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Investor-State Arbitration in International Tax Dispute Resolution-- A Cut above Dedicated Tax Dispute Resolution?

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INVESTOR-STATE ARBITRATION IN INTERNATIONAL TAX DISPUTE RESOLUTION

A CUT ABOVE DEDICATED TAX DISPUTE RESOLUTION?

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The globalization of commercial and investment operations increasingly affects and contributes to the reshaping of the practices and policies of international taxation. Increasingly, even having knowledge of international tax law is not sufficient to understand the challenges faced by investors making investments across borders. This article focuses on the impact of the international law of foreign investment on tax issues with a view to assessing the interactions between the two regimes and identifying potential signs of convergence. The last decade has witnessed a dramatic surge of investment disputes between foreign investors and host country governments. The new phenomenon of investment arbitration has brought about a number of decisions from different arbitral fora in the sector of tax, contributing to the formation of a jurisprudence that is elucidating the meaning of key provisions and contributing to the emergence of global economic regulation for tax matters. Importantly, fifteen disputes have resulted in significant compensation being paid by host states to foreign investors for breaching investment treaty commitments by imposing tax measures. The details of these fifteen disputes show that there are a number

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of principles, which have proven decisive to justify the claims of the taxpayers, namely, protection against expropriation, fair and equitable treatment, full protection and security, non-discrimination, the idea of an umbrella clause, and the notion of performance requirements. These six different investment principles indirectly constitute part of the international regime of tax matters.

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I. INTRODUCTION

Foreign investment is one of the key interests of any country's political economy. International investments can aid the host country in developing a sound economic structure by increasing and diversifying manufacturing, offering novel and more sophisticated services, creating employment, and bringing innovative technology among other benefits.[1] Additionally, countries tend to encourage well-established domestic companies to expand their footprints abroad to earn and then repatriate long-term capital gains, help build economic and political ties with other nations, and perhaps ensure access to natural resources that the home country lacks.[2] Concluding international agreements with relevant partners is one of the regulatory policy tools that work towards fostering foreign expansion of national companies.[3] An international investment agreement (IIA) signals to

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[1] *See* Andreas F. Lowenfeld, *Investment Agreements and International Law*, 42 COLUM. J. TRANSNAT'L L. 123, 127 (2003); *see also* K. Scott Gudgeon, *United States Bilateral Investment Treaties: Comments on Their Origin, Purposes, and General Treatment Standards,* 4 INT'L TAX & BUS. LAW. 105, 133 (1986); *See also* Julien Chaisse & Chistian Bellak, *Navigating the Expanding Universe of Investment Treaties—Creation and Use of Critical Index*, 18 J. INT'L ECON. 79 (2015). For the most recent statistics and economic trends, see United Nations Conference on Trade and Development, Geneva, Switzerland, Global Investment Trends Monitor No. 20, U.N. Doc. UNCTAD/WEB/DIAE/IA/2015/3 (June 5, 2015).

[2] For an overview, see ANDREAS F. LOWENFELD, INTERNATIONAL ECONOMIC LAW 391–414 (1st ed. 2002).

[3] *See* Jeswald W. Salacuse, *BIT by BIT: The Growth of Bilateral Investment Treaties and Their Impact on Foreign Investment in Developing Countries*, 24 INT'L LAW 655, 655 (1990). See also Daniel R. Sieck, *Confronting the Obsolescing Bargain: Transacting Around Political Risk in Developing and Transitioning Economies Through Renewable Energy Foreign Direct Investment,* 33 SUFFOLK TRANSNAT'L L. REV. 319, 326 (2010).

investors a favorable investment environment and provides them with guarantees that entities receiving their capital will benefit from adequate regulatory conditions in their business operations.[4]

The main purpose of IIAs is to ensure a stable and predictable environment for investment by providing investor protection (including via relative and absolute standards, as discussed below) and ensuring access to arbitration if a treaty obligation is breached.[5] As a result, IIAs interest all members of the international investment community.[6] Capital-exporting countries use these rules to seek investment opportunities abroad and to protect their investments in foreign jurisdictions.[7] Capital-importing nations use these rules to attract foreign investment by offering a stable business

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[4] For further information on the impact of these treaties on foreign direct investment (FDI) flows, see Julien Chaisse & Christian Bellak, *Do Bilateral Investment Treaties Promote Foreign Direct Investment? Preliminary Reflections on a New Methodology*, 3 TRANSNAT'L CORP. REV. 3–10, (2011). *See also* Jennifer M. Lee, *The Fervor for Foreign Direct Investment: China Becomes Key Player*, 30 INT'L TRADE REP. 1385 (2013); Jeswald W. Salacuse & Nicholas P. Sullivan, *Do BITs Really Work?: An Evaluation of Bilateral Investment Treaties and Their Grand Bargain*, 46 HARV. INT'L L.J. 67–69, 76 (2005). The United States Trade Representative's office recognized the goals of the United States Bilateral Investment Treaties Program to be the protection of United States investment abroad, the encouragement and adoption in foreign countries of policies that treat private investment fairly; and supporting the development of international law standards that are consistent with the stated goals. Jeffrey Lang, *Keynote Address*, 31 CORNELL INT'L L.J. 455, 457 (1998).

[5] Along with an increase in number of IIAs, the last decade has also witnessed an exponential surge in investment disputes between foreign investors and host country governments. Arbitral panels are charged with the task of applying the rules of IIAs in specific cases, an often complex process given the broad and sometimes ambiguous terms of these arrangements. *See generally* Kenneth J. Vandevelde, *A Brief History of International Investment Agreements*, 12 U.C. DAVIS J. INT'L L. & POL'Y 157, 173–75 (2005) (noting that foreign investors are increasingly resorting to the mechanism of international arbitration for resolving their disputes with the government of a host country). On the emerging issue of sovereign debt restructure by international Tribunals, *see* Julien Chaisse*, Greek debt restructuring, Abaclat v. Argentina and investment treaty commitments: the impact of international investment agreements on the Greek default, in* INTERNATIONAL ECONOMIC LAW AFTER THE GLOBAL CRISIS – A TALE OF FRAGMENTED DISCIPLINE 306 (Chin Leng Lim & Bryan Mercurio eds., 2015).

[6] *See generally* Zachary Elkins et al., *Competing for Capital: The Diffusion of Bilateral Investment Treaties, 1960-2000*, 2008 U. ILL. L. REV. 265, 269 n.19 (2008). *See* also Julien Chaisse, *Exploring the Confines of International Investment and Domestic Health Protections – Is a General Exceptions Clause a Forced Perspective?*, 39 AM. J.L. & MED. 332 (2013).

[7] *See* RUDOLF DOLZER & CHRISTOPH SCHREUER, *Principles of International Investment Law* 22 (2008) ("[T]he purpose of investment treaties is to address the typical risks of a long-term investment project, and thereby to provide for stability and predictability in the sense of an investment-friendly climate.").

environment in conformity with high international standards.[8]

Germany and Pakistan signed the very first bilateral investment treaty (BIT) in 1959; since then BITs have been one of the most popular and widespread forms of IIAs.[9] Since IIAs play a significant role in the economic development of all countries,[10] they have considerably expanded in number and type, creating their own specific and dynamic branch of international economic law.[11] The core of foreign investment is based on BITs[12] and, increasingly, on preferential trade agreements (PTAs).[13]

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[8] *Id.* at 22.

[9] Stephen M. Schwebel, *The Influence of Bilateral Investment Treaties on Customary International Law*, 98 PROC. ANN. MEETING (AM. SOC. INT'L L. PROC.) 27 (2004).

[10] U.N. CONFERENCE ON TRADE AND DEVELOPMENT (UNCTAD), DEVELOPMENT AND GLOBALIZATION: FACTS AND FIGURES 23–37 (2004), http://unctad.org/en/Docs/gdscsir20041c2_en.pdf (last accessed July 16, 2015). *See also* UNCTAD, *World Investment Report 2006 - FDI from Developing and Transition Economies: Implications for Development* 2006 (UNCTAD: New York & Geneva 2007); UNCTAD, *World Investment Report 2012: Towards a New Generation of Investment Policies* (UNCTAD: New York & Geneva 2013).

[11] Since NAFTA's entry into force, there has been an explosion in the number of IIAs that involve many countries. IIAs have existed primarily between developed and developing countries to protect the formers' investors. *See* LOWENFELD*, supra* note 2, at 554–564 (discussing the restrictions on government action regarding foreign investment included in bilateral investment treaties). However, in the last decade, there has been a growing number of IIAs concluded between developing countries, characterizing the evolution of emerging economies and the ascendancy of sovereign wealth funds. *See* Julien Chaisse, Debashis Chakraborty, & Jaydeep Mukherjee, *Emerging Sovereign Wealth Funds in the Making: Assessing the Economic Feasibility and Regulatory Strategies*, 45 J. WORLD TRADE 837 (2011).

[12] A BIT is a treaty between two states that ensures that investors of a state-party receive certain standards of treatment when investing in the territory of the other state-party. Jose E. Alvarez, *Empire, Contemporary Foreign Investment Law: An "Empire of Law" or the "Law of Empire"?*, 60 ALA. L. REV. 943, 957–959 (2009). The purpose of the BIT is to encourage FDI between the two state-parties, which hopefully leads to economic growth for both state-parties.

