs. These options include adjusting existing provisions, adding new ones or omitting common clauses. Many categorizations of such clauses are suggested in the latest literature.\(^{48}\) This paper proposes a classification according to the general structure of BITs. The different types of clauses are discussed in more detail in the subsequent sections.

\(^{48}\) For example, DI BENEDETTO, taking the dimension of the case law, proposes to classify environmental language found in IIAs in terms of the interpretative value for an arbitral tribunal – internal or external arguments and legal exceptions. However, this paper opts for the viewpoint of a treaty negotiator rather then to ask for the implications of such clauses within a concrete dispute settlement. Thus, it follows the usually set-up of BITs.
2.1. General references to environmental concerns in preambles

The fundamental objective of BITs is the promotion and protection of foreign investment. Yet, such instruments sometimes pursue other goals like the encouragement of mutual relationships between States or the economic development of the host State. However, these objectives are naturally related to investment and do not truly take into account environmental concerns.49

Genuine reference to the environment can be found in recent new generation agreements. According to the two latest World Investment Reports, 13 out of the 18 IIAs concluded in 2013, and 12 out of 17 IIAs concluded in 2012 contain environmental language or sustainable development goals.50 Since FTAs have a wide regulating scope, which does not only include trade and investment matters, but also social and environmental aspects, they make easier reference to the environment in their preambles as well as in their substantive parts.51

Many examples of general reference to environmental protection in preambles can be found. Such environmental language varies from a simple recognition of sustainable development52 to very extensive and far-reaching commitments53. For example the NAFTA or the Energy Charter Treaty (ECT)54 as well as many of the US BITs include favourable preambular language.55 The NAFTA, signed in 1992 and entered into force in 1994, is a precursor when it comes to preambular environmental language.56 In the bilateral context, three BITs signed by the US in 199457, all of them base on the US Model BIT 1994, initiated the US practice to include environmental language in BITs’ preambles.58 The NAFTA preamble contains the following text:

UNDERTAKE each of the preceding in a manner consistent with environmental protection and conservation;

PRESERVE their flexibility to safeguard the public welfare;

PROMOTE sustainable development;

STRENGTHEN the development and enforcement of environmental laws and regulations;59

The ECT as a sectoral agreement guiding trade and investments in the energy segment uses a more extensive language and addresses multilateral environment agreements explicitly, which is a rather unique way of drafting.60

50 UNCTAD, World Investment Report 2014, above 4, pp. 116-8; UNCTAD, World Investment Report 2013, above 45, pp. 102-3. The review only contained agreements for which a text was available.
52 For example, Benin-Canada BIT 2013.
53 See for example, EFTA-Hong Kong FTA 2011.
57 US-Uzbekistan BIT 1994; US-Georgia BIT 1994; US-Trinidad and Tobago BIT 1994. All those preambles read in the important part: Agreeing that these objectives can be achieved without relaxing health, safety and environmental measures of general application.
59 Preamble of the NAFTA.
Recalling the United Nations Framework Convention on Climate Change, the Convention on Long-Range Transboundary Air Pollution and its protocols, and other international environmental agreements with energy-related aspects; and Recognizing the increasingly urgent need for measures to protect the environment, including the decommissioning of energy installations and waste disposal, and for internationally-agreed objectives and criteria for these purposes;61

Two ways of drafting are recurrent in BITs. One of them is illustrated by the US Model BIT 2012:

Desiring to achieve these objectives in a manner consistent with the protection of health, safety, and the environment, and the promotion of internationally recognized labor rights;62

Whereas the other approach refers to the maintenance of standards which can be found for example in the Japan-Uruguay BIT 2015:

Recognizing that these objectives can be achieved without relaxing health, safety and environmental measures of general application;63

For a more extensive example, the Austrian Model BIT 2010 includes both the ‘in a manner consistent with’ wording and the ‘without relaxation of standards of protection’ phrasing. Further it leaves room for CSR by expressly incorporating soft law from this field:

COMMITTED to achieving these objectives in a manner consistent with the protection of health, safety, and the environment, and the promotion of internationally recognised labour standards;

EXPRESSING their belief that responsible corporate behaviour, as incorporated in the OECD Guidelines for Multinational Enterprises, can contribute to mutual confidence between enterprises and host countries; EMPHASISING the necessity for all governments and civil actors alike to adhere to UN and OECD anti-corruption efforts, most notably the UN Convention against Corruption (2003); TAKING NOTE OF the principles of the UN Global Compact;

ACKNOWLEDGING that investment agreements and multilateral agreements on the protection of environment, human rights or labour rights are meant to foster global sustainable development and that any possible inconsistencies there should be resolved without relaxation of standards of protection;64

The Southern African Development Community (SADC) Model BIT 2012 expressly includes the right to regulate in its preamble:

Recognizing the important contribution investment can make to the sustainable development of the State Parties, including the reduction of poverty, increase of productive capacity, economic growth, the transfer of technology, and the furtherance of human rights and human development;

Seeking to promote, encourage and increase investment opportunities that enhance sustainable development within the territories of the State Parties;

61 Preamble of the ECT (in parts).
63 Preamble of the Japan-Uruguay BIT 2015 (in parts). The Turkey Model BIT 2009 uses a similar wording, including also labour rights.
64 Preamble of the Austrian Model BIT 2010 (in parts; emphasis added).
Understanding that sustainable development requires the fulfilment of the economic, social and environmental pillars that are embedded within the concept;

Reaffirming the right of the State Parties to regulate and to introduce new measures relating to investments in their territories in order to meet national policy objectives, and—taking into account any asymmetries with respect to the measures in place—the particular need of developing countries to exercise this right;

Seeking an overall balance of the rights and obligations among the State Parties, the investors, and the investments under this Agreement.

However, none of the following Model BITs include a reference to the environment in their preambles: the German Model BIT 2008, the UK Model BIT 2008, the Colombian Model BIT 2008, the Ghanaian Model BIT 2008, the Mexican Model BIT 2008.

The treaty preamble does not set out binding obligations but plays a significant role in interpreting substantive IIA provisions. When preambular text enounces as sole objective the promotion and protection of foreign investment, then tribunals will be prone to dismantle interpretive uncertainties in favour of investors. A teleological interpretation after Article 31 of the Vienna Convention on the Law of Treaties will lead to an asymmetric interpretation allowing little room for the legitimate interests of a host State.

In contrast, when including values external to investment protection, a contextual or teleological interpretation will be much more followed and a more balanced interpretation can be reached. Thus, the investment regime would not be isolated from the body of international law, quite the contrary; such interpretation will support coherence between diverse policy objectives and bodies of law. In particular, investment rules would not be conceived as only oriented to protect property value. The Austrian Model BIT 2010 is very ambitious in this regard. It does not include an explicit reference of the objective of the protection of investments in its preamble, which is remarkable when considering that the main purpose of such treaties is (or historically was) the protection of reciprocal investment. The Norwegian Model BIT 2007, which failed to be adopted, is often cited as well, as it includes a very holistic list of recitals favouring environmental language and more broadly the right to regulate for public purposes. However, Model BITs like Austria’s 2010 or Norway’s 2007 with ample regulatory commitments are rare.

Regardless of how favourable environmental friendly language in preambles is, as mentioned above, preambles do not create rights and obligations between parties.

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65 Preamble of the SADC Model BIT 2012 (in parts; emphasis added).
69 A. Titi, The Right to Regulate in International Investment Law, above 32, p. 119. See as well Plama Consortium Limited v. Bulgaria, ICSID Case No. ARB/03/24, Decision on Jurisdiction, 8 February 2005, § 193.
They rather provide guidance for the interpretation of the objectives of the treaty.\textsuperscript{71} Consequently, in this paper it is argued that next to the preambular environmental language, it is crucial to introduce in the substantive part of the treaty a clear obligation for investors and host States to respect the (future) environmental legislation in question. If the ultimate aim is to safeguard our planet from environmental degradation, loose preambular text is not sufficient to achieve this goal. When much is left to interpretation, then also much is left to the discretion of the arbitrator. This in turn weakens legal security and predictability, fundamental basis for investment protection.

It is possible that one arbitral tribunal in its interpretation is more responsive to environmental protection and another more open to investment protection.\textsuperscript{72} The Metalclad \textit{v. Mexico}\textsuperscript{73} and the \textit{S.D. Myers \textit{v. Canada}}\textsuperscript{74} cases, both based on the very same text, namely the NAFTA, are very demonstrative in this context. In \textit{Metalclad \textit{v. Mexico}} the arbitral tribunal failed to make any reference to NAFTA’s preambular language referring to the environment,\textsuperscript{75} even though the parties addressed such language in their pleadings.\textsuperscript{76}

The facts of the case are the following: COTERIN, a Mexican company, received from the federal government of Mexico a permit to construct and operate a transfer station for hazardous wastes and a permit to construct and operate a station and a landfill. Shortly after, Metalclad, a US corporation, purchased COTERIN including all its licenses. The local government of San Luis Potosí, where the transfer station and the landfill were supposed to be located, started a campaign against the project. However, the government of Mexico repeatedly assured that Metalclad was entitled to build and operate the landfill. After the beginning of its operation, protesters blocked the site, so that Metalclad was effectively prevented from operating the landfill. In response to that, the government of Mexico and Metalclad signed a \textit{convenio} including Metalclad’s right to operate.\textsuperscript{77} However, the local government of San Luis Potosí by Ecological Decree declared the region a natural area for the protection of cactuses. According to Metalclad this definitely cancelled any possibility of opening the landfill. Metalclad entered into ICSID arbitration contenting violation of NAFTA Articles 1105 (fair and equitable treatment (FET)) and 1110 (expropriation).

The arbitral tribunal found that the municipality’s actions were imputable to Mexico and thus both FET\textsuperscript{78} and indirect expropriation\textsuperscript{79} clauses of NAFTA were

\textsuperscript{71}\footnotesize{See Article 31(1) and (2) of the Vienna Convention on the Law of Treaties.}
\textsuperscript{72}\footnotesize{Certainly, this argumentation assumes a conflict between investment and environmental protection.}
\textsuperscript{73}\footnotesize{Metalclad Corporation \textit{v. The United Mexican States}, ICSID Case No. ARB(AF)/97/1, Award, 30 August 2000.}
\textsuperscript{74}\footnotesize{\textit{S.D. Myers, Inc. \textit{v. Government of Canada}}, UNCITRAL, Partial Award, 13 November 2000.}
\textsuperscript{75}\footnotesize{The NAFTA preamble enounces in particular: \textit{UNDERTAKE} each of the preceding in a manner consistent with environmental protection and conservation; \textit{PRESERVE} their flexibility to safeguard the public welfare; \textit{PROMOTE} sustainable development; \textit{STRENGTHEN} the development and enforcement of environmental laws and regulations.}
\textsuperscript{77}\footnotesize{Metalclad Corporation \textit{v. The United Mexican States}, above 73, \S 47.}
\textsuperscript{78}\footnotesize{\textit{Ibid.}, \S\S 74-101.}
\textsuperscript{79}\footnotesize{\textit{Ibid.}, \S\S 101-12.}
violated. However, the tribunal refrained from considering any preambular environmental language or regulatory competence of Mexico.80

The paradigm changes fundamentally in the S.D. Myers v. Canada case. S.D. Myers is a US company specialized in PCB (polychlorinated biphenyls) remediation, which is mainly used in electrical equipment, highly toxic for humans and, when not correctly destructed, remains in the environment for a very long time. Canada and the USA concluded the Transboundary Agreement in 198681 allowing PCB export to each other. In 1989 Canada acceded to the Basel Convention,82 which the USA had signed but not ratified at the time the dispute arose. Consequently, Canada closed the common border with the USA for about one and a half years for cross-border movements of PCB waste. S.D. Myers therefore claimed violation of Canada’s obligation under NAFTA Chapter 11 (national treatment and FET); Canada asserted its obligations under the Transboundary Agreement and the Basel Convention. The arbitral tribunal recalled parts of the preamble83, and declared that:

The Preamble to the NAFTA, the NAAEC and the international agreements affirmed in the NAAEC suggest that specific provisions of the NAFTA should be interpreted in light of the following general principles:

• Parties have the right to establish high levels of environmental protection. They are not obliged to compromise their standards merely to satisfy the political or economic interests of other States;
• Parties should avoid creating distortions to trade;
• environmental protection and economic development can and should be mutually supportive.84

When these cases are compared to each other, it becomes apparent that they are very controversial. One does not even consider preambular environmental language, whereas the other allows environmental language to enter the arbitration. It seems that allowing environmental considerations found in preambles is entirely left to the discretion of the arbitral tribunal. To preclude such disparate case law, it is necessary to ensure clear textual language in the IIAs’ preambles.

