

**Balancing Investor Protection and Regulatory Freedom in Investor-State Arbitration:
The Complex Search for State Purpose in a National Treatment Inquiry**

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I. Introduction

The field of international investment law has attracted significant criticism in recent years. That criticism is at its most acute when directed at the decisions of arbitral tribunals constituted to rule on the broad protections offered to foreign investors under bilateral and regional investment treaties. Many of those criticisms are justified, both on substantive and methodological grounds. When it comes to the latter in particular, the hermeneutics of investment arbitration remain deeply troubling. One can discern a stubborn tendency to prioritize outcome over process in investor-state arbitral reasoning, as is often naturally the case in its close but imperfect analogue, commercial arbitration. Those hermeneutic failures are problematic on a number of fronts, not least the failure of many arbitral tribunals to follow the interpretative taxonomy mandated by the *Vienna Convention on the Law of Treaties* 1969.

Against this cloudy backdrop, there are the beginnings of a bright jurisprudential star. Arbitral tribunals ruling on national treatment have, for the most part, positioned their legal analysis by searching for a form of prohibited state purpose. This purpose-base approach is both doctrinally sound and normatively superior to other juridical candidates. In particular, it offers arbitral tribunals a powerful and rigorous technique to sanction impermissible

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(discriminatory) behavior while preserving the flexibility for states to regulate for legitimate reasons. Indeed, this remarkable “judicial” innovation dovetails *and* complements a key “legislative” response. States parties are engaged in a concerted push to pare back the extensive protections offered by the classic model bilateral investment treaty (BIT).¹ This process of recalibration has manifested itself visibly in prospective treaty change both in the tightening of substantive obligations and inclusion of general exceptions clauses.

Underpinning this strategy is a natural and sensible desire to inject greater flexibility for state regulation within the system of investor protection. Yet some of these treaty innovations – such as the delineation of predicates to a finding of indirect expropriation – now require an arbitrator to explicitly review a state’s purpose underpinning a law or regulation.² Here then is a potential role for the purpose-based approach taken in national treatment to transcend that legal norm and productively guide adjudication for breach of other investment protections.

Moreover, the sophisticated arbitral techniques developed on national treatment may well have a broader resonance than the system of investment protection alone. Across the set of WTO treaties, there are national treatment obligations on trade in goods³, trade in services⁴, the protection of intellectual property⁵, the use of technical barriers to trade⁶ and in relation to government procurement practices⁷. Yet there remains a distinct ambiguity within much of

¹ *E.g.*, José E. Alvarez, *The Once and Future Foreign Investment Regime*, in LOOKING TO THE FUTURE: ESSAYS IN HONOR OF W. MICHAEL REISMAN 607-648 (M. Arsanjani et al. eds., 2010); José E. Alvarez, *The Return of the State*, 20(2) MINN. J. INT’L L. 223-264 (2011).

² For analysis of recent treaty practice (including in the 2009 ASEAN Comprehensive Investment Agreement) requiring adjudicators to consider state purpose as a condition of determining whether a law or regulation should be classified as indirect expropriation, see *infra* [].

³ General Agreement on Tariffs and Trade, Oct. 30, 1947, 55 U.N.T.S. 194 [hereinafter GATT 1947], GATT, at Art. III.

⁴ General Agreement on Trade in Services, Apr. 15, 1994, Marrakesh Agreement Establishing the World Trade Organization, Annex 1B, in WORLD TRADE ORGANIZATION, THE RESULTS OF THE URUGUAY ROUND OF MULTILATERAL TRADE NEGOTIATIONS: THE LEGAL TEXTS 284 (1994) [hereinafter WTO Agreements], at Art. XVII.

⁵ Agreement on Trade-Related Aspects of Intellectual Property Rights, Apr. 15, 1994, Annex 1C, WTO Agreements, *supra* note [], at Arts. 2.1 and 3.

⁶ Agreement on Technical Barriers to Trade, Apr. 15, 1994, Annex 1A, WTO Agreements, *supra* note [], at Art. 2.1.

⁷ Agreement on Government Procurement, Apr. 15, 1994, Annex 4 (Plurilateral Trade Agreements), WTO Agreements, *supra* note [], at Art. III.

WTO jurisprudence and secondary analysis both on the question of whether state purpose is a condition of breach and whether key evidentiary proxies (such as individual statements of elected officials) should form part of such a test.⁸ Given the willingness of arbitral tribunals to delve into motive review, investment arbitration offers a valuable comparative laboratory by which those perceived objections might be examined and weighted and could even offer a useful guide to the future evolution of WTO law. To that extent, this article contests the (often unstated) premise held by many commentators that the older and more established WTO jurisprudence on select norms is necessarily superior to certain approaches adopted in investment arbitration

Part II begins by outlining the case for motive review in a national treatment inquiry. The interpretative claims put forward in this part intentionally track the methods of the VCLT. In other words, its primary methodology is exactly what *should* be undertaken by adjudicators when resolving national treatment claims by systematically reviewing the text of typical clauses in investment treaties and assessing those terms in light of key contextual guidance and expressions of the object and purpose of those treaties. Using these interpretative techniques, we find clear evidence that states parties intended for national treatment to guarantee competitive opportunities for foreign investors operating in host states. To protect those competitive opportunities, national treatment has a logical role to play in combating protectionism defined as the intent of the host state to confer advantage on domestic actors

⁸ For analysis on this point as a matter of WTO law, see Robert Hudec, *GATT/WTO Constraints on National Regulation: Requiem for an "Aims and Effects" Test*, 32 (3) INT'L LAW. 619 (1998); REGULATORY BARRIERS AND THE PRINCIPLE OF NON-DISCRIMINATION IN WORLD TRADE LAW (Thomas Cottier & Petros Mavroidis eds, 2000); Donald Regan, *Regulatory Purpose and "Like Products" in Article III:4 of the GATT (With Additional Remarks on Article III:2)*, 6 (3) J. WORLD TRADE 443 (2002); Lothar Ehring, *De Facto Discrimination in WTO Law: National Treatment and Most-Favoured-Nation Treatment – or Equal Treatment?*, 36 J. WORLD TRADE 921 (2002); Henrik Horn & Petros C. Mavroidis, *Still Hazy after All These Years: National Treatment in the GATT/WTO Case-Law on Tax Discrimination*, 15 (1) EUR. J. INT'L L. 39-69 (2004); Julia Qin, *Defining Nondiscrimination under the Law of the World Trade Organization*, 23 B.U. INT'L L.J. 215 (2005).

that operate in competition with “like” foreign investors. While not a primary goal, this part of the article also contradicts the occasional claim that, unlike trade in goods, the political economy of investment policy does not give rise to an appreciable and consistent risk of protectionism. Having outlined this legal and political economy case, Part II surveys a range of normative considerations to justify the particular and vital role for an examination of state purpose in this doctrinal model.

Part III then turns to a set of objections to this test, not least the perceived sensitivity of requiring an adjudicator to confront head-on the regulating state’s assertion of a legitimate rationale underpinning its measure. While not a compelling objection, it is one that must be treated seriously especially given the relative immaturity of the system of investor-state dispute settlement. Indeed, that concern of sensitivity seems to have been used by some states to improperly load the direction of a purpose-based test by inviting adjudicators to exhibit deference to their claim of a legitimate purpose. More subtly and even more problematically, some tribunals have failed to distinguish the manner in which discrimination can embed itself *both* in the formulation of a general policy goal and in the specific exercise of discretion when implementing that goal. This area of adjudication, it is argued, would benefit from close consideration of WTO law which has long recognized the importance of a rigorous approach that properly distinguishes between regulator design and enforcement.

Having argued that national treatment can and should guard against the ability of a host state to engage in protectionism at different stages of a regulatory scheme, Part IV then turns to the difficult question of how to operationalize that test. It begins by positioning national treatment in conceptual terms as a discipline on political failure, being the excessive influence of domestic interests in the formation of investment policy. Using that start-point, Part IV then

constructs a tractable model for uncovering state purpose using a broad range of evidential sources, capable of both fair and accurate disposition of national treatment claims. That model is presented with a particular eye to the specifics of investor-state arbitration and especially the question of what is reasonable for an investor (as a non-state actor) to adduce as evidence when litigating against a state party.

II. Likeness, Competition and Motive Review:

The Legal and Normative Case

One of the difficulties facing investment treaty interpreters is the typically sparse architecture of the national treatment clause under adjudication. For example, NAFTA Article 1102(1) simply requires member states “to accord to investors of another Party treatment no less favorable than that it accords, in like circumstances, to its own investors”.⁹ The treatment of foreign and domestic investors must then be compared but only insofar as these actors are “in like circumstances”. Breach will follow if the foreign investor is treated less favourably than “like” domestic investors. The text of the clause does not, of itself, conclusively indicate whether competition or some other connection is the required condition for a foreign investor to stand “in like circumstances” with domestic investors. An adjudicator might thus be tempted to resort to dictionary definitions to resolve this question as part of her obligation to uncover the “ordinary meaning” of the terms of a treaty as required by Article 31(1) of the VCLT.¹⁰ “Like” could be taken as a synonym for “similar”, which is the usual guidance offered

⁹ North American Free Trade Agreement, Dec. 17, 1992, Can.-Mex.-U.S., 32 ILM 289 & 505 (1993) [hereinafter NAFTA], Art. 1102.

¹⁰ Vienna Convention on the Law of Treaties, May 23, 1969, 1155 U.N.T.S. 331 [hereinafter VCLT], at Art. 31(1)

in dictionary definitions of that term.¹¹ But this only raises a series of further questions, most notably similar in what respect, degree and from whose perspective?¹² Two investors may be similar in certain ways but not others. They may, for example, produce the same good or service but differ in the manner in which their business operations are structured. Foreign investors often adopt complex integration strategies in order to acquire efficiency gains whereby production processes are split into various activities and carried out in locations best suited to the particular activity.¹³ The product sold or service supplied by the foreign investor in the host state could then comprise the end-point in an integrated supply chain that stretches across multiple jurisdictions. They could, in this respect, be said in formal terms to differ from domestic investors (that produce the same good or service) whose business operations are located and integrated solely within the host state.¹⁴ This then is a hypothetical in which two investors are similar with regard to some qualities (output) and different with regard to others (structure). Some external criterion must be introduced in order to understand which of these factors matter in ultimately deciding whether the two investors are like. There is, in short, no context-independent meaning of likeness that we can use to easily dispose of these hard choices.¹⁵ Certain arbitral tribunals have recognized this inherent limitation at the level of the text of the typical national treatment clause found in investment treaties.¹⁶

¹¹ See, e.g., *Pope & Talbot Inc. v Canada*, Award on the Merits of Phase 2 (UNCITRAL, Apr. 10, 2001), at para 75 and fn. 68 (extracting the Webster definition and finding that “the concept of ‘like’ can have a range of meanings, from ‘similar’ all the way to ‘identical’”).

¹² For analysis of the limitations of dictionary definitions in WTO law, see *European Communities – Measures Affecting Asbestos and Asbestos-Containing Products*, Report of the Appellate Body (WT/DS135/AB/R, Mar. 12, 2001), at para 92.

¹³ E.g., *ADF Group Inc. v U.S.*, Award (ICSID Case No. ARB(AF)/00/1, Jan. 9, 2003), at para 49-55 (concerning a Canadian company’s plan to buy U.S steel, undertake fabrication work at its facilities in Canada and then ship the processed steel back to the U.S in order to meet certain “Buy America” conditions); *SD Myers, Inc. v Canada*, Partial Award (UNCITRAL, Nov. 13, 2000), at para 93 (concerning the establishment of a subsidiary of a U.S company in Canada to contract for waste remediation services where the waste would be shipped for processing at facilities in the U.S.).

¹⁴ In *ADF*, the respondent state essentially made a submission along these lines arguing that “[NAFTA] Article 1102 does not guarantee a parent and its subsidiary corporation an ‘ability to freely transfer goods and services between [them inter se]’”. *ADF v USA*, *supra* note [], at para 98.

¹⁵ Consider also, in this respect, the following statement made by a WTO panel examining the interpretative elements referred to in Article 31 of the VCLT: “Context and object-and-purpose may often appear simply to confirm an

The same position holds true in WTO law, for example, when it comes to understanding the phrase “like products” in the guarantee of national treatment for trade in goods in GATT Article III(4).¹⁷ There is, however, a critical difference between GATT Article III(4) and the usual construction of national treatment in investment law. GATT Article III(1) offers pertinent contextual guidance to an adjudicator faced with understanding the scope and elements of GATT Article III. It explicitly states that the purpose of the national treatment guarantees in both Articles III(2) and III(4) is to prevent the application of measures “so as to afford protection to domestic production”. It is this general purpose of avoiding protectionism that confirms for us the necessity of certain dimensions of likeness.¹⁸ It is *only* if two products are in competition that a measure which affects them unequally will operate “so as to afford protection”. In sum then, GATT Article III(1) supplies the critical contextual justification that competition is a necessary condition of likeness for purposes of Article III(4).

It would be a mistake however to place too much emphasis on the simple absence of a GATT Article III(1) in the investment treaty setting. After all, the injunction against protectionism (crystallized in GATT Article III(1)) merely reflects the well-known political economy of trade policy.¹⁹ In the trade context, theorists emphasize the concentrated losses that are incurred in

interpretation seemingly derived from the ‘raw’ text. *In reality, it is always some context, even if unstated, which determines which meaning is to be taken as ‘ordinary’* and frequently it is impossible to give meaning, even ‘ordinary meaning’, without looking also to object-and-purpose.” (emphasis added) *United States- Sections 301-310 of the Trade Act of 1974*, Report of the Panel (WT/DS152/R, Dec. 22, 1999), at para 7.22.

¹⁶ E.g., *Pope & Talbot v Canada*, *supra* note [], at para 75 (“By their very nature, ‘circumstances’ are context dependent and have no unalterable meaning across the spectrum of fact situations.”).

¹⁷ I am focusing here on GATT Article III(4) rather than Article III(2) due to the latter’s bifurcation into separate sentences. My interest is on the role of GATT Article III(1) in supplying contextual guidance for the interpretation of the phrase “like products” in GATT Article III(4). The same position holds true in respect of the phrase “like products” in GATT Article III(2) (first sentence) but is complicated by the additional guidance offered in the intersection of the first and second sentences of Article III(2). With this in mind, a focus on Article III(4) is sufficient for my immediate needs.

¹⁸ For extensive analysis on this point, see Donald Regan, *Regulatory Purpose and “Like Products” in Article III:4 of the GATT (With Additional Remarks on Article III:2)*, 6 (3) J. WORLD TRADE 443, 444-5 (2002).

¹⁹ For the classic public choice account on the formation of trade policy in the domestic setting, see Gene M. Grossman & Elhanan Helpman, *Protection for Sale*, 84 (4) AM. ECON. REV. 833 (1994).

a shift towards a policy of free trade. Import-competing industry has abundant incentives to lobby incumbent governments to maintain or entrench systems of trade protection. The concentrated job losses that flow from a shift towards free trade in a given industry also align labor interests with that of industry seeking protection.²⁰ In contrast, the relatively minor benefits to individual consumers are unlikely to motivate dispersed consumers to bind together and lobby for a policy of free trade.²¹ Regulatory outcomes then may systematically prioritize the welfare of the few (import-competing industry) over the welfare of the many (consumers in the importing state). There is, in short, a structural bias towards protectionism in the formation of trade policy, at least for states whose political ordering allows for lobbying by affected interests.²²

We might then examine the political economy surrounding investment restrictions to assess whether there is a sizeable risk of protectionism in that setting. After all, if the political economy of investment policy reveals a similar risk of capture by competing domestic interests in a host state, this would offer strong justification for reading national treatment in investment treaties as a limit on protectionism (even with the absence of a GATT Article III(1)). Surprisingly however, there is very little targeted analysis of this dimension among legal scholars in the field. Where it occurs, there is a distinct tendency to commence with heuristics of foreign imports as ‘bad’ and foreign capital as ‘good’ (from the perspective of domestic

²⁰ Robert E. Baldwin, *The Political Economy of Trade Policy: Perspectives of Economists and Political Scientists*, in THE POLITICAL ECONOMY OF TRADE POLICY: PAPERS IN HONOR OF JAGDISH BHAGWATI 147, 162 (Robert C. Feenstra et al eds, 1996)

²¹ *Id.*

²² The qualification here goes to authoritarian states organized on non-democratic lines. One might imagine that the leadership of such states is less likely to be influenced by the short-term views of a small number of affected domestic interests. But even here, some political scientists have suggested that such states are not entirely immune from political pressures. There is the argument that “such leaders must still be concerned about the possibility of losing political power through military coups, riots, and mass demonstrations touched off by policies unpopular with various economic and social groups”. *Id.* at 159.

regulators.²³ There are a number of flaws with this line of reasoning. First, the heuristic may hold true for *certain* forms of foreign capital such as foreign direct investment (FDI) whose entry is often (but not always) regarded by domestic political actors as a positive input that boosts industrial development and job creation. But the scope of investment treaties extends far beyond FDI to include less sticky forms of capital such as debt or portfolio investment that is prone to sudden reversals or “herd” behavior which has often attracted restrictive regulation by host states.²⁴ Even if we focus on FDI, a careful examination of the political science literature – rather than of simple heuristics – reveals that the political economy of investment policy is not fundamentally different than the trade context. Most importantly, competing domestic industry has exactly “the same incentive to lobby for barriers to investment as it has to lobby for impediments to trade” given the displacement of its market share through foreign competition (whether in the form of FDI or imports of foreign goods/services).²⁵

National treatment then in the investment law context would seem to have a logical and principled role to play as a constraint on purposeful protectionism. There is indeed targeted contextual guidance across a grouping of investment treaties to justify this reading. For instance, Article 17(2) of the 2007 Investment Agreement of the Common Market for Eastern and Southern Africa provides that the “like circumstances” inquiry “requires an overall examination on a case by case basis of all the circumstances of an investment including, *inter alia*...(c) the sector the investor is in; (d) the aim of the measure concerned; (e) the regulatory

²³ Nicholas DiMascio & Joost Pauwelyn, *Nondiscrimination in Trade and Investment Treaties: Worlds Apart or Two Sides of the Same Coin?*, 102 (1) AM. J. INT’L L. 48, 56 (2008); Joel Trachtman, *FDI and the Right to Regulate: Lessons from Trade Law*, in UNCTAD, *The Development Dimensions of FDI: Policy and Rule-Making Perspectives* 189, UN Doc. UNCTAD/ITE/IIA/2003/4 (2003) at 191.

²⁴ On the relative stability of FDI compared to the sudden withdrawals of short-term debt capital and portfolio investment during both the Mexican peso devaluation of 1994-5 and the Asian economic crisis of 1997-8, see Asaf Razin, *Social Benefits and Losses from FDI*, in REGIONAL AND GLOBAL CAPITAL FLOWS (T. Ito & A. Krueger eds., 2001).

²⁵ Gene M. Grossman & Elhanan Helpman, *Foreign Investment with Endogenous Protection*, in THE POLITICAL ECONOMY OF TRADE POLICY: PAPERS IN HONOR OF JAGDISH BHAGWATI 199, 216 (Robert C. Feenstra et al. eds., 1996).

process generally applied in relation to the measure concerned”.²⁶ But for the most part this type of explicit formula is exceptional insofar as it obliges an adjudicator to consider both competitive interactions and the underlying purpose of the measure under review. This then raises what *other* contextual guides an adjudicator might draw upon in determining the meaning and scope of the relational condition of likeness in an investment treaty.