[13] In this paper, we use the term BITs in reference to international instruments specifically devoted to the promotion and protection of foreign investment. PTAs are meant to denote all bilateral, regional, or plurilateral arrangements that seek the preferential liberalization of investment flows, along with trade in goods and in services. PTAs also often provide rules on other areas, such as intellectual property, competition, and movement of natural persons. Both BITs and PTAs with investment disciplines are encompassed under the broader terms of IIAs. Not all PTAs deal with the protection of direct investments (as such, and not as services); direct investment matters are often included in a separate chapter of the PTA. The North American Free Trade Agreement (NAFTA) is a prime example of a PTA. Chapter XI of NAFTA is devoted to the promotion and protection of foreign investments. The Trans-Pacific Partnership (TPP) is another example of ambitious trade pact including investment matters. On the TPP, see Julien Chaisse, *The Regulation of Investment in the Transpacific Partnership—Towards a Defining International Agreement for the Asia-Pacific*

Currently, more than 2,926 BITs, involving a considerable number of jurisdictions, have been signed[14]. The annual growth rate peaked in 1996 with almost 200 IIAs signed in a single year; in 2013 there were almost 50 new IIAs.[15] Further, over 300 bilateral and regional PTAs have been signed, with 12 new PTAs signed in 2014.[16] The number of PTAs doubled between the years 2003 and 2014.[17] In total, there are now more than 3,240 IIAs, constituting a decentralized and somewhat "chaotic" global regime for foreign investment which leaves ample room for corporate structuring and restructuring aimed at maximizing the benefits of available treaties.[18]

The globalization of trade and investment profoundly affects the

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Region, in THE REGIONALIZATION OF INVESTMENT TREATY ARRANGEMENTS—DEVELOPMENTS AND IMPLICATIONS 270 (N. Jansen Calamita & Mavluda Sattorova eds., 2015). These separate investment chapters in PTAs are comparable, on average, to self-standing BITs. They can include both rules on investment liberalization (non-discrimination safeguards) and investment protection (substantive standards of treatment afforded by the host state to the foreign investor or investment). UNCTAD (2014). World Investment Report 2014: Investing in the SDGs: An Action Plan. New York and Geneva: United Nations at 22–25.

[14] UNCTAD, *World Investment Report 2015: Reforming International Investment Governance*. New York and Geneva: U.N. (UNCTAD/WIR/2015), at 106–110, http://unctad.org/en/pages/PublicationWebflyer.aspx?publicationid=1245.

[15] *Id.*

[16] *Id.*

[17] According to UNCTAD, the PTAs concluded in 2014 "can be grouped into three broad categories: [s]even agreements with BIT-equivalent provisions. The Australia–Japan EPA, the Australia–Republic of Korea FTA, the Canada–Republic of Korea FTA, the Japan–Mongolia EPA, the Mexico–Panama FTA, the Additional Protocol to the Framework Agreement of the Pacific Alliance (between Chile, Colombia, Mexico and Peru), and the Treaty on Eurasian Economic Union (between Armenia, Belarus, Kazakhstan and the Russian Federation) fall in the category of IIAs that contain obligations commonly found in BITs, including substantive standards of investment protection and ISDS. Three agreements with limited investment provisions. The European Union– Georgia Association Agreement, the European Union–Republic of Moldova Association Agreement and the European Union–Ukraine Association Agreement fall in the category of agreements that provide limited investment related provisions (e.g., national treatment with respect to commercial presence or free movement of capital relating to direct investments). Two agreements with investment cooperation provisions and/or a future negotiating mandate. The ECOWAS–United States of America Trade and Investment Framework Agreement (TIFA), and the Malaysia–Turkey FTA contain general provisions on cooperation in investment matters and/or a mandate for future negotiations on investment." UNCTAD, Recent Trends in IIAs and I, IIA Issues Note No. 1, February 2015 http://unctad.org/en/ PublicationsLibrary/webdiaepcb2015d1_en.pdf. *See also* the World Trade Organization, Regional Trade Agreements Information System (RTA-IS,) http://rtais. wto.org/UI/PublicMaintainRTAHome.aspx. NB: Search "by criteria" with "topics covered" being "investment."

[18] *See* Julien Chaisse, *Intellectual Property Rights, The Treaty Shopping Practice: Corporate Structuring and Restructuring to Gain Access to Investment Treaties and Arbitration*, 11 HASTINGS INT'L Bus. L.J. 225 (2015).

practices and policies of international taxation. Tax advisors, tax professors and government tax officials increasingly operate in a multinational world in which possessing knowledge of only domestic rules is inadequate. Increasingly even having knowledge of international tax law is not sufficient to understand the challenges faced by investors making investments across borders. This article focuses on the impact of the international law of foreign investment on tax issues with a view to assessing the interactions between the two regimes and identifying potential signs of convergence. More precisely, this article identifies all of the investment disputes, which have dealt with tax issues with a view to assessing the role played by investment treaties in the regulation of national tax policies. This article demonstrates that both international investment law and investment arbitration, although not originally designed for such a purpose, already contribute to the regulatory framework applicable to tax policies. On a theoretical level, the article identifies areas of overlap between the tax and investment regimes. On a more practical level, it also identifies the provisions of investment treaties, which national policy makers should observe and comply with in order to avoid investment arbitration.

Part II of this article provides an understanding of the convergence between investment law and tax issues. This aids in an understanding of the key characteristics of IIAs (such as the definition of investment and the use of specific tax exceptions) and the relationship between currently existing IIAs and tax disputes. Part III analyzes, both quantitatively and qualitatively, the recent trends of tax disputes in investment arbitration. Part IV discusses future prospects for tax disputes in light of the key breaches of investment treaties. Part V concludes.

II. WHEN FOREIGN INVESTMENT MEETS TAX

IIAs are very different from Double Taxation Avoidance Agreements (DTAAs). DTAAs allocate taxing jurisdiction between the source and residence countries.[19] Wherever such jurisdiction is given to both countries,

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[19] It is not unusual for a business or individual who is resident in one country to make a taxable gain (earnings, profits) in another. This person may find that he is obliged by domestic laws to pay tax on that gain locally and pay again in the country in which the gain was made. Since this is inequitable, many nations make bilateral double taxation agreements with each other. In some cases, this requires that tax be paid in the country of residence and be exempt in the country in which it arises. In the remaining cases, the country where the gain arises deducts taxation at source (withholding tax) and the taxpayer receives a compensating foreign tax credit in the country of residence to reflect the fact that tax has already been paid. To do this, the taxpayer must declare himself (in the foreign country) to be non-resident there. Therefore, the second aspect of the agreement is that the two taxation authorities exchange information about such declarations so they may investigate any

the agreements prescribe the maximum rate of taxation in the source country, which is generally lower than the rate of tax under the domestic laws of that country. Double taxation in such cases is avoided by the residence country agreeing to give credit for tax paid in the source country, thereby reducing the tax payable in the residence country by the amount of tax paid in the source country. In contrast, IIAs are not intended to impose tax reductions, exemptions, or any other measures to reduce double taxation.

Nonetheless, IIAs may play an important role in tax matters. The basic question to ask in determining whether investment treaties are applicable to tax matters is whether a given investment subject to a national tax regime constitutes a "foreign investment" within the meaning of international law. In the affirmative, the existence of an investment will trigger the application of an IIA, which provides a normative framework for assessing the validity of the foreign treatment in the host state, including the treatment in terms of taxation.

Part II.A discusses the notion of foreign investment and the role of potential tax exceptions in IIAs. Part III.B reviews the recent trends in the investment arbitration. Under IIAs, investors from one state party can seek financial compensation from another state party to the agreement for failure to comply with treaty obligations through binding arbitration.[20]

A. The Notion of Foreign Investment in IIAs

1. Subjection of Foreign Investment to Domestic Tax Regime

The investment concept is not a generally accepted definition and it is constantly changing as a result of the emergence and development of new forms of investment by entrepreneurs, financiers, and multinational companies.[21] In the absence of a generally accepted investment definition, as part of a BIT, such a definition will be unique and specific to each treaty, and hence of paramount importance as the meaning of investment will determine the application of all of the other provisions enshrined in the

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anomalies that might indicate tax evasion. While individuals or natural persons can have only one residence at a time, corporate persons, owning foreign subsidiaries, can be simultaneously residents of several countries. Control of unreasonable tax avoidance of corporations becomes more difficult and requires the investigation of the transfer pricing set for transfers of goods, intellectual property rights, and services among corporate subsidiaries.

[20] *See* Michael O'Reilly, *A Fresh Look at Arbitration Appeals*, 80 ARBITRATION 82, 82–91 (2014).

[21] The changing nature of the "investment" concept has also led to complexity and contradiction in the regulatory approaches. *See* Ramon Torrent, *The Contradictory Overlapping of National, EU, Bilateral, and the Multilateral Rules on Foreign Direct Investment: Who is Guilty of Such a Mess*, 34 FORDHAM INT'L L.J. 1378–1399 (2011).

treaty. In addition to the investment definition, it is also necessary to review the possible effect of tax exceptions.[22]

a. The Broad-encompassing Notion of "Investment"

Very often, IIAs adopt a broad definition of "investment" that refers to "every kind of asset" of a foreign investor in a host country, suggesting that any economic value is covered by the agreement.[23] This asset-based definition is usually followed by an illustrative list of assets covered. Alternatively, some IIAs that have been concerned primarily with foreign direct investment (FDI) have focused on foreign investment in an "enterprise" rather than in a variety of assets.[24] This enterprise-based definition gives attention to the investor's objective of establishing a long-term relation with the economy of the host country through the acquisition of a meaningful interest in the ownership or control of a company.

