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Fair and Equitable Treatment: Today's Contours

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I. Introduction: The Broadest and Most Prominent Standard in Investment Treaties

In 2007, the Tribunal in *PSEG v. Turkey* highlighted that the standard of fair and equitable treatment (FET) had become the prominent standard invoked before investment arbitral tribunals.[1] Ever since, the pace of this movement of FET to the centre of the investment dispute agenda has remained steady and has intensified. An empirical study to quantify the percentage volume of FET arguments in the pleadings before the International Centre for the Settlement of Investment Disputes (ICSID) tribunals would certainly point to a role of FET discourse that would not have been anticipated a decade ago.[2]

While these developments may be surprising, at first sight, it is not difficult to understand the reasons for this evolution. Firstly, bilateral investment treaties (BITs) only set forth limited number of (often seven) substantive absolute standards. Secondly, the FET rule is certainly the broadest of all of them, susceptible to cover a much wider range of activities than other rules. Accordingly, investment lawyers representing claimants naturally seek to tailor their cases and their arguments so that they will be subsumed under the FET standard.

To recognize this setting does not mean to be critical of the existence of or nature of the standard, or of its role in practice. The wide range of measures by the host state with inappropriately negative effects on the investor must be taken into account in this context. Thus, FET may be considered to be at the heart of investment arbitration because of the vastness of factual situations pertaining to host state actions affecting the rights and interests of the investor. *Noble v. Romania* has reminded us, generally, of the scope of the standard.[3] Even if a host state's measure does not fall under any particular

1. *See* PSEG Global Inc. v. Republic of Turk., ICSID Case No. ARB/02/5, Award, ¶ 238 (Jan. 19, 2007), http://italaw.com/documents/PSEGGlobal-Turkey-Award.pdf [hereinafter PSEG Award]. *See also* Saluka Invs. BV v. Czech, Partial Award, ¶ 284 (Perm. Ct. Arb. 2006) [hereinafter Saluka Partial Award], 15 ICSID Rep. 274 (2010).
2. The first tribunal to apply the standard was *Emilio Agustín Maffezini v. The Kingdom of Spain,* ICSID Case No. ARB/97/7, Award (Nov. 13, 2000) [hereinafter Maffezini Award], 5 ICSID Rep. 419 (2002).
3. Noble Ventures, Inc. v. Rom., ICSID Case No. ARB/01/11, Award, ¶ 182 (Sep. 12 2005), http://www.italaw.com/sites/default/files/case-documents/ita0565.pdf. For factual settings which do not clearly fall into one of the frequently quoted sub-categories, see, e.g., Paushok v. Gov't of Mong., Award on Jurisdiction and Liab. (UNCITRAL Arb. Trib. April 28, 2011), http://italaw.com/documents/PaushokAward.pdf [hereinafter Paushok Award] (concerning an owner of gold deprived of rights by untimely selling of gold by government); Total S.A. v. Argentine Republic, ICSID Case No. ARB/04/1, Decision on Liab. (Dec. 27, 2010), http://italaw.com/documents/TotalvArgentina_DecisionOnLiabilty.pdf [hereinafter Total Decision] (concerning the failure by government to readjust equilibrium of tariffs at the end of a state of emergency); and Alpha Projektholding GmbH v. Ukr., ICSID Case No. ARB/07/16, Award (Oct. 20, 2010), http://www.italaw.com/sites/default/files/case-documents/ita0026.pdf [hereinafter Alpha

expression of FET, this does not necessarily mean that the measure is in conformity with the standard. In other words, the standard is not amenable to all-embracing definitions that will cover all conceivable cases.

Conceptually, it is important to note that the duty to accord fair and equitable treatment extends to all subject matters. It is not the importance of an economic sector to the host state or to the investor, but the treatment of the investor by the host state which will be examined under FET clause.[4]

To decide whether or not the standard has justly found its current place in investment treaties, and in investment arbitration, is a task that is best undertaken by way of judging the results of arbitral practice in specific cases. The question to be asked is: "In view of the facts of the case, will it be appropriate to conclude that claimant was treated in fair and equitable manner?" Anecdotal experience in the classroom suggests that the answers in most cases are more uniform than may be anticipated.

As a matter of legal discourse, the key issue has been whether the understanding of the standard's nature and function and its application has matured enough to make it manageable on the operational level so that it is justified to speak of a legally distinct, manageable rule available for practical purposes of investment arbitration. The following observations will seek to address this question.

II. The Nature and Function of the FET Rule

In 2007, the Tribunal in *PSEG v. Turkey* properly characterized the nature and role of the FET rule as follows:

> The standard of fair and equitable treatment has acquired prominence in investment arbitration as a consequence of the fact that other standards traditionally provided by international law might not in the circumstances of each case be entirely appropriate. This is particularly the case when the facts of the dispute do not clearly support the claim for direct expropriation, but when there are notwithstanding events that need to be assessed under a different standard to provide redress in the event that the rights of the investor have been breached.
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> Because the role of fair and equitable treatment changes from case to case, it is sometimes not as precise as would be desirable. Yet, it clearly does allow for justice to be done in the absence of the more traditional breaches of international law standards. This role has resulted in the

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Award] (concerning government stop payments of contractual debtor and for failure of debtor to fulfill its obligations).

4. *See, e.g.,* Occidental Exploration and Prod. Co. v. Republic of Ecuador, LCIA Case No. UN 3467, Final Award, ¶ 191 (July 1, 2004), http://italaw.com/documents/Oxy-EcuadorFinalAward_001.pdf [hereinafter Occidental Final Award] (discussing application of value-added tax, not tax as such); and PSEG Award, *supra* note 1, ¶¶ 246-247 (finding that the style of negotiations may violate the FET standard).

> concept of fair and equitable treatment acquiring a standing on its own, separate and distinct from that of other standards, albeit many times closely related to them, and thus ensuring that the protection granted to the investment is fully safeguarded.[5]

In 2012, *Swisslion v. Macedonia* subscribed "to the view expressed by certain tribunals that the [FET] standard basically ensures that the foreign investor is not unjustly treated, with due regard to all surrounding circumstances, and that it is a means to guarantee justice to foreign investors." [6]

In a broad sense, acceptance of the standard is a response to the danger of the "obsolescent bargain" which may threaten an investor who was welcomed by the host state before his investment, who sunk its money into the project, but who later on finds itself subject to the upper hand of the host state. *Desert Line v. Yemen* addressed this basic issue inherent in the nature of long-term investment in the light of the circumstances of the case before it as follows:

> It would offend the most elementary notions of good faith, and insulting to the Head of State, to imagine that he offered his assurances and acceptance [of the investment] with his fingers crossed, as it were, making a reservation to the effect "that we welcome you, but will not extend to you the benefits of our BIT with your country." [7]

Similar to clauses in classical civil codes in Continental Europe, the FET standard serves to address such acts and occurrences which do not fall into the net of specific standards but nevertheless are deemed to be inconsistent with the object and purpose of the BIT, i.e., to protect and promote foreign investment and thereby to contribute to the economic goals of the host state, as often recognized in BIT preambles.

The acceptance of the standard is directly linked to the fundamental moral and legal grounding of the notion of fairness, anchored in a universally accepted sense of justice, but also in classic rules of customary law governing the protection of foreign nationals and companies. Elihu Root stated the position in a prominent article a century ago:

> There is a standard of justice, very simple, very fundamental, and of such general acceptance by all civilized countries as to form a part of the international law of the world. The condition upon which any country is entitled to measure the justice due

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5. PSEG Award, *supra* note 1, ¶¶ 238-239.
6. Swisslion DOO Skopje v. Former Yugoslav Republic of Maced., ICSID Case No. ARB/09/16, Award, ¶ 273 (July 6, 2012), http://www.italaw.com/sites/default/files/case-documents/ita1080.pdf. *See also* PSEG Award, *supra* note 1.
7. Desert Line Projects LLC v. Republic of Yemen, ICSID Case No. ARB/05/17, Award, ¶ 119 (Feb. 6, 2008), http://www.italaw.com/sites/default/files/case-documents/ita0248_0.pdf. *See also* Cont'l Cas. Co. v. Argentine Republic, ICSID Case No. ARB/03/9, Award ¶ 254 (Sept. 5, 2008), http://www.italaw.com/sites/default/files/case-documents/ita0228.pdf [hereinafter Cont'l Cas. Award] (adopting this view). FET "is aimed at assuring that the normal law-abiding conduct of the business activity by the foreign investor is not hampered without good reasons by the host government and other authorities." Cont'l Cas. Award, ¶ 254.