An additional possibility is the guidance offered by the 1976 OECD National Treatment Instrument. This Instrument adopts similar language to many investment treaties by requiring OECD member states to accord foreign investors treatment that is “no less favourable” than that provided “in like situations to domestic enterprises”.²⁷ Member states must notify one another of domestic laws which do not conform to the standard expressed in the Instrument, which are defined as “exceptions” to the Instrument. Six years after its inception, the OECD released a clarification of the substantive components of the Instrument.²⁸ By 1993, the clarification had been distilled into a final form:

As regards the expression “in like situations”, the comparison between foreign-controlled enterprises established in a Member country and domestic enterprises in that Member country is valid only if it is made between firms operating in the same sector. More general considerations, such as the policy objectives of Member countries, could be taken into account to define the circumstances in which comparison between foreign-controlled and domestic enterprises is permissible inasmuch as those objectives are not contrary to the principle of National Treatment. In any case, the key to determining whether a discriminatory measure applied to a foreign-

²⁶ Investment Agreement for the COMESA Common Investment Area, adopted at Nairobi, May 22-3 2007, at Art. 17 (National Treatment).

²⁷ The OECD National Treatment Instrument forms part of the 1976 OECD Declaration on International Investment and Multinational Enterprises. The full text of the Instrument comprises:

That Member countries should, consistent with their needs to maintain public order, to protect their essential security interests and to fulfill commitments relating to international peace and security, accord to enterprises operating in their territories and owned or controlled directly or indirectly by nationals of another Member country (hereinafter referred to as “Foreign-Controlled Enterprises”) treatment under their laws, regulations and administrative practices, consistent with international law and no less favourable than that accorded in like situations to domestic enterprises.

OECD, DECLARATION ON INTERNATIONAL INVESTMENT AND MULTINATIONAL ENTERPRISES, Art. II.1 (Jun. 21, 1976).

²⁸ OECD, MID-TERM REPORT ON THE 1976 DECLARATION AND DECISIONS Annex V (1982).

controlled enterprise constitutes an exception to National Treatment is to ascertain whether the discrimination is motivated, at least in part, by the fact that the enterprises concerned are under foreign control.²⁹

Likeness as expressed in the clarification has two key elements. A foreign investor must operate “in the same sector” as a domestic actor, which has been sensibly understood by investor-state arbitral tribunals as an inquiry directed to competitive conditions in a market. In *SD Myers v Canada* for example, the Tribunal drew on the OECD Instrument to find that “the word ‘sector’ has a wide connotation that includes the concepts of ‘economic sector’ and ‘business sector’”.³⁰ On the facts, the Tribunal ruled that the foreign investor was “in like circumstances” with Canadian operators because “[t]hey all were engaged in providing PCB waste remediation services” and the foreign investor “was in a position to attract customers that might otherwise have gone to Canadian operators”.³¹ But discrepant treatment of a foreign investor vis-à-vis its domestic competitors will not alone justify breach under the OECD National Treatment Instrument. Notice from the extract above that the “key” is whether the difference in treatment was “motivated” by the nationality of the foreign investor. Thus, where a state treats a foreign investor less favourably than a domestic competitor and has no legitimate purpose for making that distinction other than the nationality of the foreign investor, there will be breach. This approach closely approximates a test directed at purposeful protectionism.³² Indeed, certain NAFTA Tribunals, especially *Pope & Talbot v Canada*, have expressly relied on the OECD clarification of the Instrument in positioning their reading of national treatment in NAFTA Article 1102 as a limit on purposeful protectionism.³³

²⁹ OECD, NATIONAL TREATMENT FOR FOREIGN-CONTROLLED ENTERPRISES 22 (1993).

³⁰ *SD Myers v Canada*, *supra* note [], at para 250.

³¹ *Id.* at para 251.

³² My qualification here goes to the OECD’s preparedness to countenance breach (or in its terms, to find an “exception”) if protectionism is a partial motivation for the measure in question. Notice that under its formulation, a measure will comprise an exception if “the discrimination is motivated, *at least in part*, by the fact that the enterprises are under foreign control” (emphasis added). If our goal is to discipline protectionism, where an adjudicator discerns multiple motivations the measure should only be struck down if protectionism is the ultimate cause for the measure in question. In other words, the mere fact that protectionism is one of a number of purposes should not alone suffice to ground breach.

³³ *Pope & Talbot v Canada*, *supra* note [], at para 78-9 and fn 73 (extracting the 1993 OECD clarification to the National Treatment Instrument in finding that “[a] formulation focusing on the like circumstances questions... will require

The strategy (by the *SD Myers* and *Pope & Talbot* Tribunals) of using the OECD Instrument to inform their reading of national treatment in NAFTA Chapter 11 is a sound one. There are significant parallels between the two legal norms and systems which would make it artificial to read them independently from each other. All of the NAFTA states are members of the OECD and there is marked similarity in the textual formulation of the two commitments. There is still the question however of what formal justification can be found for the use of the OECD Instrument under the interpretative taxonomy of the VCLT. One, albeit marginal, possibility is to characterize the Instrument as context under Article 31(2)(a) of the VCLT.³⁴ While there is no doubt that the OECD Instrument is concerned with the substance of part of NAFTA Chapter 11 (and as such, is an agreement “relating to the treaty”), it pre-dates the finalization of NAFTA Chapter 11 and could hardly be said to have been made “in connection with the conclusion of the treaty” under Article 31(2)(a).³⁵ The OECD Instrument could still be legitimately used by a NAFTA adjudicator under the separate obligation to take into account other “relevant rules of international law” in Article 31(3)(c) of the VCLT.³⁶ That strategy may prove more difficult outside of the NAFTA, when one or more of the state parties to the investment treaty adjudication are not OECD members. Article 31(3)(c) is confined to external rules “applicable in the relations between the parties” and certain international tribunals have interpreted this particular condition narrowly to preclude consideration of an external treaty whose membership does not include all of the states parties of the treaty under adjudication.³⁷ This

addressing any difference in treatment demanding that it be justified by showing that it bears a reasonable relationship to rational policies not motivated by preference of domestic over foreign owned investments”).

³⁴ Under Article 31(2)(a), “context” includes “any agreement relating to the treaty which was made between all the parties in connection with the conclusion of the treaty”. VCLT, *supra* note [].

³⁵ See also IAN SINCLAIR, *THE VIENNA CONVENTION ON THE LAW OF TREATIES* 129 (2nd ed, 1984) (arguing that Article 31(2)(a) requires an agreement to have been “drawn up on the occasion of the conclusion of the treaty”).

³⁶ VCLT, *supra* note [], at Art. 31(3)(c).

³⁷ *European Communities – Measures Affecting the Approval and Marketing of Biotech Products*, Report of the Panel (WT/DS291/R, Sept. 26, 2006), at paras. 7.67-7.71. See also Robert Howse, *The Use and Abuse of Other “Relevant*

highly restrictive interpretation of Article 31(3)(c) has attracted significant criticism and is not without doubt.³⁸ Yet, leaving the specifics of that debate aside, it is important to bear in mind that Article 31(3)(c) is only one portal through which external legal norms can be legitimately considered under the VCLT by an adjudicator. The OECD Instrument could, for instance, still be examined as part of a comparative exercise to uncover the “ordinary meaning” (under Article 31(1) of the VCLT) of the national treatment clause of an investment treaty even where one or more state parties are not member states of the OECD. Of course, in this latter scenario it would be especially prudent for an adjudicator to assess what further contextual support can be found to buttress their chosen reading.

A further contextual guide might be located in the manner in which national treatment is articulated in *other* parts of the treaty under adjudication. In most Free Trade Agreements, there are various formulations of national treatment across dedicated subject areas. There are, for instance, six national treatment clauses in total in the NAFTA.³⁹ Not all of these additional clauses will offer pertinent guidance for the interpretation of NAFTA Article 1102. For example, NAFTA Article 301(1) (on trade in goods) simply incorporates GATT Article III as an operative obligation.⁴⁰ It thereby transplants GATT Article III(1) which, as we have seen, is precisely the interpretative guide that is absent from the text of NAFTA Article 1102. Yet

Rules of International Law” in *Treaty Interpretation: Insights from WTO Trade/Environment Litigation*, IILJ WORKING PAPER 2007/1 (www.iilj.org), at 24-8.

³⁸ *Fragmentation of International Law: Difficulties Arising from the Diversification and Expansion of International Law*, Report of the Study Group of the International Law Commission, U.N. Doc. A/CN.4/L.682 (Apr. 4, 2006) [hereinafter ILC Fragmentation Report], at paras 450 and 471-2.

³⁹ These are Articles 301(National Treatment for Trade In Goods); 904(3) (National Treatment for Standards-Related Measures); 1003 (National Treatment for Government Procurement); 1202(2) (National Treatment for Cross-Border Trade in Services); 1102 (National Treatment for Foreign Investment); 1405 (National Treatment for Financial Services); 1703 (National Treatment for Intellectual Property). NAFTA, *supra* note [].

⁴⁰ NAFTA Article 301(1) provides:

Each Party shall accord national treatment to the goods of another Party in accordance with Article III of the *General Agreement on Tariffs and Trade* (GATT), including its interpretative notes, or any equivalent provision of a successor agreement to which all Parties are party, are incorporated and made part of this Agreement.

NAFTA, *supra* note [].

certain other national treatment clauses in the NAFTA may shed crucial contextual light on the scope of Article 1102.

As a start point, NAFTA Chapter 11 applies to any measure of a member state relating to “investors” and “investments” from another member state *except* where the investment takes place in the financial services sector.⁴¹ For the latter, there is a dedicated construct – NAFTA Chapter 14 – that applies exclusively to *both* cross-border trade and foreign investment in financial services.⁴² The bifurcation between general and specific (financial services) commitments on foreign investment finds early reflection in the architecture of the 1987 Canada-US Free Trade Agreement, around which many of the later NAFTA provisions are based.⁴³ But the NAFTA significantly deepens and extends commitments on financial services⁴⁴, a key objective of some of the states parties⁴⁵. At the same time, there is textual evidence that those parties foresaw the need to carefully tailor the scope of these broader commitments to deal with specific risks thrown up by deeper liberalization of the finance sector. We find, for instance, a dedicated exception in NAFTA Article 1410 for measures taken for “prudential reasons” in the finance sector which, in turn, has little relevance for regulation

⁴¹ NAFTA, *supra* note [], at Arts. 1101(1) and (3).

⁴² *Id.* at Art. 1401(1).

⁴³ Canada-US Free Trade Agreement, opened for signature Dec. 22, 1987, 27 ILM 281 (1988) [*hereinafter* CUSFTA], at Chapters 16 and 17.

⁴⁴ In Chapter 17 of the CUSFTA for example, the commitments on financial services by both the U.S and Canada take the form of a list of very specific agreements rather than general obligations. CUSFTA, *supra* note [], at Arts. 1702-3. On the other hand, NAFTA Chapter 14 hand offers a broad range of general commitments that apply to cross-border trade and foreign investment in the finance sector. NAFTA, *supra* note [], at Arts. 1401(2); 1402-8.

⁴⁵ For example, Canada’s 1994 statement of implementation on the NAFTA details two key objectives for NAFTA Chapter 14. The first objective “was to gain access to the Mexican market” while:

The second objective was to move beyond the FTA by basing market access on a set of general rules enshrining national treatment, MFN treatment, the right of consumers to purchase financial services on a cross-border basis and the right to market access through the establishment of a commercial presence. The emphasis on defining principles, rather than the *à la carte* approach taken in the FTA is path-breaking of the best kind, building on progress made in the Uruguay Round negotiations in drafting a General Agreement on Trade in Services.

Canadian Statement on Implementation, North American Free Trade Agreement, Canada Gazette, Part 1, (Jan. 1, 1994) [*hereinafter* Canadian NAFTA Implementation Statement], at 172-3.

of foreign investment in other economic sectors.⁴⁶ Similarly, where a state invokes the prudential exception in a Chapter 14 dispute, the presiding Tribunal may not be the ultimate arbiter on the sufficiency of that defence.⁴⁷ That task can fall to a specialist Financial Services Committee, made up of expert banking and finance regulators.⁴⁸

Despite this careful tailoring, these NAFTA chapters are not set in isolation from each other. Chapter 14 expressly incorporates various substantive disciplines from Chapter 11, including the protection against expropriation (in NAFTA Article 1110) and investor-state dispute settlement for those incorporated obligations.⁴⁹ Thus, a foreign investor who has set up operations in the financial services sector of a NAFTA state can initiate investor-state dispute settlement but only in relation to these incorporated obligations including for compensation in the event of expropriation. For all other commitments in Chapter 14, investor-state arbitration is precluded and any dispute can only be resolved under the general mechanism of state-to-state processes.⁵⁰ Article 1405 on national treatment in Chapter 14 is one of these other commitments subject only to state-to-state dispute settlement.

We have then two national treatment clauses - in Articles 1102(1)-(2) and 1405(1)-(2) – both of which deal with “investment” (albeit in different sectors) and also fall within the same umbrella of a specific part of the NAFTA, being Part Five. There is also a striking degree of similarity between the text of these national treatment clauses⁵¹, which logically suggests that

⁴⁶ NAFTA, *supra* note [], at Art. 1410(1).

⁴⁷ For disputes involving the invocation of NAFTA Article 1410 and on the request of the respondent state, a Tribunal “shall refer the matter in writing to the [Financial Services] Committee for a decision”. That Committee is then empowered to “decide the issue of whether and to what extent Article 1410 is a valid defense to the claim of the investor” and its decision “shall be binding on the Tribunal”. NAFTA, *supra* note [], at Arts. 1415(1) and (2).

⁴⁸ NAFTA, *supra* note [], at Art. 1412.

⁴⁹ NAFTA, *supra* note [], at Art. 1401(2).

⁵⁰ *Id.* at Art. 1414(1).

⁵¹ Compare, for example, NAFTA Articles 1102(1) and 1405(1) which provide respectively:

the difference intended by the negotiators falls at the level of dispute settlement and exception (in particular, for prudential measures in the finance sector) rather than obligation.⁵² Indeed, in the single case decided to date under NAFTA Chapter 14, there is support for the view that national treatment has a similar scope of operation in *both* Chapters 11 and 14. In *Fireman's Fund v Mexico*, a U.S. company that had acquired debentures issued by a Mexican bank initiated proceedings against Mexico for expropriation under Chapter 14.⁵³ As part of its expropriation analysis, the Tribunal ruled that Mexico had acted in a discriminatory fashion by purchasing debt instruments of Mexican nationals (as part of a government bail-out) but failing to do so for foreign holders of the same type of debt instrument.⁵⁴ It went on to rule, albeit in *obiter*, that “[s]uch treatment might have given rise to a claim by an investor under Articles 1102 (National Treatment), Article 1105 (Minimum Standard of Treatment) or Article 1405 (National Treatment) of the NAFTA, or under two or all of them”.⁵⁵ Of course, we should be careful not to read too much into a single and sparse statement such as this. But the suggestion that the same type of discrimination can potentially fall within the scope of both forms of national treatment in Articles 1102 and 1405 is a sensible intuition on the part of the *Fireman's Fund* Tribunal. It is difficult to see the value in having two different standards of national

Each Party shall accord to investors of another Party treatment no less favorable than that it accords, in like circumstances, to its own investors with respect to the establishment, acquisition, expansion, management, conduct, operation and sale or other disposition of its investments.

Each Party shall accord to investors of another Party treatment no less favorable than that it accords to its own investors, in like circumstances, with respect to the establishment, acquisition, expansion, management, conduct, operation, and sale or other disposition of financial institutions and investments in financial institutions in its territory.

NAFTA, *supra* note [].

⁵² There is a counter-argument here that could run as follows. If the NAFTA states were prepared to incorporate commitments on expropriation from Chapter 11 into Chapter 14, the fact that they chose *not* to do so for national treatment suggests they intended different things from the two national treatment clauses. There is an obvious response to this objection. NAFTA Chapter 14 is not confined to foreign investment in financial services; it also covers cross-border trade in such services. It makes perfect sense to incorporate by reference a commitment on expropriation as, by definition, it will *only* apply to an actor who has commercial presence in a NAFTA state. National treatment, on the other hand, can potentially apply to both forms of economic exchange. For this reason, we find a tailoring of the national treatment commitment in NAFTA Article 1405 to deal with the specifics of both foreign investment (sub-paragraphs (1) and (2)) and cross-border trade (sub-paragraph (3)).

⁵³ *Fireman's Fund Insurance Company v Mexico*, Award (ICSID Case No. ARB(AF)/02/01, Jul. 17, 2006), at paras. 5-6.

⁵⁴ *Id.* at paras. 201-3.

⁵⁵ *Id.* at para 203.

treatment where the underlying economic exchange being protected - movement of capital - is the same.

If we accept an approach that looks for contextual guidance from NAFTA Article 1405 when interpreting NAFTA Article 1102, a number of pertinent points follow. The first is an explicit confirmation that the purpose of national treatment is to guarantee “equal competitive opportunities”. Article 1405(5) provides:

A Party’s treatment of financial institutions and cross-border financial service providers of another Party, whether different or identical to that accorded to its own institutions or providers in like circumstances, is consistent with paragraphs 1 through 3 if the treatment affords equal competitive opportunities.⁵⁶

If national treatment is to guarantee competitive opportunities, this necessarily requires comparison of the treatment afforded foreign vis-à-vis domestic *competing* investors to determine whether the state has complied with that obligation. Yet while competition is a necessary condition of likeness, disparate impact alone will not justify breach. Under Article 1405(7):

Differences in market share, profitability or size do not in themselves establish a denial of equal competitive opportunities, but such differences may be used as evidence regarding whether a Party’s treatment affords equal competitive opportunities.

Thus, where a state regulates so that some minor commercial disadvantage is suffered by a foreign investor which is not incurred by domestic competitors, this impact alone will not suffice to establish breach. It is merely one evidential factor among many that must be evaluated. The implied requirement of something more than disparate impact clearly leaves a path open for the adjudicator to consider whether the state had any legitimate grounds for that disparate treatment. We have then a structure (in NAFTA Article 1405) which not only

⁵⁶ NAFTA, *supra* note [], at Art. 1405(4).

confirms that competition is a necessary condition of likeness, but also suggests the ultimate target of an adjudicator's inquiry could well be protectionist purpose.

The manner in which national treatment is formulated in NAFTA Chapter 12 (Cross-Border Trade in Services) provides further contextual guidance to an adjudicator charged with interpreting NAFTA Article 1102. The national treatment obligation for cross-border trade in services (in NAFTA Article 1202(1)) uses the same "like circumstances" formulation as in NAFTA Article 1102.⁵⁷ The dimensions of "like circumstances" in NAFTA Article 1202 were in turn considered by the state-to-state NAFTA Chapter 20 Panel in *Cross-Border Trucking Services* which ruled:

The Panel in interpreting the phrase "in like circumstances" in Articles 1102 and 1203, has sought guidance in other agreements that use similar language. *The Parties do not dispute that the use of the phrase "in like circumstances" was intended to have a meaning that was similar to the phrase "like services and service providers" as proposed by Canada and Mexico during NAFTA negotiations.*⁵⁸ (emphasis added)

There is indeed clear evidence that the phrase "like services and service providers" was put forward by Canada and Mexico in early drafts of the national treatment obligation on investment in the NAFTA.⁵⁹ With this in mind, the concession by the parties before the *Trucking Services* Panel that the language of "like services and service providers" was intended to be equivalent to "like circumstances" (in NAFTA Article 1102) is important and accurately tracks state practice. The former phrase was eventually incorporated into the national treatment Article XVII(1) of the WTO General Agreement in Trade in Services (GATS).⁶⁰ But in

⁵⁷ Under NAFTA Article 1202(1):

Each Party shall accord to service providers of another Party treatment no less favorable than that it accords, in like circumstances, to its own service providers.

