THE STANDARD OF REVIEW AND THE ROLES OF ICSID ARBITRAL TRIBUNALS IN INVESTOR-STATE DISPUTE SETTLEMENT

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ABSTRACT

The International Centre for Settlement of Investment Dispute (ICSID) is one of the important dispute settle mechanisms in the world, which often deals with the exercise of public authority by the host States. Similar to any international institution, the legitimacy and the cooperation of its participants are critical to ICSID's operations. Some friction comes from the factor that the public law characteristics of ICSID investment arbitrations do not comport well with some of the procedures originating from the arbitrations' private law traditions, such as the standard of review adopted by investment arbitration tribunals when reviewing state's exercise of public power. The standard of review is important for ICSID arbitration, since the investors have been increasingly seeking recourse in the context of ICSID arbitration against the public policies of the host states. The degree of rigidness a tribunal adopts when reviewing these cases directly affects the ability of the host states to implement their public policies and to determine whether these types of policies could be adopted in similar situations in the future. In addition, the standard of review the arbitrator adopts will determine the role of ICSID arbitrators vis-à-vis *host states' governments with regard to these public policies.*

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The notion "standard of review" represents the degree of intensity or of thoroughness of review during the judicial process and addresses the limitations of judicial power. In the context of international law, the standard of review concerns the degree of deference that an international adjudicator should grant to national decision makers. The concept can allocate decision-making power, help utilize the limited resources effectively, and maintain legitimacy in adjudicating policy choices and conflicting values by determining the proper roles of the adjudicator. Nowadays, under the call for abandoning BITs among some advanced countries, it is essential to emphasize the recognition of the appropriate roles of the arbitrators and the proper functions of the BITs by shaping the power of the standard of review. This article reviews the recent development of the standard of review in ICSID arbitrations and argues that the concept should be further developed by the arbitral tribunals.

KEYWORDS: *International Centre for Settlement of Investment Dispute, ICSID, the standard of review, bilateral investment treaty, BIT, non-precluded measures.*

I. INTRODUCTION

By the end of the year 2011, there have been at least 450 known treaty-based investor-state dispute settlement (ISDS) cases filed under international investment agreements (IIAs).[1] The majority of them, now numbering 279 cases, were filed with the International Centre for the Settlement of Investment Dispute (ICSID).[2] The importance of ICSID arbitral tribunals became apparent. Notably, the subject matter ICSID arbitral tribunals deals with includes the exercise of public authority by the host States. Accordingly, in this regard, the investment arbitrations have been characterized as an administrative review mechanism.[3] William W. Burke-White and Andreas von Staden further argue that at least some investment arbitrations may even play a "quasi-constitutional function" with the adjudication that determines the fundamental rights of citizens within the state.[4] Thus, the roles of ICSID arbitral tribunals are extremely important for anyone interested in the regulatory space of the modern state. In 2011, the trend became even more apparent, as cases against governmental measures of the nature of important public policies are continually initiated, such as the cases against Australia's tobacco control legislation and the one against Germany's nuclear phase-out program.[5]

With the development of the public law aspects in the investment arbitration, controversies inevitably occurred. Some high profile cases have added to the tension. Similar to any international institution, the legitimacy and the cooperation of its participants are critical to ICSID's operations. Some frictions come from the factor that the public law characteristics of ICSID investment arbitrations do not comport well with some of the procedures originating from their private law tradition. The standard of review adopted by the investment arbitration tribunals when reviewing a state's exercise of public power is one of them. Accordingly, it is worthwhile to pay attention to the ways the states and ICSID arbitral tribunals have been adjusting to the issue of the standard of review and to the resulted regulatory space.

This paper proceeds as follows: First, the concept of the standard of review will be discussed. In addition, the functions of the standard of review will be examined. Second, the paper will discuss the changing

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[1] *See* UNCTAD, Latest Developments in Investment–State Disputes Settlement, IIA ISSUES NOTE, No. 1, at 1 (2012), *available at* http://unctad.org/en/PublicationsLibrary/webdiaeia2012d10_en.pdf (last visited May 17, 2012)

[2] *Id.* at 1.

[3] Gus van Harten & Martin Loughlin, *Investment Treaty Arbitration as a Species of Global Administrative Law*, 17 (1) EUR. J. INT'L L. 121, 145-46 (2006).

[4] William W. Burke-White & Andreas von Staden, *Private Litigation in a Public Law Sphere: The Standard of Review in Investor-State Arbitrations*, 35 YALE J. INT'L L. 283, 289 (2010).

[5] UNCTAD, *supra* note 1, at 1.

trends in the role of arbitrators in light of bilateral investment treaties (BIT). Third, the paper will examine recent arbitral decisions regarding the standard of review from the perspectives of the non-precluded measures (NPM) clauses and the State's right to regulate.