On the one hand, general preambular objectives leave much room for dynamic interpretation. In evolving fields, like the IIL and IEL, quick adaptations are required. If an agreement contains general language on environmental protection it favours the observance of the rapid evolution of environmental concerns in its interpretation. On the other hand, a more narrow approach or even defined objectives in preambular text (for example the ECT) limit the scope of considering emerging concerns regarding the

80 M. Potestà, ‘Mapping Environmental Concerns in International Investment Agreements’, above 27, p. 198; A. Kulick, Global Public Interest in International Investment Law, above 31, p. 239.
84 S.D. Myers, Inc. v. Government of Canada, above 74, § 220. Furthermore, the arbitral tribunal acknowledged that the NAFTA provided for international environmental instruments and they could trump the investment chapter, see § 214.
environment by an arbitral tribunal. However, to emphasis their importance today, it is suggested to combine generic environmental language with language that addresses more explicitly specific environmental concerns such as climate change or biodiversity. Furthermore, preambles do usually not establish a hierarchy between the different objectives they wish to attain. \(^{85}\) When including environmental objectives in the preamble next to investment protection aims, it is of paramount importance to acknowledge the mutual supportiveness of investment protection and environmental goals. \(^{86}\)

To summarise, preambles are a good place to accommodate a balance of interests between investment protection and other objectives such as environmental protection. Combining environmental preambular language with substantive obligations to protect the environment assures best the protection of the environment.

### 2.2. Defining environmental legislation

The approach to define the term environmental legislation in a clause is used by the Belgium/Luxembourg Economic Union and by the US. The Belgium/Luxembourg-Colombia BIT 2009 contains the following definition:

5. "environmental legislation" means:

5.1 In the case of the Kingdom of Belgium, the Grand-Duchy of Luxembourg, the Walloon Region, the Flemish Region and the Brussels-Capital Region, any legislation or provision thereof, the primary purpose of which is the protection of the environment, or the prevention of a danger to human, animal, or plant life or health, through:

a. the prevention, abatement or control of the release, discharge, or emission of pollutants or environmental contaminants;

b. the control of environmentally hazardous or toxic chemicals, substances, materials and wastes, and the dissemination of information related thereto;

c. the protection or conservation of wild flora or fauna, including endangered species, their habitat, and specially protected natural areas in the Contracting Party's territory; and

5.2 In the case of Colombia, any law enacted by Congress, or decree or resolution issued by the central level of government, or provision thereof, the primary purpose of which is the protection of the environment, or the prevention of a danger to human, animal, or plant life or health, through:

a. the prevention, abatement or control of the release, discharge, or emission of pollutants or environmental contaminants;

b. the control of environmentally hazardous or toxic chemicals, substances, materials and wastes, and the dissemination of information related thereto;

c. the protection or conservation of wild flora or fauna, including endangered species, their habitat, and specially protected natural areas in the Contracting Party's territory. \(^{87}\)

In the case of the Belgium/Luxembourg Economic Union the clause, which defines environmental legislation, is combined with a clause that reserves the right to establish its own levels of domestic environmental protection. \(^{88}\) It reads:


\(^{86}\) On this matter see Part II subsection 2.8.

\(^{87}\) Article I(5) of the Belgium/Luxembourg-Colombia BIT 2009.
1. Recognising the right of each Contracting Party to establish its own levels of domestic environmental protection and environmental development policies and priorities, and to adopt or modify accordingly its environmental legislation, each Contracting Party shall strive to ensure that its legislation provides for high levels of environmental protection and shall strive to continue improving this legislation.\(^90\)

In spite of the good intention of such a clause, words as ‘shall strive’ are weak language because they impose only aspirational obligations.\(^90\) Furthermore, the effectiveness of the clause is limited by the narrow definition of environmental legislation. By establishing an enumeration, the definition excludes some measures a State would be willing to take in order to attain environmental protection. Measures not falling into the list are apparently excluded. It is unclear how extraterritorial measures addressing for example transboundary pollution or climate change would fit into one of the three categories.\(^91\) Besides, it is noteworthy that the level of domestic environmental protection can either be a very high or a very low standard.\(^92\) When such a clause has reasonably a high value in an environmental protective economy, exact the opposite is true in a country with low environmental standards. Before an arbitral tribunal, the host State may argue the right of establishing its own levels of protection, which in this case would be a low level of environmental protection.

The US Model BIT 2012 enounces:

4. For the purposes of this Article, “environmental law” means each Party’s statutes or regulations,\(^16\) [Footnote 16 enounces: For the United States, “statutes or regulations” for the purposes of this Article means an act of the United States Congress or regulations promulgated pursuant to an act of the United States Congress that is enforceable by action of the central level of government,] or provisions thereof, the primary purpose of which is the protection of the environment, or the prevention of a danger to human, animal, or plant life or health, through the:

(a) prevention, abatement, or control of the release, discharge, or emission of pollutants or environmental contaminants;

(b) control of environmentally hazardous or toxic chemicals, substances, materials, and wastes, and the dissemination of information related thereto; or

(c) protection or conservation of wild flora or fauna, including endangered species, their habitat, and specially protected natural areas, in the Party’s territory, but does not include any statute or regulation, or provision thereof, directly related to worker safety or health.\(^93\)

The United States also combines the clause that defines environmental law with a clause that recognizes the important role of environmental law. It reads:

Article 12: Investment and Environment

1. The Parties recognize that their respective environmental laws and policies, and multilateral environmental agreements to which they are both party, play an important role in protecting the environment.\(^94\)

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89 Article VII(1) of the Belgium/Luxembourg-Colombia BIT 2009 (emphasis added).
92 See as well A. Kulick, *Global Public Interest in International Investment Law*, above 31, p. 70.
93 Article 12(4) of the US Model BIT 2012.
94 Article 12(1) of the US Model BIT 2012 (emphasis added).
Such a clause can at most play a role in guiding the arbitrators’ interpretation of the treaty. The term ‘recognize’ does not amount to any binding obligation. Furthermore, the clause only considers multilateral environmental agreements (MEAs) to which both States are parties.

In summary, defining environmental legislation clauses which are combined with clauses that reserve environmental laws, is at most of interpretative value when considering a case raising environmental issues. They do not create substantive obligations to protect the environment.

2.3. Non-discriminatory environmental regulation does not constitute indirect expropriation

Expropriation of foreign investment remains one of the most relevant issues discussed in the investment field. International law traditionally recognises the right of States to take alien property by virtue of their territorial sovereignty. However four requirements have to be met for the expropriation to be legal: the measure must serve a public purpose, it must be neither arbitrary nor discriminatory, the expropriation procedure must be consistent with the principles of due process and finally the measure must be accompanied by prompt, adequate and effective compensation. It is safe to conclude that these four requirements form part of customary international law today.

Further there has to be distinguished between direct and indirect expropriation. The former entails a formal transfer of the property’s title to the host State or by outright physical seizure. The latter refers to situations where measures adopted by host States by means of their regulatory action tantamount de facto to expropriation. That is when the investors’ assets and rights are deprived of any real value without a

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96 General Assembly resolution 1803 (XVII) of 14 December 1962, Permanent Sovereignty Over Natural Resources, § 4.
97 Regarding the current case law, the determining factor is the actual discriminatory effect of the measure, rather than the intent of the host State that adopted the measure in question. See for example Siemens A.G. v. The Argentine Republic, ICSID Case No. ARB/02/8, Award, 17 January 2007, § 321.
98 Regardless of whether the requirement of due process is expressly incorporated in the treaty text, or forming part of the international minimum standard and the FET principle.
99 This is the most controversial requirement. ‘Prompt’ means that the compensation follows due course. The compensation is ‘effective’ when it is offered in directly transferable currency. And for the compensation to be ‘adequate’ it is required that the amount to be paid is “based on the fair market value of the taken asset as such value is determined immediately before the time at which the taking occurred or the decision to take the asset became publicly known” (World Bank Guidelines on the Treatment of Foreign Direct Investment, Section IV(3), available at: http://www-wds.worldbank.org/servlet/WDSContentServer/WDSP/IB/1999/11/10/000094946_9909080530308 2/Rendered/PDF/multi_page.pdf (accessed on 22 April 2015)). See also European Parliament, Investor-State Dispute Settlement (ISDS) provisions in the EU’s international investment agreements, Volume 2 - Studies, above 14, p. 21.
101 With regard to indirect expropriation, general regulation and targeted measures can be distinguished. A targeted measure is not general but individual and specific (e.g. termination of a contract, not renewal of a licence, etc.), but it does not mean that the measure is therefore also discriminatory. Case law suggests that targeted measures are more likely to tantamount to indirect expropriation than general regulatory measures. General regulatory measures should only exceptionally amount to indirect expropriation. See J. E. Viñuales, Foreign Investment and the Environment in International Law, above 15, pp. 294-5, 297, 306-7.
formal transfer of the title or a seizure.\textsuperscript{102} For example, the host State may adopt new environmental laws which affect the fiscal or regulatory regime under which the investment was originally made, thus making it \textit{de facto} impossible for the investor to carry on with its business and therefore depriving its assets of any real value.

Environmental regulation is very dynamic and typically open-ended. New scientific discoveries may lead to policy changes that are hard to foresee at the beginning of a particular investment. The major concern of foreign investors is thus not the environmental regulation \textit{per se}, but rather the surprise aspect of regulatory changes that may distort the fiscal and regulatory regime under which the investment was originally made. “No foreign investor will complain about an existing high-level environmental regime prior to making the investment.”\textsuperscript{103} Foreign investors usually make a risk/reward assessment before bringing their capital into the host State. If the project seems too risky, they go elsewhere. Further, States may have different views on what constitutes effective protection of the environment. Therefore, the focus of the present analysis lies on the uncertainty of environmental regulation in the future rather than on the scrutiny of existing environmental regulations at the beginning of an investment process.\textsuperscript{104}

As will be explored below, there exists ample case law on situations of expropriations for a public purpose. It is generally accepted that the protection of the environment is a legitimate public purpose.\textsuperscript{105} Indeed, foreign investors do usually not challenge the host State’s determination of what constitutes a measure serving the public purpose, for such determination is after all an expression of the host State’s sovereignty.\textsuperscript{106} Rather the question is if the host State has to pay compensation to the foreign investor for taking the property. With regard to \textit{direct} expropriation the \textit{Santa Elena v. Costa Rica}\textsuperscript{107} case is illustrative.

In 1978, Costa Rica, by decree, declared the expropriation of the territory belonging to Santa Elena, a company whose shares were held by US nationals. The expropriation as such was not contested but the amount of compensation for the expropriation. Santa Elena claimed 6’400’000 US dollars, whereas the decree by the Costa Rican government amounted to only 1’900’000 US dollars.

First, the arbitral tribunal determined the relevant date for the evaluation of the amount due and second, analysed if simple or compound interests had to be paid since the ICSID arbitration was introduced 20 years after the expropriation. The tribunal declined to consider any evidence submitted by Costa Rica as to its international


104 The issue of attracting new investments with lax environmental regulations and standards is being addressed within IIAs with another clause: the ‘not lowering environmental standards’ clause, see Part II sub-section 2.6.


106 \textit{Ibid.}, p. 214.