Id.

⁵⁸ NAFTA Arbitral Panel Established Pursuant to Chapter Twenty, *In the Matter of Cross-Border Trucking Services*, Final Report of the Panel, (Secretariat File No. USA-MEX-98-2008-1, Feb. 6, 2001), at para 249.

⁵⁹ See, e.g., NAFTA Chapter 11, Trilateral Negotiating Draft Text, July 22, 1992, at Art. 105 (proposed by Canada) (available from www.international.gc.ca, accessed Nov. 24, 2009).

⁶⁰ Under Article XVII of the GATS:

other parts of the GATS – such as the national treatment guarantee in the Annex on Telecommunications – the WTO members chose to adopt a comparator clause focusing on “like circumstances”.⁶¹ As a matter of state practice then, these formulae are effectively opposite sides of the same coin. And within the GATS, we find explicit confirmation - just as in NAFTA Article 1405 and now by extension, NAFTA Article 1102 - that national treatment requires equality of competitive opportunities:

Formally identical or formally different treatment shall be considered to be less favorable if it modifies conditions of competition in favour of services or service suppliers of the member compared to like services or service suppliers of any other Member.

There are strong reasons for drawing on the GATS in framing an interpretative approach to national treatment in the NAFTA. The commitments in the GATS (including national treatment in Article XVII) extend to foreign investment in the service sector of a WTO member state.⁶² The NAFTA was negotiated concurrently with the GATS, and there is targeted evidence that the negotiations on rules across those agreements were intended by states parties to be complementary and mutually reinforcing.⁶³ That intent is itself formalized in the NAFTA, with the recognition in the preamble that the parties had negotiated the NAFTA to “build on their

In the sectors inscribed in its Schedule, and subject to any conditions and qualifications set out therein, each Member shall accord to services of suppliers of any other Member, in respect of all measures affecting the supply of services, treatment no less favorable than that it accords to its own like services and service suppliers. General Agreement on Trade in Services, Apr. 15, 1994, Marrakesh Agreement Establishing the World Trade Organization, Annex 1B, *in* WORLD TRADE ORGANIZATION, THE RESULTS OF THE URUGUAY ROUND OF MULTILATERAL TRADE NEGOTIATIONS: THE LEGAL TEXTS 284 (1994) [hereinafter WTO Agreements], at Art. XVII.

⁶¹ Footnote 15 to Article 5 of the GATS Annex on Telecommunications provides: “The term ‘non-discriminatory’ is understood to refer to most-favoured-nation and national treatment as defined in the Agreement, as well as to reflect sector-specific usage of the term to mean ‘terms and conditions no less favourable than those accorded to any other user of like public telecommunications transport networks or services under like circumstances’. GATS Annex on Telecommunications, *supra* note [], at Art. 5.

⁶² GATS, *supra* note [], at Art. I(2)(c).

⁶³ For example, Canada’s 1994 statement of implementation on the NAFTA acknowledges that:

The NAFTA and the Uruguay Round agreements cover much of the same ground and the two sets of rules are largely complementary and mutually reinforcing. In many respects, the NAFTA built on progress that had been made in the Uruguay Round while the Round in turn profited from the experience of Canada, the United States and Mexico in negotiating the NAFTA.

Canadian NAFTA Implementation Statement, *supra* note [], at 74.

respective rights and obligations under the General Agreement on Tariffs and Trade”.⁶⁴ Of course, the NAFTA parties agreed to provide extensive protections over and above those found in the GATS, such as protection from expropriation and investor-state dispute settlement. To that end, the NAFTA drafters must have been aware of a specific clause being negotiated in the GATS that would oblige WTO members to provide deeper levels of national treatment protection in bilateral and regional initiatives. Under Article V of the GATS, WTO members may enter into such other agreements to liberalize trade in services but only if such an agreement “provides for the absence or elimination of substantially all discrimination, in the sense of Article XVII”.⁶⁵ With this backdrop in mind, the NAFTA framers must have intended national treatment protection to be at least as strong as that in the GATS, confirming once again that competition must at a minimum play some role in assessing the likeness of foreign vis-à-vis domestic investors/investments.

Contextual guidance of this sort is really only open to an adjudicator faced with a multi-issue accord such as the NAFTA, where the investment chapter is embedded within a framework that includes a range of commitments. Such contextual support might well be absent in a dispute brought under the classic BIT model where there is a single national treatment clause. None the less, an adjudicator must still test their claimed reading under Article 31(1) of the VCLT not only against the context of the immediate treaty obligation at issue but in light of expressions of the “object and purpose” of the treaty.⁶⁶ With this in mind, we should look to how a claim that competition and motive review in a national treatment assessment matches against statements of the purpose of the investment treaty under adjudication, especially as communicated in the preambular recitals. Many of these recitals also confirm the critical role

⁶⁴ NAFTA, *supra* note [].

⁶⁵ *Id.* at Art. V(1)(b).

⁶⁶ VCLT, *supra* note [], at Art. 31(1).

of investment treaties in protecting the competitive opportunities of foreign investors in the receiving state. For example, the preambular recitals to the 2003 U.S-Singapore Free Trade Agreement include recognition that “open and competitive markets are key drivers of economic efficiency, innovation and wealth creation” as well as the explicit desire to use the commitments in that FTA “to promote competition”.⁶⁷ There is similar targeted guidance in the objectives listed in NAFTA Article 102(1), in light of which the parties are obliged to interpret and apply the NAFTA.⁶⁸ Article 102(1)(b) explicitly provides that those objectives – “as elaborated more specifically through its principles and rules, including national treatment” – extend to the promotion of “conditions of fair competition in the free trade area”.⁶⁹ Notice here that the states parties have structured an express and direct link between the national treatment obligation and the core objective of promoting “fair competition”. Moreover, that objective is not textually confined to national treatment for trade in goods or cross-border services among the NAFTA states (under Chapters 3 and 12). The fundamental goal of promoting competition extends across *all* parts of the NAFTA, including the disciplines on foreign investment in NAFTA Chapters 11 and 14.⁷⁰ There is similar targeted guidance in the generalized preambular recitals of the NAFTA, including a desire that reads as specific to foreign investment whereby the states parties resolve to “enhance the competitiveness of their firms in global markets”.⁷¹ Each of these various indicators further buttresses the strong claim that likeness requires, as a threshold inquiry into a national treatment complaint,

⁶⁷ United States – Singapore Free Trade Agreement, signed at Washington D.C, May. 6, 2003, at Recitals 2 and 10.

⁶⁸ “The Parties shall interpret and apply the provisions of this Agreement in the light of its objectives set out in paragraph 1 and in accordance with applicable rules of international law.” NAFTA, *supra* note [], at Art. 102(2).

⁶⁹ *Id.* at Art. 102(1)(b).

⁷⁰ “*The objectives of this Agreement*, as elaborated more specifically through its principles and rules, including national treatment, most-favored-nation treatment and transparency, are to...” (emphasis added). *Id.* at Art. 102(1).

⁷¹ *Id.* at Recital 8. To my mind, the language of Recital 8 is suggestive of a specific goal directed at foreign investment rather than other forms of economic exchange. This is supported by comparison with other preambular recitals with are clearly directed to cross-border trade in goods and services. The resolution in Recital 3 for instance is to “[c]reate an expanded and secure market for the goods and services *produced in their territories*” (emphasis added). On the importance of separating the diverse purposes across the NAFTA and isolating those that have relevance to foreign investment, see *The Canadian Cattlemen for Fair Trade v USA*, Award on Jurisdiction (UNCITRAL Jan. 28, 2008), at para 166.

consideration of the treatment of foreign investors as against *competing* domestic actors.⁷²

This is not to say that the NAFTA states indicated that foreign investors would be afforded legal protection against any and all risks of regulatory change encountered in the host state. Those parties also express a desire to “undertake each of the preceding [preambular goals] in a manner consistent with environmental protection and conservation”⁷³ and to “preserve their flexibility to safeguard the public welfare”⁷⁴

While older BITs tend to use less direct language than modern FTAs, even here one can discern a desire to manage competitive opportunities in the host state. For instance, the U.S. Model BIT has undergone various iterations including in 1984, 1987, 1994 and 2004.⁷⁵ The 1994 Model BIT is a good indicator of the formalized expression of core U.S. negotiating intent because it is located within the expansionary stage of the late 1980s to 1990s, during which the overwhelming number of investment treaties were concluded. It also pre-dates the specific American experience as a defendant under NAFTA Chapter 11 which would eventually trigger substantive changes to narrow down the U.S. Model BIT by 2004.⁷⁶ The first recital in the 1994 U.S. Model BIT expresses a desire by the parties “to promote greater *economic* cooperation between them, with respect to investment by nationals and companies of one Party in the territory of the other” (emphasis added).⁷⁷ Much like the NAFTA however, this is not an unqualified expression of state support for the freedom of capital to move and operate across borders. We find a counter-balance in the commitments “that these objectives can be achieved

⁷² For an analysis along these lines using the list of objectives articulated in NAFTA Article 102, see *United Postal Service of America Inc. v Canada*, Award on the Merits (NAFTA Chapter 11 Arbitration, May 24, 2007) at para 61.

⁷³ NAFTA, *supra* note [], at Recital 11.

⁷⁴ *Id.* at Recital 12

⁷⁵ See Kenneth J. Vandavelde, *A Comparison of the 2004 and 1994 U.S. Model BITs: Rebalancing Investor and Host Country Interests*, in YEARBOOK OF INTERNATIONAL INVESTMENT LAW AND POLICY 283 (K. Sauvant ed., 2009).

⁷⁶ *Id.*

⁷⁷ 1994 U.S. Model BIT, extracted in CAMPBELL MCLACHLAN, LAURENCE SHORE & MATTHEW WEINIGER, INTERNATIONAL INVESTMENT ARBITRATION: SUBSTANTIVE PRINCIPLES 201, 386 (2007).

without relaxing, health, safety and environmental measures of general application”.⁷⁸ This core objective of “economic cooperation” between the signatories is repeated with slight variances in the Model BITs of Germany⁷⁹, the Netherlands⁸⁰, and China⁸¹.

We have then a strong legal foundation – drawn from an examination of the text, context and preambular recitals of a broad range of investment treaties - to suggest that competition must play a role in assessing likeness under a national treatment test. A common-sense approach to national treatment, supportive of this claim, has indeed found reflection in the jurisprudence.

In *UPS v Canada*, a member of the Tribunal issued a separate statement arguing that:

[T]he most *natural* reading of NAFTA Article 1102, however, gives substantial weight to a showing of competition between a complaining investor and an investor of the respondent Party...Article 1102 focuses on protection of investors and investments against discriminatory treatment. A showing that there is a competitive relationship that two investors or investments are similar in that respect establishes a *prima facie* case of like circumstances.⁸² (emphasis added)

The idea that competition has a “natural” role to play in the likeness inquiry relates, once again, to its ability to flush out protectionism. This important point has been recognized, explicitly or implicitly, in much of the case-law. In *Corn Products* for instance, the Tribunal ruled:

The fact that economic competitors have – and lobby for – different interests is not at all surprising. On the contrary, it is a fact of economic and political life which may be observed in any open society. Far from suggesting that they are not in like circumstances, it tends to suggest the opposite; it is precisely because they are in close competition that they lobby against each other – if they were not competing in the market for what are effectively interchangeable products they would not trouble to maintain such

⁷⁸ *Id.*

⁷⁹ “[D]esiring to intensify economic co-operation between both States..” German Model BIT, extracted in MCLACHLAN, SHORE AND WEINIGER, *supra* note [], at 417.

⁸⁰ “Desiring to strengthen their traditional ties of friendship and to extend and intensify the economic relations between them..” Netherlands Model BIT, extracted in MCLACHLAN, SHORE AND WEINIGER, *supra* note [], at 423.

⁸¹ “Desiring to intensify the co-operation of both States on the basis of equality and mutual benefit;” Chinese Model BIT, extracted in RUDOLF DOLZER & CHRISTOPH SCHREUER, *PRINCIPLES OF INTERNATIONAL INVESTMENT LAW* 352 (2008).

⁸² *UPS v Canada*, Separate Statement of Dean Ronald A. Cass, *supra* note [], at para 17.

lobbying activities...[I]t is precisely where the interests of foreign investors and domestic investors are in conflict that the principle of non-discrimination becomes most important.⁸³

The analysis so far has isolated the critical role for competition in assessing whether foreign and domestic investors are alike in the investment treaty context. What is less clear from the sources surveyed above is whether assessment of state purpose must *also* form part of a national treatment test. To be sure, there is some useful targeted guidance in support of motive review in the form of the OECD National Treatment Instrument but the treaties themselves are not entirely conclusive on this fuller dimension. With that absence in mind, the question becomes what normative considerations might apply to justify a role for motive review when uncovering instances of protectionism.

First, and most importantly, the default value of a motive-based approach is the autonomy of host state choice which is only displaced if purposefully abused. We should generally presume that local political and regulatory processes are best equipped to make the right social and economic choices for the state concerned. Of course, national institutions are not always right. Domestic producers may have exaggerated political influence leading to protectionist outcomes that are normally domestically inefficient and at odds with the core treaty promise to extend competitive opportunities to foreign investors. But absent clear evidence of such distortion in the domestic political system, there is no compelling reason to displace the way a given society chooses to regulate in its internal sphere. This then is a legal approach that is comparatively light-handed and consistent with deep regulatory diversity, accommodating a broad range of public values. Provided a state regulates for any purpose other than protectionism, its measure will be declared legal under this test.

⁸³ *Corn Products International, Inc. v Mexico*, Decision on Responsibility (ICSID Case No. ARB(AF)/04/01, Jan. 15, 2008), at para 135.

Of course, much will depend on the methodology by which an adjudicator identifies protectionist purpose, an inquiry some regard as too sensitive and/or difficult to employ in practice. If for instance an adjudicator exhibits simple deference to a state's claim of a legitimate purpose and ignores competing factual indicators of protectionism (such as significant harm suffered by foreign vis-à-vis "like" domestic investors), this could potentially give rise to false negatives by leaving measures in operation that should be declared illegal. On the other hand, if an adjudicator were to find breach in every case involving a single statement of protectionist intent by an individual legislator, this could easily have the reverse and equally problematic effect of leading to false positives. These are important questions of how a test that isolates an impermissible state purpose might best be applied, which are examined later. My justification at this stage is a different and conceptual one of weighting and balancing state autonomy against the protection of foreign investment, and the identification of circumstances when the former value should be displaced in favour of the latter.

There is a potential, albeit weak, counter-argument for those treaties where states parties have begun to insert general exceptions clauses. Canada, for instance, has included an exception modeled on GATT Article XX in every investment treaty it has signed since the adoption of the NAFTA⁸⁴:

Subject to the requirement that such measures are not applied in a manner that would constitute arbitrary or unjustifiable discrimination between investments or between investors, or a disguised restriction on international trade or investment, nothing in this Agreement shall be construed to prevent a Party from adopting or enforcing measures necessary:

(a) to protect human, animal or plant life or health;

⁸⁴ Céline Lévesque, *Influences on the Canadian FIPA Model and the US Model BIT: NAFTA Chapter 11 and Beyond*, XLIV CAN. Y.B. INT'L L. 249, 271 (2006).

- (b) to ensure compliance with laws and regulations that are not inconsistent with the provisions of this Agreement; or
- (c) for the conservation of living or non-living exhaustible natural resources.⁸⁵

There may be a temptation to avoid consideration of regulatory purpose under the national treatment inquiry on the basis that such assessment would render such an exception redundant. If the law under review is found to have a legitimate (non-protectionist) purpose, then it will not breach the national treatment obligation and there will be no opportunity for the adjudicator to consider the list of permitted objectives delineated in the exception. Taking this line, a proponent might conceivably argue for a broader test for breach. They could, for instance, suggest that *any* measure that improves the competitive position of domestic investors vis-à-vis foreign investors should be in breach of national treatment and justified, if at all, under the exception. Under this expansive reading of national treatment – which can be described as a disparate impact test - a competitive relationship between foreign and domestic investors is necessary and sufficient for likeness and any disadvantage suffered by foreign investors will comprise “less favourable treatment” and therefore trigger breach. This is by no means a hypothetical possibility. A disparate impact approach structured along these lines has found limited reflection in the case-law, such as in *Siemens v Argentina* where the Tribunal summarily ruled that “intent is not decisive or essential for a finding of discrimination, and that the impact of the measure on the investment would be the determining factor to ascertain whether it had resulted in non-discriminatory treatment”.⁸⁶

⁸⁵ 2004 Canada Model Foreign Investment Promotion Agreement (available from <http://ita.law.uvic.ca>, accessed Feb. 5, 2010), at art. 10(1) (General Exceptions).

⁸⁶ *Siemens A.G. v Argentina*, Award (ICSID Case No. ARB/02/8, Feb. 6, 2007), at para 321. See also *LG&E Energy Corp v Argentine Republic*, Decision on Liability (ICSID Case No. ARB/02/1, Oct. 3, 2006), at para 146 (“In the context of investment treaties, and the obligation thereunder not to discriminate against foreign investors, a measure is considered to be discriminatory if the intent of the measure is to discriminate or if the measure has a discriminatory effect.”).

The superficial appeal of the redundancy argument is understandable but mistaken. For one thing, the exceptions clause would still retain its place in cases involving *other* treaty obligations such as the fair and equitable standard and guarantees on compensation in the event of expropriation. Indeed, exceptions of this sort may be more appropriate for obligations where purpose is clearly less relevant in a first-order inquiry into legality. Consider in this respect the 2009 ASEAN Comprehensive Investment Agreement (ACIA) which includes a generalized exception in Article 17 that is modeled on GATT Article XX.⁸⁷ Article 14 of the ACIA also sets out the classic obligation to pay “prompt, adequate and effective compensation” where member states either directly or indirectly expropriate foreign investment even if they are acting for a “public purpose”.⁸⁸ Yet the ASEAN states have refined the legal tests to be applied by an adjudicator in distinguishing between direct and indirect forms of expropriation. The former occurs simply “when an investment is nationalized or otherwise directly expropriated through formal transfer of title or outright seizure”.⁸⁹ By contrast, the latter implicates “an action or series of actions by a Member State [which] has an effect equivalent to direct expropriation without formal transfer of title or outright seizure”.⁹⁰ And in determining the quality of those acts which might justify in characterizing them as indirect expropriation, an adjudicator must consider a series of factors such as:

(c) the character of the government action *including its objective* and whether the action is disproportionate to the public purpose referred to in Article 14(1). (emphasis added)⁹¹

Moreover, the negotiators went on even to confirm that:

Non-discriminatory measures of a Member State that are designed and applied to protect legitimate public welfare objectives, such as public health, safety and the environment, do not constitute an [indirect] expropriation of the type referred to in sub-paragraph 2(b).⁹²

⁸⁷ ASEAN Comprehensive Investment Agreement, *signed* Feb. 26, 2009 [hereinafter ASEAN CIA], at Art. 17.