The term "every kind of asset" actually sets an open-ended definition, one which is typically followed by an illustrative list of assets that are expressly covered by the agreement.[25] The categories covered by most BITs remain substantially identical, namely: (a) movable and immovable property and other property rights; (b) interests in the property of companies; (c) claims to money and claims to a performance; (d) intellectual property rights, and (e) concession rights conferred by law or contract.[26]

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[22] However, the Article does not discuss the issue of whether tax authority decisions can trigger state responsibility (and hence action under investment treaties) as this legal issue does not raise a major difficulty. In this respect, one should be reminded that the *Oostergetel v. Slovak Republic* Final Award holds that the tax authority is a state organ. Jan Oostergetel and Theodora Laurentius v. Slovak Republic, UNCITRAL, Final Award, 152 (Apr. 23, 2012).

[23] *See* Richard J. Hunter, *Property Risks in International Business*, 15 INT'L TRADE L.J. 23, 26–28 (2006) (distinguishing foreign direct investment from passive portfolio investments not involving control). *See also* Emmanuelle Cabrol, Walid Ben Hamida and Ferhat Horchani, *International Investments - Law and Practice*, 6 INT'L BUS. L.J. 796 (2008) (observing that although investment treaties are primarily aimed at protecting property and economic values, they do not exclude, in exceptional circumstances, compensation in moral damages, to legal as well as natural persons). *See also* Julien Chaisse, *Promises and Pitfalls of the European Union Policy on Foreign Investment —How Will the New EU Competence on FDI Affect the Emerging Global Regime*, 15 J. INT'L ECON. L. 51, 57–58 (2012).

[24] *See* Céline Lévesque, *Abaclat and Others v. Argentine Republic: The Definition of Investment*, 27 ICSID REV. 247, 252 (2012). *See also* Stephan W. Schill, *Enhancing International Investment Law's Legitimacy: Conceptual and Methodological Foundations of a New Public Law Approach*, 52 VA. J. INT'L L. 57 (2011-2012).

[25] *See* Céline Lévesque, *Abaclat and Others v. Argentine Republic: The Definition of Investment*, 27 ICSID REV. 247, 253 (2012).

[26] *See, e.g.*, Agreement Between the Government of the United Kingdom of Great Britain and Northern Ireland and the Government of the Republic of Argentina for the

Today, there is no doubt that the notion of foreign investment covers both tangible and intangible assets.[27] For instance, water sanitation and water services provided through facilities invested in by foreigners (tangible assets) but also the research and development to create new technologies (intangible assets) are "investment" within the meaning of international law.

To sum up, the meaning of "investment" in international law is very broad, which explains the great scope of application of these international norms. At the same time, "foreign investment" is protected, in principle, with respect to all types of treatment adopted by the host state, which brings tax under the umbrella of investment treaties.

b. The Diversity of Tax Exceptions in Investment Treaties

Control over taxation matters is essential to sovereign states and, as such, states' fiscal policies are typically excluded from IIAs' scope of application. However, one should not believe that tax measures escape the purview of investment arbitrators so easily. In actuality, the regime of exception that may apply to tax matters is rather complex and often misunderstood.

This article clarifies the understanding of the tax exception regime by establishing a double preliminary distinction since some treaties differentiate direct and indirect taxes measures and often only subject the latter to the disciplines of the investment treaty; while other treaties rely on different exceptions which can general exceptions, limited to NT and MFN, limited to FET or combination of all these.

Promotion and Protection of Investments, U.K.-Arg., art. 1, Dec. 11, 1990, 1765 U.N.T.S. 33. See also CHESTER BROWN, COMMENTARIES ON SELECTED MODEL INVESTMENT TREATIES 1024 (Oxford, UK: Oxford University Press 2013).

[27] For instance, the tribunal in the *Tidewater v. Venezuela* Award found, as the treaty confirms, that the rights subject of an expropriation are "capable of including goodwill and know-how as well as other tangible and intangible assets, including contractual rights." *See* Tidewater Investment SRL and Tidewater Caribe, C.A. v. Bolivarian Republic of Venezuela, ICSID Case No. ARB/10/5, Award, ¶ 118 (Mar. 13, 2015). Also, the tribunal in Nova Scotia Power v. Venezuela II Excerpts of Award considers that, "[a] contractual right by its very nature has no fixed abode in the physical sense, for it is intangible; however, a lack of physical presence is not *per se* fatal to meeting the territoriality requirement." The tribunal decides that "a further enquiry regarding economic development may be appropriate as intangible assets are frequently aligned with economic development (e.g., fund raising) by a host State." *See* Nova Scotia Power Inco. v. Bolivarian Republic of Venezuela, ICSID Case No. ARB(AF)/11/1, Excerpts of Award, ¶ 130 (Apr. 30, 2014).

TABLE 1. TYPOLOGY OF TAX EXCEPTION IN INVESTMENT TREATIES

TYPE OF EXCLUSION	EXAMPLES	LEGAL EFFECT
General exclusion	"The provisions of this Agreement shall not apply to matters of taxation in the area of either Contracting Party. Such matters shall be governed by the domestic laws of each Contracting Party and the terms of any agreement relating to taxation concluded between the Contracting Parties." Agreement between the Government of Hong Kong and the Government of New Zealand for the Promotion and Protection of Investments, H.K.-N.Z., art. 8.2, July 6, 1995, 1889 U.N.T.S. 333.	Such a provision excludes tax matters from the treaty scope of application without any reservation. It is impossible to bring a tax-related disputes before an investment tribunal on the ground of such a treaty.
Conflict clauses in favour of tax treaties application	"Nothing in this Agreement shall affect the rights and obligations of either Contracting Party derived from any tax convention. In the event of any inconsistency between the provisions of this Agreement and any tax convention, the provisions of the latter shall prevail." Agreement between the Government of the United Mexican States and the Government of the Republic of Korea for the Promotion and Reciprocal Protection of Investments, S. Kor.-Mex., art. 3:3, Nov. 14, 2000, 2281. U.N.T.S. 61.	A clause providing priority of taxation treaties over the investment treaty can clarify that investment treaties still applies to taxation, but to the extent that is covered by taxation treaties, the latter shall prevail.
Specific and explicit exclusion based on the distinction between the type of taxes (direct and indirect taxes)	"Subject to paragraph 7, Article 3 and Article 4 shall apply to all taxation measures, other than taxation measures relating to direct taxes (which, for purposes of this paragraph, are taxation measures on income, capital gains, or on the taxable capital of corporations or individuals, taxes on estates, inheritances, gifts, and generation-skipping transfers), except that nothing in those Articles shall apply: (a) any most-favored-nation obligation with respect to an advantage accorded by a Party pursuant to a tax convention; (b) to a non-conforming provision of any existing taxation measure; (c) to the continuation or prompt renewal of a non-conforming provision of any existing taxation measure; (d) to an amendment to a non-conforming provision of any existing taxation measure to the extent that the amendment does not decrease its conformity, at the time of the amendment, with those Articles . . . ." Treaty	This type of provision restricts treaty application to limited types of taxes. It is also noteworthy to mention that few investment treaties introduce such a distinction which indirectly clarifies the meaning of taxation measure.

	Between the United States of America and the Oriental Republic of Uruguay Concerning the Encouragement and Reciprocal Protection of Investment, U.S.-Uru., Art. 21, Nov. 4, 2005, T.I.A.S. No. 06-1101.	
Tax veto to expropriation case	"Article VIII (Expropriation) may be applied to a taxation measure unless the taxation authorities of the Contracting Parties, no later than six months after being notified by an investor that he disputes a taxation measure, jointly determine that the measure is not an expropriation." Agreement Between the Government of Canada and the Government of Romania for the Promotion and Reciprocal Protection of Investments, Can.-Rom., art. VII:4, May 8, 2009, Global Affairs of Canadahttp://www.treaty-accord.gc.ca/text-texte.aspx?id=105170.	Investment treaties can grant the national tax authorities the competence to 'veto' a complaint by an investor alleging expropriation arising from a taxation measure by the host state.
Specific and explicit exclusion to the non-discrimination standards (NT and/or MFN standards)	"Article 4 of this Agreement shall not be construed so as to oblige one Contracting Party to extend to the investors of the other Contracting Party the benefit of any treatment, preference or privilege resulting from: . . . (b) any international agreement or arrangement relating wholly or mainly to taxation or any domestic legislation relating wholly or mainly to taxation. Nothing in this Agreement shall affect the rights and obligations of either Contracting Party derived from any international agreement or arrangement relating wholly or mainly to taxation to which either Contracting Party is a party. In the event of any inconsistency between the provisions of this Agreement and any such agreement or arrangement, the provisions of the latter shall prevail." Agreement Between the Government of the United Kingdom of Great Britain and Northern Ireland and the Government of the United Mexican States for the Promotion and Reciprocal Protection of Investment, Mex.-U.K., art. 5, May 12, 2006, U.K. GOV., https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/273286/6860.pdf.	Such a provision excludes the application of both NT and MFN from treatments resulting from 'any matter' related to taxation
Specific and explicit exclusion to fair and	NAFTA (1995) Article 2103(1) stipulates that "[e]xcept as set out in this Article, nothing in this Agreement shall apply to taxation measures'. . . . 'Articles 1102 and 1103 [i.e., NT and MFN] . . .	In this connection, since there is no explicit reference to FET, the tax measures are excluded