II. THE STANDARD OF REVIEW

A. The Definition of the Standard of Review

The notion "standard of review" represents the degree of intensity or of thoroughness of review during the judicial process.[6] It could be defined as "the level of intensity of the scrutiny that the reviewing body will exert over the decision or regulation being reviewed."[7] The concept of the standard of review addresses the limitations of judicial power. This restraint reflects a decision to grant certain degree of discretion to decision makers other than judges. When it is mandated by legal texts, this decision may be made by the legislature or treaty founders. When such clear mandate does not exist, judges may have to make the decision themselves.

In domestic legal systems, the mechanism for the standard of review usually ensures the separation of powers through the degree of deference that a judge grants to legislators and regulators.[8] It may also concern the relationship between an appellate court and a lower court.[9] However, in the domestic context, the issue of judicial standard of review is not limited to allocation of power between governmental institutions. For example, in the area of corporate governance, there could be a deferential standard of review by which courts may abstain from second-guessing the corporate directors' business decisions.[10] The overarching rationale of the judicial

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[6] SHARIF BHUIYAN, NATIONAL LAW IN WTO LAW: EFFECTIVENESS AND GOOD GOVERNANCE IN THE WORLD TRADING SYSTEM 148 (2007).

[7] CATHERINE BUTTON, THE POWER TO PROTECT: TRADE, HEALTH AND UNCERTAINTY IN THE WTO 164 (2004). *See also* LUKASZ GRUSZCZYNSKI, REGULATING HEALTH AND ENVIRONMENTAL RISKS UNDER WTO LAW: A CRITICAL ANALYSIS OF THE SPS AGREEMENT 50 (2010).

[8] BHUIYAN, *supra* note 6, at 148; Claus-Dieter Ehlermann & Nicolas Lockhart, *Standard of Review in WTO Law*, 7(3) J. INT'L ECON. L. 491, 493 (2004) (noting that in the context of any legal system, the standard of review defines the parameters within which judges, and correspondingly, legislators and regulators should work, which is one of the mechanisms that guarantees the separation of powers). *See also* HARRY T. EDWARDS & LINDA A. ELLIOTT, FEDERAL COURTS STANDARDS OF REVIEW: APPELLATE COURT REVIEW OF DISTRICT COURT DECISIONS AND AGENCY ACTIONS, at v (2007) (noting that standards of review "are critically important in determining the parameters of appellate review and in allocating authority between trial courts and agencies, on the one hand, and the appellate bench, on the other" in the context of the United States).

[9] Andrew T. Guzman, *Determining the Appropriate Standard of Review in WTO Disputes*, 42 CORNELL INT'L L. J. 45, 45 (2009); EDWARDS & ELLIOTT, *supra* note 8, at v.

[10] *See generally* Stephen M. Bainbridge, *The Business Judgment Rule as Abstention Doctrine*, 57(1) VAND. L. REV. 83 (2004) (exploring the abstention feature for the court of the business judgment rule, which enables efficient decision-making systems and processes in U.S. corporations).

standard of review for any given matter seems to rest on determining the most appropriate balance of power between decision makers.[11] However, it should be emphasized that in some types of cases the decision-making power is undisputedly allocated to the judges. Therefore no deference is due with regard to any decisions made by parties to the dispute. For example, in pure contractual disputes, even when one party is a government institution, there is no deference to determinations made by government agencies. Here, the concept of standard of review is not important in their settlement. It is thus critical to determine, at the outset, whether the standard of review is an issue that the adjudicating bodies should take into account in its decision-making process.

In the context of international law, such as the World Trade Organization (WTO) dispute settlement regime or international investment arbitration, the standard of review concerns the degree of deference that an international adjudicator should grant to national decision makers, including national legislators, regulators or judiciaries.[12] However, one should take special caution when comparing the standard of review in international dispute settlements to those of domestic tribunals, because the functions which the concept is designed to achieve may differ according to its context.[13]

With regard to ICSID arbitration, the standard of review is similarly important. As stipulated earlier, the investors have been increasingly seeking recourse in the context of ICSID arbitration against the public policies of the host states, including measures relating to cigarette plain packaging measures and nuclear phase-out. As will be further discussed below, a government's emergency measures in the middle of a financial and monetary crisis were also challenged in the forum. The degree of rigidness an arbitrator adopts when reviewing these measures directly affects the ability of the host states to implement its public policies and to determine whether these types of policies could be adopted in similar situations in the future.

In addition, the standard of review the arbitrator adopts will determine the role of ICSID arbitrators *vis-à-vis* the host states' governments with regard to these public policies. If the arbitrator adopts *de novo* review, for example, the arbitrator effectively adopts the role of the ultimate *de facto* decision maker of the disputed policy by disregarding the views and

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[11] *See* Martha S. Davis, *A Basic Guide to Standards of Judicial Review*, 33 S. D. L. REV. 469, 469 (1988) (noting that the standard of review "defines the relationship and power shared by decision makers").