⁸⁸ *Id.* at Art. 14(1).

⁸⁹ *Id.* at Annex 2(2)(a).

⁹⁰ *Id.* at Annex 2(2)(b).

⁹¹ *Id.* at Annex 2(3)(c).

This structure reflects a deliberate approach whereby a state's purpose is critical to determining the first-order legality of actions impugned as *indirect* expropriation. In contrast however, no such assessment is called for where a state *directly* expropriates through transfer of title or outright seizure. For the latter, there is presumptive breach at the level of obligation where the state's purpose *only* becomes relevant in a plea of justification under the generalized exceptions clause in Article 17.

Moreover, the list of permitted objectives in these newer exceptions clauses is exhaustive. If state purpose were considered only at the exceptions stage, this would mean that any measure that pursued a purpose not on the list and caused disparate impact on a foreign investor would be invalidated. In effect, this approach locks parties into a list of policies that may remain static for decades given the difficulty of pursuing treaty amendment. Perhaps most importantly of all, there is a symbolic reason for requiring consideration of state purpose at the level of obligation rather than exception (where justified by the terms of the treaty under review). There is something fundamentally mistaken in forcing a state - which adopts an origin-neutral measure for a totally legitimate purpose but which has a coincidental effect of advantaging domestic actors - to justify that measure before an international adjudicator. Even if the ultimate result is the same under an exceptions analysis, there is "value in having cases dealt with in a correct normative context and in not diluting the notion of discrimination with activities which should not be so branded".⁹³

A second normative justification turns on considerations of openness and integrity. A test designed to isolate purposeful protectionism provides a transparent and systematic doctrinal

⁹² *Id.* at Annex 2(4).

⁹³ Henrik Horn & Joseph H.H. Weiler, *European Communities – Measures Affecting Asbestos and Asbestos-Containing Products*, in *THE WTO CASE LAW OF 2001* 14, 30 (H. Horn & P. Mavroidis eds., 2001).

structure, derived from a clear theory of the role of national treatment for determining when host state regulation will be invalidated. Under an anti-protectionism reading, national treatment only limits a measure passed by a state with the purpose of protecting its domestic producers against competition from foreign actors. It thereby protects the foreign investor from an identifiable and actual risk of political distortion as uncovered in the political economy analysis raised earlier. In contrast, the few competing approaches to national treatment rely heavily on artificial manipulation of certain criteria often with a desire to achieve particular substantive outcomes. Cases can, of course, be decided correctly without an underlying theory. But ends-driven reasoning will normally lead to uncertainty (at best) and incoherence (at worst) and when it does so, fails a basic function of law.

Consider, for example, a definition of likeness that falls at the narrower end of a spectrum to the disparate impact test considered earlier. An adjudicator could hold that foreign investment is only “like” domestic investment to the extent that both produce the *identical* good or service in the host state (excluding thereby goods or services that may not be identical but are still competitive). There are a number of potential problems with this reading, which has also found some reflection in the case-law principally in the *Methanex v U.S.* award.⁹⁴ For one thing, it offers us no real theory of the role of national treatment other perhaps than the simplistic claim that it should be read narrowly to compensate for the absence of a list of exceptional justifications (in the subject treaty). It is difficult to see why important questions of the delineation of the scope of regulatory autonomy of host states should turn purely on a default

⁹⁴ Consider the following:

Given the object of Article 1102 and the flexibility which the provision adopts in its adoption of “like circumstances”, it would be as perverse to ignore identical comparators if they were available and to use comparators that were less “like”, as it would be perverse to refuse to find and to apply less “like” comparators when no identical comparators existed. The difficulty which *Methanex* encounters in this regard is that there are comparators which are *identical* to it. (emphasis in original)

Methanex, *supra* note [], at Pt IV, Chp. B, para 17.

reading of likeness. Furthermore, there is a serious risk of under-inclusiveness in this narrow approach as it is likely to only catch the most obvious and crude embodiments of discriminatory behaviour.⁹⁵

The third normative justification engages systemic and institutional considerations. One of the key challenges facing investment treaty system as a whole relates to the initiation of improper or speculative litigation. The commencement of such problematic claims is not theoretically surprising given that investor-state arbitration does not contain the same sort of political and legal checks for incautious invocation present, albeit imperfectly, in state-to-state systems of dispute resolution.⁹⁶ Indeed, arbitral tribunals have begun to actively explore various gatekeeper controls on problematic claims as a means of guarding against abuse of dispute settlement rights.⁹⁷ States parties too are deeply concerned with this systemic dimension. The U.S. *Bipartisan Trade Promotion Authority Act* (2002), for example, mandates that U.S. negotiators should seek to “improve mechanisms used to resolve disputes between an investor and a government through (i) mechanisms to eliminate frivolous claims and to deter the filing of frivolous claims”.⁹⁸ Similarly in 2006, the ICSID Arbitration Rules were amended to allow a party to make a preliminary objection to claims that are “manifestly without legal merit”.⁹⁹

⁹⁵ For further analysis of this point, see Jurgen Kurtz, *The Use and Abuse of WTO Law in Investor-State Arbitration: Competition and its Discontents*, 20(3) EUR. J. INT’L L. 749, 766 (2009).

⁹⁶ These include an unwillingness to disrupt the broader political relationship between the states parties plus the potential for reciprocity of legal action by a targeted states. *See further id.* at 757.

⁹⁷ E.g., *Europe Cement Investment & Trade S.A v Turkey*, Award (ICSID Case No. ARB(AF)/07/2, Aug. 13, 2009), at 32 (awarding costs against the investor so that this might ‘discourage others from pursuing such unmeritorious claims’); *Methanex, supra* note [], at Pt II, Chp I, p. 29 (criticizing the investor’s conduct of the case as having ‘offended basic principles of justice and fairness required of all parties in every international arbitration’) and Pt V (awarding costs against the losing investor).

⁹⁸ Bipartisan Trade Promotion Authority Act of 2002, Pub. L. No. 107-210, div B, tit. 21, 116 Stat. 933 [hereinafter Bipartisan Trade Promotion Authority Act], at Section 2102(3).

⁹⁹ Convention on the Settlement of Investment Disputes Between States and Nationals of Other States, Oct. 14, 1966, 575 U.N.T.S. 159 [hereinafter ICSID Convention], at Art 6(1)(c). Under this article, the ICSID Administrative Council has power to adopt rules of procedure for arbitration proceedings conducted under ICSID auspices. The right of parties to make preliminary objection to claims that are “manifestly without legal merit” is set out in Rule 41(5) of the ICSID Rules of Procedure for Arbitration Proceedings (available from www.worldbank.org/ICSID, accessed Feb. 14, 2010) [hereinafter ICSID Arbitration Rules].

Most recently, Australia – which until very recently had never been a respondent to an investor-state claim - commissioned a formal review of its bilateral and regional trade agreements which included specific assessment of the role of investor-state dispute settlement provisions within those agreements.¹⁰⁰ Having identified instances of “vexatious arbitration claims”¹⁰¹ brought against a number of states, the Australian Productivity Commission even went so far as to recommend:

[T]hat Australia should seek to avoid accepting ISDS provisions in trade agreements that confer additional substantive or procedural rights on foreign investors over and above those already provided by the Australian legal system. Nor, in the Commission’s assessment, is it advisable in trade negotiations for Australia to expend bargaining coin to seek such rights over foreign governments, as a means of managing investment risks inherent in investing in foreign countries.¹⁰²

That recommendation was accepted by the Australian Government which in 2011 publicly announced that it would no longer include investor-state arbitration in future Australian trade agreements.¹⁰³

Properly formulated, a legal approach based on protectionist purpose could impose a reasonable but very real burden on a foreign investor when initiating a claim for breach of national treatment before an investor-state arbitral tribunal. As a start point, the foreign investor would be required to submit evidence as part of its obligation to construct a *prima facie* case of protectionism (and thereby shift the burden of justification to the host state). Absent any other key evidential indicators, the foreign investor would normally need to show that the degree and quality of disparate impact is probative of an intentional policy by the state to advantage its domestic actors at the expense of “like” foreign investors (including the

¹⁰⁰ AUST. GOV’T PRODUCTIVITY COMMISSION RESEARCH REPORT, BILATERAL AND REGIONAL TRADE AGREEMENTS (DEC. 2010).

¹⁰¹ *Id.* at 274.

¹⁰² *Id.* at 276-7.

¹⁰³ AUST. GOV’T, DEP’T OF FOREIGN AFFAIRS AND TRADE, GILLARD GOVERNMENT TRADE POLICY STATEMENT: TRADING OUR WAY TO MORE JOBS AND PROSPERITY 14 (APR. 2011).

claimant). This approach explicitly entails consideration of the distribution of benefits and burdens flowing from the measure across *both* domestic and foreign investors/investments, where these groups stand “in like circumstances”. Where foreign investors/investments as a class are treated significantly worse than the class of “like” domestic investors/investments, this would naturally support the case that the host state has intentionally chosen to advantage the latter. On the other hand, if the evidential record reveals that most domestic investors/investments are treated equally to “like” foreign investors, this will conversely weaken the claimant’s argument that the host state was motivated by protectionism.

This proffered approach differs fundamentally from certain cases that *also* require consideration of protectionist purpose. In *Pope & Talbot* for instance, the Tribunal ruled that “differences in treatment will *presumptively* violate [NAFTA] Article 1102(2), unless they have a reasonable nexus to rational government policies”¹⁰⁴ (emphasis added). Later on, the *Pope & Talbot* Tribunal explains its approach as one that addresses “*any* difference in treatment demanding that it be justified by showing that it bears a reasonable relationship to rational policies not motivated by preference of domestic over foreign owned investments” (emphasis in original).¹⁰⁵ The *Pope & Talbot* taxonomy places a very light burden on foreign claimants thereby increasing significantly their incentives to search for illegality and commence litigation. The foreign investor need only show some minimal level of disadvantage (which, even of itself, may not suggest protectionism), to shift the burden of justification on the respondent state. My competing taxonomy, on the other hand, has the merit of sifting and filtering potential claims for breach and thereby acting as a partial structural check on improper or speculative commencement of investor-state arbitration. Let us assume that in its

¹⁰⁴ *Pope & Talbot Inc. v Canada*, *supra* note [], at para 78.

¹⁰⁵ *Id.* at para 79.

national treatment challenge, a foreign claimant merely shows that it competes with a group of domestic actors and that a single domestic competitor within that group is treated marginally more favourably than the foreign claimant. Absent any other evidence whatsoever, an adjudicator should - in line with the ruling of the *ADF v USA* Tribunal¹⁰⁶ - dismiss that claim because the foreign investor had failed to discharge their initial burden of building a *prima facie* case of protectionism.

Despite these strong doctrinal and normative justifications, a number of objections are classically raised when it comes to a purpose-based test which can be summarized as implicating questions either of sensitivity or difficulty. In the next two parts, I consider each of these objections in turn.

III. Sensitivity and Scope:

Distinguishing Regulatory Design Versus Application

A first objection goes to the perceived sensitivity of an adjudicatory approach that requires evidence of protectionist purpose as a condition of breach. To be sure, such a test requires an adjudicator to confront head-on the regulating state's assertion of a legitimate rationale underpinning its measure. And to reject a government's claim using this methodology, an adjudicator is effectively telling the state that "I simply do not believe you". The concern here centers on the imputation of bad faith inherent in an inquiry that explicitly isolates an impermissible purpose on the part of the regulating state.¹⁰⁷

¹⁰⁶ *ADF v U.S.*, *supra* note [], at para 157.

¹⁰⁷ In a comment on WTO law for instance, David Palmeter puts forward "the intuitive appeal of a search for protectionist purpose" but also notes that "[domestic] tribunals are reluctant to question the motives of legislatures" and that "this sensitivity might be heightened in the case of international tribunals who are asked by complainants to find, in effect, that the intentions of a government were not necessarily what that government said they were". David Palmeter,

This objection, in and of itself, is not a convincing reason for opposing a purpose-based approach. As Regan has argued in the context of WTO law, the point of adjudication is to test for invalidity and *any* ground of invalidation will necessarily involve some type of criticism of the respondent.¹⁰⁸ It is difficult to see why a properly formulated approach that carefully checks across a range of evidentiary sources to isolate protectionist purpose should be more susceptible to this criticism than any other test for national treatment. Moreover, this test targets an objective and identifiable political economy risk to foreign investors that is not specific to any host state but common across many legal systems and traditions. That is, very simply, that politics can be subject to distortions and that occasionally protectionist forces will wield excessive influence in the domestic political process.¹⁰⁹ There is also a flip side to this concern of sensitivity, alluded to among the normative justifications put forward earlier. Under a purpose-based test, a tribunal can just as easily validate a measure where there is clear evidence of legitimate purpose. In so doing, the Tribunal is publicly signaling to a range of stakeholders (especially future claimants) that the default value of the test is the political autonomy of the host state.

Although somewhat oversold, the concern of sensitivity must be taken seriously. For one thing, we are dealing with a relatively new system of law measured by the temporality in activation of its judicial arm. The first investor-state arbitral award was issued in 1990¹¹⁰ and it is really only by the late 1990s that one can discern a strong trend towards formal resolution

Comment on Facial Non-Discrimination in the WTO, in *THE ROLE OF THE JUDGE IN INTERNATIONAL TRADE REGULATION: EXPERIENCE AND LESSONS FOR THE WTO* 219, 223 (T. Cottier & P. Mavroidis eds., 2003). For a similar analysis which draws out this perceived sensitivity of a purpose-based test, *see also* Joseph H.H. Weiler, *Law, Culture and Values in the WTO – Gazing into the Crystal Ball*, in *THE OXFORD HANDBOOK OF INTERNATIONAL TRADE LAW* 752, 770 (D. Bethlehem et al. eds., 2009).

¹⁰⁸ Regan, *supra* note [], at 461.

¹⁰⁹ *Id.*

¹¹⁰ *Asian Agricultural Products Ltd v Sri Lanka*, Award (ICSID Case No. ARB/87/3, Jun. 27, 1990).

of investment disputes through investor-state arbitration¹¹¹. Such a new system of adjudication requires time both to gain confidence and to earn the confidence of various stakeholders.¹¹² With that in mind, arbitrators may well be tempted – as is occasionally the case in the WTO – to use euphemisms to mask an underlying assessment of state purpose.¹¹³ While this may be an understandable strategy (at least in the short-term), it is important that adjudicators guard against any attempt by either disputing party to load the direction of a purpose-based test. Perhaps banking on an arbitrator’s likely unease in applying such a test, some states appear to have invited them to exhibit deference to the *state’s* claim of a legitimate purpose underlying the measure under review. In *UPS v Canada* for instance, Canada argued that:

In connection with the determination of like circumstances, *Canada emphasizes the role of government determinations* respecting reasons for particular treatment of investors and investments. Canada argues that *any* public policy rationale for distinguishing between two entities or investors makes them unlike. It is sufficient, in Canada’s view, for differences in treatment to be based on “legitimate policy considerations or public interest grounds” or to have *any* “rational basis” and suggests that dispute resolution tribunals should not “second-guess the validity of public policy objectives” or whether “there is a better way to meet these objectives.” (emphasis added)¹¹⁴

One could potentially read Canada’s defence as arguing that an adjudicator has no mandate to “second-guess the validity” of the host state’s choice of a specific non-discriminatory purpose. Canada might, for instance, be suggesting that an arbitrator should not inquire into whether

¹¹¹ UNCTAD, INVESTOR-STATE DISPUTE SETTLEMENT AND IMPACT ON INVESTMENT RULE-MAKING 7 (2007).

¹¹² For an analysis of this point in the context of the more mature WTO legal system, see Weiler, *supra* note [], at 770-1.

¹¹³ Palmeto, *supra* note [], at 221, 223. In a related vein, consider also Robert Hudec, *GATT/WTO Constraints on National Regulation: Requiem for an “Aims and Effects” Test*, 32 (3) INT’L LAW. 619 (1998) (arguing that: “The normal response of most tribunals is ...to decide the case as best they can by making a seat-of-the pants judgement about whether the defendant government is behaving correctly or incorrectly – a process of judgment known in some circles as the ‘smell test’. Once the tribunal comes to a conclusion about who should win, it fashions an analysis, terms of the meaningless criteria it has been asked to apply, that makes the case come out that way.”).

¹¹⁴ *UPS v Canada*, Separate Statement of Dean Ronald A. Cass, *supra* note [], at para 9. See also para 131 (“Canada asserts that so long as it advances a public policy rationale for its action, as it has in this proceeding, my inquiry should be at an end.”).

the costs imposed by a measure are excessive or disproportionate to the benefits of the policy objective. If that is the underlying thrust of Canada's defence, then the claim is on entirely solid grounds. Proportionality review of this type involves complex and value-laden empirical judgments and it is highly doubtful that courts and tribunals are better assessors of values and empirical questions than elected representatives. Yet the extract could be equally – and probably more accurately¹¹⁵ – understood as suggesting that an arbitrator should exhibit full deference to the host state and not even test whether the asserted non-discriminatory purpose was its actual purpose.

An exhibition of full deference of this latter sort would certainly address a perceived concern of sensitivity, as it would preclude any real investigation by the adjudicator into the state's actual purpose. But it would thereby render national treatment largely ineffectual. A finding of breach would depend on the state choosing not to present a non-protectionist purpose before the adjudicator, an improbable scenario at best. In *UPS v Canada*, Canada's defence was understood by one of the tribunal members as extending a blunt invitation for deference. Arbitrator Cass noted that "Canada's proposed test would grant the government of any NAFTA Party extensive power to avoid national treatment obligations, [by] giving conclusive weight to a Party's assertions that public policy supports divergent treatment of domestic and foreign investors"¹¹⁶ and that under such an approach, "rejection of complaints would be virtually axiomatic"¹¹⁷. We find equally robust treatment of such invitations in parts of WTO law. In *Chile – Alcohol* for instance, Chile advanced four objectives for its differential taxation of alcoholic beverages based on alcohol content but "decline[d] to explain the relationship between the design, architecture and structure of the New Chilean System and the objectives it

¹¹⁵ Consider for example this later distillation of Canada's defence: "Canada asserts that so long as it advances a public policy rationale for its action, as it has in this proceeding, my inquiry should be at an end." *Id.* at para 9.

¹¹⁶ *Id.* at para 15.

¹¹⁷ *Id.* at para 51.

stated that System sought to realize”.¹¹⁸ The Appellate Body was quick to reject the implicit invitation for it to defer to Chile’s claim of legitimate objectives. After identifying the heavy burden of the Chilean tax on foreign alcoholic products¹¹⁹, the Appellate Body ruled: “The conclusion of protective application reached by the Panel becomes very difficult to resist, in the absence of countervailing explanations by Chile. *The mere statement of the four objectives pursued by Chile does not constitute effective rebuttal on the part of Chile.*” (emphasis added)¹²⁰ *Chile – Alcohol* is not the only WTO case which has teased out the problematic implications of extending deference to a respondent state. The Appellate Body has, for instance, expressed similar resistance when assessing the application of the WTO Agreement on the Application of Sanitary and Phytosanitary Measures in *EC- Hormones*.¹²¹

Unfortunately, not all investor-state arbitral tribunals have been as rigorous as Arbitrator Cass in *UPS v Canada* when confronted with explicit or implicit invitations to defer to a state’s claimed innocent purpose. The *GAMI v Mexico* award is most representative of this lax approach. In *GAMI*, a foreign investor who owned shares in a Mexican company (GAM) operating sugar mills in that country brought proceedings under NAFTA Chapter 11. The investor claimed, *inter alia*, that Mexico’s expropriation (with compensation) of GAM’s sugar mills breached national treatment because other sugar mills without foreign ownership had

¹¹⁸ *Chile – Taxes on Alcoholic Beverages*, Report of the Appellate Body (WT/DS87/AB/R, Dec. 13, 1999) at paras. 69-70.