equitable treatment	shall apply to all taxation measures,' and 'Article 1106(3), (4) and (5) [i.e., Performance Requirements] shall apply to taxation measures." North American Free Trade Agreement, art. 2103.1, Can.-Mex.-U.S., Dec. 17, 1992, 32 I.L.M. 289 (1993).	from consideration in the context of Article 1105. Treaties can also exclude the application of the obligation of fair and equitable treatment on taxation measures.
Combination of diverse exceptions within exclusion	"Except as set out in this Article, nothing in this Agreement shall apply to taxation measures. Nothing in this Agreement shall affect the rights and obligations of the Contracting Parties under any tax convention. In the event of any inconsistency between the provisions of this Agreement and any such convention, the provisions of that convention shall apply to the extent of the inconsistency. Subject to paragraph 2, a claim by an investor that a tax measure of a Contracting Party is in breach of an agreement between the central government authorities of a Contracting Party and the investor concerning an investment shall be considered a claim for breach of this Agreement unless the taxation authorities of the Contracting Parties, no later than six months after being notified of the claim by the investor, jointly determine that the measure does not contravene such agreement. Article VIII (Expropriation) may be applied to a taxation measure unless the taxation authorities of the Contracting Parties, no later than six months after being notified by an investor that he disputes a taxation measure, jointly determine that the measure is not an expropriation. If the taxation authorities of the Contracting Parties fail to reach the joint determinations specified in paragraphs 3 and 4 within six months after being notified, the investor may submit its claim for resolution under Article XIII (Settlement of Disputes between an Investor and the Host Contracting Party)." Agreement Between the Government of Canada and the Government of Romania for the Promotion and Reciprocal Protection of Investments, Can-Rom., art. VII, May 8, 2009, GLOBAL AFFAIRS CANADA, http://www.treaty-accord.gc.ca/text-texte.aspx?id=105170.	All types of exclusion do not preclude each other. In fact, some IIAs combine several exceptions within the exclusion, resulting in a complex structure, which requires careful scrutiny to identify the scope of application.

Source: compiled by the author

One group of IIAs distinguishes between direct and indirect tax measures when it comes to crafting exceptions. A key example is the North American Free Trade Agreement (NAFTA) Article 2103.1, which states that "[e]xcept as set out in this Article, nothing in this Agreement shall apply to taxation measures."[28] The same NAFTA article further confirms that exceptions to national treatment (NT) and most favored nation (MFN) treatment relating to tax matters shall explicitly apply to "all taxation measures, other than those on income, capital gains or on the taxable capital of corporations, taxes on estates, inheritances, gifts and generation-skipping transfers and those taxes listed in paragraph 1 of Annex 2103.4"[29] It is explicit that exceptions will apply to direct taxes, while indirect taxes will not be subject to these exceptions. As a result, indirect taxes are regulated by the NAFTA substantive provisions on investment.

In the same vein, exceptions to national treatment and most favored nation treatment relating to tax matters are also contained in the United States and Canadian Models. Article 21 of the U.S. Model provides that, except as provided in Article 21 (which only addresses obligations on expropriation and performance requirements), "nothing in Section A shall impose obligations with regard to taxation measures,"[30] and in case "of any inconsistency between the Model and any tax convention, that convention shall prevail to the extent of the inconsistency."[31] The Canadian Model follows a very similar approach in Article 16.[32]

Another group of treaties does not establish a difference between direct and indirect tax matters. Instead, some of these treaties may, by way of specific exceptions, exclude the application of specific treaty standards to tax matters. The Norway Model of 2008 provides a general exception, stating "[n]othing in this Agreement shall affect the imposition, enforcement or collection of direct or indirect taxes imposed by a Party."[33] The Norwegian approach explicitly excludes tax matters from the coverage of investment treaties and investment arbitration.[34] Exceptions to tax

[28] North American Free Trade Agreement, art. 2103.1, Can.-Mex.-U.S., Dec. 17, 1992, 32 I.L.M. 289 (1993).

[29] *Id.* at 2103.4.

[30] 2012 U.S. Model Bilateral Investment Treaty, art. 21, https://ustr.gov/sites/default/files/BIT%20text%20for%20ACIEP%20Meeting.pdf.

[31] *Id.*

[32] Canada 2004 Model BIT, http://www.italaw.com/investment-treaties. However, it also adds, "Nothing in this Agreement shall be construed to require a Party to furnish or allow access to information the disclosure of which would be contrary to the Party's law protecting information concerning the taxation affairs of a taxpayer." *Id.* at art. 16.2.

[33] Norway 2008 Model BIT, http://www.italaw.com/sites/default/files/archive/ita1031.pdf.

[34] Article 28.3 of the Norway Model BIT states that "[a]ny dispute as to whether

matters can also be crafted in such a manner that they only apply to specific investment standards such as NT and MFN.[35] Actually, most IIAs allows parties to discriminate in the way they design tax rules and policies. In this respect, the French Model of 2006 provides that "[t]he provisions of this article (national treatment and most favored nation treatment) do not apply to tax matters."[36] In a slightly different manner, the German Model specifies that "the treatment granted under this article shall not relate to advantages which either Contracting States accords to investors of third States by virtue of a double taxation agreement or other agreement regarding matters of taxation."[37] Once again, this has the effect of allowing Germany to discriminate between nationals and foreigners or among foreigners in tax policy matters.[38]

If the treaty does not incorporate such an exception to NT and MFN, it must be assumed to impose the non-discrimination principles to tax policies. Furthermore, certain treaties explicitly specify the application of a substantive standard (such as the fair and equitable treatment) to tax matters. In this respect, the U.S.-Ecuador BIT "exhorts both countries to provide fair and equitable treatment to investors with respect to tax policies. However, tax matters are generally excluded from the coverage of the prototype BIT, based on the assumption that tax matter are properly

paragraphs 1 and 2 apply, may only be brought before the Competent Tax Authorities of the Parties according to the procedure of Article [The Joint Committee] or the national courts or appeal organs of a Party, and shall not be covered by Section [Dispute Settlement Provisions] of this Agreement." Norway 2008 Model BIT, art. 28.3, http://www.italaw.com/sites/default/files/archive/ ita1031.pdf.

[35] The tribunal in *Occidental Exploration v. Ecuador*, Final Award, states that "the purpose of national treatment is to protect investors as compared to local producers, and this cannot be done by addressing exclusively the sector in which the particular activity is undertaken." Occidental Exploration and Production Company v. Republic of Ecuador, LCIA Case No. UN3467, Final Award, 1 July 2004 at ¶ 173. More specifically, the tribunal in *Champion v. Egypt*, Award, analyzes national treatment by: (i) determining whether the parties involved were in like situations, and (ii) comparing the treatment received by foreign investments with the treatment received by local investors. Champion Trading Company and Ameritrade International, Inc. v. Arab Republic of Egypt, ICSID Case No. ARB/02/9, Award, 27 October 2006 at ¶ 128. In any event, as discussed in *Bogdanov v. Republic of Moldova*, "discrimination can take many different forms. In the context of the treatment of foreign investments, however, a very frequent problem is discrimination on the basis of nationality." See Yuri Bogdanov and Yulia Bogdanov v. Republic of Moldova, SCC Case No. V091/2012, Final Award, 16 April 2013 at 215.

[36] *See* France 2006 Model BIT, Art. 4:4, 5, http://www.italaw.com/investment-treaties.

[37] German 2008 Model BIT, http://www.italaw.com/investment-treaties.

[38] The Korea–Japan BIT follows a similar approach. *See* Agreement Between the Government of Japan and the Government of the Republic of Korea for the Liberalization, Promotion and Protection of Investment, Japan-S. Kor., art. 19, Mar. 22, 2002, http://www.mofa.go.jp/policy/treaty/submit/session154/agree-6-1.pdf.

covered in bilateral tax treaties."[39] Similarly, the Japan-Korea BIT stipulates that "[n]othing in this Agreement shall apply to taxation measures except as expressly provided in paragraphs 2, 3 and 4 of this Article," which provides an exception for NT and MFN.[40] However, the same treaty says that "Articles 1, 3, 7, 10, 22 and 23 shall apply to taxation measures," covering definitions, NT in access to justice, transparency, FET and expropriation, sub-national authorities, and the date of commencement of the treaty respectively.[41]

These exceptions do exist but are not present in all treaties. As a result, those treaties that do not exclude tax from the scope of application may apply to tax issues and generate tax disputes under investment treaties.

In terms of interpretation, investment tribunals have developed specific approaches to the interpretation of taxation exclusions which reflect the unique regime created by these exceptions. The *Occidental Exploration v. Ecuador* Final Award interprets a taxation provision to permit claims based on the BIT's fair and equitable treatment (FET) standard.[42] The *Pan American Energy v. Argentina* case disagrees with the approach taken in *Occidental Exploration v. Ecuador*.[43] Importantly, the *Burlington*

[39] Investment Treaty with the Republic of Ecuador, Ecuador-U.S., art. X.1., Aug. 27, 1993, Senate Treaty Doc. 103-15, http://www.state.gov/documents/organization/ 43558.pdf.

[40] Agreement Between the Government of Japan and the Government of the Republic of Korea for the Liberalization, Promotion and Protection of Investment, Mar. 22, 2002, Japan-S. Kor., art. 19, http://www.mofa.go.jp/policy/treaty/submit/session 154/agree-6-1.pdf.

[41] *Id.* The BIT between Laos and Japan provides the same type of regime stating, "1. Nothing in this Agreement shall apply to taxation measures except as expressly provided for in paragraphs 2, 3 and 4 of this Article; 2. Article 1, paragraph 1 of Article 5, Articles 6, 9, 12, 25 and 27 shall apply to taxation measures." Agreement Between Japan and the Lao People's Democratic Republic for the Liberalization, Promotion and Protection of Investment, Japan-Laos, art. 22, Jan. 16, 2008, http://www.mofa.go.jp/ region/asia-paci/laos/ agree0801.pdf.