> from it to an alien by the justice which it accords to its own citizens is that its system of law and administration shall conform to this general standard. If any country's system of law and administration does not conform to that standard, although the people of the country may be content or compelled to live under it, no other country can be compelled to accept it as furnishing a satisfactory measure of treatment to its citizens.[8]

Often is has been assumed that the traditional capital-exporting countries in general have stood for a wide version of the standard, whereas southern countries preferred a narrow one. However, from today's perspective, this generalisation is flawed. What is well-known is that the United States has turned to a narrow approach. What has received less attention is that China, with the most BITs worldwide except for Germany, has adopted the widest possible approach, that is, an unqualified version of FET. Essentially, the United States has become concerned about the need to defend cases concerning inward investments as respondent, while China has focused on its role as outward investor and the need for fair treatment of Chinese investments abroad. In other words, the FET standard does not, at least not today, pitch northern and southern states against each other. The landscape of investment arbitration has been transformed in the past decade, and the role of FET with it.

Is it fair to expect fair and equitable treatment by a host state? To rephrase the question is helpful: "Should a state inviting foreign investment claim to have the right of unfair and inequitable treatment of the foreign investors with their capital and technology to be employed in the foreign host state?" This, of course, is a rhetorical question.

III. Methodology: Applying the Rule

As regards the methodology of applying the standard, the effort to deduce a conclusion directly from the standard, as such, has not appeared to be attractive, for understandable reasons.[9] While the facts of a case may be subject to a general sense of justice, tribunals will properly seek to articulate their reasoning with more specificity. Efforts to employ abstract reasoning with the help of broad ancillary definitions of FET (such as those

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8. Elihu Root, *The Basis of Protection to Citizens Residing Abroad*, 4 AM. J. INT'L L. 517, 521-22 (1910).
9. *But see* The Rompetrol Group NV v. Rom., ICSID Case No. ARB/06/3, Award, ¶¶ 195-197 (May 6, 2013), http://www.italaw.com/sites/default/files/case-documents/italaw1408.pdf. The Tribunal seems to agree with the list approach but then proceeds to state that it will "follow the ordinary meaning of the words used, in their context, and in the light of the object and purpose of the BIT." *Id.* ¶ 197. The Tribunal adds that "it will take into particular account the two general elements that other tribunals have found come into play in connection with claims to 'fair and equitable treatment,' namely the way in which the foreign investor or the foreign investment have been treated by the organs of the host State (whether in a regulatory context or otherwise), measured against the expectations legitimately entertained by the foreign investor in making its investment." *Id.*

found in dictionaries) may be of some argumentative value as starting points for the more concrete discussion of the case.

The preferred method has been to unfold the standard on the basis of casuistic sub-groups which will be seen as typical emanations of the standards. More and more tribunals have turned to such sub-groups and found them useful for the articulation of and application of the standard. A tribunal may focus only on one criterion relevant to its case. An increasing number of tribunals, however, have assumed the broader task to set forth a list of components which, in their entirety, may compose the full reach of the FET standard.

For the first time, the "list approach" was employed in *Tecmed v. Mexico* (*Tecmed*):

> The Arbitral Tribunal considers that this provision of the Agreement, in light of the good faith principle established by international law, requires the Contracting Parties to provide to international investments treatment that does not affect the basic expectations that were taken into account by the foreign investor to make the investment. The foreign investor expects the host State to act in a consistent manner, free from ambiguity and totally transparently in its relations with the foreign investor, so that it may know beforehand any and all rules and regulations that will govern its investments, as well as the goals of the relevant policies and administrative practices or directives, to be able to plan its investment and comply with such regulations . . . . The foreign investor also expects the host State to act consistently, i.e. without arbitrarily revoking any preexisting decisions or permits issued by the State that were relied upon by the investor to assume its commitments as well as to plan and launch its commercial and business activities. The investor also expects the State to use the legal instruments that govern the actions of the investor or the investment in conformity with the function usually assigned to such instruments, and not to deprive the investor of its investment without the required compensation. [10]

For the assessment of the present state of the law, it bears emphasis that the *Tecmed* Award has been, and remains, the award most often cited in arbitral jurisprudence, obviously with more persuasive power than other attempts to approach the standard. As we shall see, not every single word of the *Tecmed* Award has to be accepted uncritically.

Other tribunals have set forth lists similar in nature, albeit not identical.[11] A stock-taking today will record at the outset that this rise of the standard has not come about

10. Tecnicas Medioambientales Tecmed S.A. v. United Mexican States, ICSID Case No. ARB(AF)/00/2, Award, ¶ 154 (May 29, 2003) [hereinafter Tecmed Award], 10 ICSID Rep. 134 (2006).

11. *See* Deutsche Bank AG v. Dem. Socialist Republic of Sri Lanka, ICSID Case No. ARB/09/2, Award, ¶ 420 (Oct. 31, 2012), http://www.italaw.com/sites/default/files/case-documents/italaw1272.pdf (citing Waste Mgmt., Inc. v. United Mexican States, ICSID Case No. ARB(AF)/00/3, Award (April 30, 2004), 43 I.L.M. 967 (2004)); Spyridon Roussalis v. Rom., ICSID Case No. ARB/06/1, Award, ¶ 314 (Dec. 7, 2011), http://www.italaw.com/sites/default/files/case-documents/ita0723.pdf [hereinafter Spyridon Roussalis Award] (citing Rumeli Telekom A.S. v. Republic of Kaz., ICSID Case No. ARB/05/16, Award, ¶ 605 (July 29, 2008), http://italaw.com/sites/default/files/case-documents/ita0728.pdf [hereinafter Rumeli Award]); Toto Costruzioni Generali S.p.A. v. The

without criticism.[12] Neither has this rise been straightforward as regards the views and practice of states, with the consequence of the introduction of a number of variations of the standards, sometimes seriously or drastically restricting its scope.

The values inherent and embodied in the rule notwithstanding, the standard may be seen from a critical perspective in view of the subjectivity to which its application may subject the host state. Here, we get to the centre of the debate surrounding FET. Two separate issues must be distinguished in this context. Firstly as we all know, the current system of investment arbitration has not been designed in order to promote uniformity or consistency of either rule-making or rule-interpretation,[13] with the sprawling consequences which we have seen, producing diversity of approaches to most rules, including FET. The second issue of the FET standard which, it is said, renders its application unpredictable and unmanageable, pertains to the argument of its inherently subjective nature.

No one will doubt the inherent breadth of the terms fair and equitable which are in practice understood together as one concept. At the same time, it will also be recognized that arbitral jurisprudence has succeeded enough to unfold the concept in a casuistic manner leading to groups and clusters of subgroups with more defined contours. My own count of these, leads me to these clusters, with some overlap: good faith in the conduct of a party, consistency of conduct, transparency of rules, recognition of the scope and purpose of laws, due process, prohibition of harassment, a reasonable degree of stability and predictability of the legal system, and, in particular, recognition of the legitimate expectation on the part of the investor to which I will turn later. I consider that arbitrariness and discrimination also fall under the heading of FET, even though separate, specific rules in investment treaties may (or may not) address these concepts.