107 \textit{Compañía del Desarrollo de Santa Elena, S.A. v. Republic of Costa Rica, ICSID Case No. ARB/96/1, Final Award, 17 February 2000.}
obligations to preserve the environment. It held that since every expropriation requires a public purpose, the Costa Rican government still had to pay compensation:

Expropriatory environmental measures — no matter how laudable and beneficial to society as a whole — are, in this respect, similar to any other expropriatory measures that a State may take in order to implement its policies: where property is expropriated, even for environmental purposes, whether domestic or international, the State’s obligation to pay compensation remains.

In sum, if the direct expropriation served a public purpose, e.g. environmental protection, was conducted in a non-discriminatory manner and was in accordance with due process of law, the host State has to pay prompt, adequate, and effective compensation and the expropriation will in turn be legal. Thus, when a host State expropriates a foreign investor directly, even for genuine reasons aimed at protecting the environment, customary international law does not exclude the host State’s obligation to pay compensation.

However, this principle is far from consolidated in the event of an alleged indirect expropriation. Indeed, drawing the line between legitimate non-compensable regulations by host States affecting adversely the economic value of foreign investments and indirect expropriation requiring compensation is a difficult task. It is commonly recognised that States have the sovereign power to adopt environmental regulations of general application. However, if States would have to pay full compensation every time they regulate environmental matters which affect the investors’ interests adversely, then States might tend not to expropriate for the reason of fearing to have to pay huge amounts of compensation. The duty to compensate environmental regulations depriving the investor of its investment could lead to the phenomenon of ‘regulatory chill’. That is to say, if treaty provisions are limited to mere reservations of policy space, States may continue to be exposed to compensation claims for indirect expropriations. This in turn discourages modifications of environmental regulations or makes them very onerous. Hence, it is crucial to distinguish between regulatory measures that amount to indirect expropriation and measures that form part of the legitimate competence of a State to regulate.

An OECD report in 2004 noted the reluctance of scholars to introduce clear criteria for distinguishing legitimate regulatory measures not requiring compensation from indirect expropriation measures requiring compensation. The report noted the scholar’s preference of leaving the problem to the development of arbitral case law.

108 Ibid., § 71.
109 Ibid., § 72.
110 J. E. Vínuales, Foreign Investment and the Environment in International Law, above 15, p. 299.
113 OECD, Indirect Expropriation and the "Right to Regulate" in International Investment Law, above 102, pp. 9-10. See as well C. N. Brower and E. R. Hellbeck, ‘The Implications of National and International Environmental Obligations for Foreign Investment Protection Standards, Including Valuation: A Report from the Front Lines’, in International Investments and Protection of the Environment, The Role of Dispute Resolution Mechanisms, The International Bureau of the Permanent Court of Arbitration (ed.), Kluwer Law International, 2000, p. 28. BROWER and HELLEBECK note the dilemma tribunals are confronted with, when deciding if it is a legitimate regulation or if it is “the wolf of expropriation, dressed in regulatory sheep’s clothing”.

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While the Iran-United States Claims Tribunal and decisions arising under Article 1 of Protocol No. 1 of the European Convention for the Protection of Human Rights\textsuperscript{115} are prominent sources, further case law has been developed under the NAFTA and BITs.

At this point, it is of interest to note the police power doctrine that States may apply as a defence. The roots of this doctrine lay in North American scholarship and practice and in general international law. The police power doctrine was mainly applied in connection with non-compensable expropriations. It provides that general regulatory practice that pursues a public purpose is not to be considered an expropriation and thus does not entail an obligation to compensate, if the measure is enacted with due process and in a non-discriminatory manner, unless specific commitments had been given to the investor. The effect of the doctrine is thus not to exclude compensation. It is to exclude the qualification of the measure as amounting to expropriation. When the regulation does not amount to expropriation, then no compensation is due.\textsuperscript{116}

In a number of cases, arbitral tribunals have decided that general environmental regulations if enacted for a public purpose, with due process and in a non-discriminatory manner do not amount to expropriation and consequently no compensation was due.\textsuperscript{117} The \textit{Methanex case}\textsuperscript{118} opposed Methanex, which was the world’s largest producer of methanol, a feedstock for the gasoline additive MTBE (Methyl tert-butyl ether) and the US. Methanol and ethanol being interchangeable, ADM, a US corporation and the world’s largest producer of ethanol, lobbied heavily until California banned MTBE. Thereon, Methanex claimed violation of national treatment, FET and expropriation under NAFTA Articles 1102, 1105 and 1110.

The Tribunal dismissed Methanex’s claim on expropriation considering the adoption of general regulatory standards a basic attribute of State sovereignty. The investor is thus not entitled to compensation, provided that the host State enacts the measure with due process and in a non-discriminatory manner or unless specific commitments had been given.\textsuperscript{119}

In the Tribunal’s view, Methanex is correct that an intentionally discriminatory regulation against a foreign investor fulfils a key requirement for establishing expropriation. But as a matter of general international law, a non-discriminatory regulation for a public purpose, which is enacted in accordance with due process and, which affects, inter alios, a foreign investor or investment is not deemed expropriatory and compensable unless specific commitments had been given by the regulating government to the then putative foreign investor contemplating investment that the government would refrain from such regulation.\textsuperscript{120}


\textsuperscript{117} S.D. Myers, Inc. v. Government of Canada, above 74, § 281; Methanex Corporation v. United States of America, UNCITRAL, Final Award, 3 August 2005, Part IV, Ch. D, § 7; Glamis Gold Ltd v. United States of America, UNCITRAL, Award, 16 May 2009, §§ 356, 366; Chemtura Corporation (formerly Crompton Corporation) v. Government of Canada, UNCITRAL, Award, 2 August 2010, § 266.

\textsuperscript{118} Methanex Corporation v. United States of America, above 117.

\textsuperscript{119} \textit{Ibid.}, Part IV, Ch. D, §§ 6-18.

\textsuperscript{120} \textit{Ibid.}, § 7.
The *Glamis v. USA* case enounces with regard to regulatory takings, that tribunals:

often assess whether measures of a State constitute a non-compensable regulation or a compensable expropriation by examining, *inter alia*, (1) the extent to which the measures interfered with reasonable and investment-backed expectations of a stable regulatory framework, and (2) the purpose and character of the governmental actions taken.\(^{122}\)

To qualify as indirect or direct expropriation the property has to be taken. Whereas, the qualification for direct expropriation is simple, in the case of indirect expropriation, the threshold is determined by the degree of interference with the property right. For that, the *Glamis* tribunal proposes to consider the severity of the economic impact and its duration.\(^{123}\)

The *Saluka v. Czech Republic*\(^{124}\) tribunal did go even further, claiming that:

262. In the opinion of the Tribunal, the principle that a State does not commit an expropriation and is thus not liable to pay compensation to a dispossessed alien investor when it adopts general regulations that are “commonly accepted as within the police power of States” forms part of customary international law today.\(^{125}\)

As a response to the increasing case law in this field, new generation agreements provide explicit criteria of what constitutes an indirect expropriation.\(^{126}\) Generally today, three factors determine whether a case of indirect expropriation has occurred: the economic impact and duration of the measures, the degree of interference with reasonable investment-backed expectations and the object, context and intent of the measures.\(^{127}\)

More importantly, new generation agreements address the right to regulate. Clauses that enounce, that non-discriminatory environmental measures do not constitute indirect expropriations, were first introduce in US FTAs and the US and

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\(^{121}\) *Glamis Gold Ltd v. United States of America*, above 117.

\(^{122}\) *Ibid.*, § 356 (footnotes omitted).


\(^{124}\) *Saluka Investments BV v. Czech Republic*, UNCITRAL, Partial Award, 17 March 2006. Interestingly the Czech Republic-Netherlands BIT 1991 does neither specify what constitutes indirect expropriation nor does it contain a clause that excludes non-discriminatory public purpose regulation from the scope of indirect expropriation. The latter type of clause will be considered in the analysis below. It is precisely from the case law they developed.

\(^{125}\) *Saluka Investments BV v. Czech Republic*, above 124, § 262. However, the case concerned non-environmental regulation.


\(^{127}\) European Parliament, *Investor-State Dispute Settlement (ISDS) provisions in the EU’s international investment agreements, Volume 2 - Studies*, above 14, p. 20, fn. 83; OECD, *Indirect Expropriation and the "Right to Regulate" in International Investment Law*, above 102, pp. 10-20 (including reference to case law). The US Model BIT 2012 reads in Annex B(4): (a) The determination of whether an action or series of actions by a Party, in a specific fact situation, constitutes an indirect expropriation, requires a case-by-case, fact-based inquiry that considers, among other factors: (i) the economic impact of the government action, although the fact that an action or series of actions by a Party has an adverse effect on the economic value of an investment, standing alone, does not establish that an indirect expropriation has occurred; (ii) the extent to which the government action interferes with distinct, reasonable investment-backed expectations; and (iii) the character of the government action.
Canada Model BITs.\textsuperscript{128} In the last decade, these clauses have spread to BITs as well as other countries’ Model BITs. A 2011 OECD report notes that clauses, which state that environmental regulations do not constitute indirect expropriations, remain relatively rare,\textsuperscript{129} yet these clauses penetrate steadily into IIAs. Clauses that preclude environmental regulation from indirect expropriation claims can be found either in the provision addressing expropriation or in the annex of the specific agreement. Probably the most common phrasing of such a clause reads:

(4) Except in rare circumstances, such as when a measure or series of measures are so severe in the light of their purpose that they cannot be reasonably viewed as having been adopted and applied in good faith, non-discriminatory measures of a Contracting Party that are designed and applied to protect legitimate public welfare objectives, such as health, safety and the environment, do not constitute indirect expropriation.\textsuperscript{130}

The US or Ghanaian approach uses the following language:

(b) Except in rare circumstances, non-discriminatory regulatory actions by a Party that are designed and applied to protect legitimate public welfare objectives, such as [national security,]\textsuperscript{131} public health, safety, and the environment, do not constitute indirect expropriations.\textsuperscript{132}

The Gabon-Turkey BIT 2012 excludes the ‘except in rare circumstances’ and changes the term ‘regulatory actions’ to ‘legal measures’:

2. Non-discriminatory legal measures designed and applied to protect legitimate public welfare objectives, such as health, safety and environment, do not constitute indirect expropriation.\textsuperscript{133}

The Colombia-UK BIT 2010 uses a weaker phrasing, changing the ‘do not constitute’ to ‘shall not constitute’ and introduces a proportionality test:

(c) non-discriminatory measures that the Contracting Parties take for reasons of public purpose or social interest (which shall have a meaning compatible with that of “public purpose”) including for reasons of public health, safety, and environmental protection, which are taken in good faith, which are not arbitrary, and which are not disproportionate in light of their purpose, shall not constitute indirect expropriation.\textsuperscript{134}

\textsuperscript{128} OECD, Indirect Expropriation and the "Right to Regulate" in International Investment Law, above 102, p. 21.
\textsuperscript{130} Article 7(4) of the Austria-Nigeria BIT 2013. See as well Benin-Canada BIT 2013, Annex I, using the singular. The Belgium/Luxembourg-Colombia BIT 2009 uses in its Article IX a very similar phrasing, and enounces expressly environment protection. Similar wording can be found in the Colombia-Singapore BIT 2013, Anexo 2(4b). See as well Annex X.11(3) of CETA: 3. For greater certainty, except in the rare circumstance where the impact of the measure or series of measures is so severe in light of its purpose that it appears manifestly excessive, non- discriminatory measures of a Party that are designed and applied to protect legitimate public welfare objectives, such as health, safety and the environment, do not constitute indirect expropriations.
\textsuperscript{131} Included in the Ghana Model BIT 2008.
\textsuperscript{132} US Model BIT 2012, Annex B.
\textsuperscript{133} Article 6(2) of the Gabon-Turkey BIT 2012. The Turkey Model BIT 2009 adds in its Article 5(2) that such measures are not subject to any compensation requirements, it reads: 2. Non-discriminatory legal measures designed and applied to protect legitimate public welfare objectives, such as health, safety and environment, do not constitute indirect expropriation and are not subject, therefore, to any compensation requirements.
\textsuperscript{134} Article VI(2c) of the Colombia-UK BIT 2010 (emphasis added).
However, for example, recently concluded Japan BITs do not embrace this type of clause.\textsuperscript{135}

Provisions, stating that non-discriminatory environmental regulations do not constitute indirect expropriations, are conceived in very general terms. It is hard to identify a clear distinction in these clauses between indirect compensable expropriation and non-compensable regulatory action. However, it might be argued that it is an almost impossible task to exactly establish which measures require compensation and which do not. Indeed, the list of public policy measures to attain environmental protection is long and as science develops policy aims to protect the environment do too. Furthermore, it is hard to foresee how such measures will affect a given investment. Hence, an immense variety of different constellations are possible in practice. However, clauses like the above address the right to regulate. They state arbitral jurisprudence, namely that non-discriminatory good faith regulation relating to the protection of the environment does not constitute indirect expropriation and that thus no compensation is due. Insofar they combat ‘regulatory chill’ and allow for policy changes.