[12] *See* Ehlermann & Lockhart, *supra* note 8, at 493; MATTHIAS OESCH, STANDARDS OF REVIEW IN WTO DISPUTE RESOLUTION 13 (2003); BHUIYAN, *supra* note 6, at 148.

[13] *See* GERNOT BIEHLER, PROCEDURES IN INTERNATIONAL LAW 39 (2008) ("[C]ertain procedural rules may fulfill an entirely different function in international law than they do in the national legal context").

determinations of the host governments. A more deferential standard of review, however, could render the role of the tribunal into one as a reviewer of the policies. In this case, the tribunal could adopt a benchmark against which the policies are reviewed. The tribunal would not substitute its own judgment for that of the national authorities. The standard of review thus decides the role of the ICSID arbitrators.

It should be noted, however, that a proper standard of review would not render an arbitration procedure useless by deferring to a host state. An arbitral tribunal with a role of a reviewer does not mean that the tribunal would simply accept all allegations of the host state.[14] On the contrary, even when applying a deferential standard of review, the tribunal has to review whether the measure of the host state meets the benchmark established by the adopted standard of review. For example, the tribunal has to make sure whether the measure was unreasonable or arbitrary. If the tribunal finds that the host state's measure does not meet such established benchmark, the tribunal would still determine that the relevant obligations are violated. Accordingly, this paper argues that a deferential standard of review would still preserve ICSID arbitrations' important functions.

B. The Functions of the Standard of Review

1. Allocation of Decision-making Power. — The proper allocation of power is one of the key rationales behind the standard of review within any judicial system.[15] The standard of the judicial review determines the allocation of power between institutional organs or parties.[16] The purpose of the allocation is to allow the most appropriate decision maker to make the decisions. The judicial organ may not be the ideal actor to make final determinations regarding every imaginable issue that comes before it. For example, democracy and accountability may require a certain measure of judicial restraint. Daniel Lovric suggests that the deference connected to the separation of powers and the democratic mandate of legislature is common when courts deal with challenges to legislation, whether in an international or domestic context.[17] The underlying reasons for judicial deference reflect courts' need to present themselves as politically neutral and judicial comities that recognize the different roles other decision makers play.[18] Accordingly, the standard of review is an important mechanism for guaranteeing separation of powers within and between legal

[14] The author would like to thank the comment of one senior advisor of the Contemporary Asia Arbitration Journal regarding this point.
[15] *See* OESCH, *supra* note 12, at 23.
[16] *Id.* at 24.
[17] DANIEL LOVRIC, DEFERENCE TO THE LEGISLATURE IN WTO CHALLENGES TO LEGISLATION 59 (2010).
[18] *Id.* at 60.

systems.[19] It achieves this function through variations in the nature and intensity of a judicial organ's review of the legal validity of legislative, administrative, or other types of decisions.[20]

2. Efficient Utilization of Limited Resources. — Practical considerations provide important rationales for the formation of the standard of review.[21] In some situations, there are not enough time, resources, or even qualifications for judges to conduct all of the factual determinations necessary in dispute settlement procedures. It is particularly apparent in the review of fact-extensive determinations and judgments involving complex scientific basis. This applies for ICSID tribunals, as the settlement of ICSID cases relies, among other factors, on the establishment of facts. National authorities may also enjoy institutional advantages in determining factual aspects closer to its location.[22] Accordingly, different standards of review which allow for the most efficient decision makers to make the decision might help ICSID tribunals utilize their limited resources while still reaching appropriate outcomes.

3. Maintaining Legitimacy in Adjudicating Policy Choices and Conflicting Values by Determining the Proper Roles of the Adjudicators. — In ICSID, the issue of the standard of review becomes acute in situations where the adjudicating bodies have to deal with competing values between investment and non-investment issues such as financial crisis, environment, and health. In such situations, the legitimacy of the adjudicating bodies is at risk.[23] Also, ICSID tribunals may be considered democratically deficient and, as a result, cannot be held fully accountable to the people who are subject to their rulings. Christopher Arup argues that international tribunals, such as the WTO adjudicating bodies, "need to be particularly aware of the need for deference,"[24] since they do not have a popular mandate. As a result, international courts have to be careful "not to act beyond their delegation."[25] In the course of adjudicating national laws and policies while respecting a range of diverse values and interests other than trade, international adjudicators should offer some

[19] BHUIYAN, *supra* note 6.
[20] *Id.*
[21] *Id.* at 23.
[22] For the situation in the WTO dispute settlement, *id.* at 57.
[23] For the need of legitimacy under conflicting interests in the context of the WTO, *see* Robert Howse, *Adjudicative Legitimacy and Treaty Interpretation in International Trade Law: The Early Years of WTO Jurisprudence*, *in* THE EU, THE WTO AND THE NAFTA: TOWARDS A COMMON LAW OF INTERNATIONAL TRADE 35, 38-39 (Joseph Weiler ed., 2000).
[24] Christopher Arup, *The State of Play of Dispute Settlement "Law" at the World Trade Organization*, 37(5) J. WORLD TRADE 897, 915 (2003).
[25] LOVRIC, *supra* note 17, at 61.

measure of deference to national government decisions.[26] The standard of review could contribute to the system of checks and balances in both domestic and international governance, which would help to ensure the accountability of decision makers.[27] It could also allocate decision-making authority and resources among different branches and levels of governance in an efficient fashion.[28] Accordingly, the standard of review is a key tool for achieving legitimacy in the international dispute settlement system because, by determining the most suitable decision maker, the appropriate standard can help achieve the proper balance between goals pursued by the involved treaty and other conflicting interests.