[42] The tribunal stated, "The first is that concerning fair and equitable treatment in tax matters. The Tribunal notes that the reference in paragraph 1 of Article X to 'strive to accord fairness and equity' in respect of tax policies concerning the treatment of the investment by the host country is not devoid of legal significance. It imposes an obligation on the host State that is not different from the obligation of fair and equitable treatment embodied in Article II, even though admittedly the language of Article X is less mandatory. This legal effect is not derogated from by the 'nevertheless' proviso with which paragraph 2 opens, as this expression cannot be read to mean that in respect of tax policies the host State could pursue an unfair or inequitable treatment. It only means that such obligation is concerned with the three categories of tax matters therein listed, that is, expropriation, transfers and the observance and enforcement of an investment agreement or authorization." Occidental Exploration and Production Company v. Republic of Ecuador, LCIA Case No. UN3467, Final Award, 1, 24–25 (Jul. 1, 2004).

[43] Pan American Energy LLC and BP Argentina Exploration Company v. Argentine

Resources v. Ecuador case holds that under Article X of the BIT, "matters of taxation" are as a rule excluded from the scope of the treaty and examines the claims advanced by claimant individually in order to ascertain whether the taxation law is challenged or not with respect to each claim.[44] Also, the *Nations Energy v. Panama* case interprets the BIT to exclude claims stemming from taxation matters based on the FET standard.[45] Finally, in a very straightforward manner, the *Quasar de Valors v. Russia* Award on Preliminary Objections notes that a taxation exclusion cannot provide a loophole to escape the central undertakings of investor protection. Complaints about types and levels of taxation are one thing; complaints about abuse of the power to tax are something else.[46]

B. Explaining the Multiplication of Tax Disputes before Investment Tribunals

Most agreements allow the foreign investor to choose the venue for arbitration. Ad hoc arbitration allows the parties to agree on the procedural rules to the dispute, although countries commonly rely on the established United Nations Commission on International Trade Law (UNCITRAL) arbitration rules. The parties may also submit to organizations that provide a venue and have developed their own arbitral procedures. The International Centre for Settlement of Investment Disputes (ICSID), established in 1967

Republic and BP America Production Company, Pan American Sur SRL, Pan American Fueguina, SRL and Pan American Continental SRL v. Argentine Republic, ICSID Case No. ARB/03/13 & ARB/04/8, Decision on Preliminary Objections, 1, 46 (Jul. 27, 2006).

[44] Burlington Resources Inc. v. Republic of Ecuador, ICSID Case No. ARB/08/5, Decision on Jurisdiction, 1, 28, 200–208, 211, 215 (Jun. 2, 2010).

[45] Nations Energy, Inc. and Others v. Republic of Panama, ICSID Case No. ARB/06/19, Award, 1, 39 (Nov. 24, 2010) [Spanish].

[46] The Tribunal explained that "Russia also argues preliminarily that the Danish BIT is automatically excluded from application here because it states in Article 11(3): 'The provisions of this Agreement shall not apply to taxation.' The present claimants could therefore not have proceeded even if they were Danish investors because they complain precisely of tax measures taken with respect to Yukos. This argument was not pursued with great insistence. Nor should it have been. The claimants allege that Russia imposed a bogus reassessment of taxes in order to effect a spoliation of Yukos assets. To think that ten words appearing in a miscellany of incidental provisions near the end of the Danish BIT would provide a loophole to escape the central undertakings of investor protection would be absurd. Complaints about types and levels of taxation are one thing. Complaints about abuse of the power to tax are something else. A 'decree' to the effect that 'all tax inspectors are henceforth instructed to collect everything they can get their hands on from Danish investors' would not be insulated because of Article 11(3) of the BIT. Abuse and pretext are at the heart of the claimants' allegations. Whether they are true is a matter for the merits." Quasar de Valors SICAV S.A. et al. (Formerly Renta 4 S.V.S.A et al.) v. Russian Federation, SCC Case No. 24/2007, Award on Preliminary Objections, 1, 32 (Mar. 20, 2009).

under the umbrella of the World Bank, specializes in investor–state disputes and is the preferred choice of parties submitting to arbitration, totaling well over half of the investor–state claims brought to date.[47] For the most part, investment agreements feature more than one option for international arbitration.[48] Most investment agreements allow resort to the ICSID and to ad hoc arbitration under the UNCITRAL rules. Some agreements additionally allow a claim to be brought to other institutions, such as the Stockholm Chamber of Commerce or the International Chamber of Commerce. As of now, thirty-two investment claims have dealt with the taxation regime of foreign investments in various economic sectors (Annex 1).

The multiplication of tax disputes before international investment tribunals represents a significant change in the landscape of international investment. It results from two endogenous factors (i.e., those which are inherent to the investment regime) and one exogenous factor (i.e., that which does not come from the investment regime but rather from the limits and shortcomings of the tax regime).

1. Endogenous Factors

In terms of endogenous factors, first, one of the key features of investment protection consists of allowing foreign investors to challenge the host government's actions before an international arbitral court. Domestic judicial systems may be biased against foreign interests, and national courts may come under pressure from other branches of government. The ability of foreign investors to bring their disputes to independent arbitrators provides an extra guarantee that domestic authorities will live up to their international obligations, thereby ensuring a favorable and stable investment climate in the host country. As a matter of fact, in recent years, investors have been increasingly relying on investment treaties. Second, the expansion of foreign investment into an increasing number of types of investments, ranging from infrastructure to sovereign bonds to intellectual property rights, inevitably generates tension with host states that may result

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[47] The United Nations Conference on Trade and Development (UNCTAD) monitors the raise on investor–state disputes and the selected institutions, as well as the main substantial developments in court decisions: "Investors continue to use the investor–State dispute settlement (ISDS) mechanism. In 2014, claimants initiated 42 known treaty-based ISDS cases. With 40 per cent of new cases initiated against developed countries, the relative share of cases against developed countries has been on the rise (compared to the historical average of 28 per cent)." *See* UNCTAD, Recent Trends in International Investment Agreements, IIA Issues Note No. 1, February 2015, http://unctad.org/en/PublicationsLibrary/webdiaepcb2015d1_en.pdf.

[48] Julien Chaisse, *Assessing the Exposure of Asian States to Investment Claims,* 6 COMPTEMP. ASIA ARB. J. 187, 201 (2013).

in disputes that only an arbitral tribunal can resolve. The growing role of international arbitration must be analyzed by looking not only at the types of services currently provided by foreign investors but also at the details of the claims arising from breaches of treaties, which have resulted in large compensatory awards.

2. Exogenous Factors

The right of direct access to international arbitration provided by international investment treaties and BITs is one of the reasons why foreign investors have brought claims based on BITs instead of international tax treaties, which implicitly points out the weaknesses of the tax dispute resolution mechanisms.[49] The dispute resolution mechanism of international tax treaties is usually the Mutual Agreement Procedures (MAPs), but it is only a mutual agreement; the MAPs do not guarantee that an investor can bring a case to international arbitration because arbitration is only supplementary to the MAPs, and investors have to go through a lengthy process to have a case heard by an arbitration tribunal.[50]

For MAPs, Arts. 25 (1) and (2) of the OECD Model Convention provide the regulations on how taxpayers/ investors should proceed during tax disputes.[51] The MAPs state that "the taxpayer may present his matter to the competent authority of the contracting state of which he is a resident . . . [i]f the case is justified, the competent authority has to endeavor to settle the controversy."[52] This procedure is not likely to protect the taxpayer or investor making an impartial claim because it grants the competent authority, i.e., the local tax authority, an absolute power to decide whether to accept or reject the case.[53]

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[49] *See generally* Calvin A. Hamilton & Paula I. Rochwerger, *Trade and Investment: Foreign Direct Investment Through Bilateral and Multilateral Treaties*, 18 N.Y. INT'L L. REV. 11 (2005).

[50] *See* Hugh J. Ault, *Improving the Resolution of International Tax Disputes*, 7 FLA. TAX REV. 137, 140 (2005); UNITED NATIONS: UNITED NATIONS HANDBOOK ON SELECTED ISSUES IN ADMINISTRATION OF DOUBLE TAX TREATIES FOR DEVELOPING COUNTRIES 3 (Alexander Trepelkov, Harry Tonino and Dominika Halka eds., 2013), http://www.un.org/esa/ffd/wp-content/uploads/2014/08/UN_Handbook_DTT_Admin.pdf; *see also* Asif H. Qureshi, *Coherence in the Public International Law of Taxation: Developments in International Taxation and Trade and Investment Related Taxation*, 10 ASIAN J. WTO & INT'L HEALTH L. & POL'Y 193 (2015).

[51] *See* OECD, MODEL CONVENTION WITH RESPECT TO TAXES ON INCOME AND ON CAPITAL, art. 25 (2014), http://www.oecd.org/ctp/treaties/oecd-model-tax-convention-available-products.htm.

[52] *Id.*

[53] *See* Limor Riza, *Taxpayers' Lack of Standing in International Tax Dispute Resolutions: An Analysis based on the Hybrid Norms of International Taxation*, 34 PACE L.

One drawback to the MAPS is that how the tax authority makes the decision to accept or reject the case is not transparent, e.g., the tax authority may reject the case because of the political or diplomatic reasons. The competent authority in some countries may not accept a case for MAPs if the case involves particular issues such as penalties or tax avoidance.[54] Also, the MAPs imposes a relaxed responsibility on the competent authority, who just needs to "endeavor" to settle the controversy but is not "obliged" to settle the dispute.[55] The competent authority just needs to make its best effort to negotiate and find a settlement or solution but is under no obligation to reach a conclusion.[56] The MAPs do not give a right to taxpayers/investors to be treated fairly and be allowed to bring their claims to an impartial institution.[57] When the parties cannot reach a final resolution of their tax disputes, the validity of the applicable international tax treaties or double tax treaties is cast in doubt. The taxpayer/ investor must suffer double taxation, and the inability of the competent authority to resolve the tax dispute may mean there is a limitation to the application of international tax treaties and, therefore, a lack of protection of the investor's legal rights as a national of the contracting state.