With regard to the burden of proof, the case law is not conceptually clear on whether the investor has to show that the State’s regulatory action amounted to expropriation or whether the State has to proof that it acted in conformity with the law.\textsuperscript{136} In fact, if the investor only has to establish the deprivation of the value of its investment by the regulatory action of the host State, this would then shift the burden of proof to the host State. The host State would have to demonstrate that its regulation was non-discriminatory, enacted with due process and that no specific commitment to the investor had been given. Hence, if the burden of proof would lie on the host State to demonstrate the above requirements, it would imply that general regulatory action by the host State would amount generally to indirect expropriation. The threshold for the investor to show that he has been expropriated would be low. However, if the burden of proof lies on the investor to establish that the host State’s regulatory action was discriminatory, not enacted with due process and/or that specific commitments had been received, it would infer that general regulatory actions would not easily amount to indirect expropriation. In that case, a State’s regulatory action will only exceptionally amount to an indirect expropriation.

Two paramount reasons argue in favour of the latter view. First, regulatory powers are an essential component of sovereignty and limitation to it should not be presumed. Second, in practice, “regulatory chance is not the exception but the rule”\textsuperscript{137} especially in highly regulated markets, such as the energy market, the mining sector or when an investor operates with chemical products. New scientific discovery makes environmental regulation very dynamic. This argumentation is in line with the current treaty drafting. As has been seen above, most of these clauses refer to ‘except in rare circumstances’; hence, in general, non-discriminatory environmental regulations do not amount to indirect expropriation.

To conclude, this paper welcomes clauses that state that general regulations do not constitute indirect expropriations as they acknowledge legitimate public policy making and hence, the host State’s right to regulate in the public interest, e.g. the environment. It is of paramount importance that these provisions guarantee both, sufficient flexibility for the host State to adopt general regulations pursuing a public

\textsuperscript{135} See Japan-Myanmar BIT 2013; Japan-Saudi Arabia BIT 2013; Japan-Uruguay BIT 2015.
\textsuperscript{136} J. E. Vihuales, \textit{Foreign Investment and the Environment in International Law}, above 15, p. 306.
\textsuperscript{137} \textit{Ibid.}, p. 306.
purpose without having to compensate adversely affected investors and adequate protection of foreign investment against direct and indirect expropriation.

2.4. Performance requirements

Environmental language in performance requirements clauses is occasionally found in Canadian or US BITs modelled after the NAFTA clause. The Canada Model BIT 2004 clause states:

Article 9
Performance Requirements
1. A Party may not impose or enforce the following requirements, or enforce a commitment or undertaking, in connection with the establishment, acquisition, expansion, management, conduct or operation of a covered investment or any other investment in its territory:
   [...] (f) to transfer technology, a production process or other proprietary knowledge to a person in this territory; or
   [...] 2. A measure that requires an investment to use a technology to meet generally applicable health, safety or environmental requirements is not inconsistent with subparagraph 1(f).

The US Model BIT clause is more extensive than the Canadian clause. It is drafted as follows:

Article 8: Performance Requirements
1. Neither Party may, in connection with the establishment, acquisition, expansion, management, conduct, operation, or sale or other disposition of an investment of an investor of a Party or of a non-Party in its territory, impose or enforce any requirement or enforce any commitment or undertaking:
   [...] 3. (c) Provided that such measures are not applied in an arbitrary or unjustifiable manner, and provided that such measures do not constitute a disguised restriction on international trade or investment, paragraphs 1(b), (c), (f), and (h), and 2(a) and (b), shall not be construed to prevent a Party from adopting or maintaining measures, including environmental measures:
   [...] (ii) necessary to protect human, animal, or plant life or health; or (iii) related to the conservation of living or non-living exhaustible natural resources.

The International Institute for Sustainable Development (IISD) in its Model BIT 2005 proposes the inverse approach. Especially Article 26(B) suggests that a host State may impose performance requirements to promote domestic development benefits from investments.

Clauses, like the one used in the US Model BIT 2012, are usually extensive and confusing because they incorporate several hypotheses, exceptions and requirements for exceptions. Basically, the clause assures that the parties can adopt or maintain the necessary measures for the protection of the environment even though they might be considered as being contrary to the general prohibition of performance requirements.

138 Article 9 of the Canada Model BIT 2004 (in parts).
139 Article 8 of the US Model BIT 2012 (in parts).
These clauses can be seen as reserving policy space with regards to performance requirements.\textsuperscript{140}

2.5. Explicit right to regulate clauses

The right to regulate is maybe the most prominent but also the most controversial concept today. According to an OECD survey from 2011, a right to regulate clause was introduced already back in 1985,\textsuperscript{141} which makes this type of clauses the oldest recurring clause with environmental language. In this section, explicit right to regulate clauses are the subject of discussion. Sometimes general exceptions clauses are mentioned in the same breath; notwithstanding, the paper proposes to distinguish explicit right to regulate clauses and general exception clauses.

It is understood that explicit right to regulate clauses are incorporated in the substantive part of an agreement and often entitled as such or found in the Article entitled as Investment and Environment. An explicit right to regulate clause can be drafted as it was done in Article 12(5) of the US Model BIT 2012. NAFTA uses the same language in its Article 1114.1.

\begin{quote}
Article 12: Investment and Environment

\[\ldots\]
5. Nothing in this Agreement [\textsuperscript{142}] shall be construed to prevent a [Contracting]\textsuperscript{143} Party from adopting, maintaining or enforcing any measure otherwise consistent with this Agreement [\textsuperscript{144}] that it considers appropriate to ensure that investment activity in its territory is undertaken in a manner sensitive to environmental concerns.\textsuperscript{145}
\end{quote}

Another similar example is Article 4.6(1) of the EFTA-Hong Kong FTA found in the chapter on investment:

Right to Regulate

1. Nothing in this Chapter shall be construed to prevent a Party from adopting, maintaining or enforcing any measure consistent with this Chapter that is in the public interest, such as measures to meet health, safety or environmental concerns and reasonable measures for prudential purposes.\textsuperscript{146}

The same FTA addresses the right to regulate again in its chapter on trade and the environment:

\begin{quote}
ARTICLE 8.3

Right to Regulate and Levels of Protection

1. Recognising the right of each Party to establish its own level of environmental protection and to adopt or modify accordingly its domestic law and policies in a manner consistent\textsuperscript{147}
\end{quote}

\textsuperscript{141} First introduced through the China-Singapore BIT 1985. Its Article 11 reads: The provisions of this Agreement shall not in any way limit the right of either Contracting Party to apply prohibitions or restrictions of any kind or take any other action which is directed to the protection of its essential security interests, or to the protection of public health or the prevention of diseases and pests in animals or plants.
\textsuperscript{142} Used in the NAFTA Article 1114.1.
\textsuperscript{143} Used in the US Model BIT 2012.
\textsuperscript{144} Used in the NAFTA Article 1114.1.
\textsuperscript{145} Article 12(5) of the US Model BIT 2012 (emphasis added).
\textsuperscript{146} Article 4.6(1) of the EFTA-Hong Kong FTA 2011 (emphasis added).
with this Agreement, each Party will seek to ensure that its domestic law, policies and practices provide for and encourage high levels of environmental protection, consistent with standards, principles and agreements referred to in Article 8.5, and will strive to further improve the level of protection provided for in domestic law and policies.

2. The Parties recognise the importance, when preparing and implementing measures related to environmental protection that affect trade and investment between them, of taking account of relevant scientific, technical and other information, and relevant international standards, guidelines and recommendations.\(^\text{147}\)

The Economic Cooperation Agreement between New Zealand and Taiwan concluded in 2013 is of interest as well. It explicitly recognises the right to regulate in its Article 1 of the Investment Chapter:

Article 1 Objectives

The objectives of this Chapter are to encourage and promote the flow of investment between the Parties on a mutually advantageous basis, under conditions of transparency within a stable framework of rules to ensure the protection and security of investments by investors of the other Party within each Party, while recognising the rights of Parties to regulate and the responsibility of governments to protect public health, safety and the environment.\(^\text{148}\)

However, it employs then the same language as the clauses above in its Article on Investment and Environment:

Article 16 Investment and Environment

Nothing in this Chapter shall be construed to prevent either Party from adopting, maintaining, or enforcing any measure otherwise consistent with this Chapter that it considers appropriate to ensure that investment activity is undertaken in a manner sensitive to environmental concerns.\(^\text{149}\)

Clauses like the above were criticised by the current literature.\(^\text{150}\) In fact, drafted in this manner, they only allow the host State to take measures consistent with the investment agreement. However, a genuine right to regulate would precisely go beyond. Measures that are in line with the host State’s obligation to protect the foreign investment do not pose any problem. It is exactly when the host State adopts a measure that violates the protection afforded to the foreign investors under the agreement that a genuine right to regulate in the public interest would intervene to offset the alleged violation. Furthermore, as TITI notes correctly, “express Right to

\(^{147}\) Article 8.3 of the EFTA-Hong Kong FTA 2011 (emphasis added).

\(^{148}\) Article 1 of Chapter 12 of the New Zealand-Taiwan Economic Cooperation Agreement 2013 (emphasis added).

\(^{149}\) Article 16 of Chapter 12 of the New Zealand-Taiwan Economic Cooperation Agreement 2013 (emphasis added).

regulate clauses fall short of their ambition to introduce this right. In that the ‘otherwise consistent with’ phrasing may a contrario lead to the conclusion that any measure that is not consistent with the treaty is de iure incompatible with the obligations it imposes, this provision may conduce to a narrowing of policy space rather than the opposite. “151 Keeping this in mind, the purpose of such a clause might not be to insert a genuine right to regulate into the agreement. Such clause can indeed be an explanatory clause whose purpose is to impose soft obligations (CSR standards) on investors by importing them into the agreement through the back door.152

Not all IIAs contain an explicit right to regulate clause that includes the ‘otherwise consistent with this treaty’ phrase. For example, instead of the requirement of the consistency with the investment agreement, the Colombian Model BIT 2008 introduces a proportionality test. The right to regulate clause reads:

INVESTMENT AND ENVIRONMENT
Nothing in this Agreement shall be construed to prevent a Contracting Party from adopting, maintaining, or enforcing any measure that it considers appropriate to ensure that an investment activity in its territory is undertaken in accordance with environmental law of the Contracting Party, provided that such measures are proportional to the objectives sought.153

Another approach consists in requiring the measure to be non-discriminatory. To this effect, a clause drafted like the one below is not far from a general exceptions clause, which also requires the measure to be non-discriminatory. Keeping this in mind, it can already be noted that a general exceptions clause usually demands the measure in question, in addition to the non-discriminatory requirement, to be necessary and not a disguised restriction on international trade or investment.154 A right to regulate clause requiring the measure to be non-discriminatory reads as follows:

ARTICLE 4 Right to Regulate
1. Nothing in this Agreement shall be construed to prevent a Contracting Party from adopting, maintaining, or enforcing any non-discriminatory measures:
   a) designed and applied for the protection of human, animal or plant life or health, or the environment;
   b) related to the conservation of living or non-living exhaustible natural resources.155

Furthermore, it is possible to omit any requirement for the measure as illustrated by the Belgium/Luxembourg-Colombia BIT 2009. This clause is combined with a definition of the term environmental legislation.156 Article VII(4) of the Belgium Luxembourg-Colombia BIT 2009 reads:

151 A. Titi, The Right to Regulate in International Investment Law, above 32, p. 115.
152 Ibid., p. 113. See as well Part II subsection 2.9.
153 Article VIII of the Colombian Model BIT 2008 (emphasis added). Compare to Article VII(4) of the Belgium Luxembourg-Colombia BIT 2009, and Article VIII of the UK-Colombia BIT 2010. The Belgium Luxembourg-Colombia BIT 2009 leaves out the requirement of the measure to be proportionate to the objectives sought. The UK-Colombian BIT 2010 raises the threshold for the host State to maintain, adopt or enforce an environmental measure, as it has to be not only proportionate to the objectives sought, the measure in question must also meet the non-discriminatory test.
154 See for example Article 18(1) of the Canada Model BIT 2004.
155 Article 4(1) of the Turkey Model BIT 2009 (emphasis added).
4. Nothing in this Agreement shall be construed as to prevent a Contracting Party from adopting, maintaining, or enforcing any measure that it considers appropriate to ensure that an investment activity in its territory is undertaken in accordance with the environmental law of the Party.\textsuperscript{157}

Another and far more extensive approach is proposed by the IISD and the SADC Model BITs. Surely, they come the closest to a genuine right to regulate. Reference is made to international law, implying that the right to regulate is a basic attribute of State sovereignty. As a starting point the host State has the right to regulate in the public interest, a right which should only be restricted exceptionally.\textsuperscript{158} To this effect, the clause embodies the aim of the right to regulate in order to attend a proper balance between public and private interests. The clause reads in the important parts:

(B) In accordance with customary international law and other general principles of international law, host States\textsuperscript{159} have the right to take regulatory or other measures to ensure that development in their territory is consistent with the goals and principles of sustainable development, and with other [legitimate]\textsuperscript{160} social and economic policy objectives.

(C) Except where the rights of a host State are expressly stated as an exception to the obligations of this Agreement, the pursuit of these rights shall be understood as embodied within a balance of the rights and obligations of investors and investments and host States, as set out in this agreement, [and consistent with other norms of customary international law]\textsuperscript{161}.

In conclusion, the IISD and the SADC approach in drafting an explicit right to regulate clause should be preferred because it assures best a genuine right to regulate.

2.6. Not lowering environmental standards

Certain treaties include a provision that discourages the lowering of environmental standards. These clauses address the concern that some States tend to relax their national environmental laws in a so-called ‘race to the bottom’ in order to attract foreign investment. By providing regulatory incentives at the expense of the environment, companies located in countries with a high standard will move to jurisdictions with lower environmental standards, so-called ‘pollution heavens’\textsuperscript{163}. Hence, these clauses “seek to ensure the respect of existing environmental standards and to avoid that States compete for investment by lowering environmental standards.”\textsuperscript{164} In this subsection only provisions found in substantive parts of agreements are analysed. Yet, it is worth noting an emerging trend to include

\textsuperscript{157} Article VII(4) of the Belgium Luxembourg-Colombia BIT 2009 (emphasis added).
\textsuperscript{158} See discussion in Part I subsection 3.4.
\textsuperscript{159} The SADC Model BIT 2012 opts for the employment of the singular.
\textsuperscript{160} Only in Article 20 of the SADC Model BIT 2012.
\textsuperscript{161} Only in Article 25(C) of the IISD Model International Agreement on Investment for Sustainable Development 2005 (below IISD Model BIT 2005).
\textsuperscript{162} Article 25(C) of the IISD Model BIT 2005 (emphasis added).
references to the not lowering of environmental standards in the preamble text. The wording of the provisions varies slightly with respect to the origin of the investment and with regard to the territorial scope of the measure. The following language is used for example:

The Parties recognize that it is inappropriate to encourage investment by relaxing domestic health, safety or environmental measures. Accordingly, a Contracting Party should not waive or otherwise derogate from, or offer to waive or otherwise derogate from, those measures to encourage the establishment, acquisition, expansion or retention in its territory of an investment of an investor. If a Contracting Party considers that the other Contracting Party has offered such an encouragement, it may request consultations with the other Contracting Party and the two Contracting Parties shall consult with a view to avoiding the encouragement.166

Japan’s wording in its BITs is the following:

Health, Safety and Environmental Measures and Labor Standards

Each Contracting Party shall refrain from encouraging investment by investors of the other Contracting Party or of a non-Contracting Party by relaxing its health, safety or environmental measures or by lowering its labor standards. To this effect each Contracting Party should not waive or otherwise derogate from such measures or standards as an encouragement for the establishment, acquisition or expansion in its Area of investments by investors of the other Contracting Party and of a non-Contracting Party.167

The Austrian Model BIT 2010 uses a different language:

Investment and Environment

The Contracting Parties recognise that it is inappropriate to encourage an investment by weakening domestic environmental laws.168

The language is vague and phrasings such as ‘recognise’ and ‘shall refrain’ are weak. Furthermore, these clauses are often couched in language that creates obligations of conduct rather than of results.169

It is important to note that the addressees of clauses that seek to not lower environmental standards are the States Parties themselves. This means that these provisions do not set out binding rules for the investors. When such a clause is aimed at combatting the ‘race to the bottom’, it is crucial that IIAs address investors’ obligations to respect the environment as well because in practice, it is often the investor who disrespects environmental standards. Treaty negotiators have thus chosen to introduce CSR standards or even environmental obligations for the investors in IIAs. This matter will be explored below in Part II subsection 2.9.

Nevertheless, one question remains. Who will invoke a clause that disapproves the lowering of environmental standards in a dispute? The investor will most likely be the one infringing the obligation to protect the environment and he is not the direct addressee of the ‘not lowering environmental standards’ clause. Thus, except in (until

165 See for example Japan-Saudi Arabia BIT 2013; Austrian Model BIT 2010; Gabon-Turkey BIT 2012.
166 Article 15 of the Benin-Canada BIT 2013 (emphasis added).
167 Article 27 of the Japan-Uruguay BIT 2015 (emphasis added).
168 Austrian Model BIT 2010, Article 4 (emphasis added).
today) rare cases where investors claim legitimate expectations of high environmental protection, investors are unlikely to invoke the above clauses.  

The question is whether a State will invoke a ‘not lowering environmental standards’ clause in a dispute opposing it to its contracting party? Again, the answer has to be no. States are very prudent not to deteriorate international relations. Further, disputes concerning the interpretation or application of a treaty are rare. A State will invoke the ‘not lowering environmental standards’ clause most probably in an investor-State dispute. Keeping this in mind, a State can only do so when the investor has brought a case against it. Since the investor is not the immediate recipient of the ‘not lowering environmental standards’ clause, it is unclear if an arbitral tribunal will consider the defence based on such a clause. Furthermore, the Canada Model BIT 2004 excludes explicitly the ‘not lowering environmental standards’ clause from the scope of investor-State disputes settlement and proposes thus consultation as a dispute settlement mechanism. 

To conclude, ‘not lowering environmental standards’ clauses discourage the competition between States for foreign direct investment (FDI), but they do not go very much further.

### 2.7. Encourage progress of environmental protection and cooperation

Sometimes, clauses that state the promotion of environmental protection and general cooperation in the environmental domain are introduced. For example:

3. The Contracting Parties recognise that cooperation between them provides enhanced opportunities to improve environmental protection standards.

FTAs are more likely to include such cooperation because their scope is wider than the sole promotion and protection of foreign investment. The recent Association Agreement between the EU and Georgia uses comprehensive language:

- **Environment**
  - **Article 301**
    
    The Parties shall develop and strengthen their cooperation on environmental issues, thereby contributing to the long-term objective of sustainable development and greening the economy. It is expected that improved environmental protection will bring benefits to citizens and businesses in Georgia and in the EU, including through improved public health, preserved natural resources, increased economic and environmental efficiency, as well as

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171 See Article 21(1a) of the Canada Model BIT 2004. See as well for the BIT mentioned above, Article 23(1a) of the Benin-Canada BIT 2013.

172 Article VII(3) of the Belgium/Luxembourg-Colombia BIT 2009.
use of modern, cleaner technologies contributing to more sustainable production patterns. Cooperation shall be conducted considering the interests of the Parties on the basis of equality and mutual benefit, as well as taking into account the interdependence existing between the Parties in the field of environment protection, and multilateral agreements in the field.\textsuperscript{173}

Article 19 of the ECT is an interesting example, it reads in the important parts:

\textbf{ARTICLE 19 ENVIRONMENTAL ASPECTS}

(1) In pursuit of sustainable development and taking into account its obligations under those international agreements concerning the environment to which it is party, each Contracting Party shall strive to minimize in an economically efficient manner harmful Environmental Impacts occurring either within or outside its Area from all operations within the Energy Cycle in its Area, taking proper account of safety. In doing so each Contracting Party shall act in a Cost-Effective manner. In its policies and actions each Contracting Party shall strive to take precautionary measures to prevent or minimize environmental degradation. The Contracting Parties agree that the polluter in the Areas of Contracting Parties, should, in principle, bear the cost of pollution, including transboundary pollution, with due regard to the public interest and without distorting Investment in the Energy Cycle or international trade. Contracting Parties shall accordingly:

(a) take account of environmental considerations throughout the formulation and implementation of their energy policies;\textsuperscript{174}

The obligations contained in Article 19 are soft law. Nevertheless, tribunals can rely upon the environmental obligations contained in Article 19 when interpreting other provisions of the treaty.\textsuperscript{175} Article 19 of the ECT is also interesting because it does not use generic language; rather it touches upon a set of current environmental concerns.\textsuperscript{176} It addresses even the precautionary and polluter pays principles.

Clauses that encourage progress of environmental protection and cooperation can help to guide the arbitrators’ interpretation by allowing environmental concerns to be considered in a given case. Furthermore, these clauses can provide a fertile basis for institutional cooperation between the host and home State in environmental related matters.

2.8. \textbf{Reference to and coordination with international environmental instruments}

Most likely, reference to international environmental instruments is found in FTAs since they are usually drafted as comprehensive agreements attaining a wide variety of objectives. As such they often incorporate a specific chapter on the environment. In contrast, traditional BITs do not address the relationship they have with other international instruments. This section proposes to look at clauses in IIAs that intend coordination with other bilateral or multilateral environmental agreements. For example, the EFTA-Hong Kong FTA 2011 includes the following language in its environmental chapter:

\begin{quote}
Multilateral Environmental Agreements and Environmental Principles
\end{quote}

\textsuperscript{173} Article 301 of the EU-Georgia Association Agreement 2014.
\textsuperscript{174} Article 19 of the ECT.
\textsuperscript{175} T. W. Wälde, ‘International Disciplines on National Environmental Regulation: With Particular Focus on Multilateral Investment Treaties’, above 23, p. 46.
The Parties reaffirm their commitment to the effective implementation in their respective domestic law and practices of the multilateral environmental agreements applicable to them, as well as their adherence to environmental principles reflected in the international instruments referred to in Article 8.1.\(^{177}\)

The language employed remains declaratory.\(^{178}\) Furthermore, the relationship between the investment chapter and the environmental chapter is not always clear. For example, the cited FTA between the EFTA States and Hong Kong does not coordinate between the two chapters.\(^{179}\) It was argued that, in the event of conflict between the obligations contained in the FTA and those possibly arising under international environmental instruments, it is not fully clear to the interpreter to which obligations should be given precedence.\(^{180}\)

NAFTA is a well-know precursor, when it comes to reference to and coordination with international environmental instruments. NAFTA does not only make binding reference, it establishes also a hierarchy between the obligations contained in different international environmental instruments and the obligations resulting from the trade and investment agreement, letting the environmental obligations prevail. NAFTA’s Article 104 can be thus seen as a true conflict clause,\(^{181}\) It reads:

*Article 104: Relation to Environmental and Conservation Agreements*

1. In the event of any inconsistency between this Agreement and the specific trade obligations set out in:
   b) the *Montreal Protocol on Substances that Deplete the Ozone Layer*, done at Montreal, September 16, 1987, as amended June 29, 1990,
   c) the *Basel Convention on the Control of Transboundary Movements of Hazardous Wastes and Their Disposal*, done at Basel, March 22, 1989, on its entry into force for Canada, Mexico and the United States, or
   d) the agreements set out in Annex 104.1,
   such obligations shall prevail to the extent of the inconsistency, provided that where a Party has a choice among equally effective and reasonably available means of complying with such obligations, the Party chooses the alternative that is the least inconsistent with the other provisions of this Agreement.\(^{182}\)

It is definitely of interest establishing a hierarchy between different obligations for greater certainty and not leaving the decision on the importance of international instruments to the decision of a tribunal. However, recent scholarly work on treaty

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\(^{178}\) M. Potestà, ‘Mapping Environmental Concerns in International Investment Agreements’, above 27, p. 199.