In addition, scholars have argued that whether the national authority's decision process is a democratic one is an important factor for determining the appropriate standard of review. In the context of WTO, Robert Howse and Kalypso Nicolaidis argue that WTO panels cannot easily substitute themselves for "domestic democratic processes which have often painstakingly shaped fundamental tradeoffs between economic, social, political cost-benefit considerations and values"[29] often demanded in policy areas other than trade. Accordingly, the appropriate standard of review is much needed here. One caveat for this argument, however, is that the WTO does not seem to value Member decisions derived from democratic processes any higher than those decisions derived from an autocratic one.[30] It is nonetheless correct to argue that for difficult questions of competing values, a domestic process has more legitimacy when making hard choices. This concern may equally apply in some international investment arbitrations, when the subject matters of the arbitrations deal with public law issues involving tradeoffs between important conflicting values. On the one hand, judicial restraint, which can be achieved by a deferential standard of review, may be needed for such sensitive cases. Indeed, an overly intrusive review standard would undermine the support of the system and reduce the legitimacy of the international institution. On the other hand, however, judicial restraint should not undermine the balance of the rights and obligations of the parties to the agreement in dispute, which is often embedded in the text and structure of the agreement. It is thus critical for a tribunal to identify when and how to apply a deferential standard of

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[26] In the context of the WTO, *see* JOHN HOWARD JACKSON, THE WORLD TRADE ORGANIZATION: CONSTITUTION AND JURISPRUDENCE 90 (1998). *But see* Howse, *supra* note 23, at 62 (criticizing that this view lacks guidance as to how far restraint or deference should go).
[27] Ehlermann & Lockhart, *supra* note 8, at 493. *See also* BHUIYAN, *supra* note 6, at 149.
[28] *Id.*
[29] Robert Howse & Kalypso Nicolaidis, *Legitimacy through "Higher Law"? Why Constitutionalizing the WTO Is a Step Too Far*, *in* THE ROLE OF THE JUDGE IN INTERNATIONAL TRADE REGULATION: EXPERIENCE AND LESSONS FOR THE WTO 307, 332 (Thomas Cottier et al. eds., 2003).
[30] LOVRIC, *supra* note 17, at 85-86.

review.[31] These issues are still being developed. This paper does not attempt to answer these questions. Instead, this paper will review the trend of a more deferential standard of review represented in recent BITs and ICSID cases. As will be demonstrated in the next section, changing substantive provisions in BITs represent the evolving attitudes of states.

III. CHANGING BITS PROVISIONS

States' attitudes towards foreign direct investments (FDI) have changed in recent years. Liberalization without conditions seems no longer the only prescription for development. The importance of government is once again recognized by states. Jose E. Alvarez calls the trend in the international investment regime "the return of the State."[32] The standard of review is one of the most important vehicles through which the states are making the adjustment of their roles in the international investment regime.

As Alvarez has described, unlike the investor-protective U.S. Model BIT of 1984, recent BITs, such as the U.S. Model BIT of 2004, have reserved greater maneuvering room for the host states.[33] With regard to the standard of review, the new public management (NPM) provisions, and their provision providing general exceptions, reflect this trend. In the U.S. Model BIT of 1984, Article X provides that: "This Treaty shall not preclude the application by either Party of measures necessary in its jurisdiction for the maintenance of public order, the fulfillment of its obligations with respect to the maintenance or restoration of international peace or security, or the protection of its own essential security interests."

This clause provides only limited exceptions and provides little support for a standard of review with the regulatory space of states in mind. The recognized exceptions a state could invoke to justify deviation from the treaty obligations are limited to the maintenance of public order, the fulfillment of its obligations with respect to the maintenance or restoration of international peace or security, or the protection of its own essential security interests. This indicates the strong will of states at the time to enhance the functions of BITs and the protection of investors. For the issues that are in need of a more deferential standard of review as stipulated in the previous section, these limited exceptions provide little, if any, textual support for a deferential standard of review. It is safe to assume that, generally, the fulfillment of a state's obligations with respect to the maintenance or restoration of international peace or security is not related to the issues concerning the regulatory space that is in need of a deferential

[31] The author would like to thank one senior advisor of Contemporary Asia Arbitration Journal for pointing this out.
[32] J. E. Alvarez, *The Return of the State*, 20 MINN. J. INT'L L. 223, 253-54 (2011).
[33] *Id.* at 235.