Republic of Leb., ICSID Case No. ARB/07/12, Award, ¶¶ 151-159 (June 7 2012), http://www.italaw.com/sites/default/files/case-documents/ita1013.pdf [hereinafter Toto Award] (citing and describing earlier relevant cases); Bosh Int'l, Inc. v. Ukr., ICSID Case No. ARB/08/11, Award, ¶ 212 (Oct. 5, 2012), http://www.italaw.com/sites/default/files/case-documents/italaw1118.pdf (citing Lemire v. Ukr., ICSID Case No. ARB/06/18, Decision on Jurisdiction and Liab., ¶ 284 (Jan. 14, 2010), http://italaw.com/sites/default/files/case-documents/ita0454.pdf); Total Decision, *supra* note 3, ¶ 110; Oostergetel v. Slovk., UNCITRAL Ad Hoc Arb., Final Award, ¶ 222 (Apr. 23, 2012), http://old.italaw.com/documents/OostergetelvSlovakRepublic.pdf [hereinafter Oostergetel Final Award] (citing cases for legitimate expectations); and Paushok Award, *supra* note 3, ¶ 253 (following the Rumeli Award).

12. *See, e.g.*, MTD Equity Sdn. v. Republic of Chile, ICSID Case No. ARB/01/7, Decision on Annulment, ¶ 67 (Mar. 21, 2007), http://www.italaw.com/sites/default/files/case-documents/ita0546.pdf [hereinafter MTD Award] (proposing a standard for legitimate expectations which would, in effect, come close to abandoning this component). The Committee's reasoning is circular in nature.

13. *See* R. Dolzer, *Perspectives for Investment Arbitration: Consistency as a Policy Goal*, 3 TRANSNAT'L DISP. MGMT. J. (2012), www.transnational-dispute-management.com/article.asp?key=1823 (available by subscription or purchase).

The point here is to emphasize the evolution of the jurisprudence in general of the FET standard by way of developing operationally distinct subcategories of conduct meant to detail the meaning of the standard. These sub-categories, if rightly understood, do not depend on subjective views of the investor, but on the objective conduct of the host state.

Here, it also needs to be recalled that the degree of protection granted cannot be determined from the individual vantage point of the investor above; instead the laws, regulations and the conduct of the host state, expressed in objectively demonstrable terms, must serve as the appropriate framework for legitimate expectations.

Otherwise, the unilateral viewpoint of the investor would determine the application of the standard. As regards the *Tecmed* approach, I consider that its phrase "basic expectations" must be understood as the sum of the objective elements discussed in the subsequent passage.[14]

IV.The Current Architecture of the FET Standard

The multifaceted jurisprudence on FET shall now be reconstrued and reduced to its recurrent individual components as they appear in arbitral jurisprudence. As pointed out earlier, these components do not cover the entire scope of the rule's application. Also, it will be recognized that the components may overlap in their restrictive reach. It is generally recognized today that legitimate expectations arise out of the objective conduct of the host state and not out of subjective postulates of the investor. No BIT standard exists which derives its content from the unilateral viewpoint of one side, be it the investor or the host state. A point that remains to be decided concerns the manner in which the investor must show that the state's objective conduct gave rise to expectations on the part of the investor.

A. Good Faith

As is well known, the principle of good faith is recognized as a general principle of law, and thus a source of international law under Article 38 of the Statute of the International Court of Justice.[15] Article 31 of the Vienna Convention on the Law of Treaties recognizes the role of the principle specifically for the purpose of interpreting a treaty.[16]

As to the significance of good faith in investment law, it has been said that the principle "permeates the whole approach"[17] to investor protection and, more particularly,

14. Tecmed Award, *supra* note 10, ¶ 154.
15. Statute of the International Court of Justice, art. 36, para. 1, *available at*, http://www.icj-cij.org/documents/index.php?p1=4&p2=2&p3=0.
16. Vienna Convention on the Law of Treaties art. 31, May 23, 1969, 1155 U.N.T.S. 331, *available at* http://treaties.un.org/Pages/CTCTreaties.aspx?id=23&subid=A&lang=en.
17. Sempra Energy Int'l v. Argentine Republic, ICSID Case No. ARB/02/16, Award, ¶ 299 (Sept. 28, 2007), http://italaw.com/sites/default/files/case-documents/ita0770.pdf.

that is "at the heart of the concept of fair and equitable treatment,"[18] as a "guiding beacon . . . to the obligation[s]."[19] In a similar way, *Waste Management v Mexico*, for instance, addressing Article 1105 of the North American Free Trade Agreement (NAFTA), has considered the obligation to act in good faith as a "basic obligation" under the FET standard.[20]

One obvious application of the notion of good faith is the duty to act for cause, and not for purely arbitrary reasons of domestic politics.[21] Good faith may overlap with the rule on arbitrary treatment and often with other components such as consistency. In many cases, good faith will be subsumed, and only the other components may be discussed.

B. Legitimate Expectations: The State of the Law

The inherent legal affinity between fair and equitable treatment, good faith, and the protection of the investor's legitimate expectations has rightly been recognized and highlighted by investment tribunals. The protection of legitimate expectations by the FET standard will today properly be considered as the central pillar in the understanding and application of the FET standard. In 2012, the Tribunal in *Electrabel v. Hungary*[22] highlighted that "the most important function" of the FET standard is the protection of the investor's legitimate expectations.

The rationale and justification for the recognition of legitimate expectations seems obvious. The investor makes its calculations and decisions in the light of the law of the host state as it is made available to it by the host state, and the investor's assumptions about the return for its investment will depend upon the stability and predictability of those laws. Had the legal order been different, this decision to invest might have been different.

From the viewpoint of the host country, it appears not unreasonable to accept the benchmark of the legal order which it has adopted for itself at the time of the investment. This way, the host state's exercise of its sovereign rights is respected, albeit focused on the time it admitted the investment.

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18. *Id.* ¶ 298.
19. *Id.* ¶ 297.
20. Waste Mgmt., Inc. v. United Mexican States, ICSID Case No. ARB(AF)/00/3, Award, ¶ 138 (April 30, 2004) [hereinafter Waste Mgmt. Award], 43 I.L.M. 967 (2004).
21. Eureko B.V. v. Republic of Poland, Partial Award, ¶ 233 (Aug. 19, 2005) [hereinafter Eureko Partial Award], 12 ICSID Rep. 335 (2007).
22. Electrabel S.A. v. Hung., ICSID Case No. ARB/07/19, Decision on Jurisdiction, Applicable Law and Liab., ¶ 7.75 (Nov. 30, 2012), http://www.italaw.com/sites/default/files/case-documents/italaw1071clean.pdf [hereinafter Electrabel Decision].

1. The Rise of Legitimate Expectations: Consolidated Jurisprudence

In a series of decisions, arbitral jurisprudence has unfolded the essence of fair and equitable treatment and has identified the significance of legitimate expectations for understanding the standard.[23] The main points in this evolution over the past decade will be traced below in a brief consideration of the relevant decisions. The key issue has been to identify the parameters of those types of conduct, on the part of the host state, which determine the boundaries of the sphere of legally relevant expectations.