¹¹⁹ *Id.* at paras. 63-8.

¹²⁰ *Id.* at para 71.

¹²¹ Consider, for example, the following extract:

So far as fact-finding by panels is concerned, their activities are always constrained by the mandate of Article 11 of the DSU: the applicable standard is neither *de novo* review as such, nor “total deference”, but rather “the objective assessment of the facts”. Many panels have in the past refused to undertake *de novo* review, wisely, since under current practice and systems, they are in any case poorly suited to engage in such a review. On the other hand, “total deference to the findings of the national authorities”, it has been well said, “could not ensure an ‘objective assessment’ as foreseen by Article 11 of the DSU”. (footnotes omitted)

European Communities – Measures Concerning Meat and Meat Products (Hormones), Report of the Appellate Body, (WT/DS26/AB/R; WT/DS48/AB/R, Jan. 16, 1998), at para 117.

not been expropriated.¹²² Mexico had justified the expropriation program on the grounds of public purpose formally expressed on the face of the measure.¹²³ The expropriation program was designed as a response to a crisis in the Mexican sugar industry driven by overproduction caused partly, according to Mexico, by the failure of the U.S. to meet NAFTA commitments and open its market to imports of Mexican sugar.¹²⁴ In a remarkably sparse ruling on national treatment, the Tribunal found for Mexico on the basis that:

[It] has not been persuaded that GAM's circumstances were demonstrably so "like" those of non-expropriated mill owners that it was wrong to treat GAM differently. *Mexico determined that nearly half of the mills in the country should be expropriated in the public interest.* The reason was not that they were prosperous and the Government was greedy. To the contrary: Mexico perceived that mills operating in conditions of effective insolvency needed public participation in the interest of the national economy in a broad sense. *The Government may have been misguided. That is a matter of policy and politics. The Government may have been clumsy in its analysis of the relevant criteria for the cutoff line between candidates and non-candidates for expropriation.* Its understanding of corporate finance may have been deficient. But ineffectiveness is not discrimination. *The arbitrators are satisfied that a reason exists for the measure which was not itself discriminatory.* (emphasis added)¹²⁵

The problem here lies in the failure of the Tribunal to draw a distinction between the Mexico's *general* policy goal of remedying over-production by intervening into the sugar market and the *specific* exercise of discretion when implementing that goal. States may elect to embed discrimination in the application of discretion, even where the overall regulatory scheme is directed at a perfectly rational policy. In *GAMI v Mexico*, the foreign investor was alleging discrimination at the implementation stage (being Mexico's choice to only expropriate mills with foreign shareholders) rather than the formulation of the overall policy goal *per se*. A close

¹²² *GAMI Investments, Inc. v Mexico*, Final Award (UNCITRAL, Nov. 15, 2004) at para 24.

¹²³ "The Expropriation Decree recited that it had been enacted on the grounds of public purpose identified in the *Ley de Expropiación* of 1997." *Id.* at para 17.

¹²⁴ On this point, *see id.* at para 77.

¹²⁵ *Id.* at para 114.

analysis of the factual record reveals a respectable set of contextual indicators to suggest that this was, at the very least, an arguable claim that deserved far more careful consideration.¹²⁶

Here is an example of an important issue on which WTO law might productively guide an investment treaty adjudicator. The importance of reviewing both the general design of a measure and any exercise of discretion under that measure is formally enshrined in key WTO provisions. GATT Article XX, for example, requires a WTO member invoking this exception to first show that its law or regulation is justified under one of the substantive heads of exemption (in paragraphs (a) to (j)) for reason such as, *inter alia*, being “necessary to protect human, animal or plant life or health”.¹²⁷ Once the regulating state has passed this provisional level of review, a WTO adjudicator must still consider whether any application of the otherwise permitted measure meets the conditions of the *chapeau* of Article XX. The *chapeau* in turn explicitly guards against the contingency that a WTO member might have intentionally “*applied* [its measure] in a manner which would constitute a means of arbitrary or unjustifiable discrimination” (emphasis added).¹²⁸ This dual-stage check in the architecture of GATT Article XX – focusing on both the design of a measure and its application - was clearly endorsed by the Appellate Body in the *Shrimp-Turtle* case.¹²⁹ Indeed, the Appellate Body in that case rejected the U.S.’ invocation of GATT Article XX to defend an environmental measure (provisionally justified under sub-paragraph (g)) precisely because the U.S. agency concerned had exercised its discretion in such a way to intentionally cause “arbitrary or unjustifiable discrimination” in

¹²⁶ These include: (i) the fact that the expropriation program had its origins in the failure of the U.S (the home state of the investor) to meet its NAFTA commitments on market access for Mexican sugar; (ii) resulting imports of high-fructose corn syrup from the U.S displaced sales of sugar in the Mexican market given rise to the need on the part of the Mexican government to intervene in the market-place; (iii) GAMI is a U.S investor in Mexico.

¹²⁷ GATT, *supra* note [], at Art. XX (General Exceptions).

¹²⁸ *Id.*

¹²⁹ *United States – Import Prohibition of Certain Shrimp and Shrimp Products*, Report of the Appellate Body (WT/DS58/AB/R, Oct. 12, 1998), at paras. 116; 149.

breach of the *chapeau*.¹³⁰ Of course, those arbitrators resistant to using WTO law as guidance when interpreting investment treaty protections might criticize this comparison because, while the chapeau is embodied in the text of GATT Article XX, there is no equivalent textual hook in investment law. But the force of the conceptual distinction between purposeful discrimination embodied in the design of a measure compared to its application has a broader resonance in WTO law beyond the textual strictures of GATT Article XX. In *U.S. – Section 301* for instance, the WTO Panel sensibly acknowledged outside of the context of GATT Article XX: “[E]ven though the statutory language granting specific powers to a government agency may be *prima facie* consistent with WTO rules, the agency responsible, within the discretion given to it, may adopt internal criteria or administrative procedures inconsistent with WTO obligations which would, as a result, render the overall law in violation.”¹³¹

In contrast to these nuanced tests in WTO law, the *GAMI* Tribunal’s blunt approach approximates a type of crude deference to the state.¹³² By failing to recognize that discrimination can exist at various levels of a regulatory scheme, this ruling significantly and problematically reduces the ambit of national treatment protection. It potentially enables a state to hide its discriminatory exercise of discretion behind the façade of an otherwise legitimate regulatory scheme. There are, however, the early and promising signs of a more rigorous arbitral approach that properly distinguishes between regulatory design and enforcement. In the recent case of *AES v Hungary*, the Tribunal ruled albeit in *obiter*: “[A] rational policy is not enough to justify *all* the measures taken by a state in its name...[T]here needs to be an appropriate correlation between the state’s public policy objective and the

¹³⁰ *Id.* at 161-186.

¹³¹ *United States – Sections 301-310 of the Trade Act of 1974*, Report of the Panel (WT/DS152/R, Dec. 22, 1999), at para 7.27.

¹³² For further strong criticism and a slightly different perspective on *GAMI v Mexico*, see MCLACHLAN, SHORE & WEINIGER, *supra* note [], at 189.

measure adopted to achieve it. This has to do with the nature of the measure *and the way it is implemented.*" (emphasis added)¹³³ The AES Tribunal's instincts here, which clearly track the claim made by the WTO Panel in *U.S. –Section 301*, are sound and deserve strong endorsement. Yet this tentative break-through, measured against the earlier and crude approach in *GAMI v Mexico*, strictly relates only to the scope of the adjudicatory inquiry. That is, national treatment in the investment treaty context can and should guard against the ability of the state to practice purposeful protectionism at different stages of a regulatory scheme. While an important and compelling recognition, there is still the more difficult question of what *indicia* an adjudicator should examine in assessing whether a state has in fact acted for protectionist or legitimate reasons, whether at the level of regulatory design or enforcement.

IV. Operationalizing an Inquiry into State Purpose

There are a number of conceptual issues implicated in a jurisprudential test that requires evidence of such purpose as a condition of breach. First, there is the obvious but essential question of what precisely do we mean by the "purpose" of the host state in question? It must, by definition, mean the purpose of the originator of the law or administrative agency in question. Yet, the legislature or regulatory agencies promulgating these measures are normally corporate entities made up of a collection of individual members. How then do we isolate the "purpose" or collective mind of such groupings? One possibility is to look at express statements – avowals or denials of protectionist purpose – of individual legislators or other officials within the collective group. We might then try to examine, weigh and compare those statements in coming to an overall view of the purpose of the agency in question. In putting

¹³³ *AES Summit Generation Limited, AES-Tisza Erömü KFT v The Republic of Hungary*, Award (ICSID Case No. ARB/07/22, Sept. 23, 2010) at para 10.3.9.

forward an assessment of such statements, I am not suggesting that an adjudicator engage in a simple process of aggregating these different statements. My interest at the moment is in isolating both the legal justification and the probative value of statements of individual legislators as part of a contextual and qualitative inquiry into state purpose.

A. “Subjective” and “Objective” Evidence of State Purpose

In WTO law, an inquiry into what has often been characterized as “subjective” intent – written or oral statements by individual public officials on the purpose of law or regulation - has been formally resisted in a number of cases. The Appellate Body in *Japan-Alcohol* ruled that, in assessing whether a domestic tax has been applied so as to afford protection under GATT Article III(2), “[i]t is not necessary for a panel to sort through the many reasons legislators and regulators often have for what they do and weigh the relative significance of those reasons to establish legislative or regulatory intent”.¹³⁴ This apparent resistance¹³⁵ should not control how investor-state tribunals construct a test for impugned purpose. For one thing, in ruling in this direction, the Appellate Body relies heavily on the unique structure of GATT Article III(1) and especially the textual direction that GATT Article III is designed to discipline domestic measures “applied” in a protectionist manner.¹³⁶ This has led to a greater *formal* emphasis on so-called “objective” evidence – including the design, structure and impact of a measure – in operationalizing the search for state purpose under GATT Article III.¹³⁷

¹³⁴ *Japan – Taxes on Alcoholic Beverages*, Report of the Appellate Body (WT/DS8/AB/R, Oct. 4, 1996), at 27-8.

¹³⁵ For an analysis that shows that WTO adjudicators have used such evidence as part of an inquiry into regulatory purpose in select cases, see Regan, *supra* note [], at 458-464.

¹³⁶ In *Japan-Alcohol* for instance, the Appellate Body ruled: “This is an issue of how the measure in question is *applied*.” (emphasis in original). *Japan-Alcohol*, Report of the Appellate Body, *supra* note [], at 28.

¹³⁷ “Although it is true that the aim of a measure may not be easily ascertained, nevertheless, its protective application can most often be ascertained from the design, the architecture and the revealing structure of a measure. The very magnitude of dissimilar taxation in a particular case may be evidence of such a protective application, as the Panel rightly concluded in this case. Most often, there will be other factors to be considered as well. In conducting this inquiry,

Yet investor-state arbitral tribunals do not operate under this weak textual constraint. There is no GATT Article III(1) in operation and by extension, no formal reason whatsoever to discount or even reject express statements of individual legislators. Some commentators in the investment law field have none the less cast doubt on the relevance of subjective evidence of this sort and indeed, question the ability of arbitrators to properly evaluate the probative nature of such evidence. Baetens for instance claims that examination of “hard-to-prove subjective state intent” such as where “one minister has uttered a biased remark” would be an “impossible exercise for an arbitral tribunal”.¹³⁸ Yet to my mind, there are strong and compelling conceptual reasons to draw on such evidence, where it exists. A test requiring evidence of protectionist purpose ultimately positions national treatment as a discipline on political failure, being the excessive influence accorded to protectionist forces – usually domestic industry that competes with foreign investors – in the political process of the host state.¹³⁹ An adjudicator will then be charged with identifying what political forces are responsible for the adoption of the specific law or practice in question. This will require careful assessment of the legislative process as a whole to isolate the causal political forces responsible for the measure under review. Explicitly protectionist statements necessarily form part of the legislative record and deserve close attention – together with *all* other evidential sources – in coming to a view on the controlling purpose of the state in promulgating and enforcing the relevant law or regulation. Indeed, the positioning of national treatment as an

panels should give full consideration to all the relevant facts and all the relevant circumstances in any given case.” *Id.* at 29.

¹³⁸ Freya Baetens, *Discrimination on the Basis of Nationality: Determining Likeness in Human Rights and Investment Law*, in *INTERNATIONAL INVESTMENT LAW AND COMPARATIVE PUBLIC LAW* 279, 306 (S. Schill ed., 2010).

¹³⁹ For comprehensive analysis of this idea from which I have learnt much, see Donald H. Regan, *Judicial Review of Member-State Regulation of Trade Within a Federal or Quasi-Federal System: Protectionism and Balancing, Da Capo*, 99 (8) *MICH. L. REV.* 1883-9 (2001).

inquiry across the full suite of evidential indicators has found explicit reflection in the arbitral case-law. In his Separate Opinion in *SD Myers v Canada* for instance, Arbitrator Schwartz ruled:

[T]he intent of government is a complex and multifaceted matter. Government decisions are shaped by different politicians and bureaucrats with differing philosophies and perspectives. Every person involved may tailor his or her recommendation or vote to address a variety of different policy objectives and may sometimes take into account partisan political factors or career concerns. *As challenging as the task is, a tribunal such as this can fairly characterize the motivation or intent of government by examining the evidence as a whole. The record may include statements or texts that in law carry the authority of the government as a whole, and it may be possible to determine which particular participants were especially influential in arriving at a decision.* (emphasis added)¹⁴⁰

Expressions of protectionist intent by individual actors may, on occasion, be intensely pertinent in this inquiry. They have the potential to offer a sharp and compelling insight into the causal factors that operated in the legislature. Consider, for example, the statement of the Canadian Minister for the Environment in *Myers* that “it is still the position of the government that the handling of PCBs be done in Canada by Canadians”.¹⁴¹ This explicit avowal of protectionist purpose was made in the Canadian Parliament, recorded by Hansard and available on the public record.¹⁴² Of course, one should not confer too much weight on just *any* sort of expression of intent made by individual legislators. Yet in a case like *Myers*, where the statement was made by the very Minister responsible for administering the scheme in question, an adjudicator can safely accept such a statement as probative that the measure was passed for protectionist reasons rather than some other legitimate goal.¹⁴³

¹⁴⁰ *SD Myers, Inc. v Canada*, Partial Award (UNCITRAL, Nov. 13, 2000), Separate Opinion by Dr Brian Schwartz, at para 147.

¹⁴¹ *SD Myers v Canada*, *supra* note [], at para 116.

¹⁴² *Id.*

¹⁴³ Indeed, this seems to be the approach taken by the *SD Myers* Tribunal. It ruled that: “Insofar as intent is concerned, the *documentary record as a whole* clearly indicates that the Interim Order and the Final Order were *intended primarily* to protect the Canadian PCB disposal industry from U.S. competition. Canada produced no convincing witness testimony to rebut the thrust of the documentary evidence. (emphasis added)” *Id.* at para 194.

The Tribunal in *AES v Hungary* adopted a similar methodology to *SD Myers v Canada* by also carefully drawing on communications between key individual legislators when casting light on state purpose. In that case, Hungary had introduced legislation capping the price of electricity sold by private generators triggering a claim for loss of profits brought by a foreign investor under the Energy Charter Treaty. Hungary had attempted to defend that claim by arguing, *inter alia*, that the legislation had been motivated by a legitimate justification of complying with its obligations as a member of the European Union.¹⁴⁴ Specifically, Hungary claimed that the price-cap had been introduced in response to the commencement of an inquiry by the European Commission that above-market prices in the Hungarian electricity sector constituted a form of prohibited state aid under the law of the European Union.¹⁴⁵ The Tribunal reviewed various evidential factors in assessing the veracity of that defence, before concluding that the legislation was not in fact based on the European Commission's investigation. It ruled instead that the price cap "was motivated principally by widespread concerns relating to...excessive profits earned by generators and the burden on consumers".¹⁴⁶ In coming to this conclusion, the Tribunal pointedly noted that "virtually all of the debate in parliament at the relevant time was about 'profits'", without any reference at all to Hungary's commitments under European state aid.¹⁴⁷ Moreover, much like *SD Myers v Canada*, the *AES v Hungary* Tribunal paid particular attention to the statements of the Minister responsible for the particular scheme under review by recording that the "government minister Mr Tibor Kovács specifically asked the opposition parties if they were prepared to support the proposal, which he said 'gives tools for the government to limit the alleged and so-called luxury profits'"¹⁴⁸.

¹⁴⁴ *AES v Hungary*, *supra* note [], at paras. 7.2.1-7.2.5.

¹⁴⁵ *Id.* at para. 10.3.15.

¹⁴⁶ *Id.* at para. 10.3.31.

¹⁴⁷ *Id.* at para. 10.3.32-10.3.33.

¹⁴⁸ *Id.* at para. 10.3.32.

Subjective evidence of this sort cannot be the sole *indicia* for an inquiry into state purpose for two key reasons. First, there may in fact be no such evidence before the adjudicator in a given case. She must then necessarily supplement her inquiry with other available forms of evidence – including the text of the measure and its effects – in coming to a view on what political forces were responsible for the measure in question. Secondly, even where such statements exist, there is a danger in automatically affording them dispositive weight, or “smoking gun” status. Protectionist claims may only be made by one or two individual legislators who have no direct authority over the specific measure under review and as a result, those claims may simply reflect opportunist attempts to harness interest group support rather than representing an embedded failure in the legislative process as a whole. To be sure, there is a concern that adjudicators could be over-impressed with *any* sort of individual statement of protectionism. While that concern is a real one, it can be managed. Most importantly, adjudicators should treat such statements as only one part of the evidential record and thoroughly review the entirety of those sources to isolate the causal political forces at play.