\(^{179}\) Sometimes, in other agreements a provision is included at the beginning of the investment chapter, stipulating that other chapters of the agreement should prevail over the investment chapter to the extent of the inconsistency. See for example Article 11.2(1) of the Korea-US FTA 2007 (the final text is available at: https://ustr.gov/trade-agreements/free-trade-agreements/korus-fta/final-text (accessed on 25 April 2015)).

\(^{180}\) M. Potestà, ‘Mapping Environmental Concerns in International Investment Agreements’, above 27, pp. 199-200.

\(^{181}\) Ibid., p. 200.

\(^{182}\) Article 104 of the NAFTA.
interpretation advances the so-called legal principle of mutual supportiveness. The rise of this principle can be traced back to the debates concerning the interplay between trade agreements and multilateral environmental agreements. Although its content has not yet been entirely defined, the principle of mutual supportiveness enhances positive and constructive interaction between different subsystems of international law (as are the trade and the environment regimes) focusing more on the similar and common objectives pursued (for example sustainable development) than on the substantive rights and obligations contained in the international treaties. The principle has to be distinguished from related concepts such as harmonization insofar as mutual supportiveness excludes the very idea of conflict between the different treaty regimes. Whereas harmonization implicitly accepts that normative conflicts may arise, mutual supportiveness seeks coherence in the international legal system and thereby transcends the logic of conflicts. Mutual supportiveness goes further than to seek mere compatibility between different treaty systems and it was thus argued that it is capable of tackling fragmentation. With regard to mutual supportiveness it is important that States, when they negotiate new international agreements, take into account pre-existing international instruments. This ex ante coordination might have the effect of an ex post synchronization between the different international instruments under similar or common objectives. Since the different international instruments pursue similar or common objectives, there is no need to establish a hierarchy between environmental treaties and other international agreements.

The principle of mutual supportiveness has not yet been significantly transferred from the trade/environment to the investment/environment regime; BITs do not mention it; one exception is the abandoned Norway Model BIT 2007. However, the principle of mutual supportiveness can be found in recent FTAs. For example reference to mutual supportiveness is made in the Korea-US FTA 2007:

 ARTICLE 20.10: RELATION TO MULTILATERAL ENVIRONMENTAL AGREEMENTS

1. The Parties recognize that certain multilateral environmental agreements play an important role globally and domestically in protecting the environment. The Parties further recognize that this Chapter and the ECA can contribute to realizing the goals of such agreements. Accordingly, the Parties shall continue to seek means to enhance the mutual supportiveness of multilateral environmental agreements to which they are both party and trade agreements to which they are both party.

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186 Ibid., pp. 1617-9.
187 Ibid., p. 1626.
188 M. Potestà, ‘Mapping Environmental Concerns in International Investment Agreements’, above 27, p. 201.
189 Article 29 of the Norway Model BIT 2007 stipulates: RELATION TO OTHER INTERNATIONAL AGREEMENTS

The provisions of this Agreement shall be without prejudice to the rights and obligations of the Parties under other international agreements.
2. To this end, the Parties shall consult, as appropriate, with respect to negotiations on environmental issues of mutual interest.

3. In the event of any inconsistency between a Party’s obligations under this Agreement and a covered agreement, the Party shall seek to balance its obligations under both agreements, but this shall not preclude the Party from taking a particular measure to comply with its obligations under the covered agreement, provided that the primary purpose of the measure is not to impose a disguised restriction on trade.190

Such wording was criticised as consisting in a rather minimal implementation of mutual supportiveness as it is drafted in programmatic language and as only seeking the mutual supportiveness of agreements to which both States are party.191

Finally, the same FTA uses stronger language in its Article 20.2 and provides for consultation up to binding third-party adjudication in case of disagreement between the parties concerning the adoption, maintenance and implementation of measures to comply with the MEAs.192 It thus offers a remedy for violations of international environmental agreements that the agreements themselves rarely provide.193 Article 20.2 states:

**ARTICLE 20.2: ENVIRONMENTAL AGREEMENTS**

A Party shall adopt, maintain, and implement laws, regulations, and all other measures to **fulfill its obligations under the multilateral environmental agreements** listed in Annex 20-A (“covered agreements”).194

Nowadays, the international investment regime cannot stay a self-contained regime. It will be interesting to see how both the investment and the environment regime will further develop and interact.

### 2.9. Promotion of social corporate responsibility and investors’ environmental obligations

As seen above, the respect of environmental standards can be achieved either through incorporation of a host State obligation (see *supra* Part II subsection 2.6) or through the incorporation of CSR195 standards or environmental obligations, which

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190 Article 20.10 of the Korea-US FTA 2007 (emphasis added; footnotes omitted; the final text is available at: [https://ustr.gov/trade-agreements/free-trade-agreements/korus-fta/final-text](https://ustr.gov/trade-agreements/free-trade-agreements/korus-fta/final-text) (accessed on 25 April 2015)).


194 Article 20.2 of the Korea-US FTA 2007 (emphasis added; footnotes omitted; the final text is available at: [https://ustr.gov/trade-agreements/free-trade-agreements/korus-fta/final-text](https://ustr.gov/trade-agreements/free-trade-agreements/korus-fta/final-text) (accessed on 25 April 2015)).

195 CSR is a modern concept and the term is yet not unanimously defined. For example the EU defines CSR as: “a concept whereby companies integrate social and environmental concerns in their business operations and in their interaction with their stakeholders on a voluntary basis.” (European Commission, *Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions. A renewed EU*
address the investors. 196 The integration of CSR standards and investors’ environmental obligations into IIAs imbeds to the greater debate on sustainable development and the perception that the “the private sector, including both large and small companies, has a duty to contribute to the evolution of equitable and sustainable communities and societies.” 197 The topic is one of the most discussed in the international fora, especially with regards to TNCs. 198

When considering the incorporation of CSR standards into IIAs it is sometimes referred to explicit right to regulate clauses, not lowering environmental clauses or general exception clauses, On the basis of such clauses, CSR standards might be introduced in the domestic regulatory framework, as measures aimed at protecting the environment, in compliance with the corresponding international obligations. 199

Explicit reference to CSR in IIAs remains until today relatively rare. Canada and Norway have proposed a more direct inclusion of CSR into IIAs. 200 The Canada Model BIT 2004 includes a CSR clause in its substantive text:

Corporate Social Responsibility
Each Party should encourage enterprises operating within its territory or subject to its jurisdiction to voluntarily incorporate internationally recognized standards of corporate social responsibility in their practices and internal policies, such as Statements of principle that have been endorsed or are supported by the Parties. These principles address issues such as labour, the environment, human rights, community relations and anti-corruption. 201

The Austrian Model BIT 2010 includes a reference to CSR in its preamble:

EXPRESSING their belief that responsible corporate behaviour, as incorporated in the OECD Guidelines for Multinational Enterprises, can contribute to mutual confidence between enterprises and host countries; EMPHASISING the necessity for all governments and civil actors alike to adhere to UN and OECD anti-corruption efforts, most notably the UN Convention against Corruption (2003); TAKING NOTE OF the principles of the UN Global Compact; 202

It must be immediately asked whether CSR creates binding obligations on investors or only positive language. CSR clauses, such as the above, create positive language, that is to say they do not create legally enforceable rights and obligations for the investors. 203 However, it is not barred making binding reference to


196 A. Titi, The Right to Regulate in International Investment Law, above 32, pp. 107-11.
201 Article 16 of the Canada Model BIT 2004.
202 Preamble of the Austrian Model BIT 2010.
203 A. Titi, The Right to Regulate in International Investment Law, above 32, pp. 105, 107-11.
international instruments such as OECD Guidelines for Multinational Enterprises, UN Global Compact’s Ten Principles or The International Labour Organization’s Tripartite Declaration. Keeping this in mind, until today CSR compliance remains voluntary; it has not crystallized into a rule of customary international law. Further treaty drafting will shed light on CSR standards that are legally binding and arbitrable.

A second issue remains: A host State can only invoke this clause when the investor has initiated arbitration. Thus, arguably, introducing CSR standards in IIAs, to which the States are parties, is not the best place for such incorporation. States may chose to include CSR standards in domestic law and make reference in the IIAs that investors have to comply with national law (definition of covered investment). Furthermore, CSR standards do not leave more regulatory freedom to host States.

The second approach consists in including environmental obligations for the investor. The Ghana Model BIT 2008 enounces in its Article 12:

**ARTICLE 12**
Responsibilities of Nationals and Companies of a Contracting Party in the Territory of the other Contracting Party

1. **Nationals and companies** of one Contracting Party in the territory of the other Contracting Party shall be bound by the laws and regulations in force in the host State, **including its laws** and regulations on labour, health and the environment.
2. Nationals and companies of one Contracting Party in the territory of the other Contracting Party shall to the extent possible, encourage human capital formation, local capacity building through close cooperation with the local community, create employment opportunities and facilitate training opportunities for employees, and the transfer of technology.
3. Nationals and companies of one Contracting Party in the territory of the other Contracting Party shall behave in accordance with relevant guidelines and other internationally accepted standards applicable to foreign investors.

The IISD Model BIT 2005 and the SADC Model BIT 2008 propose a similar approach. Namely, combatting the perceived imbalance in IIAs of only granting rights to investors without responsibilities. Their Model BITs include thus a variety of rights and obligations for investors. This approach is mostly welcome because it introduces binding obligations on investors to respect environmental laws.

Soft law played a major role in the law-making process and in the development of principles within the environmental area. In contrast, IIL developed as a branch of the law on diplomatic protection of alien property and evolved in a wide network of IIAs. Until today, norm-creation and the formation of concepts in the field of IIL is thus mainly performed through the negotiation of BITs and FTAs and through reliance on arbitral jurisprudence. Arguably, the role soft law can play in investment-law making is less important than within the area of environmental law, because no comparable ‘gap’ exists in IIL. Soft law can however assume a bridging

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205 A. Titi, *The Right to Regulate in International Investment Law*, above 32, pp. 110-11.
206 Article 12 of the Ghana Model BIT 2008 (emphasis added).
207 See Part 3 of the IISD Model BIT 2005; see as well Part 3 of the SADC Model BIT 2008.
208 K. Miles, ‘Soft law instruments in environmental law: models for international investment law?’, above 204, p. 91.
function, “giving States time to become comfortable with controversial ideas before actually assuming” binding obligations.\(^{211}\)

In summary, whereas CSR standards remains today voluntary, a slight trend towards including binding obligations on investors is noticeable. This approach should be further developed.