- In 2003, *Tecmed* required that the host state respect the basic expectations of the investor at the time of the investment and act without revoking any decisions, in an arbitrary manner upon which the investor had relied in planning its investment.[24]

- A year later, in 2004, *Occidental v. Ecuador* confirmed that the unilateral change of the legal and contractual framework existing at the item of the original investment would frustrate the investor's legitimate expectations and thereby violate the FET standard.[25]

- In 2006, the Tribunal in *LG&E v. Argentina* stated that the understanding of FET involves consideration of the investor's expectations when making its investment in reliance on the protections to be granted by the host state.[26]

- Also in 2006, *Thunderbird v. Mexico* ruled that an investor may rely on the host state's conduct which creates justifiable expectations:

> [T]he concept of "legitimate expectations" relates . . . to a situation where a Contracting Party's conduct creates reasonable and justifiable expectations on the part of an investor (or an investment) to act in reliance on such conduct, such that a failure by the Party to honor those expectations could cause the investor (or the investment) to suffer damages.[27]

- In *National Grid v. Argentina*, the Tribunal ruled that the FET standards protect the investor's expectations, which were "reasonable and legitimate in the context in which

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23. The terminology is not uniform. Some tribunals speak of "reasonable" or "justified" expectations. However, "legitimate" expectations is preferred here as it provides for a more contextual argumentative basis. The use of the term "basic expectations" in the Tecmed decision raises the issue whether the subjective views of the investors by themselves should be considered as the yardstick for legitimate expectations.
24. Tecmed Award., *supra* note 10, ¶ 159.
25. Occidental Final Award, *supra* note 4, ¶¶ 184-192.
26. LG&E Energy Corp. v. Argentine Republic, ICSID Case No. ARB/02/1, Decision on Liab., ¶ 127 (Oct. 3, 2006) [hereinafter LG&E Decision], http://italaw.com/sites/default/files/case-documents/ita0460.pdf.
27. Int'l Thunderbird Gaming Corp. v. United Mexican States, Award, ¶ 147 (NAFTA Ch. 11 Arb. Trib. Jan. 26, 2006), http://italaw.com/sites/default/files/case-documents/ita0431.pdf [hereinafter Thunderbird Award].

the investment was made."[28] Here, the Tribunal pointed to the economic situation to the regulatory legal framework of the host state and to the inducement of the investment by the host state.[29]

- In 2010, the Tribunal in *Suez v Argentina* summarized the state of the law and highlighted the investor's legitimate reliance on the host state's laws and regulations:

> In examining the various cases that have justifiably considered the legitimate expectations of investors and the extent to which the host government has frustrated them, this Tribunal finds that an important element of such cases has not been sufficiently emphasized: that investors, deriving their expectations from the laws and regulations adopted by the host country, acted in reliance upon those laws and regulations and changed their economic position as a result. Thus, it was not the investor's legitimate expectations alone that led tribunals to find a denial of fair and equitable treatment. It was the existence of such expectations created by host country laws, coupled with the act of investing their capital in reliance on them, and a subsequent, sudden change in those laws that led to a determination that the host country had not treated the investors fair and equitably.[30]

- In a further step, in *Lemire v. Ukraine*, the Tribunal, addressing an investment in the radio section, ruled to include, in the protection granted by the FET standard, "the common level of legal comfort which any protected foreign investor in the radio sector could expect."[31]

- The new dominance of the role of legitimate expectations for the understanding of fair and equitable treatment was confirmed in 2011 in *El Paso v. Argentina*. "There is an overwhelming trend to consider the touchstone of fair and equitable treatment to be found in the legitimate and reasonable expectations of the Parties, which derive from the obligation of good faith."[32]

The situation so described was not entirely new. As early as 2006, *Saluka v. Czech Republic* (Saluka) had observed the same position.[33]

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28. National Grid P.L.C. v. Argentine Republic, Award, ¶ 175 (UNCITRAL Arb. Trib. Nov. 3, 2008), http://www.italaw.com/sites/default/files/case-documents/ita0555.pdf [hereinafter National Grid Award].
29. *Id.* ¶¶ 176-180.
30. Suez v. Argentine Republic, ICSID Case No. ARB/03/19, Decision on Liab., ¶ 226 (July 30, 2010), http://italaw.com/sites/default/files/case-documents/ita0826.pdf.
31. Lemire v. Ukr., ICSID Case No. ARB/06/18, Award, ¶ 70 (Mar. 28, 2001), http://italaw.com/sites/default/files/case-documents/ita0454.pdf [hereinafter Lemire Award].
32. El Paso Energy Int'l Co. v. Argentine Republic, ICSID Case No. ARB 03/15, Award, ¶ 348 (Oct. 27, 2011), http://italaw.com/sites/default/files/case-documents/ita0270.pdf [hereinafter El Paso Award].
33. Saluka Partial Award, *supra* note 1, ¶ 302.

2. A Summary of the Current State of the Law

In the light of the arbitral jurisprudence, the details of the current state of the law will be summarized by way of five components, the existence of which determines whether the FET standard will protect the expectations of the investor in a given case:

- The objective conduct of the host state inducing legitimate expectations on the part of the foreign investor;

- reliance on that conduct on the part of the foreign investors;

- frustration of investor's expectation by subsequent conduct of the host state;

- unilateralism of conduct of the host state, i.e., absence of meaningful communication and/or consent with investors; and

- damages for the investor.

C. Detailing the Concept of Legitimate Expectations

1. Stability and Consistency of the Host State's Legal Order

Inconsistent conduct by the host state confuses the investor, stands in the way of proper planning, and is not conducive to an investment-friendly climate. Not surprisingly, arbitral tribunals have confirmed that inconsistency of conduct by the host state, as regards the investor's obligations, is not compatible with the requirement of FET.[34]

In *MTD v. Chile*, the Minister of Economy, Development, and Reconstruction of Chile approved the investor's project in a way which prima facie indicated that the project was feasible in the location chosen by the investor.[35] Subsequently, however, another agency of the host state determined that the zoning regulations stood in the way of the project. The Tribunal ruled that such inconsistent conduct violated the FET rule. "What the Tribunal emphasizes here is the inconsistency of action between two arms of the same Government *vis-à-vis* the same investor even when the legal framework of the country provides for a mechanism to coordinate."[36]

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34. *See* Metalclad Corp. v. United Mexican States, ICSID Case No. ARB(AF)/97/1, Award, ¶ 99 (Aug. 30, 2000) [hereinafter Metalclad Award], 5 ICSID Rep. 212 (2002). *See generally* Tecmed Award, *supra* note 10, ¶ 154; Encana Corp. v. Republic of Ecuador, LCIA Case No. UN 3481, Award, ¶ 158 (Feb. 3, 2006), http://www.italaw.com/sites/default/files/case-documents/ita0285_0.pdf; Saluka Partial Award, *supra* note 1, ¶¶ 248, 307, 417; PSEG Award, *supra* note 1, ¶ 248; Biwater Gauff (Tanz.) Ltd. v. Republic of Tanz., ICSID Case No. ARB/05/22, Award, ¶ 1602 (July 24, 2008), http://www.italaw.com/sites/default/files/case-documents/ita0095.pdf; LESI, S.p.A. v. People's Dem. Republic of Alg., ICSID Case No. ARB/05/3, Award (Nov. 12, 2008), http://www.italaw.com/sites/default/files/case-documents/ita0457.pdf; and Lemire Award, *supra* note 31, ¶ 284.

35. *See* MTD Award, *supra* note 12.

36. MTD Award, *supra* note 12, ¶ 163. *See also* Metalclad Award, *supra* note 34, ¶¶ 97-100 (attributing liability to the host state from actions of an administrative agency).

Another case in point was *Eureko v Poland*.[37] Here, Poland had agreed that Eureko would, after the initial investment being the acquisition of the majority of shares of a local company, have the right to acquire further shares. Poland subsequently reversed course and refused to offer Eureko more shares. Here, as well, the Tribunal found a violation of FET.[38]

In a broader sense, an alteration of the applicable rules by the host state may also be considered from the viewpoint of consistency. In this respect, the requirement of consistency overlaps with the need for stability under the FET rule.

Consistency may not be required under circumstances in which the host state had convincing reason to change course. As regards its legislative power, the host state will, in principle, have the right to pursue its interests in the light of the new circumstances, but not ignore the interests of the investor who had earlier adjusted his conduct to the previous course required by the host state. The power to regulate operates within the limits of rights conferred upon the investor. Correspondingly, it will have to be assumed that the reversing of a position in a dramatic manner with serious negative effects upon the investor will be consistent with FET only in the presence of serious exceptional reasons, compelling the host state to reverse its previous decision and to require the investor to re-adapt its business.