standard of review. Traditionally, essential security interests as well as the maintenance of public order are not related to a state's regulatory need, either. Perhaps more importantly, the wording of the NPM provision provides no requirement on the part of the adjudicator to apply a deferential standard of review. The provision stipulates that a measure with permissible purposes has to be one that is "necessary." Whether it is necessary seems to depend on the consideration of the adjudicator, instead of that of the national authority

On the contrary, the U.S. Model BIT of 2004 provides more exceptions and prescribes clear instructions on the issue of the standard of review. On essential security, Section 2 of the Article 18 provides that "Nothing in this Treaty shall be construed . . . to preclude a Party from applying measures *that it considers necessary* for the fulfillment of its obligations with respect to the maintenance or restoration of international peace or security, or the protection of its own essential security interests." (emphasis added)

The text of this provision is similar to the security exception provided in Article XXI of the General Agreement on Tariffs and Trade 1994 (GATT 1994). Article XXI of the GATT 1994 provides that:

> Nothing in this Agreement shall be construed . . .
>
> (*b*) to prevent any contracting party from taking any action which *it considers necessary* for the protection of its essential security interests
>
> (i) relating to fissionable materials or the materials from which they are derived;
>
> (ii) relating to the traffic in arms, ammunition and implements of war and to such traffic in other goods and materials as is carried on directly or indirectly for the purpose of supplying a military establishment;
>
> (iii) taken in time of war or other emergency in international relations; or . . . (emphasis added).

As the text shows, a proper interpretation of the text of the Article XXI of GATT 1994 would result in the conclusion that this provision grants a Member "exclusive authority to determine what is in its essential security interest and to deviate from WTO obligations to protect those interests."[34] This result is required as the Members, through the relevant treaty provisions, have explicitly retained "exclusive competence" to determine their own interests for national security.[35]

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[34] Artuhr E. Appleton & Veijo Heiskanen, *Decision-Making in Dispute Settlement: Bridging the Perception Gap*, *in* TEN YEARS OF WTO DISPUTE SETTLEMENT: COMMENTARY AND ANALYSIS FROM THE TRADE AND CUSTOMS LAW COMMITTEE OF THE INTERNATIONAL BAR ASSOCIATION 73, 76 (Dan Horovitz et al. eds., 2007).

[35] *Id.* at 78.

By adopting the model of the security exception provided in GATT 1994, Article 18 of the U.S. Model BIT of 2004 states clearly that the essential security exception in the U.S. Model BIT of 2004 should be determined by states, not the arbitral tribunals. Arbitrators have to accord considerable deference, at the very least, when reviewing claims invoking such exceptions. Whether a measure is necessary for the fulfillment of the state's obligations with respect to the maintenance or restoration of international peace or security, or the protection of its own essential security interests is now determined by the state. The arbitrator is not allowed to substitute his or her own judgment for that of the national government.

With regard to environment protection measures, the deference is significantly less. Section 2 of Article 12 of the US Model BIT of 2004 provides that: "Nothing in this Treaty shall be construed to prevent a Party from adopting, maintaining, or enforcing any measure otherwise consistent with this Treaty *that it considers appropriate* to ensure that investment activity in its territory is undertaken in a manner sensitive to environmental concerns." (emphasis added)

Here, the deference is less as the measure still has to be consistent with the obligations contained in the BIT elsewhere. However, the existence of Paragraph 2 of Article 12 indicates awareness of the issue and will support a deferential attitude of an arbitrator who is aware of the governing need of a host state. It should also be noted that the substantive provisions stated above are kept the same in the U.S. Model BIT of 2012.

An even clearer example is the NPM clause of the United States – Peru Trade Promotion Agreement, which provides:

> Nothing in this Agreement shall be construed: . . . to preclude a Party from applying measures that it considers necessary for the fulfillment of its obligations with respect to the maintenance or restoration of international peace or security, or the protection of its own essential security interests. (Original Footnote 2)
>
> Original Footnote 2: For greater certainty, if a Party invokes Article 22.2 in an arbitral proceeding initiated under Chapter Ten (Investment) or Chapter Twenty-One (Dispute Settlement), the tribunal or panel hearing the matter shall find that the exception applies.

The footnote to the provision makes it clear that once the essential security exception is invoked by a host state, the tribunal reviewing the

claims shall find any violation of the obligations provided in the Investment Chapter is justified. The state action is thus in fact not reviewable.[36]

Exception clauses are the most important aspects of the BITs that reflect the conflicting values in investment disputes between the rights of the investors and the interests of the host states. The trend discussed above has shown efforts of the states in ensuring the roles of the arbitral tribunals to be a reviewer instead of the primary decision maker when it comes to the identification of essential interests of a state and whether measures addressing these concerns are necessary or not. It should be noted, however, that the new type of exception clause is still not common among BITs. More importantly, the provisions adopted are limited to essential interests instead of areas more related to regulatory concerns. Still, in light of the controversy around the nature of the exception clauses in some arbitration proceedings to be discussed below, it is possible for this new trend to continue.