Additionally, international tax treaties cannot achieve their objective of resolving issues of double taxation, transfer pricing, etc. under the MAPs because the MAPs fails to determine the allocation of taxes each contracting country should receive.[58] Therefore, predictability and consistency are lacking and the foreign investor can easily lose faith in the MAPs. This may be a reason why more and more international investors put claims in front of international tribunals through the BITs or international investment treaties.

The second important element of the dispute resolution mechanism within international tax treaties or the OECD Model Convention is arbitration. However, unlike the arbitration provisions in BITs, a taxpayer/investor cannot directly access arbitration though tax treaties or the OECD Model Convention; he or she must first go through Arts. 25(1) and (2) of the OECD Model Convention. Also, the arbitration clause is only

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REV. 1068 (2014).

[54] Hugh J. Ault, *Improving the Resolution of International Tax Disputes*, 7 FLA. TAX REV. 137, 140 (2005).

[55] *Id.* at 139; *see also* UNITED NATIONS, MANUAL FOR THE NEGOTIATION OF BILATERAL TAX TREATIES BETWEEN DEVELOPED AND DEVELOPING COUNTRIES 4 (2003), http://www.un.org/esa/ffd/wp-content/uploads/2014/09/UNPAN008579.pdf.

[56] Hugh J. Ault, *Improving the Resolution of International Tax Disputes*, 7 FLA. TAX REV. 137, 139 (2005).

[57] *See generally id.*

[58] *See generally* Susan C. Borkowski, *Electronic Commerce, Transnational Taxation, and Transfer Pricing: Issues and Practices*, 28 INT'L TAX J. 1 (2002).

available for particular matters, such as transfer pricing issues, so its application is limited.

Although there is a trend of expanding the scope of issues which can be put to arbitration under recent international tax treaties, the arbitration clause serves only as an extension of the MAPs (and only for the issues which cannot be solved in the MAPs process but not for the whole dispute as stated in Art. 25(5) of OECD Model Convention).[59] The arbitration clause is a supplement to the MAPs and cannot replace them. The OECD has commented that the arbitration clause is an "additional dispute resolution technique which can help to . . . [ensure that] international tax disputes will to the greatest extent possible be resolved in a final, principled, fair and objective manner for both the countries and the taxpayers concerned."[60] The MAPs should still be the main dispute resolution mechanism for tax disputes. Therefore, before an investor would be able to press for an international arbitration tribunal, the investor must first face a long and difficult process.

Furthermore, Art. 25(5) of the OECD Model Convention states that "[t]hese unresolved issues shall not, however, be submitted to arbitration if a decision on these issues has already been rendered by a court or administrative tribunal of either State."[61] This means if the local court has resolved a tax dispute, then the taxpayer/investor cannot put the case before an international arbitration. The OECD Model Convention may avoid bestowing parallel authority (i.e., to a domestic court and an international tribunal) to deal with the matter because of political or diplomatic concerns. States might not want to submit to independent and international arbitration to determine their taxation powers, as it might hinder their sovereignty and discretion on tax policy within their borders.

Also, if the competent authorities have reached an agreement on the tax disputes, the taxpayer/investor may not take the case to the arbitration even if he or she is not satisfied with the solution reached by them.[62] So long as the competent authority or domestic court has arrived at a decision, the taxpayer/investor may be blocked from further recourse even though he or she may have suffered an unfair or nontransparent proceeding. Moreover, even if the taxpayer/investor can eventually proceed to international arbitration, he or she must have already waited for two years, which is the

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[59] *See* OECD, MODEL CONVENTION WITH RESPECT TO TAXES ON INCOME AND ON CAPITAL, art. 25(5), (2014), http://www.oecd.org/ctp/treaties/oecd-model-tax-convention-available-products.htm.

[60] OECD, IMPROVING THE RESOLUTION OF TAX TREATY DISPUTES 4 (2007), http://www.oecd.org/ctp/dispute/38055311.pdf.

[61] *See id.*

[62] *Id.*

waiting period stated in Art. 25(2) of OECD Model Convention.[63] Another interpretation of the arbitration clause is that the taxpayer/investor has to waive the right to access the domestic courts in order to request that tax disputes be submitted to arbitration under the OECD Model Convention or international tax treaties (to avoid parallel authority). All of these variations make the MAPs a costly exercise to both the investor and contracting state.

Another point to note is that the OECD Model Convention and most international tax treaties exclude the taxpayer/investor as claimant in arbitration and standing is given to the contacting state's competent authority, i.e., the tax authority.[64] This means that the arbitration provided under the OECD Model Convention and international tax treaties can only be a state vs. state case and the taxpayer/investor can never have the *locus standi* to directly present the case to the arbitration tribunal. This being the case, the arbitration clause within the international tax law regime does not really protect taxpayers/investors, because direct access to arbitration is lacking and their cases may be abandoned for diplomatic reasons (e.g., to preserve the political relationship between the two contracting states).

In addition, regarding the enforcement of the arbitration tribunal's decision, Art. 25(5) of the OECD Model Convention mentions that "[u]nless a person directly affected by the case does not accept the mutual agreement that implements the arbitration decision, that decision shall be binding on both Contracting States and shall be implemented notwithstanding any time limits in the domestic laws of these States."[65] The decision only binds the two contracting states, and if the losing contracting state does not comply with the arbitral decision, the winning contracting state or the taxpayer/investor can do nothing. Remarkably, there is no enforcement mechanism under the international tax treaties, and no sanction or confiscating measures can be imposed upon the losing contracting state for any non-compliance of the arbitral decision.

III. THE JUDICIAL REVIEW OF TAX REGULATIONS BY INVESTMENT TRIBUNALS

Since 1999, at least thirty-two tax-related cases have been brought to international arbitration; it should, however, be kept in mind that this could be only the tip of the iceberg. Many arbitration cases remain unknown to

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63 *See id.* at art. 25(2)

64 *See generally* Maira de Melo Vieira, *Regulation of Tax Matters in Bilateral Investment Treaties: A Dispute Resolution Perspective*, 8 DISPUTE RESOLUTION INTERNATIONAL, 63 (2014).

65 *See* OECD, MODEL CONVENTION WITH RESPECT TO TAXES ON INCOME AND ON CAPITAL, art. 25(5), (2014), http://www.oecd.org/ctp/treaties/oecd-model-tax-convention-available-products.htm.

the public, are hidden, or are still being negotiated. Before going any further, it is appropriate to review the typology of tax disputes and briefly define the types of tax matters that have been at play in investment arbitration disputes. A look at the diversity of the tax matters under discussion will provide a better understanding of the environment as well as what is at risk in these tax disputes.

A. Recent Trends in Investment Arbitration

1. Tax Disputes not Won by the Investor

Not all investment claims result in an award that the host state will have to pay. Actually, the data show that slightly more than 50% of the investment claims dealing with tax matters resulted in a tribunal decision in favor of the state. This article has identified seventeen disputes that resulted in a decision denying a breach of the relevant treaty. This first category of decisions indicates that foreign investors considered using investment treaties to complain against a number of countries and tax measures. Such a trend shows that investment treaties are a potential recourse against some domestic tax measures. The table below provides the details of each of these seventeen disputes.

TABLE 2. INVESTMENT DISPUTES NOT WON BY THE INVESTOR

CASE NAME	TAX AREA	TREATY	YEAR OF CLAIM	AWARD DATE	OUTCOME
CORN PRODUCTS INTERNATIONAL INC. V. MEXICAN STATES	Imposition of a new tax on soft drinks and syrups sweetened by sweeteners other than sugar	NAFTA	2003	August 18, 2009	Not public.
PAUSHOK V. MONGOLIA	Resource management (oil and gas), tax (windfall profits tax), employment (performance	Russia - Mongolia BIT	2007	April 28, 2011	Tribunal accepted jurisdiction over claims, denied claims except the taking of the gold. The claimants had 60 days to claim

	requirements)				damages.
BURLINGTON RESOURCES V. ECUADOR	Windfall profits tax, enforcement of that tax, physical takeover of the oil fields	USA - Ecuador	2008	December 14, 2012	Tribunal rejected jurisdiction over umbrella clause but accepted jurisdiction over *caucidad* decrees. Tribunal decided Ecuador expropriated claimant's investment unlawfully. Other claims are dismissed.
PHOENIX ACTION V. CZECH REPUBLIC	Administration of justice (court decisions), tax (investigations), border control (customs)	Croatia - Czech Rep BIT	2004	April 15, 2009	Tribunal rejected jurisdiction over claim. The claimant had to pay all arbitration costs.
NOBLE ENERGY V. ECUADOR	Utilities (electricity), privatization (energy), tax (value-added tax), public order (enforcement of electricity rates), energy (subsidies)	USA - Ecuador BIT	2005	Settled	Tribunal accepted jurisdiction. Case subsequently settled by agreement between claimant and respondent state.
GOTTLIEB V. CANADA	Tax (taxation of income trusts), resource management (oil and gas)	NAFTA	2007		Claim rejected following agreement of respondent state and claimant's state of nationality that taxation measure did not constitute an expropriation.
TCW V. DOMINICAN REPUBLIC	Utilities (electricity), privatization	CAFTA	2007	Consent Award/July 16, 2009	Case settled by agreement of claimant and