Beyond administrative consistency, investment tribunals have also ruled that the FET standard includes a requirement to maintain a stable legal framework.[39] For instance, the Tribunal in *Occidental v. Ecuador* explained, "there is certainly an obligation not to alter the legal and business environment in which the investment has been made."[40]

Other cases have addressed the need for consistency and stability of the legal framework and the investor's legitimate expectation. In *El Paso v. Argentina*, the tribunal stated that a host state "*should not unreasonably modify the legal framework or modify it in contradiction with a specific commitment*."[41] This interpretation was also adopted by the tribunal in *Oostergetel v. Slovak Republic*.[42]

The Tribunal in *LG&E v. Argentina* held that FET requires that a host state maintains "stability of the legal and business framework" in the state party.[43] Similarly, *Alpha v. Ukraine* emphasized the duty of the host state not to arbitrarily change the rules to the detriment of the investor.[44]

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37. Eureko Partial Award, *supra* note 21.
38. *Id.* ¶ 234.
39. Occidental Final Award, *supra* note 4, ¶ 183.
40. *Id.* ¶ 191. *See also* Marion Unglaube v. Costa Rica, Award, May 12, 2012, para. 220 et. seq.
41. El Paso Award, *supra* note 32, ¶ 364.
42. Oostergetel Final Award, *supra* note 11, ¶ 224.
43. LG&E Decision, *supra* note 26, ¶ 124.
44. *See* Alpha Award, *supra* note 3, ¶ 420.

In a case involving several changes of rules and policies after the making of investment, one Tribunal ruled that a "roller-coaster" policy violates the FET rule:

> [T]he Tribunal also finds that the fair and equitable treatment obligation was seriously breached by what has been described above as the "roller-coaster" effect of the continuing legislative changes. This is particularly the case of the requirements relating, in law or practice, to the continuous change in the conditions governing the corporate status of the Project, and the constant alternation between private law status and administrative concessions that went back and forth. This was also the case, to a more limited extent, of the changes in tax legislation.[45]

2. Expectations Based on the Host State's Legal Order

The appropriate starting point to determine legitimate expectations is the legal order of the host state at the time when the investor made its investment. A number of investment tribunals have relied on the nexus between legitimate expectations and the host state's legal order at the time of the investment.[46]

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45. PSEG Award, *supra* note 1, ¶ 250.

46 . Azinian v. United Mexican States, ICSID Case No. ARB(AF)/97/2, Award, ¶¶ 95-97 (Nov. 1, 1999), 14 ICSID Rev. For. Inv. L. J. 535 (1999), *available at* http://www.italaw.com/sites/default/files/case-documents/ita0057.pdf. *See also* Mondev Int'l Ltd. v. U.S., ICSID Case No. ARB(AF)/99/2, Award, ¶ 156 (Oct. 11, 2002) [hereinafter Mondev Award], 6 ICSID Rep. 192 (2004), *available at* http://italaw.com/sites/default/files/case-documents/ita1076.pdf; Feldman v. United Mexican States, ICSID Case No. ARB(AF)/99/1, Award, ¶ 128 (Dec. 16 2002), 7 ICSID Rep. 341 (2005), *available at* http://www.italaw.com/sites/default/files/case-documents/ita0319.pdf; LG&E Decision, *supra* note 26, ¶ 130; Enron Corp. v. Argentine Republic, ICSID Case No. ARB/01/3, Award, ¶ 262 (May 22, 2007), http://www.italaw.com/sites/default/files/case-documents/ita0293.pdf [hereinafter Enron Award]; BG Group Plc. v. Republic of Arg., Final Award, ¶¶ 297-298 (UNCITRAL Arb. Trib. Dec. 24, 2007), http://www.italaw.com/sites/default/files/case-documents/ita0081.pdf [hereinafter BG Group Final Award]; Duke Energy Electroquil v. Republic of Ecuador, ICSID Case No. ARB/04/19, Award, ¶¶ 340, 365 (Aug. 18, 2008), http://italaw.com/sites/default/files/case-documents/ita0256.pdf [hereinafter Duke Award]; Jan de Nul N.V. v. Arab Republic of Egypt, ICSID Case No. ARB/04/13, Award, ¶ 265 (Nov. 6, 2008), http://italaw.com/sites/default/files/case-documents/ita0440.pdf; Bayindir Insaat Turizm Ticaret Ve Sanayi A.S. v. Islamic Republic of Pak., ICSID Case No. ARB/03/29, Award, ¶¶ 190-191 (Aug. 27, 2009), http://www.italaw.com/sites/default/files/case-documents/ita0075.pdf; EDF (Services) Ltd. v. Rom., ICSID Case No. ARB/05/13, Award, ¶ 219 (Oct. 8, 2009), http://www.italaw.com/sites/default/files/case-documents/ita0267.pdf; AES Summit Generation Ltd. v. Republic of Hung., ICSID Case No. ARB/07/22, Award, ¶¶ 9.3.8-9.3.18 (Sept. 23, 2010), http://italaw.com/sites/default/files/case-documents/ita0014_0.pdf; Frontier Petroleum Services Ltd. v. Czech Republic, Final Award, ¶¶ 287, 468 (UNCITRAL Arb. Trib. Nov. 12, 2010), http://italaw.com/sites/default/files/case-documents/ita0342.pdf; and National Grid Award, *supra* note 28. Specifically on the relationship with the right to regulate, see PSEG Award, *supra* note 1, ¶ 255. ("While noting that no investor 'may reasonably expect that the circumstances prevailing at the time the investment is made remain totally unchanged,' the Tribunal in *Saluka* held that the investor can still expect that the conduct of the host State subsequent to the investment will be fair and equitable as the investor's decision to invest is based on 'an assessment of the state of the law and the totality of the business environment at the time of the investment.'"). *See also* Saluka Partial Award, *supra* note 1, ¶ 301.

From a broader perspective, to deny the relevance of the legal order of the host state in the context of legitimate expectations would assume that stability and predictability of the laws of the host state have no bearing upon the object and purpose of an investment treaty and the notion of fair and equitable treatment.

Such assumptions would contravene the spirit in which investments agreements are generally concluded. It is well-known that major investments are concluded with a long-term perspective, often for more than twenty years. The willingness of foreigners to invest is linked to the degree of stability in a host state, and stability is one factor for an investor to determine the location of its investment. BITs are meant to contribute to stability for these very reasons. The FET standard with its focus on legitimate expectations appropriately reflects the connection between the flow of investments and legal stability. The ECT expressly recognizes an obligation on the part of the host state to provide for legal stability.[47]

The significance of the laws of the host state for the purpose of determining legitimate expectations was addressed in *Total v. Argentina*,[48] an ICSID case, decided in 2010. In a split decision, the majority in this case decided that the legal order could not serve as a basis for legitimate expectations.[49] The majority explained that the legal order would have been relevant only in case the relevant laws would have been prospective in nature:

> Indeed, the most difficult case is (as in part in the present dispute) when the basis of an investor's invocation of entitlement to stability under a fair and equitable treatment clause relies on legislation or regulation of a unilateral and general character. In such instances, investor's expectations are rooted in regulation of a normative and administrative nature that is not specifically addressed to the relevant investor. This type of regulation is not shielded from subsequent changes under the applicable law. This notwithstanding, a claim to stability can be based on the inherently prospective nature of the regulation at issue aimed at providing a defined framework for future operations. This is the case for regimes, which are applicable to long-term investments and operations, and/or providing for "fall backs" or contingent rights in case the relevant framework would be changed in unforeseen circumstances or in case certain listed events materialize. In such cases, reference to commonly recognized and applied financial and economic principles to be followed for the regular operation of investments of that type (be they domestic or foreign) may provide a yardstick. This is the case for capital intensive and long term investments and operation of utilities under a license, natural resources exploration and exploitation, project financing or Build Operate and Transfer schemes. The concept of "regulatory fairness" or "regulatory certainty" has been used in this respect. In the light of these criteria when a State is empowered to fix the tariffs of a public utility it must do so in such a way that the concessionaire is able to recover its operations costs, amortize its investments

47. Energy Charter Treaty, Dec. 17, 1994, 2080 U.N.T.S. 95.
48. Total Decision, *supra* note 3
49. Total Decision, *supra* note 3.