VI. THE ICSID ARBITRAL DECISIONS AND THE ARBITRATORS' ROLES

The subject matter that involves public law characteristics in international investment arbitrations is complicated and sensitive. Traditional intrusive review standards originating from the commercial arbitration make the arbitrators' jobs harder. It is no wonder ICSID arbitral tribunals are trying to reassess their roles when reviewing regulatory decisions of the host states.

A. NPM Clauses

The changing trend of the role of ICSID arbitral tribunals can be found in their adjudication of NPM clauses. Traditionally the clause has been construed narrowly.[37] As Burke-White and von Staden have analyzed,[38] in *CMS Gas Transmission Company v. The Argentine Republic*,[39] *Enron v. The Argentine Republic*,[40] and *Sempra v. The Argentine Republic*,[41] the tribunals all applied a strict test regarding the invocation of the NPM clause by the host state, Argentina. Article XI of the Treaty between United States

[36] *See* Alvarez, *supra* note 32, at 235.
[37] *See* Burke-White & von Staden, *supra* note 4, at 298.
[38] *Id.* at 297-98.
[39] CMS Gas Transmission Company v. The Argentine Republic, ICSID Case No. ARB/01/8, Award (May 12, 2005) [hereinafter CMS].
[40] Enron Corporation Ponderosa Assets, L.P. v. The Argentine Republic, ICSID Case No. ARB/01/3, Award (May 22, 2007) [hereinafter Enron].
[41] Sempra Energy International v. The Argentine Republic, ICSID Case No. ARB/02/16, Award (Sept. 28, 2007) [hereinafter Sempra].

of America and the Argentine Republic Concerning the Reciprocal Encouragement and Protection of Investment [hereinafter Argentina – U.S. BIT] reads, "This Treaty shall not preclude the application by either Party of measures necessary for the maintenance of public order, the fulfillment of its obligations with respect to the maintenance or restoration of international peace or security, or the Protection of its own essential security interests."

In applying the NPM clause in the U.S. – Argentina BIT, these tribunals relied on the requirements of the necessity defense of article 25(1)(a) of the Draft Articles on the Responsibility of States for Internationally Wrongful Acts, which provides that the necessity defense requires that the actions adopted by the states invoking this defense have to be "the only way for the State to safeguard an essential interest against a grave and imminent peril." These tribunals held that, since there are always other ways for a government to deal with a financial and economic crisis, the measure adopted by Argentine government is not the only way available to address the problem. Accordingly, Argentina cannot invoke the NPM clause to justify its violations of the BIT. The effectiveness, the cost and the difficulty of other lawful choices are not considered by the three tribunals. The interpretation adopted by these tribunals affect the standard of review of these cases. Here, the arbitrators assumed the role of policy makers themselves relating to the necessity of the adopted measures by disregarding the Argentinean government's perception of the crisis.

Later tribunals took a different position. *LG&E v. The Argentine Republic*[42] tribunal was the first to adopt a legal test different from the earlier strict "only means available" test.[43] In *LG&E*, the tribunal recognized the grave threat faced by Argentina during the crisis and recognized that even though there may be other ways to draft the economic recovery plan, the response of the host state was necessary,[44] which provides a larger space for the host state in choosing its regulatory measures in response to a crisis. In *Continental Casualty v. The Argentine Republic*,[45] the tribunal explicitly adopted the WTO's least restrictive alternative test when dealing with exceptions provided by GATT jurisprudence of *Korea-Beef, Brazil-Retreaded Tyres*, and *U.S.-Gambling*. The *Continental Casualty* tribunals found that in invoking the NPM clause, the tribunal must find a legitimate aim and no "reasonably available alternatives" more compliant with the host state's obligations "while

[42] LG&E Energy Corp. et al. v. The Argentine Republic, ICSID Case No. ARB/02/1, Decision on Liability (Oct. 3, 2006) [hereinafter LG&E].
[43] Burke-White & von Staden, *supra* note 4, at 324.
[44] LG&E, *supra* note 42, at ¶ 257.
[45] Continental Casualty Co. v. The Argentine Republic, ICSID Case No. ARB/03/9, Award (Sept. 5, 2008) [hereinafter Continental Casualty].

providing an equivalent contribution to the achievement of the objective pursued."[46] The *Continental Casualty* tribunal explicitly noted that in reviewing the NPM clause, a "significant margin of appreciation for the State applying" the measures must be accorded.[47] By noting "a time of grave crisis is not the time for nice judgments, particularly when examined by others with the disadvantage of hindsight,"[48] the tribunal assumed the role of a reviewer that accorded a margin of error for the host states. The *Continental Casualty* tribunal concluded that the measures adopted by Argentina were "sufficient in their design to address the crisis and were applied in a reasonable and proportionate way at the end of 2001-2002." This statement further implies that the standard of review applied by the tribunal is a relatively deferential one.