This fuller approach was certainly the strategy adopted both in *SD Myers v Canada* and *AES v Hungary*. In *SD Myers* for instance, the Tribunal reviewed a range of factors in addition to the Minister’s protectionist statements, in coming to a view on Canada’s motivation in closing its border to exports of PCB waste. In particular, the Tribunal drew out a logical weakness in Canada’s defence that the ban was implemented for legitimate environmental reasons¹⁴⁹, by recording the fact that the Canadian bureaucracy had given expert advice that an open border would represent “a technically and environmentally sound solution to the destruction of some

¹⁴⁹ “Canada says that the measure was made because Canada believed PCBs are a significant danger to health and the environment when exported without appropriate assurances of safe transportation and destruction.” *SD Myers*, *supra* note [], at para 152.

of Canada's PCBs"¹⁵⁰. Matched against the Minister's statements (and the abundant documentary evidence of lobbying by domestic industry)¹⁵¹, the *SD Myers* Tribunal eventually ruled that protectionism was the controlling purpose underlying the ban.¹⁵² In a similar vein, the *AES* Tribunal did not simply examine the statements of individual legislators in the Hungarian Parliament in isolation. It considered them in light of the legislative record as a whole when testing Hungary's defence of an innocent purpose (of complying with its external state aid obligations). Much like in *SD Myers v Canada*, we find a factual mismatch in *AES* between Hungary's asserted innocent purpose and the activities of the relevant government bureaucracy. In particular, the *AES* Tribunal recorded the fact that "the Hungarian agency in charge of dealing with state aid issues had not even been consulted when the government reintroduced regulated pricing".¹⁵³

More generally, arbitral tribunals have proven themselves highly capable of distinguishing between probative expressions of subjective intent (such as that of the ministers in *SD Myers* and *AES*) from simple protectionist speeches of individual legislators. In *Methanex* for instance, the Tribunal ruled: "Statements by individual California politicians thereafter declaring the need or desire for ethanol incentives that could conversely harm MTBE and methanol did not reflect California law, but only their own or their constituents' aspirations; even less so did statements by lobbyists or interested citizens reflect Californian law."¹⁵⁴

¹⁵⁰ *Id.* at para 164.

¹⁵¹ *Id.* at para 168.

¹⁵² It is worth extracting the relevant part of the Tribunal's award, as it shows the Tribunal's focus on isolating the causal political forces responsible for the measure under review:

The evidence establishes that Canada's policy was shaped to a very great extent by the desire and intent to protect and promote the market share of enterprises that would carry out the destruction of PCBs in Canada and that were owned by Canadian nationals. Other factors were considered, particularly at the bureaucratic level, *but the protectionist intent of the lead minister in this matter was reflected in decision-making at every stage that led to the ban.* (emphasis added)

Id. at para 162.

¹⁵³ *AES v Hungary*, *supra* note [], at para 10.3.17.

¹⁵⁴ *Methanex v U.S.*, *supra* note [], at Part III, Chp. B, para 8.

Similarly in *Corn Products*, the investor had presented evidence of protectionist statements made by individual members of the Mexican Congress.¹⁵⁵ But the Tribunal also “expressed doubts about the extent to which such comments can be legitimately treated as evidence of the intent of the Legislature as a whole, let alone of the State itself, in imposing a measure of this kind”.¹⁵⁶ Clearly then, arbitrators have approached the task of evaluating evidence of “subjective” intent with appropriate care and sensitivity. For the most part, they have done exactly what they should do when assessing the relevance of such evidence in casting light on state purpose. They have used it along with *all* other pertinent evidence when locating what political forces are responsible for the measure in question. Indeed, arbitral tribunals have – with different emphases and integrity – traversed a remarkably broad range of evidentiary sources in addition to subjective statements when constructing a ruling on state purpose. I explore these below and highlight strengths and weaknesses in the arbitral evaluation of such evidence, with the aim of continuing to develop a template to guide future and rigorous application of a purpose-based test.

B. Text, Structure and Effect of Measure

In many cases, a tribunal will be first presented with evidence of the text, structure and effect of the measure under review. Indeed, as argued earlier, the complainant should bear the initial burden of constructing a *prima facie* case of protectionist purpose on the part of the respondent state. Absent exceptional factual matrices involving targeted subjective evidence in the form of ministerial statements (such as that made in *SD Myers*), the claimant would typically seek to build their case by focusing on objective indicators of protectionist purpose.

¹⁵⁵ *Corn Products International, Inc. v Mexico*, Decision on Responsibility (ICSID Case No. ARB(AF)/04/01, Jan. 15, 2008) at para 137.

¹⁵⁶ *Id.*

Such objective evidence must however be of a type and quality sufficient to shift the burden to the respondent to adduce proof of a legitimate purpose that justifies the measure in question.

Tribunals have, on occasion, structured their inquiry into state purpose by commencing with the text of the measure. In *ADM v Mexico* for instance, the Tribunal explicitly approached “its review of the intent of the IEPS Amendment by first examining its text”.¹⁵⁷ The measure in that case was a Mexican tax on soft drinks and syrups that used any sweetener other than cane sugar.¹⁵⁸ The claimant owned a plant in Mexico that produced high-fructose corn syrup (HFCS), a sweetener that competed with cane sugar and therefore attracted the tax.¹⁵⁹ Mexico had argued that its tax was not protectionist but was justified instead as a countermeasure under customary international law. According to Mexico, the tax was structured as a direct response to the failure of the U.S to meet its NAFTA obligations to increase market access for Mexican sugar and to comply with the dispute settlement mechanism for such disputes under NAFTA Article 20.¹⁶⁰ The question of whether a countermeasure of this sort (even if permitted under customary international law) can ever be anything but protectionist is considered later, given the distinct targeting of foreign producers of products that compete with domestic cane sugar.¹⁶¹ But for current purposes, what is important is that Mexico seems to understand this purpose as legitimate¹⁶² and how the Tribunal evaluates Mexico’s claim of a legitimate motive.

The Tribunal clearly understands its role as one of reviewing the purpose underlying the measure. By commencing its analysis with the text of the Mexican tax, it also identifies an early

¹⁵⁷ *ADM v Mexico*, *supra* note [], at para 142.

¹⁵⁸ *Id.* at para 2.

¹⁵⁹ *Id.* at para 42.

¹⁶⁰ *Id.* at paras. 106-7.

¹⁶¹ *See infra* [] (External Justifications).

¹⁶² Consider for example: “The Respondent contends that the Tax does not breach Article 1102 (National Treatment) because it did not target U.S. investors as such. The Tax was not intended to inflict harm upon HFCS producers and manufacturers, but was a reaction and compensatory measure to the restrictions adopted by the U.S Government against Mexican sugar.” *ADM v Mexico*, *supra* note [], at para 107.

flaw in Mexico's defence. For the Tribunal, Mexico's problem was that: "Nothing in the text of the IEPS Amendment indicates that it was enacted as a countermeasure against the United States. Rather it was a device to protect domestic cane sugar producers from competition by the HFCS industry."¹⁶³ The *ADM* Tribunal's start-point of testing the claimed purpose of the state against the text under review may be a sensible one in certain settings. The absence of a textual reference could potentially be probative in reviewing the veracity of a state's asserted motive especially where the state has chosen to list *other* purposes on the face of the law. Obviously however, an adjudicator should display some sensitivity in tackling this dimension. She might, for instance, be examining a measure that originates from a political and legal culture that has no tradition of formally outlining the underlying purpose of the law or regulation in question. Where that is the case, the absence of any stated purpose is unlikely to have much probative force.

A further and potentially far more important evidential source that would normally be submitted by the claimant as part of its burden of production will go to the disparate impact caused by the measure in question. Where for instance there is evidence showing that foreign investors as a class suffer significantly more than a group of "like" domestic actors, this may indeed suggest protectionist intent on the part of the state. In the WTO, adjudicators have used evidence of disparate impact explicitly as a means of uncovering a state's purpose underlying a measure under review. In *Chile-Alcohol* for instance, the Appellate Body paid careful attention to the jagged structure of a Chilean tax, whereby most imports were subject to the highest tax rate while a significant proportion of competing domestic alcoholic products attracted the lowest tax rate.¹⁶⁴ For the Appellate Body, this structural evidence of deep disparate impact

¹⁶³ *Id.* at para 142.

¹⁶⁴ *Chile-Alcohol*, Report of the Appellate Body, *supra* note [], at para 63-6.

can be used “to permit identification of a measure’s objectives or purposes” and those purposes in turn “*are* intensely pertinent to the task of evaluating whether or not that measure is applied so as to afford domestic production” (emphasis in original) in breach of GATT Article III(2).¹⁶⁵

In investment law, there are similar examples of deep disparate impact which – just as in the WTO – can be used productively by an adjudicator to uncover state purpose. In *Corn Products* for instance, the Tribunal found that HFCS (the disfavoured product under the measure) was *only* produced by foreigners while production of cane sugar (the favoured product) was largely domestic, suggesting that the disparate impact was not accidental but part of a deliberate strategy to target foreign ownership in the sweeteners market.¹⁶⁶ Even here, the Tribunal is careful to rule that disparate impact was only one of a series of factors probative of “an intention on the part of Mexico to treat the claimant differently because of its nationality”.¹⁶⁷ Of course, at the other end of the spectrum, an adjudicator could be confronted with a measure that merely causes incidental harm to foreign vis-à-vis “like” domestic investors. This would be the case, for instance, where all but a very small percentage of domestic producers are treated equally (or even worse) than the foreign claimant. In this setting, without any other evidence whatsoever, it is difficult to see how the advantage enjoyed by the small group of domestic producers is likely to be the result of a deliberate policy. Confronted with such a

¹⁶⁵ *Id.* at para 71.

¹⁶⁶ “[T]he uncontradicted evidence in this case was that production of HFCS in Mexico was wholly concentrated in foreign-owned enterprises (predominantly CPI, which had [redacted] of the HFCS share of the market for soft drink sweeteners), whereas production of sugar was largely carried out by Mexican nationals (with the Mexican State itself owning a substantial part of sugar production.” *Corn Products v Mexico*, *supra* note [], at para 132.

¹⁶⁷ The Tribunal examines a number of indicators of protectionism on the part of Mexico, including its assertion that the tax was justified as a countermeasure under customary international law. For the Tribunal, “the very fact that such a justification has been advanced amounts to a recognition by Mexico that HFCS producers and suppliers were targeted, in part at least, because of the extent of their links to the United States”. *Corn Products v Mexico*, *supra* note [], at paras. 137-8.

minimal evidential record, an adjudicator can legitimately – as did the Tribunal in *ADF v USA*¹⁶⁸ – rule that the claimant has failed to discharge its burden of proof in constructing a case of protectionist purpose on the part of the respondent state.

C. Legislative History

The inquiry into text, structure and disparate impact should always be placed in context, in order to determine whether the harm suffered by the foreign investor resulted from a deliberately protectionist policy. This will, firstly and fundamentally, require an adjudicator to situate her assessment of the measure in question against its overall legislative history. This critical point finds reflection in the jurisprudence of the U.S. Supreme Court. In an equal protection case - *Village of Arlington Heights v Metropolitan* – the Supreme Court made the sensible point that impact of official action will rarely be determinative in casting light on state purpose and concluded that it must look to other “such circumstantial and direct evidence of intent as may be available”.¹⁶⁹ The Court then expressly recognized that “[t]he historical background of the decision is one evidentiary source” where, *inter alia*, “[t]he specific sequence of events leading up to the challenged action also may shed some light on the decisionmaker’s purposes”.¹⁷⁰

If we turn to investor-state arbitration, there are promising signs of careful attention to legislative history as a means of determining the intent of a regulating state. In *Methanex*, the Tribunal ultimately ruled in favour of the respondent state by adopting an artificially narrow

¹⁶⁸ “The Investor did not sustain its burden of proving that the U.S. measures imposed (de jure or de facto) upon ADF International, or the steel to be supplied by it in the U.S., less favorable treatment vis-à-vis similarly situated domestic (U.S.) fabricators or the steel to be supplied by them in the U.S.” *ADF v U.S.*, *supra* note [], at para 157.

¹⁶⁹ *Village of Arlington Heights v Metropolitan*, 429 U.S. 252, 266 (1977) (Powell J.).

¹⁷⁰ *Id.* at 267.

reading of the likeness requirement. Specifically, it found that the Californian ban on MTBE (as a gasoline oxygenate) was justified because it extended equal treatment to the foreign claimant (who produced methanol as an input into MTBE) as to “like” domestic methanol producers. But in a separate part of the award, the *Methanex* Tribunal also engaged in extensive assessment of the factual chronology of the election of the Californian legislature to ban the use of MTBE while continuing to allow ethanol (as a substitute to MTBE) to be sold in the Californian market. The Tribunal’s careful review of the history underpinning the ban uncovers a legitimate justification for the Californian legislature to treat MTBE and ethanol differently. To that extent, this part of the *Methanex* award offers an instructive example of how an adjudicator can use legislative history to cast light on the purpose underlying a measure. The Tribunal begins by tracing the origins of the ban on MTBE to the decision of the Californian legislature to commission the University of California to scientifically assess various risks associated with the use of MTBE.¹⁷¹ These included the risk to human health and the environment through MTBE leaking from underground storage tanks into groundwater supplies.¹⁷² In November 1998, the University of California released its 600 page report which concluded that there were “significant risks and costs associated with water contamination due to the use of MTBE”.¹⁷³ The Report recommended a phase-out of the use of MTBE provided that assessment is undertaken “of the environmental impact of using other oxygenates such as ethanol”.¹⁷⁴ In December 1999, the Californian Environmental Protection Agency released its own report finding that the “impacts [on water contamination] associated with the use of ethanol would be significantly less and more manageable than those associated with continued use of MTBE”.¹⁷⁵ It was only *after* the release of this second report and following a series of public hearings and

¹⁷¹ *Methanex v U.S.*, *supra* note [], at Part III, Chp. A, para 1.

¹⁷² *Id.* at Part III, Chp. A, para 2 (Topic Three).

¹⁷³ *Id.* at Part III, Chp. A, para 9.

¹⁷⁴ *Id.* at Part III, Chp. A, paras. 14 and 16.

¹⁷⁵ *Id.* at Part III, Chp. A, paras. 30-1.

testimony¹⁷⁶, that the Californian legislature elected to phase out the use of MTBE while continuing to allow ethanol to be used as an oxygenate¹⁷⁷. The Tribunal also reviews extensive witness testimony on the rigour and sufficiency of the scientific justification offered in these reports.¹⁷⁸ This ultimately leads to a conclusion that the ban on MTBE was “not the product of a political sham engineered by California” but “a serious, objective and scientific approach to a complex problem”.¹⁷⁹ This careful and extensive assessment of the environmental justifications for the MTBE ban receives no attention whatsoever in the Tribunal’s legal analysis of national treatment. It is instead quarantined in the factual findings of the award. Yet this review of the legislative record provides clear and compelling evidence, as the Tribunal itself determines, of a legitimate, non-protectionist reason.

ADM v Mexico is a case that uses the same careful inquiry into legislative history but unlike *Methanex v U.S.*, does so *expressly* as a means of casting light onto state purpose. Here the Tribunal uncovers a historical context of a very different sort to that at play in *Methanex*. The measure at issue in *ADM* was a 2001 Mexican tax that gave preference to sugar over HFCS as a sweetener in soft drinks. As we saw earlier, Mexico had argued that its tax was not protectionist. It justified the tax instead as a countermeasure under customary international law, taken in response to the failure of the U.S to meet its NAFTA obligations to increase market access for Mexican sugar and to comply with the dispute settlement mechanism for such disputes under NAFTA Article 20.¹⁸⁰ The *ADM* Tribunal examines a series of evidential factors surrounding the passing of the measure to evaluate the veracity of the Mexico’s

¹⁷⁶ There were three days of public hearings on the University of California Report. At these hearings, “government officials and members of the public (including MTBE and methanol producers” including federal agencies had an opportunity to ask questions and present oral testimony”. This testimony “indicated broad-based support for the finding by the University of California that MTBE usage in gasoline constituted a serious threat to California’s drinking water and that a ban on the use of MTBE in California RFG was warranted”. *Id.* at Part III, Chp. A, paras. 17-9.

¹⁷⁷ *Id.* at Part III, Chp. A, para 32.

¹⁷⁸ *Id.* at Part III, Chp. A, paras. 37-100.

¹⁷⁹ *Id.* at Part III, Chp. A, para 101.

¹⁸⁰ *ADM v Mexico*, *supra* note [], at paras. 106-7.

asserted purpose. It traces at some length the background to 2001 tax, including the fact that it was preceded in 1998 by anti-dumping duties imposed against HFCS imported from the U.S.¹⁸¹ Those duties in turn were ruled to be contrary to Mexico's obligations under both the WTO and NAFTA in a series of disputes heard over the course of 2000 to mid 2001.¹⁸² After these disputes, Mexico attempted to impose import restrictions on HFCS which were ruled to be unconstitutional before a Mexican administrative court.¹⁸³ Critically, the Tribunal positions its inquiry into this period "just prior to the enactment of the Tax" as "important in terms of the context for the passage of the tax and Mexico's *intent* in enacting it" (emphasis added).¹⁸⁴ That context reveals a close temporal connection between explicitly discriminatory measure on imports of HFCS (including the illegal anti-dumping duties) and the later tax on HFCS as a sweetener, suggesting the latter was taken as a substitute for the former:

The evidence on record before the Tribunal indicates that the most immediate relevant context in which the dispute over the Tax arose were the Mexican anti-dumping measures, the WTO and NAFTA rulings against these measures, and the order for their final repeal. The evidence before us indicates that this was the setting for the enactment of the Tax, rather than the dispute between Mexico and the United States over access to the U.S. market of Mexican-produced excess sugar, a dispute that ripened in the year 2000, well after the imposition of the anti-dumping measures.¹⁸⁵

This part of the *ADM v Mexico* award is a crucial reminder of the close connection between foreign investment and cross-border trade as mechanisms of economic exchange. The American company in *ADM* both exported HFCS from its operations in the U.S *and* had established plant and equipment in Mexico to produce HFCS for sale in the Mexican market.¹⁸⁶

The latter form of FDI enables a company to legitimately insulate itself from the risk of

¹⁸¹ *Id.* at para 72.

¹⁸² *Id.* at paras. 73-5.

¹⁸³ *Id.* at para 76.

¹⁸⁴ *Id.* at para 136.

¹⁸⁵ *Id.* at para 137.

¹⁸⁶ *Id.* at para 53.

contingent protection applied to cross-border trade (such as the anti-dumping duties on HFCS). Those duties, like tariffs, only attach to foreign imports, increase the cost of those foreign imports vis-à-vis competing domestic goods in the importing state's market and thus are by their very nature inherently protectionist. Yet here, the historical record clearly shows that Mexico only implemented its domestic tax on HFCS (applied to both imports and domestic production) after its first-order strategy of using anti-dumping duties had been ruled illegal. This strongly suggests that the tax itself was but a substitute for the earlier anti-dumping duty, evidencing the deeply fluid and fungible nature in the way protectionism can manifest itself (against both cross-border trade and foreign investment).

In *ADM v Mexico*, the analysis of the historical record was, as it should be, only one part of the Tribunal's assessment of the veracity of Mexico's claimed purpose in passing the tax. The Tribunal also examined protectionist statements made by the Mexican legislators who had proposed the tax¹⁸⁷ as well as pronouncements of the Mexican judiciary that had considered the constitutional validity of the tax¹⁸⁸. But by paying careful attention to the chronological sequence of key events in the factual record, the Tribunal is able to come to a highly plausible conclusion that Mexico's "true motive and intent" was one of "protection of the Mexican sugar industry".¹⁸⁹

D. Timing: *Ex Post* Justification?

When evaluating a state's claim of an innocent purpose underlying the measure, the timing of that assertion may be especially pertinent when considered in light of the overall legislative

¹⁸⁷ *ADM v Mexico*, *supra* note [], at para 80.

¹⁸⁸ *Id.* at para 146-7.

¹⁸⁹ *Id.* at para 150.

history. In particular, the fact that an innocent purpose is first asserted *ex post* (in litigation) without any evidence of *ex ante* reliance (at the time of enactment) may naturally suggest that it is not the state's actual policy goal.