### 2.10. General exception clauses

General exception clauses found in IIAs are modelled after Article XX of the General Agreement on Tariffs and Trade (GATT)\(^{212}\) or Article XIV of the General Agreement on Trade in Services (GATS)\(^{213}\). Their intent is that a host State can achieve specific policy goals without breaching the IIA’s obligations. There are drafting differences, but the basic structure is modelled after XX GATT. Article XX enounces a list of legitimate objectives for which the measure in question must be necessary or must be related and fulfil the further requirements in the chapeau. These future requirements include the measure to be non-discriminatory and not to be a disguised restriction on international trade - or investment in the case of a general exceptions clause found in an IIA. This sets the threshold for a State to adopt a measure already high. Article XX of the GATT reads:

**Article XX: General Exceptions**

Subject to the requirement that such measures are not applied in a manner which would constitute a means of *arbitrary or unjustifiable discrimination* between countries where the same conditions prevail, or a *disguised restriction on international trade*, nothing in this Agreement shall be construed to prevent the adoption or enforcement by any contracting party of measures:

(a) **necessary** to protect public morals;

(b) **necessary** to protect human, animal or plant life or health;

[…]

(d) necessary to secure compliance with laws or regulations which are not inconsistent with the provisions of this Agreement, including those relating to customs enforcement, the enforcement of monopolies operated under paragraph 4 of Article II and Article XVII, the protection of patents, trade marks and copyrights, and the prevention of deceptive practices;

[…]

(f) **imposed** for the protection of national treasures of artistic, historic or archaeological value;

(g) relating to the conservation of exhaustible natural resources if such measures are made effective in conjunction with restrictions on domestic production or consumption.\(^{214}\)

With respect to the investment context and environmental protection especially letter b and g are important.\(^{215}\) GATS does not include an express exception for the conservation of natural resources, while Article XX(g) GATT does. The reason could

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\(^{211}\) Ibid., pp. 89-90.


\(^{214}\) Article XX of the GATT (in parts; emphasis added).

\(^{215}\) In virtue of the WTO case law, there are mainly two exceptions in favour of the environment, namely those of letter (b) and letter (g), justifying measures inconsistent with the other obligations of GATT. See for an example United States – Import Prohibition of Certain Shrimp and Shrimp Products, DS58/AB/R, Report of the Appellate Body of 12 October 1998, § 128-134.
be the fact that GATS focuses on services. General exception clauses modelled after XX GATT have to be distinguished from exceptions or non-precluded measures related to specific exceptions for essential security interests, public order, prudential measures or taxation. Canada is a unique example because the majority of its Foreign Investment Promotion and Protection Agreements (FIPAs, which have the same function as BITs) contain Article XX GATT-like general exceptions. In its Article 2101 the NAFTA enounces general exceptions but by the same token excludes the investment chapter. However, one author proposes that some arbitral tribunals have adopted systemic interpretation of the model of general exceptions and “so overcome the impossibility of directly applying Article 2101”.

The ECT adopts a similar approach: it includes in Article 21 general exceptions that extend to the investment section, but the rule on expropriation is excluded. Article 22(1) of the COMESA does not include the requirement of the necessity of the measure. It reads:

**ARTICLE 22 General Exceptions**

1. Subject to the requirement that such measures are not applied in a manner which would constitute a means of arbitrary or unjustifiable discrimination between investor where like conditions prevail, or a disguised restriction on investment flows, nothing in this Agreement shall be construed to prevent the adoption or enforcement by any Member State of measures:
   (a) designed and applied to protect national security and public morals;
   (b) designed and applied to protect human, animal or plant life or health;
   (c) designed and applied to protect the environment; or
   (d) any other measures as may from time to time be determined by a Member State, subject to approval by the CCIA Committee.

Furthermore general exceptions clauses have emerged in comprehensive bilateral FTAs among Asian States.

An author makes an interesting comment when considering transposing the GATT/WTO system and its relevant case law to the investment regime: Within the WTO dispute settlement mechanism the choice is simply to maintain (when it is lawful) or not to maintain (when it is unlawful) the given measure adopted by the host State. However, investment arbitration claims are based on monetary compensation; the investors do usually not demand the change or withdrawal of the alleged unlawful measure. In fact, only in a small number of cases, arbitral tribunals did order the restitution or specific performances. That is why the formula of ‘nothing shall be construed to prevent the adoption or enforcement of measures’ is somewhat strange in the investment law system. It would be more appropriate to write that a host State does not have to pay compensation when it adopts a measure pursuing a public purpose, which violates a protection rule of the same agreement. This would not entail a black or white solution because compensation may be graduated.

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217 For example see S.D. Myers, Inc v. Government of Canada, above 74.
219 Article 22(1) of the COMESA.
The legal meaning of general exceptions clauses modelled after Article XX GATT is to connect autonomous systems of law that is to import a cluster of rules with a similar rationale to the IIA. States “maintain some prerogatives that would otherwise be affected, or even impaired, by the strict fulfilment of treaty obligations.” Another author contents that in the absence of general exceptions clauses, the case law has already acknowledged that many forms of host State regulation in the interest of public purposes do not breach investment agreement obligations. Indeed, in the absence of express general exceptions clauses, arbitral tribunals have to some extent implied them. Incorporating general exceptions clauses into IIAs contains thus the risk that they might be interpreted narrowly, because general exceptions clauses provide a closed list of legitimate public policy objectives. And secondly, they may only be invoked where they are necessary and satisfy the requirements of the chapeau. Arbitral tribunals might interpret an express general exceptions clause as limiting the range of legitimate objectives available to the State and hence, providing less regulatory flexibility than what is currently permitted in most IIAs.

As demonstrated by the SGS v. Philippines and the Siemens v. Argentine case, some arbitral tribunals stress the preamble and title, which are enouncing the promotion and protection of the foreign investment. Some tribunals have thus suggested that exceptions to obligations contained in the same agreement should be interpreted narrowly or restrictively and consistent with the purpose of the treaty. For example, the preamble to the US-Argentina BIT has been used to bolster a restrictive interpretation of exceptions clauses. However, such an interpretation finds no support neither in the text of the treaty nor in Article 31 of the Vienna Convention.

NEWCOMBE suggests that exceptions should not be interpreted narrowly to leave more flexibility and regulatory freedom to the host State. However, this paper suggest another approach, namely that the right to regulate is an inherent right of States, finding it basis in State sovereignty, hence exceptions to limit the right to regulate should be introduced in IIAs and not the reverse as currently illustrated with general exceptions clauses.

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224 Ibid., p. 161.
225 See as well Part I subsection 3.4.
226 However, the article omits reference to the case law.
227 In this context it is interesting to know what ‘necessary’ means: indispensable or just a nexus requirement between the objective and the measure.
229 Ibid., pp. 357-8.
233 For example Canfor Corporation v. United States of America and Terminalforest Products Ltd. v. United States of America, UNCITRAL, Decision on Preliminary Questions, 6 June 2006, § 187. This case referred to the GATT jurisprudence.
234 Enron Corporation and Ponderosa Assets, L.P., v. Argentine Republic, ICSID Case No. ARB/01/3, Award, 22 May 2007, § 331. Argentine, the respondent in the case argued that it had to protect its essential security interests following the economic crisis.
2.11. Limiting access to ISDS

Some IIAs provide clauses, which exclude environmental provisions as a basis for investor-State arbitration claims. For example the Canada-Jordan BIT 2009 reads:

**ARTICLE 22**

Claim by an Investor of a Party on Its Own Behalf

1. An investor of a Party may submit to arbitration under this Section a claim that the other Party has breached an obligation under Articles 2 to 5, paragraph 6 (1), paragraph 6 (2), Articles 7 to 10 and Articles 12 to 18, and that the investor has incurred loss or damage by reason of, or arising out of, that breach. 236

Article 11 on Health, Safety and Environmental Measures is not included in the list of arbitrable claims of Article 22. This is a rather extreme approach fuelling the debate on limiting access to ISDS in international fora.

2.12. Environmental experts

Some States, most prominently Canada and the US, chose to include clauses that provide for the recourse to environmental experts by arbitral tribunals. For example:

**Article 32: Expert Reports**

Without prejudice to the appointment of other kinds of experts where authorized by the applicable arbitration rules, a tribunal, at the request of a disputing party or, unless the disputing parties disapprove, on its own initiative, may appoint one or more experts to report to it in writing on any factual issue concerning environmental, health, safety, or other scientific matters raised by a disputing party in a proceeding, subject to such terms and conditions as the disputing parties may agree. 237

Theses clauses are a positive novelty to arbitral procedure. Environmental experts may be better placed to assess the possible risk of a certain action or measure for the environment. Evaluating environmental damages needs often scientific knowledge that a panel of arbitrators might not have.

After having analysed the current environmental language commonly found in IIAs, the impact these clauses can have is studied in Part III.

PART III

In the last part of this paper the impact of environmental language in IIAs will be analysed. A review of each individual clause has already been given in Part II. In Part III, after the discussion of some general matters concerning the implementation of environmental language into IIA, the effect which environmental friendly clauses in IIAs can have on the environment and its protection will be analysed.

1. Bargaining power and the preference for public policy agendas

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236 Article 22 of the Canada-Jordan BIT 2009.
237 Article 32 of the US Model BIT 2012.
An important issue is the so-called bargaining power of States when negotiating IIAs. Some States, with bigger political influence, high FDI flows and more experience in treaty negotiating, do have the power and the budget to impose their way of treaty drafting. Other States, with smaller political power and less FDI flows might adapt to the regime proposed by more influential States. An illustrative example is the use of the explicit right to regulate clause by Colombia. The Colombia Model BIT 2008 requires the measures to be proportionate to the objectives sought. The UK-Colombian BIT 2010 raises the threshold for the host State to maintain, adopt or enforce an environmental measure, which has to be not only proportionate to the objectives sought, but must also meet the non-discriminatory test. To the attentive observer it seems that the United Kingdom, traditionally a capital exporting country, with over hundred negotiated BITs, was mindful of raising the protection of its investors vis-à-vis the right to regulate of the host State, Colombia in this case. Colombia contrariwise only started to conclude BITs in 1994 and negotiated until today only 17 different agreements.

In this context, the current trend to ‘negotiate in block’, most prominently promoted by the US, Canada and the EU, but as well seen with Asian States, should as well be noted. Such ‘megaregional agreements’, once concluded, may have systemic implications on the IIA regime. Regional grouping can marginalize non-participating third parties and eventually lead to impose a way of drafting to non-participating economies. There is a risk of non-participating countries turning from ‘rule makers’ to ‘rule takers’. Or in other words, ‘megaregional agreements’ make it more difficult for non-parties to effectively contribute to the shaping of the global IIA regime. At the same time, this may also present opportunities. ‘Megaregional agreements’ can have a demonstrating effect on other negotiations, for example if they provide for a reinforced inclusion of sustainable development features. Regional investment agreements could contribute to the overall coherence of IIAs and hence reduce fragmentation within the international investment regime.

Furthermore, it should not be forgotten that States pursue different policy agendas. For some States environmental protection is a very important objective, whereas for other States different objectives, for example security issues or the fight against corruption, are more relevant. Thus, the implementation of environmental language into IIAs depends to a great extent on the bargaining power and the pursued public policy agendas of the contracting parties.

239 See Part II subsection 2.5.
241 See as well J. E. Viñuales, Foreign Investment and the Environment in International Law, above 15, p. 15.
243 See the on-going negotiations of the TTIP (EU 28 and United States) and the CETA (EU 28 and Canada) or the RCEP (ASEAN countries and Australia, China, Japan, India, Republic of Korea and New Zealand). UNCTAD, World Investment Report 2014, above 4, pp. 118-24.
244 UNCTAD, World Investment Report 2014, above 4, pp. x, xxiii-xxv.
245 Ibid., pp. 123-4.
2. The combination of different environmental clauses

The combination of different clauses addressing environmental language is crucial. This paper identifies mainly three positive effects the introduction of environmental language in IIAs should have. First, it is important to find a proper balance between investor protection and environmental protection which ensures the overall legitimacy of the investment system. Second, a clear and precise treaty text assures legal security and limits the arbitrators’ discretion. Third and most importantly, the ultimate purpose of introducing environmental language in IIAs should safeguard or at least benefit environmental protection. Whether it is possible to achieve all these desired effects is highly dependent on the combination of different clauses. A clause can perhaps achieve one goal, but not achieve the desired total impact. Some selected aspects merit further comment below.