	(energy), public order (theft of electricity), tax (investigations)				respondent state before any decision on jurisdiction.
LACICH V. CANADA	Tax (taxation of income trusts), resource management (oil and gas)	NAFTA	2009	Withdrawn	Claim withdrawn before tribunal established.
LINK-TRADING V. MOLDOVA	Tax (import taxes), border control (customs), industrial policy (free economic zones)	USA - Moldova BIT	1999	April 18, 2002	Tribunal accepted jurisdiction over claim, but decided that respondent state did not violate treaty. The claimant was required to pay approximately $23,000 toward legal costs of respondent.
TOKIOS TOKELES V. UKRAINE	Culture (print publishing), tax (investigations)	Lithuania - Ukraine BIT	2002	July 26, 2007	Tribunal accepted jurisdiction over claim, but decided that respondent state did not violate treaty. Tribunal split arbitration costs between claimant and respondent state.
ENCANA V. ECUADOR	Tax (value-added tax), public contracting (oil production), resource management (oil)	Canada - Ecuador BIT	2003	February 3, 2006	Tribunal rejected jurisdiction over claim except expropriation, decided that respondent state did not violate treaty. The respondent state had to pay all arbitration costs.
PLAMA CONSORTIUM LIMITED V. BULGARIA	Environmental protection (environmental liability), administration	ECT & Bulgaria - Cyprus BIT	2003	August 27, 2008	Tribunal accepted jurisdiction over claims arising from ECT, but decided that the claimant is

	of justice (bankruptcy administration), public order (occupations of oil refinery), tax (corporate income tax), privatization (oil refinery)				not entitled to any of the substantive protections provided by the ECT and respondent state did not violate treaty. Tribunal required claimant to pay all arbitration costs as well as legal costs of respondent state.
GRAND RIVER V. USA	Public health (anti-smoking), administration of justice (settlement with cigarette manufacturers), tax (tax stamps on cigarettes)	NAFTA	2004	January 12, 2011	Tribunal rejected jurisdiction over claims of Grand River, accepted jurisdiction over claims of Arthur Montour but decided that the respondent state did not violate the treaty and split the arbitration costs.
AMTO LLC. V. UKRAINE	Tax procedure (energy, industrial policy, privatization)	ECT	2005	March 26, 2008	Tribunal accepted jurisdiction over claim, but decided that respondent state did not violate treaty. The arbitration costs were split between the parties and each party bore its own legal costs.
EDF V. ROMANIA	Public order (corruption investigations), border control (customs), tax (duty-free regime), international relations (European Union	UK-Romania BIT	2005	October 8, 2009	Tribunal accepted jurisdiction over claim, but decided that respondent state did not violate treaty. Tribunal split arbitration costs between claimant and respondent state, but required claimant to pay $6

	accession)				million toward legal costs of respondent state.
The Rompetrol Group N.V. v. Romania.	Irregularities during the privatization, tax fraud, corruption, abuse of power, money laundering,	Nether-lands - Romania BIT	2005	May 6, 2013	The tribunal accepted jurisdiction over claims, decided that there was no breach of the treaty.
Jan Oostergetel and Theodora Laurentius v. The Slovak Republic	Bankruptcy, tax arrears	Nether-lands - Slovak Republic BIT	2006	April 23, 2012	Tribunal decided that respondent state did not breach treaty, ordered the claimants to bear the arbitration costs and to pay the respondent EUR 2 million as contribution to legal and other costs.

Source: International Investment Arbitration and Public Policy (IIAPP) Database (available at http://www.iiapp.org) and relevant awards. Table compiled by author.

In these seventeen disputes, there is a great diversity of tax measures that were at the origin of the dispute, namely, windfall profits tax, tax investigations, value-added tax, taxation of income trusts, import taxes, corporate income tax, tax stamps on cigarettes, duty-free regime, etc. Unsurprisingly, the broad scope of application of investment treaties allows tribunals to look at a wide variety of tax measures.

There is also diversity in the countries involved in these disputes since Mongolia, Czech Republic, Ecuador, Canada, Dominican Republic, Moldova, Bulgaria, USA, Ukraine, Romania, and Slovakia certainly do not belong to the same economic category. That being said, it is hard to expand the analysis further because, in most of these disputes, the states have proven that they use tax laws or regulations in a manner compatible with the relevant IIA. Alternatively, if the tribunal rejected the claim for lack of jurisdiction, nothing can be concluded as to the potential breach of investment law by a domestic tax measures. The scenario is radically different when one looks at the disputes lost by various host states.

2. Tax Disputes Lost by the Host States

Out of the thirty-two disputes dealing with tax matters, fifteen have been lost by the host states. These disputes are the most interesting because they show what can go wrong in terms of designing tax policy in accord with investment treaties. Table 2 below produces the details of each of these fifteen disputes.

TABLE 3. INVESTMENT DISPUTES LOST BY HOST STATES

CASE NAME	TAX AREA	TREATY	YEAR OF CLAIM	AWARD DATE	OUTCOME
FELDMAN V. MEXICO	Tax (excise tax on cigarettes), border control (customs, gray market exports of cigarettes)	NAFTA	1999	December 16, 2002	Tribunal accepted jurisdiction over claim, decided that respondent state violated treaty (NT). The court awarded specifically "$16,961,056 Mexican pesos (principal amount of $9,464,627.50 plus interest of $7,496,428.47). Tribunal split arbitration costs between claimant and respondent state.
GOETZ V. BURUNDI	Cancellation of license to to operate in a free economic zone	Belgium - Luxemburg - Burundi BIT	1999	February 109, 1999	Indirect expropriation subject to compensation amounted to roughly $3 million
ENRON CORPORATION & PONDEROSA ASSETS LP V. THE ARGENTINE REPUBLIC	Stamp tax	Argentine - USA BIT	2001	May 22, 2007	Tribunal decided that Argentina breached FET and umbrella clauses and awarded a compensation of $106.2 million.

OCCIDENTAL EXPLORATION AND PRODUCTION COMPANY V. ECUADOR CASE NO. UN 3467	Tax (value-added tax), public contracting (oil production)	USA - Ecuador BIT	2002	July 1, 2004	Tribunal accepted jurisdiction over claim, decided that respondent state violated treaty (NT and FET), and awarded approximately $75.0 million (plus interest) against respondent state. Tribunal required respondent state to pay 55% of arbitration costs.
ARCHER DANIELS MIDLAND CO. & TATE LYLE INGREDIENTS AMERICAS, INC. V. UNITED MEXICAN STATES	Imposition of a new tax on soft drinks and syrups sweetened by sweeteners other than sugar	NAFTA	2003	November 21, 2007	Tribunal decided that Mexico breached articles on NT and Performance requirement and that the tax imposed does not amount to a valid countermeasure. Tribunal awarded US$33.0 million.
EL PASO ENERGY INTERNATIONAL COMPANY V. ARGENTINE REPUBLIC	Resource management (oil and gas), utilities (electricity), privatization (energy), monetary system (financial crisis, currency reform)	Argentina - USA BIT	2003	October 31, 2011	Tribunal decided that the Argentine Republic breached FET, awarded a compensation of $43.0 million plus interest, split the arbitration costs. Parties bear their own legal costs and expenses.
DUKE ENERGY V. ECUADOR	Utilities (electricity), public contracting (electric power	USA - Ecuador BIT	2004	August 18, 2008	Tribunal accepted jurisdiction over claim except custom duties, decided that respondent state violated treaty (NT

	procurement), border control (customs), tax (import taxes)				and umbrella clause), and awarded approximately $5.6 million (plus interest) against respondent state. Tribunal split arbitration costs between claimant and respondent state.
HULLEY V. RUSSIA	Tax (tax evasion investigations), public order (seizures of facilities), administration of justice (court decisions), privatization (oil industry)	ECT	2005	July 18, 2014	Tribunal accepted jurisdiction, decided that Russia breached expropriation article, awarded damages of $40. billion.
ROSINVESTCO V. RUSSIA	Tax (tax evasion investigations), public order (seizures of facilities), administration of justice (court decisions), privatization (oil industry)	UK - USSR BIT	2005	December 22, 2010	Tribunal accepted jurisdiction, decided that Russia breached expropriation article, awarded damages of $3.5 million, split the arbitration costs.
YUKOS UNIVERSAL V. RUSSIA	Tax (tax evasion investigations), public order (seizures of facilities), administration of justice (court decisions),	ECT	2005	July 18, 2014	Tribunal accepted jurisdiction, decided that Russia breached expropriation article, awarded damages of $1.8 billion.

	privatization (oil industry)				
MOBIL V. VENEZUELA	Resource management (oil), public contracting (oil production), tax (corporate income tax)	Netherlands - Venezuela BIT	2007	October 9, 2014	The Tribunal accepted jurisdiction over claims except the claim arising out of increase in the income tax rate. It awarded compensation of about $1,411 million plus interest for expropriation and $9.0 million plus interest for the production and export curtailments. It split the arbitration costs.
QUASAR DE VALORES SICAV SA V. THE RUSSIAN FEDERATION	tax (tax evasion investigations), public order (seizures of facilities), administration of justice (court decisions)	Spain - USSR BIT	2007	July 20, 2012	Tribunal accepted jurisdiction, decided that Russia breached expropriation article, awarded damages of around $2.0 million in total.
RENTA 4 V. RUSSIA	Tax assessment, public order (seizures of facilities), administration of justice (court decisions), privatization (oil industry)	Spain - USSR BIT	2007	March 30, 2009	Quasar case was formerly known as Renta 4 case. In the jurisdictional award, the Tribunal accepted jurisdiction over claims of only 4 of the 7 Claimants of the Renta 4 Case. Therefore the case is renamed as Quasar.
TZA YAP SHUM V. REPUBLIC OF PERU	Tax assessment	China - Peru BIT	2005	July 7, 2011	Expropriation case is not available in English

VETERAN PETROLEUM V. RUSSIA	Tax (tax evasion investigations), public order (seizures of facilities), administration of justice (court decisions), privatization (oil industry)	ECT	2005	July 18, 2014	Tribunal accepted jurisdiction, decided that Russia breached expropriation article, awarded damages of $50,020,867,798.