The importance of giving careful consideration to the sequence and timing of a state's justification has, on occasion, been raised in adjudication before the WTO.¹⁹⁰ But it is in the investment treaty context that this dimension has been applied with targeted effect. The key arbitral case that draws out this point is *UPS v Canada*. One of the key measures at issue in that case was Canada's Publications Assistance Program (PAP), which was designed to ensure the distribution of Canadian cultural products (and especially publications) throughout Canada. Because of high subscription and low newsstand sales in Canada, the Canadian Government sought to achieve this goal through subsidization of the costs of mail delivery of Canadian publications.¹⁹¹ The PAP extended subsidy payments to eligible Canadian publications (including magazines and periodicals) to offset the cost of delivery throughout the country.¹⁹² However, publishers seeking these funds were required to use Canada Post – a state-owned entity that maintained a monopoly on letter mail but also operated in the competitive courier services market – to deliver their publications.¹⁹³ UPS, an American investor in the Canadian courier services market, challenged the exclusive provision of subsidy funds to Canada Post (under the PAP) as discriminatory in breach of NAFTA Article 1102.

¹⁹⁰ In *Japan – Alcohol* for instance, the U.S. argued that the protective aim of the Japanese tax on alcoholic beverages was apparent from, *inter alia*, “the stated policy objective and whether it was known at the time the legislation was enacted that it would draw a line between a group of products that would be foreign and another group of that would be domestic (ex-ante knowledge)”. Japan had argued that the measure was imposed to “maximize tax revenue” according to the “tax-bearing ability” of consumers. The U.S. noted that “this objective is nowhere stated in the law” and that record of actual deliberations of the Japanese legislature “demonstrates that the operative considerations in passing the legislation was the economic well-being of the domestic shochu producers, not a neutral tax policy”. *Japan – Taxes on Alcoholic Beverages*, Report of the Panel (WT/DS10/R, WT/DS11/R, Jul. 11, 1996), at para 4.107.

¹⁹¹ *United Postal Service of America Inc. v Canada*, Award on the Merits (NAFTA Chapter 11 Arbitration, May 24, 2007) at para 147.

¹⁹² *Id.* at para 151.

¹⁹³ *Id.* at para 153.

Canada presented a number of defences to UPS' claim, most importantly that there were legitimate, non-protectionist grounds for its exclusive use of Canada Post for the distribution of PAP benefits. Canada argued that, as Canada Post had a statutory obligation to deliver mail to every address in Canada, it was the *only* actor which could implement the PAP's goal of universal distribution of Canadian publications across the country.¹⁹⁴ In contrast, Canada claimed that UPS would only deliver to "large retail customers" and "customers in shopping malls" and was thus unable to meet the legitimate goal of universal distribution.¹⁹⁵ This defence is fundamentally a claim that exclusive delivery through Canada Post as a state-owned entity is justified because it comprises part of a vital public good, rather than simple protectionism. In a sparse few paragraphs¹⁹⁶, the majority accepted Canada's defence of fundamentally different capabilities and ruled that UPS was not "in like circumstances" with Canada Post in respect of the PAP.¹⁹⁷ Yet although exclusive use of a single government actor (such as Canada Post) *may* reflect a legitimate choice to achieve an outcome that is superior to market-based mechanisms, the claim that this was Canada's *actual* purpose when promulgating the PAP must still be tested in adjudication. The majority's approach here comes very close to simply accepting, without any real rigour, Canada's asserted justification that the involvement of Canada Post was integral to the PAP. There is, for instance, no attempt to identify whether Canada had actually engaged in any systematic assessment of the relative

¹⁹⁴ "The Program seeks to ensure the widest-possible distribution of Canadian publications to individual Canadian consumers at affordable and uniform prices throughout the country. As a matter of fact, by virtue of its statutory obligation to deliver to every address in Canada (in fulfillment of Canada's universal service obligation), only Canada Post is in a position to ensure that the Government of Canada is able to attain this objective." *Id.* at para 175.

¹⁹⁵ *Id.* at para 176.

¹⁹⁶ *Id.* at paras. 174-181.

¹⁹⁷ Consider for example, the following: "[UPS] is in fact incapable of assuming all of the benefits and responsibilities assumed by Canada Post under the PAP. In the circumstances, we conclude that UPS Canada is not 'in like circumstances' to Canada Post in respect of its program and, indeed, for essentially the same reasons, is not accorded less favourable treatment than Canada Post or treated differently because of nationality." *Id.* at paras. 180-1.

merits and limitations of private vis-à-vis governmental delivery mechanisms, before electing to tie PAP benefits to a publisher's use of Canada Post.

In contrast to the majority in *UPS*, Arbitrator Cass adopts a very different approach to testing Canada's assertion of a non-protectionist goal for exclusive use of Canada Post. Arbitrator Cass examines whether Canada's justification was its actual motive through careful analysis of the timing and other procedural elements of that asserted claim a legitimate rationale. He begins with the sharp observation that Canada "did not articulate publicly its current rationale for limiting benefits to Canada Post at the time it framed the current structure for delivery associated with the PAP" and that no distinction between Canada Post and UPS with respect to their eligibility for delivering periodicals "appears to have been made independent of this proceeding".¹⁹⁸ This concern of the timing of Canada's claim of a legitimate purpose is also set against key parts of the factual chronology. Cass records the fact that publishers had expressed frustration with Canada Post's performance and had even lobbied the regulator for a choice of delivery vendors.¹⁹⁹ Against this backdrop, Canada's procedure for structuring the PAP "on its face seemed to ask only *how* to give PAP benefits to Canada Post, not *why* it was important to broader public policy goals" (emphasis in original).²⁰⁰ In conclusion:

[Canada is] free to adopt any reasonable design to implement its policy of promoting widespread distribution of Canadian periodicals, but it is not free to assert for the first time during a dispute resolution proceeding an ex post rationalization that would limit availability of a government benefit to a single (domestic) recipient.²⁰¹

Once again, it is important to reiterate that Arbitrator Cass is not examining the timing of the state's claim of a legitimate purpose in isolation. He is using it instead as one key indicator

¹⁹⁸ *UPS v Canada*, Separate Statement of Dean Ronald A. Cass, *supra* note [], at para 127.

¹⁹⁹ *Id.* at paras. 115; 129.

²⁰⁰ *Id.* at para 130.

²⁰¹ *Id.* at para 124.

among many that Canada's claimed justification (that exclusive delivery via Canada Post was a form of public good) was not its actual purpose.

E. Domestic Court Rulings

On occasion, an arbitral tribunal may be presented with the ruling of a domestic court in the host state concerning facts and/or legal issues which are also implicated in the investment treaty dispute. There are strong substantive as well as strategic reasons for an arbitral tribunal to pay careful attention to this evidence. A domestic court in a host state will stand in closer position to the world of regulation and regulatory politics than an international tribunal. All things equal, they will be better equipped to make critical findings of fact, not least when assessing the value of evidence of the purpose underlying the measure under review. Careful attention to such domestic rulings may also serve a tribunal well by shielding it from criticism of motive review in especially sensitive cases. It may also contribute in some small way to the broader project of improving the legitimacy of the system of investment treaty arbitration. By interacting with national judges (through sensitive consideration of domestic court rulings), investment treaty arbitrators can begin to erode the evident mistrust among some national courts of the penetration of extra-domestic protections for foreign investment.²⁰²

Arbitral tribunals could be presented with a variety of domestic court rulings. At one of the spectrum, there may be evidence that a domestic court has explicitly pronounced on the measure under review and found it to be driven by protectionist goals perhaps in breach of domestic constitutional guarantees against discrimination. *ADM v Mexico* is a case of this type.

²⁰² Adam Liptak, *NAFTA Tribunals Stir U.S. Worries. Obscure Courts Reviewing American Judgments*, N.Y. TIMES (Apr. 18, 2004), at A1 (recording interviews with U.S. judges in the aftermath of the NAFTA Chapter 11 awards in *Mondev v USA* and *Loewen v USA*, with the Chief Justice of the Californian Supreme Court stating that “[i]t’s rather shocking that the highest courts of the state and federal governments could have their judgments circumvented by these tribunals”).

We saw a little earlier that the *ADM* Tribunal positioned its inquiry into the purpose underlying the Mexican tax by examining the legislative record as a whole. As part of that exercise, the Tribunal paid careful attention to a constitutional challenge brought by the Chamber of Deputies of the Mexican Congress (the originators of the tax) in the Mexican Supreme Court against a decision by the Mexican President to suspend the application of the tax, which the Tribunal ruled “*also* confirmed that the design and operation of the Tax was to afford protection to Mexican production of cane sugar” (emphasis added).²⁰³ In so doing, the Tribunal quoted in full the finding of the Mexican Supreme Court that:

The legislator’s intent when extending the aforementioned tax to gasified waters, soft drinks, hydrating drinks and other taxed goods and activities, when they use fructose in their production rather than cane sugar, was that of protecting the sugar industry.²⁰⁴

ADM is not the only case which has featured a conclusion of this sort by a domestic court. The Tribunal in *Feldman v Mexico* was faced with a series of changes and administrative practices under Mexican law concerning rebates of tax on exported cigarettes. The claimant, CEMSA, operated a cigarette exporting business and had received those rebates in 1990-1991. The tax system was then changed in so that *only* cigarette producers could receive the export rebate thereby excluding a reseller-exporter such as CEMSA.²⁰⁵ CEMSA mounted a successful domestic challenge to that change, with the Mexican Supreme Court ruling that “measures allowing [tax] rebates only to producers and their distributors violated constitutional principles of tax equity and non-discrimination”.²⁰⁶ Mexico then amended its laws to allow rebates to all cigarette exporters (including CEMSA) but *also* activated a dormant requirement that claimants present a special invoice for tax paid on cigarette purchases which had the effect

²⁰³ *ADM v Mexico*, *supra* note [], at para 146.

²⁰⁴ *Id.* at para 147.

²⁰⁵ *Feldman v Mexico*, *supra* note 21, at paras 9-10.

²⁰⁶ *Id.* at para 16

of continuing to preclude CEMSA's ability to access the rebate.²⁰⁷ Unlike *ADM*, the domestic court ruling recorded in *Feldman* does not directly address the measure under review being the activation of the invoice requirement. It does, however, form an important part of the factual record leading up to that critical change in policy by the tax authority. In particular, the Supreme Court's ruling raises justifiable doubt as to whether the later and sudden activation of the discretion under the tax law was for legitimate purposes such as tax evasion, as pleaded by Mexico. The timing of the change - in the immediate aftermath of the foreign investor's successful domestic court challenge - suggests instead that the state is simply using different means to achieve the same discriminatory goal.

Explicit legal rulings by a domestic court of the sort seen in *ADM v Mexico* and *Feldman v Mexico* may be somewhat exceptional. It is perhaps more likely that an arbitral tribunal will be presented with a key finding of fact made by a domestic court, which may also weaken the respondent state's claim of a legitimate purpose. *Occidental v Ecuador* offers an instructive example of this type of case. Ecuador had attempted to defend its failure to provide VAT refunds to the foreign investor (who produced oil for export) on the basis that Ecuadorian tax law limited such VAT refunds to "manufactured exports" and excluded them for "production exports" such as oil and other natural resources.²⁰⁸ In assessing this claim of a legitimate justification, the *Occidental* Tribunal paid careful attention to both the various iterations of the tax law²⁰⁹ as well as rulings of Ecuadorian courts that had heard challenges by oil producers on the legality of the refusal to provide them with VAT refunds²¹⁰. On the latter, the Tribunal was especially influenced by a decision of the Special Taxation Chamber of the Ecuadorian Supreme

²⁰⁷ *Id.* at paras. 14-15.

²⁰⁸ *Occidental Exploration and Production Company v Ecuador*, Final Award (UNCITRAL, LCIA Case No. UN 3467, Jul. 1, 2004), at para 135

²⁰⁹ *Id.* at para 119-135.

²¹⁰ *Id.* at paras 137-143.

Court which had decided that the imposition of VAT under Ecuadorian law “depends not on the source of the good but its final destination”.²¹¹ The Tribunal then pointedly – and with good reason – ruled that “as held by the Ecuadorian courts”, the foreign investor as an exporter (whether of manufactures or resources) was fully entitled to VAT refunds, at odds with a key part of Ecuador’s defence to the investment treaty claim.²¹²

F. External Justification

There have been a variety of arbitral awards where a respondent state has justified its measure as complying with an external treaty or customary commitment. Indeed, the broader obligations of a member state at international law can penetrate investment treaty adjudication in a variety of complex ways. At one of the spectrum, there are *jus cogens* norms which protect values so fundamental within international law that derogation from them can never be allowed. Where investment treaty obligations conflict with such a peremptory norm, the latter will always prevail which is a hierarchy enshrined in positive law in the VCLT.²¹³ Article 103 of the U.N. Charter also establishes a formal priority rule whereby the obligations of member states of the United Nations under the Charter prevail over conflicting obligations under any other international agreement.²¹⁴ Outside of these few cross-cutting structures, states parties may also construct specific mechanisms within investment treaties to regulate the interaction of their commitments with other areas of international law. The NAFTA, for example, elevates the obligations of its member states under a number of external environmental and conservation treaties over the commitments set out in the NAFTA in

²¹¹ *Id.* at para 141.

²¹² *Id.* at para 143.

²¹³ VCLT, *supra* note [], at Arts. 53; 64.

²¹⁴ Charter of the United Nations, Jun. 26, 1945, 58 Stat. 1031, at Art. 103.

particular settings.²¹⁵ Each of these formalized conflict mechanisms must be given effect in the event they are triggered by the specifics of a dispute brought under a given investment treaty. But those formulae do not exhaust the possibilities by which external legal commitments can enter and shape the adjudication of an investment treaty claim. Where there is no relevant conflict clause in operation, a state may still seek to introduce an external commitment as part of its general defence to breach of its investment treaty commitments.

When it comes to national treatment, this strategy will often reflect an attempt by the state to use its obligations or permitted discretion under the external legal norm as evidence of a legitimate purpose other than protection of domestic industry. The operation of another international legal regime on the measure under review may well be a highly pertinent factor for an adjudicator to test the *bona fides* of the respondent state, especially in an inquiry into constructed purpose. There are, however, five general qualifications that must be borne in mind by an adjudicator when drawing on such evidence. First and perhaps most obviously, the subject-matter of the external norm must have some relevance to the state's claim of a non-protectionist rationale. Where, for instance, an environmental treaty compels or enables a state to regulate in such a way that causes incidental harm to the foreign investor, the state's commitments under that treaty might bolster its defence that it is acting for environmental rather than protectionist reasons. But not all external norms pleaded by respondents to date

²¹⁵ "In the event of any inconsistency between this Agreement and the specific trade obligations set out in:

- (a) the *Convention on International Trade in Endangered Species of Wild Fauna and Flora*, done at Washington, March 3, 1973, as amended June 22, 1979,
- (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 Waste 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 any 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."

NAFTA, *supra* note [], at Art. 104(1).

will work in this way. Some may have the opposite effect and support instead the investor's claim for breach. Consider, for example, Mexico's defence in *ADM* and *Corn Products* that its tax was authorized as a countermeasure under customary international law. Mexico argued that its tax was structured as a response to the failure of the U.S. to meet its NAFTA obligations to increase market access for Mexican sugar and to comply with the dispute settlement mechanisms for such disputes under NAFTA Article 20.²¹⁶ Under customary international law, an injured state is permitted to take measures that would otherwise be contrary to their international obligations, but they can only do in response to an internationally wrongful act of the other state in order to procure cessation and reparation.²¹⁷ As a type of self-help mechanism in the decentralized system of international law, countermeasures are open to abuse and their invocation is subject to strict conditions. One of these conditions is that any countermeasure must be directed against the responsible state to *induce* it to comply with its legal obligations.²¹⁸

The tribunals in *ADM* and *Corn Products* adopt opposing positions on whether a countermeasures defence is – as a matter of principle – applicable to a treaty system that confers rights on non-state actors.²¹⁹ That important point aside, the very invocation of a countermeasure justification weakens Mexico's claims of a non-protectionist justification for its tax. We have already seen that one of the key conditions of a countermeasure is that it must be taken to induce the state in breach to comply with its legal obligations. If, as Mexico argued,

²¹⁶ *ADM v Mexico*, *supra* note [], at paras. 106-7.

²¹⁷ International Law Commission, *Draft Articles on the Responsibility of States for Internationally Wrongful Acts With Commentaries*, U.N. GAOR, 56th Sess., Supp. 10, Ch. 4, UN Doc. A/56/10 (2001), at 128.

²¹⁸ “An injured State may only take countermeasures against a State which is responsible for an internationally wrongful act in order to induce that State comply with its obligations under Part Two”. *Id.* at 129; Article 49(1) (Object and limits of countermeasures).

²¹⁹ Compare *ADM v Mexico*, *supra* note [], at paras. 117-123 (finding that “countermeasures may service as a defence under a [NAFTA] Chapter Eleven case”) with *Corn Products v Mexico*, *supra* note [], at paras. 167-176 (finding that foreign investors have substantive rights under NAFTA Chapter 11 and a countermeasure taken by one NAFTA state against another “cannot deprive that investor of its rights”).

its tax on sweeteners other than cane sugar was a countermeasure directed at inducing the U.S to comply with its NAFTA Chapter 20 obligations, it is then acknowledging that the harm caused by the tax was both intentional and directed at American producers of HFCS (being the competing and disfavoured product under the tax). Of the two awards, it is only the *Corn Products* Tribunal that draws out the protectionist implications in Mexico's invocation of custom.²²⁰ Of course, these cases may be exceptional and unlikely to be repeated in the near future. They none the less illustrate the importance of paying careful attention to the story told by the invocation of the external norm on the part of the respondent state.

Secondly, the mere presence of an external norm should not be sufficient to automatically ground a finding of legitimate purpose on the part of the regulating state. If an adjudicator simply accepts a state's plea of justification using an external legal commitment, they will then be effectively conferring a type of deference to that claim. She should instead consider both the degree and nature of the connection between the external commitment and the measure under review. Most importantly, there is the first-order issue of whether the external commitment imposes a hard legal obligation on the state. Thus, where a treaty strictly requires a state to enact the type of measure under review, an adjudicator would be well placed to accept this as strong evidence of a *bona fide* purpose. In *Pope & Talbot v Canada* for instance, the Canadian measure – allocation of quotas for softwood lumber exports from “covered” provinces in Canada to the U.S. – was one of Canada's specific obligations under the 1996 Softwood Lumber

²²⁰ “[N]ationality was a highly pertinent factor in the imposition of the tax...[i]t is the countermeasures justification advanced by Mexico which we consider important. If the HFCS tax was intended as a countermeasure targeted against the United States, it had to have been crafted in such a way that it bore especially heavily upon US interests, otherwise it would have had no chance of being effective or of being a lawful countermeasure. As counsel for Mexico said in the course of the oral hearing, ‘the model countermeasure is one that causes pain’. But that pain has to be caused to the State against whom the countermeasure is targeted, in this case the United States. While the Tribunal will consider whether the HFCS tax amounted to a lawful countermeasure in the next Part of the Decision, we must at this stage say that the very fact that such a justification has been advanced amounts to a recognition by Mexico that HFCS producers and suppliers were targeted, in part at least, because of the extent of their links to the United States.” (footnotes omitted). *Corn Products v Mexico*, *supra* note [], at para 137.