The difference of the *Continental Casualty* tribunal in terms of the standard of review is apparent. In the earlier decisions, the earlier tribunals in effect adopted a *de novo* review standard, which represents the role of the tribunals that decided whether the measure was necessary all by themselves in hindsight. How the measure was adopted was of no significance in their decision. On the contrary, by explicitly invoking the margin of appreciation of the host states, the *Continental Casualty* tribunal recognizes that it is not appropriate for it to assume the role of the ultimate decision maker in this case. By adopting a more deferential standard of review, the *Continental Casualty* tribunal thus stepped in the shoes of the host state when the crisis was unfolding. The tribunal adopts a benchmark of sufficiency, reasonableness and proportion. This is the quality the tribunal asks for in the disputed measure as a reviewer. This standard allows the host states a certain flexibility and regulatory space in the public sphere.

The deferential standard of review adopted in *Continental Casualty*, however, is not common. Most ICSID tribunals did not elaborate on their standards of review explicitly, and did not adopt a deferential review.[49] A consensus has not formed in this area. Some annulment decisions that point to a more deferential attitude when reviewing NPM clauses are noteworthy. The annulment decision in *CMS* and *Sempra* opined that it is incorrect to equate the treaty's NPM clause, to the customary defense of necessity. The *Sempra* annulment decision even changed the former practice[50] and held that the original tribunal manifestly exceeded its powers in applying the customary defense of necessity instead of the NPM clause of the BIT, and

[46] *Id.* at ¶ 198 (citing Brazil-Retreaded Tyres, ¶ 156).
[47] *Id.* at ¶ 181.
[48] *Id.*
[49] *See* Burke-White & von Staden, *supra* note 4, at 327-28.
[50] *See* UNCTAD, Latest Developments in Investment – State Disputes Settlement, IIA ISSUES NOTE, No. 1, at 6 (2011), http://unctad.org/en/docs/webdiaeia20113_en.pdf (last visited May 26, 2012).

annulled the award even though it was basically an instance of erroneous application of the law.[51] The implication of the decision of the *ad hoc* Committee in *Sempra* is that the "no other means available" test could be considered too strict.

The ICSID annulment committee in *Enron* similarly annulled the tribunal's award on the ground of a manifest excess of powers and failure to state reasons regarding the application of the NPM. The *Enron* annulment committee annulled the *Enron* award on different grounds than the *Sempra* annulment committee. The *Enron* annulment committee did not find that the reliance on the customary necessity defense was wrong. Instead, the committee found that the original tribunal based its finding that there were other measures that could have been adopted by Argentina entirely on the statement of an economist. The committee found that this approach did not fully address the question of whether the "only way" requirement was met.[52] The committee did not prescribe a specific reading of the requirement, but it did elaborate on other possible interpretations that the original tribunal did not address, such as the least restrictive alternatives[53] and the relative effectiveness of alternative measures.[54] More relevant to the topic of this article, the committee provided the issue that a tribunal should ask:

> A third question that is not specifically addressed by the Tribunal is who makes the decision whether there is a relevant alternative, and in accordance with what test? Does the Tribunal determine this at the date of its award, when the Tribunal may have the benefit of knowledge and hindsight that was not available to the State at the time that it adopted the measure in question? Or does the Tribunal determine whether, on the basis of information reasonably available at the time that the measure was adopted, a reasonable and appropriately qualified decision maker would have concluded that there was a relevant alternative open to the State? Or does customary international law recognise that reasonable minds might differ in relation to such a question, and give a "margin of appreciation" to the State in question? In that event, the relevant question for the Tribunal might be whether it was reasonably open to the State, in the

[51] Sempra Energy International v. The Argentine Republic, ICSID Case No. ARB/02/16, Decision on the Application for Annulment of the Argentine Republic, ¶ 164 (June 29, 2010).
[52] Enron Corporation Ponderosa Assets, L.P. v. The Argentine Republic, ICSID Case No. ARB/01/3, Decision on the Application for Annulment of the Argentine Republic, ¶ 368 (July 30, 2010).
[53] *Id.* at ¶ 370.
[54] *Id.* at ¶ 371.

> circumstances as they pertained at the relevant time, to form the opinion that no relevant alternative was open.

In this paragraph, the *Enron* annulment committee succinctly provides several possible standards of review regarding the NPM clause. The effect of this paragraph is that future ICSID arbitral tribunals will have to address the issues and declare the standards of review they choose. It would be conceivably harder for future tribunals to adopt a strict review standard, as they will have to provide a reason for this choice. Furthermore, if the newer type of BIT provision regarding essential security interests is adopted, the flexibility of governmental regulatory power could be better preserved.