> and make a reasonable return over time, as indeed Argentina's gas regime provided.[50]

Apart from an assessment of the general approach favored by the majority, the *Total* decision on legitimate expectations raises the obvious issue how to define those laws which should be considered as 'prospective' in nature. What was at stake in the *Total* case was the legal order of the host State regulating tariffs, taxes and an indexation scheme set forth in a law.

In my view, it is difficult to understand why rules on tariffs, taxes and on indexation should not be considered as forward-looking or prospective; but then, of course, nearly all substantive laws regulating economic affairs seem to fall into that category of laws which the *Total* decision would not classify as prospective. In other words, the principle of the relevance of the laws of the host state at the time of the investment, for purposes of determining the scope of legitimate expectations, would in effect be largely undermined by an exception in case of the lack of a prospective law as postulated by the majority in *Total*.

The core of the argumentative structure of the ruling in *Total* stands in direct contrast to the widely accepted rule that laws of the host state, at the time of the investment, will be central for the determination of legitimate expectations. The *Total* majority fails to provide for a plausible explanation for its view and, therefore, will not be considered to be persuasive.

3. Expectations Based upon Representations

An important component of legitimate expectations, often invoked, concerns representations by the host state upon which the investor has relied. Here, it needs to be recognized that unilateral statements are binding, in any event, under customary law if they are clear and unequivocal, irrespective of the context of fair and equitable treatment.[51] The legitimacy of reliance of representation by the host state to the investor flows directly from the principle of good faith.

It may be asked be asked whether representations to the investor will be the only factor to determine the range of legitimate expectations. Obviously, it would be a very narrow approach to conclude that no other element than representation would be relevant in this context. There will be no plausible ground, in terms of the inherent purpose and meaning of either FET in general, or legitimate expectations in particular, to restrict the sphere of legitimate considerations to representations alone. In particular, a narrow view restricting legitimate expectations to representations would be

50. Total Decision, *supra* note 3, ¶ 122 (emphasis added).
51. *See* W. Michael Reisman & Mahnoush H. Arsanjani, *The Question of Unilateral Governmental Statements as Applicable Law in Investment Disputes*, 19 ICSID Rev. 328 (2004).

inconsistent with the broadly accepted reference to the state of the law at the time of the investment as the primary guideline. Such an approach would also be not compatible with the assumption that all circumstances must be taken into account for the determination of legitimate expectations.[52]

4. Expectations Based upon Contractual Commitments

Issues concerning legitimate expectations may also arise in the context of contractual stability. Total stability for a contract is only guaranteed when the contract is guaranteed by an umbrella clause.[53] On the other hand, it is also widely accepted that a repudiation of a contract by the host state will violate the rights of the investor even in the absence of a BIT under the minimum standard of international law.[54] It is equally recognized that ordinary commercial disputes are not subject to the rules of a BIT in the absence of an umbrella clause.[55] Within these broader parameters governing contractual disputes between a host state and a foreign investor, the legitimate expectations of the investor will have to be identified.

In arbitral practice, the significance of contracts has overlapped with that of the legal order in cases in which contractual commitments are anchored in general laws. Recent cases with Argentina as the respondent fall into this category; tribunals have been inclined in this setting to consider the existence of legitimate expectations in these cases without distinguishing the role of laws from those arising out of contracts.[56] These rulings have properly considered the general legal order and the applicable contracts in conjunction and concluded that the investor's legal expectations were guided by the laws and the contracts.

As to cases dealing specifically with contracts, the decisions in *Parkerings v. Lithuania*,[57] and in *Hamester v. Ghana*,[58] questioned whether contractual commitments

52. Electrabel Decision, *supra* note 22, ¶ 7.78. The Electrabel Decision properly pointed out that while specific assurances may reinforce investor's expectations, such assurance is not always indispensable.
53. On umbrella clauses, see RUDOLF DOLZER & CHRISTOPH SCHREUER, PRINCIPLES OF INTERNATIONAL INVESTMENT LAW 166 (2nd ed. 2012).
54. RESTATEMENT (THIRD) OF FOREIGN RELATIONS LAW § 712 (1987).
55. *See* DOLZER & SCHREUER, *supra* note 53, at 152-54.
56. *See e.g.*, Enron Award, *supra* note 46, ¶ 43; National Grid Award, *supra* note 28, ¶¶ 177-178; LG&E Decision, *supra* note 26, ¶ 50; BG Group Final Award, *supra* note 46, ¶¶ 21-23; and EDF Int'l S.A. v. Argentine Republic, ICSID Case No. ARB/03/23, Award, ¶¶ 999, 1005 (June 11, 2012), http://www.italaw.com/sites/default/files/case-documents/ita1069.pdf [hereinafter EDF Int'l Award]. In *EDF Int'l*, the Tribunal had to address the failure of the host state to adjust the economic equilibrium of a concession after a state of emergency had passed. The Tribunal found a violation of "an integral part of fairness and equity." *Id.* ¶ 1005.
57. *See* Parkerings-Compagniet AS v. Republic of Lith., ICSID Case No. ARB/05/8, Award (Sept. 11, 2007), http://www.italaw.com/sites/default/files/case-documents/ita0619.pdf [hereinafter Parkerings Award].

may serve as the basis for legitimate expectations. In contrast, in *Rumeli v. Kazakhstan*,[59] the Tribunal held that the termination of a contract violated the claimant's legitimate expectations. More broadly, *Toto v. Lebanon* stated that legitimate expectations "may follow from explicit or implicit representations by the host state, *or from its contractual commitments*."[60]

From a different angle, and looking at legislative changes affecting contractual agreements from a broader perspective, *Vivendi II v. Argentina*[61] suggests that corrective measures reversing course should not be adopted unilaterally, but on the basis of transparent and non-coercive renegotiations.[62] Along the same lines, in 2010, *Alpha v. Ukraine*[63] has ruled that a host state should not unilaterally arbitrarily change the rules of the game.

Obviously, the jurisprudence on this point has not yet crystallized in a consistent manner. In general, it will be noted that on the scale of different types of commitments by the host state, a contractual obligation is closer to a specific representation than to a general law. Legitimate expectations will have to be adopted accordingly.

5. Expectations Based on All Circumstances

A third aspect often considered in the discussion of legitimate expectations pertains to the recognition of all manifestations of FET, being their dependence on context. A number of tribunals have repeated that legitimate expectations must be determined in the light of all specific circumstances of each case.[64]

Often, a close-up view of individual decisions will indeed confirm and emphasize the relevance of specific circumstances for the outcome of a case. The ruling in *Methanex v U.S.* (Methanex) is on point with the case concerning legislation in California.[65] At first sight, this case seems to contradict the position that the adoption of legislation shortly after the time of the investment will be difficult to square with the requirement of FET and the protection of legitimate expectations. However, the Tribunal clearly pointed to

58. *See* Gustav F W Hamester GmbH & Co KG v. Republic of Ghana, ICSID Case No. ARB/07/24, Award (June 18, 2010), http://www.italaw.com/sites/default/files/case-documents/ita0396.pdf.
59. Rumeli Award, *supra* note 11, ¶ 615.
60. Toto Award, *supra* note 11, ¶ 159 (emphasis added).
61. Compañiá de Aguas del Aconquija S.A. and Vivendi Universal S.A. v. Argentine Republic, ICSID Case No. ARB/97/3, Award, ¶ 7.4.31 (Aug. 20, 2007), http://www.italaw.com/sites/default/files/case-documents/ita0215.pdf.
62. *See also* Meg Kinnear, *The Continuing Development of the Fair and Equitable Treatment Standard*, *in* INVESTMENT TREATY LAW: CURRENT ISSUES III 207, 225 (Andrea K. Bjorklund et al. eds. 2008).
63. Alpha Award, *supra* note 3, ¶ 420.
64. *See, e.g.*, Mondev Award, *supra* note 46, ¶ 118 and Spyridon Roussalis Award, *supra* note 11, ¶ 316.
65. *See* Methanex Corp. v. U.S., Final Award of the Trib. on Jurisdiction and Merits (NAFTA Ch. 11 Arb. Trib. Aug. 3, 2005), http://www.state.gov/documents/organization/51052.pdf.

special circumstances. At the time of the Methanex investments, the substance to be produced by Methanex in California was under broad scrutiny, and the legislative change that affected Methanex was clearly "on the horizon" at the time of the investment. In such a specific setting, absent specific reasons and absent any kind of contractual or other commitment, it would indeed be difficult to speak of legitimate expectations on the part of the investor.