Agreement (SLA) which had been negotiated to settle a trade dispute with the U.S.²²¹ The *Pope & Talbot* Tribunal explicitly reads national treatment as a constraint on purposeful protectionism, whereby a measure will be excused “if it bears a reasonable relationship to rational policies not motivated by preference of domestic over foreign owned investments”.²²² The Tribunal then went on to dismiss the foreign investor’s claim because, *inter alia*, the quota system was directly connected to the SLA and thus “reasonably related to the rational policy of removing the threat of [countervailing duty] actions”.²²³

On the other hand, one could not necessarily draw the same inference where the external norm places no strict obligation on the state to act and/or leaves significant discretion of the choice of means by which to comply with its external commitments. In *AES v Hungary*, the Tribunal sensibly questioned Hungary’s plea that its price-cap legislation in the energy sector was directly caused by its obligations as a member of the European Union, because the European Commission had not rendered a binding decision on whether the existing scheme constituted a form of prohibited state aid.²²⁴ The hardest cases will involve external regimes where the exact balance between obligation and discretion cannot be simply discerned from a general examination of the treaty text. Faced with this scenario, it could be appropriate for the adjudicator to draw on the expert views of the secretariat of the particular international regime in question (where one exists) to discern the precise nature of the external treaty commitment and its intended relationship to domestic regulation.²²⁵

²²¹ *Pope & Talbot v Canada*, *supra* note [], at para 18.

²²² *Id.* at para 79.

²²³ *Id.* at para 87.

²²⁴ “Had Hungary been motivated to reintroduce price regulation with a view to address the EC’s state aid concerns, there is no doubt that this would have constituted a rational policy measure. However, the Tribunal notes that as long as the Commission’s state aid decision was not issued, Hungary had no legal obligation to act in accordance with what it believed could be the result of the decision and to start a limitation of potential state aid.” *AES v Hungary*, *supra* note [], at para 10.3.16.

²²⁵ For a discussion of this possibility in the context of disputes heard concerning the WTO Agreement on Technical Barriers to Trade, see Robert Howse, *A New Device for Creating International Legal Normativity: The WTO Technical*

But this is not say that soft law norms or treaties that merely impose “best endeavours”-type commitments have no role to play in testing a state’s claimed purpose. Even here, tribunals should strive to resolve cases as best they can to reconcile overlapping international legal systems, given the strong presumption against normative conflict in international law.²²⁶ Investment arbitrators can contribute to this goal of minimizing system friction by paying careful attention to the role such “weaker” external norms play in the story of the measure under review. On those lines, one of the arbitrators in *AES v Hungary* displayed welcome sensitivity to the *likely* pressure brought to bear on Hungary by the European Commission’s investigations, even though those investigations had not been concluded.²²⁷ Similarly, in *Chemtura Corporation v Canada*, the Arbitral Tribunal examined the cumulative impact of the growth of international legal commitments progressively restricting the use of lindane as a pesticide, in upholding Canada’s review and eventual ban on lindane for health reasons.²²⁸

Thirdly, an adjudicator must assess not only the *degree* but also the *nature* of the connection between the external commitment and the measure at issue. For instance, where a host state has a choice among equally effective and reasonable available means of complying with its non-investment related obligations, the election to adopt a measure which is *most* restrictive towards foreign investment could weaken its ability to rely on the external norm as part of its

Barriers to Trade Agreement and ‘International Standards’, in CONSTITUTIONALISM, MULTILEVEL TRADE GOVERNANCE AND SOCIAL REGULATION 383, 386 (C. Joerges & E-U. Petersmann eds., 2006).

²²⁶ ILC Fragmentation Report, *supra* note [], at para 37.

²²⁷ “Arbitrator Stern considers that it was not exclusively so motivated, but that the enquiry and subsequent pressures from the Commission certainly was in the Hungarian authorities’ mind when they decided to reintroduce price regulation. In her view, it appears from the record that the high prices were also a serious problem for the Commission and it is quite evident that even before Hungary was under a legal obligation to follow the Commission’s decision, it had been made abundantly clear to Hungary that the PPAs raised considerable concerns at the European level, as being in contradiction with the European free market policies...To arbitrator Stern, the evidence is overwhelming that the decision to reintroduce maximum administrative prices was a rational, non-arbitrary response to a complex set of legitimate policy concerns.” *AES v Hungary*, *supra* note [], at para 10.3.19.

²²⁸ *Chemtura Corporation v Canada*, Award (UNCITRAL Arbitration, Aug. 2, 2010).

defence. In a similar vein, the inquiry should also assess the extent to which the external norm mandates or provides for the *specific* type of regulation applied by the host state. We find differing approaches to this critical dimension in the case-law. The majority in *UPS v Canada*, for instance, were prepared to accept the simple presence of an external norm as sufficient in finding the foreign investor was not “in like circumstances” with its domestic competitors. This part of the case dealt with Canada’s enforcement of its customs laws. UPS (an American company) competed with Canada Post (a state-owned entity) in the courier services market. Canada Post also maintained a statutory monopoly on the delivery of letter mail. UPS argued that Canada’s enforcement of its custom laws breached national treatment.²²⁹ For present purposes, the two key claims of “less favourable treatment” were: (i) Canada Customs paid handling fees to Canada Post for services (in support of compliance with customs requirements) that UPS performed without compensation; and (ii) that Canada Customs did not levy the same fines and penalties against Canada Post as it levied on UPS.²³⁰ Canada’s primary defence to this allegation was to point to a series of external treaty commitments that allowed for specialized customs treatment of express mail products (such as couriered mail) as against letter mail.²³¹

These external norms were enough for the majority of the Tribunal to summarily rule that UPS did not stand “in like circumstances” with Canada Post on the customs treatment claim:

The evidence is compelling. Canada, like the US and UK, has adopted customs procedures which are fully compliant with the Universal Postal Convention and the Kyoto Convention. Customs administrations

²²⁹ For the full list of claims made by UPS on Canada’s enforcement of its customs laws, see *UPS v Canada*, *supra* note [], at para 80

²³⁰ *UPS v Canada*, Separate Statement of Dean Ronald A. Cass, *supra* note [], at 28-32.

²³¹ “Canada places primary reliance on international agreements respecting mail under the Universal Postal Union and the separate annex respecting mail under the Kyoto Convention of the World Customs Organization.” *Id.* at 37.

throughout the world accord different treatment to postal traffic than is accorded to express consignment operators for the simple reason that circumstances are not like.²³²

There are two serious flaws with the deference accorded by the majority to these external commitments. First, UPS' claim was *only* about Canada's different treatment of UPS vis-à-vis Canada Post, in the particular sector in which they competed together. In other words, UPS did not deny Canada's general right – confirmed by the postal conventions - to maintain different customs procedures for letter mail (in which Canada Post operated exclusively) and courier mail (where UPS and Canada Post operated in competition). UPS' claim was limited only to Canada's disparate treatment of UPS vis-à-vis Canada Post in the *common* sector of operation, being the courier services market.²³³ Second, a review of the *specifics* of these external conventions offers no justification for the particular differences in treatment that form the subject of the complaint. Here again, Arbitrator Cass' approach is instructive and preferable to the summary review undertaken by the majority. After examining the text of the external sources in question, he notes that that “nothing in any of the [postal conventions]...requires the differences challenged before this Tribunal”²³⁴ before concluding that “Canada's reliance on the existence of differences between the exclusive postal franchise recognized in most nations and other imports, thus, is misplaced”²³⁵.

As a fourth general factor, an adjudicator should not look to a particular element of the external norm in isolation. It would be prudent to bear in mind the complete architecture of the external commitment in order to assess how it relates to the specific measure in question. In *SD Myers* for example, Canada had attempted to justify the closure of the U.S-Canadian border to exports of PCB waste as complying with its environmental commitments under the

²³² *UPS v Canada*, *supra* note [], at para 118.

²³³ *UPS v Canada*, Separate Statement of Dean Ronald A. Cass, *supra* note [], at 39 and 42.

²³⁴ *Id.* at para 40.

²³⁵ *Id.* at para 44.

Basel Convention on the Control of Transboundary Movements of Hazardous Wastes and Their Disposal 1989.²³⁶ Individual components of that treaty do indeed offer credence to Canada's claim. The Basel Convention puts in place a system to limit trans-boundary movement of hazardous waste and requires member states to maintain sufficient domestic disposal facilities.²³⁷ These are not, however, absolute obligations. They allow, for instance, export of waste where the exporting state does not have "the necessary facilities, capacity, or *suitable* disposal sites in order to dispose of the wastes in question in an environmentally sound and efficient manner" (emphasis added).²³⁸ As a factual matter, domestic facilities for waste remediation were located in parts of Canada (Alberta) that were geographically distant from the main inventory of such waste (Ontario and Quebec). The foreign investor's plant in Ohio was in turn geographically closer to that inventory than any of its Canadian competitors.²³⁹ Moreover, the Canadian Department of Environment had expressly advised federal and provincial governments in Canada that an open border represents "a technically and environmentally sound solution to the destruction of some of Canada's PCBs"²⁴⁰, directly in line with the qualified exemption enshrined in the Basel Convention. Finally, the two states had concluded a bilateral agreement allowing for transit of hazardous waste across their common border²⁴¹, a tailored solution itself permitted under the Basel Convention²⁴². In sum then, open-access between the two states for transport of hazardous waste was, contrary to

²³⁶ *SD Myers v Canada*, *supra* note [], at paras. 150, 185. See also *SD Myers v Canada*, Separate Opinion by Dr Brian Schwartz, *supra* note [], at para 150.

²³⁷ Basel Convention on the Control of Transboundary Movements of Hazardous Wastes and Their Disposal, Mar. 22, 1989, 1673 U.N.T.S. 126; 28 I.L.M. 657 (1989), at arts. 4(1) (requiring member states to prohibit export of hazardous waste) and 4(2)(b) (requiring member states to "[e]nsure the availability of adequate disposal facilities...that shall be located, to the extent possible, within it") [hereinafter Basel Convention].

²³⁸ *Id.* at Art. 4(9)(a).

²³⁹ *SD Myers v Canada*, *supra* note [], at para 112.

²⁴⁰ *Id.* at para 165.

²⁴¹ Agreement between the Government of the United States of America and the Government of Canada concerning the Transboundary Movement of Hazardous Wastes, *entry into force* Aug. 11, 1986, 39 C.T.S. (1986), at Art. 2. For analysis of this bilateral convention and its contemplation of cross-border trade in hazardous waste, see *SD Myers v Canada*, *supra* note [], at para 103; *SD Myers v Canada*, Separate Opinion by Dr Brian Schwartz, *supra* note [], at paras 99-100.

²⁴² Basel Convention, *supra* note [], at Art. 11 (authorizing member states to conclude, *inter alia*, bilateral agreements regarding transboundary movement of hazardous waste).

Canada's assertion, confirmed by an overall assessment of the full suite of external legal norms at issue.²⁴³

Finally, an external norm may be a relevant factor in certain settings but it will rarely be determinative on its own. An adjudicator should, once again, bear in mind the overall factual context of the measure to assess the precise role that an external legal norm might play in evidencing a given purpose on the part of the regulating state. *Parkerings v Lithuania* offers useful guidance in this respect.²⁴⁴ That case involved a claim by a foreign investor for breach not of national but most-favoured-nation treatment. The investor had applied to build a car park in the Old Town area of Vilnius in Lithuania but was denied permission by city authorities.²⁴⁵ It claimed breach of the most-favoured-nation obligation of the applicable investment treaty because investors from third states had been granted permission to build in the Old Town.²⁴⁶ The Tribunal commences its analysis by considering Lithuania's defence that parts of the Old Town were listed as a protected cultural area under UNESCO and as such, construction in that zone legitimately required the approval of various administrative agencies.²⁴⁷ But this factor alone was not sufficient to justify Lithuania's rejection of the claimant's application because *both* projects fell within the boundary of the protected UNESCO zone.²⁴⁸ The Tribunal went on, however, to identify two objective factual elements which gave the city "legitimate grounds to distinguish between the two projects".²⁴⁹ These were firstly

²⁴³ In a similar vein, consider: "The [Canadian] government did not ask for internal or independent legal opinion to be prepared on whether leaving the border open from the Canadian side would be contrary to the Basel Convention. As purported reliance on Basel was a centrepiece of the government's public justification for its policy, this failure is remarkable." *SD Myers v Canada*, Separate Opinion by Dr Brian Schwartz, *supra* note [], at para 150.

²⁴⁴ *Parkerings-Compagniet AS v Lithuania*, Award (ICSID Arbitration No. ARB/05/8, Sept. 11, 2007).

²⁴⁵ *Id.* at para 363.

²⁴⁶ *Id.* at paras. 362, 364, 371.

²⁴⁷ *Id.* at para 382.

²⁴⁸ *Id.* at para 381.

²⁴⁹ *Id.* at para 396.

that the claimant's project was much larger (than that of the third state investor)²⁵⁰ and critically, that it was far more proximate to the "culturally sensitive area of the Cathedral"²⁵¹ located in the protected zone of the Old Town.

G. Multiple Purposes

There is one final issue implicated in a purpose-based test to national treatment. A statute is not necessarily enacted with a single purpose in mind: "Rarely can it be said that a legislature or administrative body operating under a broad mandate made a decision motivated solely by a single concern, or even that a particular purpose was the 'dominant' or 'primary' one."²⁵² The legislator may instead be driven both by legitimate (such as environmental) and protectionist goals, reflecting in part the propensity of different domestic interest groups to bind together for strategic outcomes.²⁵³ This raises the obvious question: what is an adjudicator to do when confronted with evidence of multiple purposes on the part of a host state?

In some legal settings, it has been argued that so long as protectionist purpose is one of the motives for the enactment of the measure and its role is not ancillary and insignificant, this should suffice to strike down the measure. Danusso and Denton, for instance, have suggested that this strict approach should apply to the European Court of Justice when reviewing tax measures under Article 95 of the EEC Treaty.²⁵⁴ There are features unique to the project of

²⁵⁰ *Id.* at paras. 391, 396.

²⁵¹ *Id.* at paras. 392, 396.

²⁵² *Village of Arlington Heights v Metropolitan*, 429 U.S. 252, 265 (1977).

²⁵³ For analysis of the manner in which divergent domestic interest groups (including import competing industry and environmental interests) will bind together to lobby for trade protection, see Michael Trebilcock & Robert Howse, *Trade Liberalization and Regulatory Diversity: Reconciling Competitive Markets with Competitive Politics*, 6(5) EUR. J. LAW & ECON. 5, 6-7 (1998).

²⁵⁴ M. Danusso & R. Denton, *Does the European Court of Justice Look for a Protectionist Motive under Article 95?*, 1 LEGAL ISSUES IN EUR. INTEGRATION 67, 87 (1990). For a similar approach in the general context of U.S. constitutional law, see Paul Brest, *Palmer v Thompson: An Approach to the Problem of Unconstitutional Legislative Motive*, 1971 SUP.

European integration that might support this view, although Danusso and Denton do not explicitly articulate them. Miguel Maduro, for instance, has argued that the tendency towards proportionality review under Article 30 of the EC Treaty has been carefully chosen as part of a broader normative project. Maduro has presented the increased judicial activism of the European Court of Justice in applying this test as reflecting a normative goal of positive integration or “market building” in the European context.²⁵⁵ The Court’s activism is in turn a response to the failure of the legislative arms of the European political process to implement this broader goal.²⁵⁶ Viewed through this lens, one could imagine a similar case to support a strict test for invalidation (such as that put forward by Danusso and Denton) - where protectionism is one of a number of motivations – advanced to support the normative project of European integration.

There is, however, little justification for such a strict approach when it comes to the heterogeneous network of investment treaties. The key institutional imperatives that have traction in the European context are absent in this setting. The dominant strategic goal is instead for *greater* levels of freedom for states when regulating in their domestic sphere. Another important factor to consider when coming to a view on how to approach mixed purposes is the remoteness of the adjudicator from the subject of her inquiry. Unlike, say, constitutional courts in a domestic setting, investor-state arbitral tribunals have no natural familiarity with the political and legal traditions in the host state. This is an important dimension when it comes to adjudicating on multiple purposes driving a given measure. Those

CT. REV. 95, 119 (1971) (“It should suffice to demonstrate that illicit motivation played a non-trivial part in the decisionmaking process, so that it might have affected the outcome.”). *But cf.* Regan, *supra* note [], at 1884 (arguing that when it comes to the dormant Commerce Clause of the U.S. constitution, a law should only count as having been adopted with protectionist purpose “when the contribution of the protectionist forces was a but-for cause of the decision”).

²⁵⁵ MIGUEL MADURO, WE THE COURT: THE ECJ AND THE EUROPEAN ECONOMIC CONSTITUTION - A CRITICAL READING OF ARTICLE 30 OF THE EC TREATY 88 (1998).

²⁵⁶ *Id.* at 98.

multiple purposes will often reflect an inevitable dimension of liberal democratic politics which is the attempt by governments to justify policies by appealing to diverse constituencies. Without deep familiarity in the political tradition and system giving rise to the law or regulation, “inferences about motive may often be little more than an intuition that a ‘normal’ regulatory state would never have bothered about this or that risk, or saving this or that species, but for protectionism”.²⁵⁷

We have then an issue of considerable delicacy for which there is no easy answer. Taking these factors into consideration, I put forward the following broad test: An adjudicator should only invalidate a measure where there is clear and convincing proof across the entire suite of evidential indicators that protectionism was the state’s *dominant* purpose. The most important element of this test is that it does not prioritize any evidential source. In other words, it would be impermissible for the adjudicator to seize on individual protectionist speeches by legislators as a smoking gun proving a dominant (protectionist) purpose. It would be equally insensible for an adjudicator to prioritize evidence of voting patterns as conclusive indicators of which particular interest group were successful in achieving a given regulatory outcome. All evidential sources surveyed above must be considered in the assessment of the state’s dominant purpose.

To date, there have been few cases where arbitral tribunals have been confronted with the problem of multiple purposes. The sole conceivable award is *ADM v Mexico* where the Tribunal’s method is in line with this approach. In *ADM*, the Tribunal ruled:

Perhaps the Tax could have been enacted for both purposes, i.e., protection of the domestic sugar industry in Mexico, as well as inducing the U.S. Government to comply with its NAFTA obligations. But

²⁵⁷ Howse, *supra* note [], at 147.

the evidence before us, as well as the Respondent's statements in the instant case, indicate that protection of the Mexican sugar industry was the true motive and intent underlying the enactment of the tax. For a successful defense of inducement, even coupled with protection, the Tribunal would expect to see substantial evidence supporting inducement at the time of the enactment of the Tax. But inducement when the Tax was enacted is not in evidence here.²⁵⁸

The *ADM* Tribunal examines the *totality* of the evidential record in coming to a view on which of the differing motives – protection and inducement – is the dominant cause of the tax. This is a principled and in my view, sufficiently tractable mechanism of dealing with the problem of mixed purposes. In *ADM* we have already seen that various evidential indicators – including legislative history, text structure and effect as well as select domestic court rulings – *all* point to protectionism as the controlling impulse for the Mexican tax. The *ADM* Tribunal's method once again buttresses the critical point underlying an inquiry into state purpose. An adjudicator's fundamental task is to review all possible forms of evidence relevant to a claim of state purpose without prioritizing any one proxy in their analytical structure.

V. Conclusion

[To be completed.]

²⁵⁸ *ADM v Mexico*, *supra* note [], at para 150.