B. Right to Regulate

The next frontier of the changing role of the ICSID tribunals may be the right of the host States to regulate in the public interest. The right to regulate is an inherent right of the States.[55] In 2010, two tribunals have addressed the issue with respect to the fair and equitable treatment standard (FET standard).[56] They noted that there is a need to balance investors' expectations with the right of host States to regulate. In *Lemire v. Ukraine*,[57] the tribunal noted that the protection of foreign investors should be "balanced against the legitimate right of Ukraine to pass legislation and adopt measures for the protection of what as a sovereign it perceives to be its public interest."[58] The tribunal also noted that the object and purpose of the BIT "is not to protect foreign investments per se, but as an aid to the development of the domestic economy."[59] The other arbitral case — *AWG v. Argentina*[60] — even though not an ICSID case — is also important. The tribunal held that "in interpreting the meaning of fair and equitable treatment to be accorded to investors, the Tribunal must balance the legitimate and reasonable expectations of the Claimants with Argentina's right to regulate the provision of a vital public services."[61]

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[55] Chang-fa Lo, Plain Packaging and Indirect Expropriation of Trademark Rights Under BITs: Does FCTC Help Establish a Right to Regulate Tobacco Products?, at 23 (Aug. 5-6, 2011), *Addressed at* 2011 Conference on International Health and Trade: Globalization and Related Health Issues; Howard Mann, *The Right of States to Regulate and International Investment Law: Comment*, at 5 (2002), http://www.iisd.org/pdf/2003/investment_right_to_regulate.pdf (last visited May 17, 2012).

[56]. UNCTAD, Latest Developments in Investment–State Disputes Settlement, IIA ISSUES NOTE, No. 1, at 3 (2011), *available at* http://unctad.org/en/Docs/webdiaeia20113_en.pdf (last visited May 25, 2012).

[57] Joseph Charles Lemire v. Ukraine, ICSID Case No. ARB/06/18, Decision on Jurisdiction and Liability (Jan. 14, 2010) [hereinafter Lemire].

[58] *Id.* ¶ 273.

[59] *Id.*

[60] AWG v. Argentina, ICSID Case No. ARB/03/19, Decision on Liability (July 30, 2010).

[61] *Id.* ¶ 336.

Furthermore, based on the need for balancing, the *Lemire* tribunal explicitly articulated a deferential standard of review in its review of the FET standard. The tribunal clearly noted that it did not suggest that the breach occurs if the national authority "makes a decision which is different from the one the arbitrators would have made if they were the regulators."[62] The tribunal noted that "arbitrators are not superior regulators" and that "they do not substitute their judgment for that of national bodies applying national laws."[63] The tribunal held that a claim that a regulatory decision is "materially wrong" would not suffice. Instead, the proper standard should be that the State organ "acted in an arbitrary or capricious way."[64] By this statement, the *Lemire* tribunal adopted a deferential standard of review when determining whether the FET standard has been breached. In addition, the *Lemire* tribunal explicitly stipulated its proper roles as a reviewer of the disputed measure who checked whether the host state acted in an arbitrary or capricious way and thus violated the FET standard, instead of "super regulators" who would strike down the measure as long as the tribunal would have had made a different decision themselves.

In addition to the FET standard, the right to regulate may be relevant when determining issues involving indirect expropriation, especially for regulations that intend to regulate non-investment related issues. Professor Lo argues that the right to regulate could be invoked as a defense to indirect expropriation in the context of the plain packing regulation.[65] Professor Lo also suggests that the right to regulate defense is satisfied if the protected values apparently outweigh the affected economic interests and that there are strong justifications to adopt the measure at issue.[66] As noted by the *Lemire* tribunal, the purpose of BITs should not be the protection of foreign investors per se. It would be quite absurd to argue that by entering into BITs, the States forgo the right to regulate in the areas of economic development, public health or environmental protection. The question, then, is how to review the regulatory measures once a dispute arises. In light of the increasing awareness of the public law characteristics of the subject matter in international investment arbitration, it would not be surprising if arbitrators adopt a deferential standard of review in reviewing the right to regulate defense. Indeed, here, the proper role of arbitral tribunals should be as reviewers of the host state measures and should appropriately take into account the host state's right to regulate.

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[62] Lemire, *supra* note 57, ¶ 283.
[63] *Id.*
[64] *Id.*
[65] Lo, *supra* note 55, at 24.
[66] *Id.* at 25-26.

V. CONCLUSION

The changing roles of investor-state dispute arbitrators can best be illustrated by the trends of the standard of review. These trends came from both the texts of BITs and ICSID tribunal decisions. Alvarez noted that the overall trend of the returning state diminishes the value of the BITs and business groups fear that it will render a BIT negotiation "an entirely pointless exercise."[67] However, it seems that this trend is also inevitable considering the ever-expanding subject matter ICSID arbitral tribunals cover. Indeed, if the failure to recognize the appropriate role of arbitrators and the proper functions of BITs continue, the call for abandoning BITs among advanced countries may gain attraction. It is thus important for arbitrators and BIT negotiators to note the trend and consider allowing more regulatory space for the host states in certain cases.

[67] Alvarez, *supra* note 32, at 241.

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