6. Circumstances Opposed to Stability

Another approach was set forth in *Duke Energy v. Ecuador* (Duke).[66] This decision recognizes that such expectations of the investor will be protected that are "legitimate and reasonable at the time when the investor makes the investment."[67] The special element here is that in the view of the Tribunal, all circumstances, including not only the facts surrounding the investment, but also the "political, socioeconomic, cultural and historical conditions prevailing in the host State" must be taken into account.[68] At the same time, the Tribunal considered the requirement of a "stable and predictable legal framework."[69]

Inasmuch as the Duke decision points to "political, socio-economic, cultural and historical conditions" shaping the investor's legitimate expectations, it is not clear why and to what extent these conditions need to be considered. The object and purpose of an investment treaty being the promotion and protection of foreign investment, the relevant circumstances to be assessed for the determination of legitimate expectations must be of a nature that is not inconsistent with that object and purpose. As a consequence, respect for a political history of instability or of hostility toward foreign investment, for instance, would not be considered to be conducive to the purposes of an investment treaty; indeed, such a treaty is concluded to overcome such traditions, and the accepted principles of interpretation relevant to an investment agreement will not allow to introduce elements of interpretation that stand in contrast to the object and purpose of the treaty.

7. Legitimate Expectations and the Right to Regulate

In this context, it is also worthwhile to consider such awards of tribunals which have sought to address the particular relationship between the right of the state to regulate and the existence of legitimate expectations. Is there an irreconcilable inconsistency between the right to regulate and the principle of legitimate expectations?

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66. *See* Duke Award, *supra* note 46.
67. *Id.* ¶ 340.
68. *Id.*
69. *Id.* ¶ 347.

Saluka v. Czech Republic has stated that the host state's legitimate right subsequently, i.e., after the investment in the public interest must be taken into consideration as well, and may be cited in this context. [70]

However, the Tribunal's position is quite nuanced. In a second, following passage, the Tribunal calls for "a weighing of the Claimant's legitimate and reasonable expectations on the one hand and the Respondent's legitimate regulatory interests on the other."[71] In the third passage, the Tribunal considers that a host state must implement its policies bona fide by conduct that is, as far as the investor's investment is concerned, reasonably justifiable by public policies. Moreover, the decision adds that the State's conduct must not violate the requirements of "consistency, transparency, even-handedness and non-discrimination,"[72] and also must not disregard "procedural propriety and due process."[73]

Lemire v. Ukraine also speaks of a balance of the right of the investor and of the host state, but also goes on to say that regulatory measures must not be unfair and must not hinder a level playing field.[74]

These considerations by the *Saluka* and the *Lemire* Tribunals are multifaceted and ultimately seem to point in broad terms to a weighing process whose elements seem to escape generalization. Generally speaking, the Tribunals do not answer the question why in the context of a BIT, the interests of the state will have the same weight as the legitimate expectation of the investor, given the BITs nature and its specific purpose to promote and protect the investor's interest. BITs are drafted in a one-sided manner with the aim to provide an investor-friendly climate and to attract foreign investors; absent a special treaty clause, a rebalancing of interests in the case of a dispute by a tribunal would not be appropriate.

Another decision addressed the right to regulate and the existence of legitimate expectations is *Parkerings v. Lithuania*, rendered in 2007.[75] The case concerned a project in Lithuania in the period of transition from communism to the free market. In this context, the Tribunal emphasized "each State's undeniable right and privilege to exercise its sovereign legislative power" and also that an investor knows that "laws will evolve over time."[76]

However, this Tribunal as well emphasized the limits of that power under a BIT, and qualified the right to regulate by adding that a state is prohibited "to act unfairly,

70. Saluka Partial Award, *supra* note 1, ¶¶ 304-308.
71. *Id.* ¶ 306.
72. *Id.* ¶ 307.
73. *Id.* ¶ 308 (citation omitted).
74. Lemire v. Ukr., ICSID Case No. ARB/06/18, Decision on Jurisdiction and Liab., ¶ 267 (Jan. 14, 2010), http://italaw.com/sites/default/files/case-documents/ita0454.pdf.
75. *See* Parkerings Award, *supra* note 57.
76. *Id.* ¶ 332.

unreasonably or inequitably in the exercise of its legislative power."[77] Ultimately, therefore, the *Parkerings*' decision, as well, rests on the conventional position that a state has the right to regulate but that it must do so in a fair manner.

The general issue of the relationship between the FET rule and the right to regulate was properly addressed in *ADC v. Hungary*:

> The Tribunal cannot accept the Respondent's position that the actions taken by it against the Claimants were merely an exercise of its rights under international law to regulate its domestic economic and legal affairs. It is the Tribunal's understanding of the basic international law principles that while a sovereign State possesses the inherent right to regulate its domestic affairs, the exercise of such right is not unlimited and must have its boundaries. As rightly pointed out by the Claimants, the rule of law, which includes treaty obligations, provides such boundaries. Therefore, when a State enters into a bilateral investment treaty like the one in this case, it becomes bound by it and the investment-protection obligations it undertook therein must be honoured rather than be ignored by a later argument of the State's right to regulate.
>
> The related point made by the Respondent that by investing in a host State, the investor assumes the "*risk*" associated with the State's regulatory regime is equally unacceptable to the Tribunal. It is one thing to say that an investor shall conduct its business in compliance with the host State's domestic laws and regulations. It is quite another to imply that the investor must also be ready to accept whatever the host State decides to do to it. In the present case, had the Claimants ever envisaged the risk of any possible depriving measures, the Tribunal believes that they took that risk with the legitimate and reasonable expectation that they would receive fair treatment and just compensation and not otherwise. [78]

D. Due Process

Fair procedure is a basic component of the rule of law and a vital element of FET. A current expression is found in Article 5 (2)(a) of the U. S. Model BIT 2012: "[FET] includes the obligation not to deny justice in criminal, civil, or administrative adjudicatory proceedings in accordance with the principle of due process embodied in the principle legal systems of the world . . . ."[79]

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77. *Id.*
78. ADC Affiliate Ltd., v. Republic of Hung., ICSID Case No. ARB/03/16, Award of the Trib., ¶ 423-424 (Oct. 2, 2006), http://www.italaw.com/sites/default/files/case-documents/ita0006.pdf [hereinafter ADC Award].
79. U.S. Model Bilateral Investment Treaty art. 5(2)(a), 2012, http://www.state.gov/documents/organization/188371.pdf.

Arbitral Tribunals have repeatedly confirmed the significance of fair procedure. For instance, in *Metalclad v. Mexico*, a construction permit had been denied to the claimant.[80] The Tribunal ruled that the failure to hear the investor amounted to a violation of the FET standard, stating, "[m]oreover, the permit was denied at a meeting of the Municipal Town Council of which Metalclad received no notice, to which it received no invitation, and at which it was given no opportunity to appear."[81]

Tecmed v. Mexico also concluded that a failure to notify the claimant in the context of a revocation of a license was inconsistent with FET, given that the claimant had no opportunity to express its position.[82]

In *Middle East Cement v. Egypt*, the Tribunal found a violation of FET when the host state had failed to notify the claimant of an upcoming seizure and auctioning of its ship.[83]

Thunderbird v. Mexico agreed that due process is relevant for administrative proceedings.[84] *Genin v. Estonia*[85] and *Waste Management v. Mexico*[86] confirmed that due process and the right to be heard are embodied in FET.