2.1. Preambles v. substantive obligations

As noted above, general preambular language does not create binding obligations for the treaty’s parties, therefore other binding environmental clauses should be introduced in the substantive part of the agreement. If an agreement features both preambular and substantive environmental language it assures best the protection of the environment.

2.2. Right to regulate v. promotion and protection of investment

Interestingly, the general structure of BITs or investment chapters in FTAs is not affected. Treaty negotiators opt mostly to keep promotion and protection provisions untouched at the beginning of the treaty to then insert an environmental clause, which addresses the relationship between investment and the environment. Furthermore, standards of treatment provisions of BITs or FTAs are not modified. The current approach to achieve environmental protection consists in inserting – next to the environmental clause – general exceptions or explicit right to regulate clauses, whose scope usually covers the whole treaty and assures that the government can act in favour of the public interest and hence for the environment.

One exception to the general hesitance to modify promotion and protection provisions of IIAs is the ‘environmental regulation, which does not constitute an indirect expropriation’ clause. Explicitly, adjustments of existing clauses were made to define when a regulatory measure amounts to indirect expropriation or should be considered as a non-compensable regulation. When it is true that an agreement, which already incorporates a general exception clause, contains further clause stating that non-discriminatory expropriation does not constitute an indirect expropriation, seems to address twice the same issue. That is to say, that the host State has the right to regulate for environmental purposes and does not have to compensate the investors adversely affected by the regulatory measure. Nevertheless, until today it is unclear if a general exceptions clause would set of the protection accorded to the investor under the agreement.

In light of this consideration it seems appropriate to include an

246 For example Article VIII of the Colombia Model BIT 2008; Article 12 of the US Model BIT 2012; Article 4 Austria Model BIT 2010; see as well Article 15 of the Canada Model BIT 2004.

environmental regulation, which does not constitute an indirect expropriation clause regardless of the general exception clause. This would enhance legal certainty.

Other standards of treatment, like national treatment²⁴⁸, most-favoured nation treatment²⁴⁹ or minimum international standards rules are generally not adapted. However, it should be reminded that standards of treatment provisions are conceived in a very broad language and that they can be used by investors to distort the adoption of new environmental laws or regulations by threatening with expensive arbitration claims. The fear of the host State to take environmental measures due to the unknown but latent and expensive consequences of vague IIAs provisions have led to the phenomenon of ‘regulatory chill’.²⁵⁰ Precision and clarity of the treaty text would provide for governments’ security to act in the public interest and thus overcome the ‘regulatory chill’. Yet, if the incorporation of environmental language in standards of treatment provisions is the proper approach to address environmental protection is beyond the scope of this paper.²⁵¹ Current new generation approaches welcoming environmental language, tend however not to modify the promotion and protection provisions, rather they insert or extend the right and obligations rules of investors and State Parties.²⁵²

Whether incorporating general exception clauses or an explicit right to regulate clause or even both should also be considered carefully. According to the knowledge of the author only the SADC Model BIT 2012 incorporates both a general exception clause and an explicit right to regulate clause.²⁵³

It has been noted that general exception clauses can either be interpreted as providing for more regulatory flexibility, codifying regulatory flexibility like the one

²⁴⁸ According to a 2011 OECD study, a national treatment exception, was only found once in Article 3(3) of the Russian Federation-Sweden BIT 1995, the clause reads: “Each Contracting Party may have in its legislation limited exceptions to national treatment provided for in Paragraph (2) of this Article. Any new exception will not apply to investments made in its territory by investors of the other Contracting Party before the entry into force of such an exception, except when the exception is necessitated for the purpose of the maintenance of defence, national security and public order, protection of the environment, morality and public health.” (K. Gordon, and J. Pohl, Environmental Concerns in International Investment Agreements: A Survey, above 23, p. 19.). This clause is an exception to the exception, providing that new exceptions to national treatment that are necessary to protect the environment, will apply to investment before the entry into force of the same exception. This is a rather untypical clause. Recent agreements concluded by Russia or Sweden, do not include such a clause. See for example the Sweden Model BIT 2002; Sweden-Kazakhstan BIT 2004; Sweden-Lebanon BIT 2001; Sweden-Ethiopia 2004 or the Russia-Guatemala BIT 2013.

²⁴⁹ With regard to fresh water and non-discrimination clauses see L. Boisson de Chazournes, Fresh Water in International Law, Oxford University Press, 2013, pp. 102-3. This author highlights that “a State may attempt to carve out express exclusions [of the guarantee of national treatment] during investment agreements negotiations.” And further “specific sectors or regulatory areas relevant to fresh water can be excluded from the general scope of most-favoured-nation treatment during the negotiation of the investment agreement.”


²⁵¹ The concrete analysis of the interplay between environmental obligations and standards of treatment of foreign investment is usually left to the development by the case law. For an interesting discussion relating to the energy sector see M. M Mbengue and D. Raju, ‘Energy, Environment and Foreign Investment’, above 169, pp. 171-91. For an analysis related to fresh water see L. Boisson de Chazournes, Fresh Water in International Law, above 249, pp. 96-108.

²⁵² Mostly they extend the host State’s rights and the investors’ obligations. See for example Part 3 of the SADC Model BIT 2012 or Part 3 to 6 of the IISD Model BIT 2005.

²⁵³ Article 20 of the SADC Model BIT 2012 states the right to regulate, whereas Article 25.1 of the same Model includes exceptions to pay compensation for adopting regulatory measures in the public interest.
existing in case law, or interpreted restrictively providing for less regulatory flexibility to the host State. For example, the IISD Model International Agreement on Investment for Sustainable Development 2012 does not include a general exceptions clause, it does however include a comprehensive explicit right to regulate clause. Apparently, one of the reasons why the drafters chose not to include a general exceptions clause was the concern of its restrictive interpretation by arbitral tribunals, which would result in a limitation of regulatory space of the host State.\(^{254}\) Thus, the risk of a restrictive interpretation exists. Furthermore, general exceptions clauses usually require the measure adopted by the host State to pass different tests of non-discrimination and necessity and not to be a disguised restriction to international trade or investment. Hence, it is notable that explicit right to regulate clauses assure both more regulatory freedom to the host State and a better balance of public and private interest than general exceptions clauses do.

However, whether explicit right to regulate clauses ultimately will be decisive to ensure a host State’s right to regulate in the interest of the environment, will need more thorough analysis and will be finally decided by a case-to-case approach.\(^{255}\)

### 2.3. Domestic v. international law

To create a safe investment climate most States adopted favourable domestic law regulations and concluded IIAs. In addition, a high quality of the local public administration and an effective system of dispute settlement contribute to attract foreign investment.\(^{256}\) Likewise, States pursue environmental objectives and therefore conclude MEAs and adapt their domestic environmental legislation.

The investment regime is not isolated from the rest of the body of international law; different fields of international law interact with each other. It is thus appropriate to include the Contracting Parties’, which are the States’, obligations to protect the environment into IIAs. The obligation of the host and home States to respect a given level of environmental standards is usually assured through the ‘not lowering environmental standards’ clause.\(^{257}\) Besides, a welcoming approach consists in including binding reference to multilateral environmental treaties.

However, in many cases, conflicts result from a clash between international rules protecting investment interests and national legislation that provides for environmental protection.\(^{258}\) It seems therefore important to include as well the obligation of the investors’ to respect environmental laws and standards into IIAs. This is far more difficult to assure since the parties to an IIA are the contracting States. The obligations of *investors* do usually not originate from IIAs but from the domestic law of the host State or from an investment contract.\(^{259}\) Yet, such obligation can be introduced by binding reference to domestic environmental law and general environmental principles.

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\(^{254}\) A. Newcombe, ‘General Exceptions in International Investment Agreements’, above 30, p. 366. See as well Part II subsection 2.10.


\(^{257}\) The value and scope of such a clause has been considered in Part II subsection 2.6.


In summary, it is crucial that new generation IIAs address both the contracting and the investors’ obligations to protect the environment.

2.4. IIA v. investment contract

VIÑUALES raises an interesting point. According to his own estimation there are notable differences between countries depending on whether they include environmental language or not. Most likely to include environmental concerns into their IIA is a non-OECD country concluding an agreement with an OECD country. Second most likely to make reference to environmental language are agreements concluded between OECD countries. Third and less likely to contain environmental language are agreements concluded between non-OECD countries.

Considering the first grouping, namely agreements concluded between a non-OECD and an OECD country, which generally speaking provide for more regulatory freedom for the host State to regulate for the purpose of the environment, then in the investment contracts concluded between investors and the non-OECD country, the investors seek and obtain broader contractual guarantees in connection with stability to their investment. This has led VIÑUALES to conclude that when IIAs are more permissive with regards to environmental protection, they have the undesired effect that investors seek and obtain stronger contractual protection.

This is an alarming phenomenon and should be observed and studied more closely in current studies on investment protection and the environment.

3. Enforcement and arbitration

Most investor-State disputes are not mere investment disputes, but involve issues of public policy. Investors increasingly challenge measures that relate to environmental protection or other issues of public governance.

Since decision on these matters are usually taken by three individuals, one day arbitors and the other day counsels, the qualification as such of an arbitral tribunal to decide on essentially issues of public policy can be questioned. Furthermore, until today the State is the perpetual respondent in investment arbitration. The investor acts as claimant, which makes it nearly impossible to tackle environmental violations committed by the investor. There is no general unlimited jurisdiction. The jurisdiction of an arbitral tribunal is based on the consent of the parties and limited by the scope of such consent. The arbitral tribunal risks an annulment of the award when excessing its power. However, arbitral tribunals have limited jurisdiction to mere investments disputes that means that environmental claims, to be adjudicated, have to form part of investment claims. Finally, amicus curiae interventions are highly debated. A State might for various reasons not be in the position to advocate an

environmental cause. The participation of third parties in the dispute is a positive novelty making it available for all stakeholders to defend their cause.

The procedural framework established by IIAs remains in various aspects inadequate for addressing environmental concerns.\textsuperscript{265} Efforts are needed to reconsider the procedural aspects in order to cope with wider issues of public policy and meet the complexity of environmental and investment protection.

\textbf{CONCLUSION}

The purpose of this paper is to contribute to a better understanding of how environmental language is included in IIAs. In this context it replies to three fundamental questions, to wit why to incorporate environmental protection into IIAs, how to do so and finally the impact these clauses can have and if they ultimately benefit environmental protection.

The paper starts with the simple statement that new generation treaties include increasingly environmental considerations. Twelve different but recurring clauses are identified in a network of BITs and FTAs that contain more than 3000 instruments. The willingness of different actors in the investment field is clearly towards incorporating environmental protection, however not always do the clauses assure this goal. Further resources and research are required to look for the best way to implement environmental language into IIAs.

The investment system becomes the more and more complex and interacts with other fields of international law. It was harshly criticised for restraining too much the ability of the host States to regulate in the public interest. IIAs were disapproved because they prone in favour of the investors and do not embrace a proper balance between public and private interests. As well international arbitration is in the negative spotlight in favouring the investors.

To counteract, this paper contents that clear and precise language in IIAs fosters the predictability of the investment system and reduces the risk of unintended or even adverse interpretation of treaty formula. In turn it is beneficial to all - investors, States and the environment. The investment system is not isolated from other fields of international law; hence, including environmental protection into IIA would enhance the overall legitimacy of the investment system. The negotiators of IIAs are the States: it is in their power to draft agreements that benefit investors, States and society as a whole.

Environmental protection cannot be postponed until tomorrow - the time is now, let us hope that treaty negotiators heard the call.

\textsuperscript{265} M. M. Mbengue and D. Raju, ‘Energy, Environment and Foreign Investment’, above 169, p. 191.
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WTO DISPUTE SETTLEMENT BODY


SELECTED LEGAL INSTRUMENTS