In *ADC v. Hungary*, the Tribunal discussed the meaning of due process and concluded, in the context of an expropriation clause, that "reasonable advance notice" and a fair hearing are required to satisfy the due process standard.[87]

For arbitral proceedings, the Annulment Committee in *Fraport v. Philippines*[88] highlighted the importance of due process, albeit in its own way.

The above case law indicates that the right to be heard will also be applicable in administrative proceedings, even though a right to judicial review may exist with stricter procedural guarantees.

E. Transparency

So far, issues of transparency in a narrow sense have not often been before tribunals in recent years. In the past, a violation of the FET standard was assumed, for instance, when the host state failed to clarify the rights of an investor, when the circumstances of an act affecting the investor's rights were obscure, or when a governmental entity refused

80. *See* Metalclad Award, *supra* note 34.
81. *Id.* ¶ 91.
82. Tecmed Award, *supra* note 10, ¶ 162.
83. Middle East Cement Shipping & Handling Co. S.A. v. Arab Republic of Egypt, ICSID Case No. ARB/99/6, Award, 143 (April 12, 2002), ICSID Rep. 173 (2005), *available at* http://www.italaw.com/sites/default/files/case-documents/ita0531.pdf.
84. Thunderbird Award, *supra* note 27, ¶ 197-200.
85. Genin v. Republic of Est., ICSID Case No. ARB/99/2, Award, ¶ 358 (June 25, 2001), 17 ICSID Rev. 395 (2002), *available at* http://italaw.com/sites/default/files/case-documents/ita0359.pdf.
86. Waste Mgmt. Award, *supra* note 20, ¶ 98.
87. ADC Award, *supra* note 78, ¶ 435.
88. Fraport AG Frankfurt Airport Services Worldwide v. Republic of Phil., ICSID Case No. ARB/03/25, Decision on the Application for Annulment, ¶¶ 197-203 (Dec. 23, 2010), http://italaw.com/sites/default/files/case-documents/ita0341.pdf.

to grant a right which had earlier been accorded by another agency of the host state.[89] Also, transparency may, in some settings, be closely linked to require a state to avoid a prolonged state of legal uncertainty and ambiguity.[90]

F. Freedom from Harassment and Coercion

Harassment and coercion are forms of conduct not to be expected in the ordinary relationship between the host state and the investor. And yet, arbitral practice has had to deal with such phenomena. States have come up with various ways of particular maltreatment, often disguised in the cloak of lawful investigations, unacceptable options, and forced conduct.[91] States may be inclined to invoke their power to tax or to protect the environment in this context. However, investors must show credible, relevant evidence to succeed on a claim of this kind.

G. Acting for Cause, Arbitrary Treatment

Tribunals have properly recognized that the fair and equitable treatment does not allow arbitrary conduct in the relations between the host state and the investor.[92] Indeed, it would seem difficult to reconcile arbitrary treatment with fair and equitable treatment.[93]

In an investment-friendly climate, fair and equitable treatment requires that the host state does not affect the foreign investor's rights without cause. Thus, an official may not act vis-à-vis an investor because of reasons of a personal nature. On a different level, the host state government must not act out of xenophobic motives. More important in practice, fair and equitable treatment will stand in the way of conduct of the host state that is driven by domestic politics instead of arising out of considerations related to the investment. Governmental action will also be suspect in case it is not based on a proper review of facts relevant to a decision. Here, the prohibition of arbitrary treatment overlaps with the FET rule.

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89. *See* Metalclad Award, *supra* note 34, ¶ 76; Maffezini Award, *supra* note 2, ¶ 83; and MTD Award, *supra* note 12, ¶ 163.
90. *See* Tecmed Award, *supra* note 10, ¶ 164, and PSEG Award, *supra* note 1, ¶ 246.
91. *See* DOLZER & SCHREUER, *supra* note 53, 159.
92. *See, e.g.*, Parkerings Award, *supra* note 57, ¶ 315, and Pantechniki S.A. v. Albania, ICSID Case No. ARB/07/21, Award, ¶ 87 (July 30, 2009), http://www.italaw.com/sites/default/files/case-documents/ita0618.pdf.
93. In Tecmed, the Tribunal ruled that the arbitrary revocation of a license violates the FET standard. *See* Tecmed Award, *supra* note 10, ¶ 154.

H. Failure to Readjust Equilibrium

A government taking measures which seriously affects an investor's interests during an economic crisis will violate the FET standard if it fails to readjust the economic equilibrium after the crisis has subsided;[94] the rules of necessity remain unaffected.

I. Unilateralism in the Adaptation of Terms

Unilateralism in the adaptation of the basic terms of an investment, contractual or otherwise, and the ensuing dismantling of the legal framework is, in principle, antithetic to fair and equitable treatment and to good faith. Depending on the circumstances, unilateral acts may violate the FET standard.

V. Relationship to Other Principles

Whereas stability and predictability are more abstract concepts linked to the general contours of an investment-friendly climate, the notion of legitimate expectations concerns, in a normative-operational mode, the affirmation and the limitations of stability and predictability in the light of the particular circumstances of a case. Umbrella clauses and stabilization clauses are, in principle, meant to provide for the full and unqualified preservation of certain types of obligations during relevant periods.

VI. Future Evolution

How will the FET concept evolve in the coming years? In my view, the standard will continue to occupy corporations, investment lawyers, arbitrators and host states alike. This will simply be so because a range of grievances of foreign companies do not fall, at least not clearly, into the ambit of the more specific categories of protection granted by BITs.

In practice, the types of actions which affect the foreign investor's interests have turned out to be very broad, ranging from tax matters to contractual issues, from tariff regulations to the conduct of renegotiation, from open communication among state and investor, including to the organization of a bidding process. In all such areas, and multiple others, issues of fair treatment may arise, and FET will remain relevant because other standards may not be applicable.

As to the meaning of the standard, tribunals will likely continue to follow the current trend and to turn away from broad, subjective assertions and instead apply subcategories amenable to objective criteria tied to objective conduct on the part of the host state. This approach has the advantage of a plausible objective and higher degree of persuasiveness.

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94. *See, e.g.*, EDF *Int'l* Award, *supra* note 56.

The evolving case law has identified, as we have seen, a number of rationally manageable subcategories. In practice, these will be suitable to decide the practical issues before tribunals in most cases. In other words, the interpretations and application of the standard has matured so that subjective views based solely on the arbitrator's notion of fairness will, as a rule, no longer be necessary or appropriate.

The task of relevant jurisprudence in the future will be to develop and to refine the subcategories.

The topic of legitimate expectations will likely remain in the foreground of the FET rule. The further definition of this central topic remains the most important component in the development of the FET standard. Fact specific considerations will continue to dominate its application, and the law as it stands at the time of the investment will likely permeate the circumstances deciding the individual case.

The ultimate benchmark by which the FET standard and the unfolding relevant jurisprudence will be judged is whether the results reached by the tribunals, based on the subgroups, are generally considered by the investment community to be just, and whether they render justice in a transparent manner, regardless of the more specific language and explanation upon which the arbitrators may agree. When it is asked what accounts for the extraordinary career of the FET rule in general and of the principle of legitimate expectations in particular, the answer must turn to the acceptance of the results on the basis of the subgroups.

The most plausible explanation of the rise of the FET standard will look to this question. Was the investor in effect treated in a hospitable climate in a fair manner? It appears that in most cases, most arbitrators, and equally important, most commentators, have agreed on the answer reached in the specific cases in light of the given circumstances. In this way, the usefulness and the operational manageability of the standard has generally been confirmed by a broad consensus on the concrete results delivered under the auspices of this cardinal rule of foreign investment law.