Source: International Investment Arbitration and Public Policy (IIAPP) Database (available at http://www.iiapp.org) and relevant awards. Table compiled by author.

These fifteen disputes have been lost by only seven countries, all of which are developing countries or transition economies: Mexico, Burundi, Peru, Argentina, Ecuador, Venezuela, and Russia.

The majority of cases (exactly nine awards) concluded with a finding of expropriation.[66] However, two claims were consolidated into a single case for *Renta 4* and *Quasar de Valores v. Russia*. Also, as part of the *Yukos* case, three separate lawsuits by former Yukos shareholders were filed by Hulley Enterprises Limited (Cyprus), Yukos Universal Limited (Isle of Man) and Veteran Petroleum Limited (Cyprus). As a result, there are only six truly different tax disputes that resulted in a finding of expropriation.

The *Señor Tza Yap Shum v. Peru* dispute offers an excellent overview

[66] Antoine Goetz et consorts v. République du Burundi, ICSID Case No. ARB/95/3, Award, (Feb. 10, 1999) [French Only]; RosInvestCo UK Ltd. v. The Russian Federation, SCC Case No. V079/2005, Final Award, (Sept. 12, 2010); Señor Tza Yap Shum v. The Republic of Peru, ICSID Case No. ARB/07/6, Award, (July 7, 2011) [Spanish]; Renta 4 S.V.S.A, Ahorro Corporación Emergentes F.I., Ahorro Corporación Eurofondo F.I., Rovime Inversiones SICAV S.A., Quasar de Valors SICAV S.A., Orgor de Valores SICAV S.A., GBI 9000 SICAV S.A. v. The Russian Federation, SCC No. 24/2007, Award, (July 20, 2012); Mobil Corporation, Venezuela Holdings, B.V., Mobil Cerro Negro Holding, Ltd., Mobil Venezolana de Petróleos Holdings, Inc., Mobil Cerro Negro, Ltd., and Mobil Venezolana de Petróleos, Inc. v. Bolivarian Republic of Venezuela, ICSID Case No. ARB/07/27, Award of the Tribunal, (Oct. 9, 2014); Hulley Enterprises Ltd. (Cyprus) v. The Russian Federation, UNCITRAL, PCA Case No. AA 226, Final Award, (July 18, 2014); Yukos Universal Ltd. (Isle of Man) v. The Russian Federation, UNCITRAL, PCA Case No. AA 227, Final Award, (July 18, 2014); Veteran Petroleum Ltd. (Cyprus) v. The Russian Federation, UNCITRAL, PCA Case No. AA 228, Final Award, (July 18, 2014).

of the type of problematic interactions between a taxpayer and an administration that may result in an investment dispute. The *Tza Yap Shum* case (named after the Chinese owner of TSG Peru SAC (TSG)) is a good example of how a tax dispute (under national law) can also be an investment dispute (under international law).[67] In 2002, Mr. Tza Yap Shum established TSG with a $400,000 investment. TSG purchased raw fish, delivered the fish to third-party factories to process into fish meal, and then exported the finished product. Sales reached $20 million per year. In 2004, the Peruvian tax authority, the SUNAT, conducted a routine audit of TSG after TSG had requested sales tax refunds. During the tax audit, the SUNAT decided that TSG had not properly declared the amounts and values of the raw materials it had purchased, which the SUNAT believed meant TSG had under-declared sales, as well. The SUNAT issued a new tax assessment based on a "presumed basis"[68] of $4 million. TSG did not agree with the assessment. Shortly after the audit, the SUNAT also took so-called "interim measures"[69] to enforce the tax assessment that had been imposed to secure money for the Treasury. All banks in Peru were directed to retain any funds related to TSG passing to them and to redirect such funds to the SUNAT. Almost immediately, TSG's business became inoperable because the company was unable to pay suppliers or receive payments from its

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[67] *See* Señor Tza Yap Shum v. The Republic of Peru, ICSID Case No. ARB/07/6, Decision on Jurisdiction and Competence, (June 19, 2009) [Spanish]; *see also Señor Tza Yap Shum*, ICSID Case No. ARB/07/6, Award on Merits.

[68] *See* Señor Tza Yap Shum v. The Republic of Peru, ICSID Case No. ARB/07/6, Decision on Jurisdiction and Competence, (June 19, 2009) [Spanish].

[69] *See generally* J. G. Merrils, *Interim Measures of Protection in the Recent Jurisprudence of the International Court of Justice*, 44 INT'L & COMP. L. Q. 90, 91–100, 106–113; Robert Volterra, *Provisional Measures (Interim Measures) and Investment Treaty Arbitration under ICSID and UNCITRAL: Developments and Trends*, *in* THE BRITISH INST. OF INT'L & COMP. LAW, INVESTMENT TREATY LAW: CURRENT ISSUES III 22 (Andrea Bjorklund, Iian Laird & Sergey Ripinsky eds 2009). In the case-law, the tribunal *Perenco v. Ecuador*, Decision on Provisional Measures states interim measures may restrain a State from enforcing a law pending final resolution of the dispute on the merits. See Perenco Ecuador Ltd. v. Republic of Ecuador & Empresa Estatal Petróleos del Ecuador, ICSID Case No. ARB/08/6, Decision on Provisional Measures, ¶ 50 (May 8, 2009). The tribunal in *Anderson v. Costa Rica*, Award notes that it refused to grant interim measures of protection (in the form of security for costs) because (i) the facts presented by the respondent did not constitute an urgent situation that risked irreparable harm to the respondent's rights; (ii) the respondent had only a mere expectation and not a right with respect to an eventual award of costs; (iii) the request to order the claimants to be held joint and severally liable for the payment of any costs eventually awarded to the respondent is not in the nature of a provisional measure to preserve existing rights; and (iv) a tribunal's decision in this respect might constitute a prejudgment on the responsibility of individual parties. See Alasdair Ross Anderson et al v. Republic of Costa Rica, ICSID Case No. ARB(AF)/07/3, Award, ¶ 9 (May 19, 2010).

customers.

TSG commenced proceedings in Peru to have the tax claim lifted. An appeal to the SUNAT was rejected, although the amount of back-taxes was reduced. TSG's challenge before the Peruvian Fiscal Tribunal was rejected as well. By 2005, TSG had to commence a debt restructuring. Presumably, the company was forced to stop operations not long after that, and TSG started arbitration procedures. The tribunal determined that the interim measures taken by the SUNAT did in fact amount to expropriation. The tribunal concluded that the interim measures significantly interfered with the operation of TSG, that TSG depended entirely on letters of credit from its overseas customers being properly processed through Peruvian banks, and that the SUNAT should have known these things based on audits it conducted. The tribunal held that the SUNAT imposed the interim measures in an arbitrary manner, that it did not respect the internal rules and guidelines for its own interim measures (which state that the measures taken are exceptional, need to be justified and accompanied by evidence, and that efforts must be made to mitigate harm to the taxpayer's business), and that the SUNAT's regulators did not make any effort to verify whether these rules were followed. The upshot was that the interim measures were ineffective. The only real result of the measures was that TSG could no longer operate. Almost no cash was actually seized.

Once the tribunal decided that the SUNAT's bank block had indeed led to the expropriation of TSG, the amount of damages had to be determined. TSG had asked for $25 million, which was based on the discounted future profits of the company. Although international law does recognize this calculation method, the tribunal found it inappropriate in this case. The tribunal noted that TSG owed a lot of debt, was operating in a high-risk industry and was already beginning to lose market share in 2004. The tribunal decided that the damages should instead be calculated without taking possible future profits into account and should be mostly based on the adjusted book value of the company. This resulted in compensation of $786,000, much less than the plaintiff sought.

The recovery measures a state takes to collect tax debts are sensitive from the perspective of the protection foreign investors have under BITs as well as under general international law. Such measures may easily have an expropriatory effect, even when the amount of tax that is recovered is in itself not confiscatory. A tax debt that is not enormous, but that is disputed and hence not finally determined, may be collected by the state with the use of measures that are so drastic and disproportionate that they result in the discontinuation of the investment. A temporary closure of business facilities, the seizure of business assets or bank accounts, or even the temporary imprisonment of executives of the local company on allegations of tax fraud may all result in the investment losing all value and prospects.

In this case, the amount of tax due is secondary to the effect of the recovery measures themselves.

In the *TSG* case, a tax auditor imposed an additional assessment of $4 million on a company that was created just a few years prior with a $400,000 investment. Most likely, the company simply had no means of paying the assessment, even if it was justified. Instead of calmly going through the tax dispute process that exists under local laws to decide whether the claim was justified (note that both the appeal and the tax court procedure later resulted in a lower tax claim), the tax authority seized the bank accounts of the company almost immediately after the audit without respecting its relevant internal rules for taking such an exceptional action.[70] The tax claim might have been justified, but the temporary enforcement measures taken before court proceedings had played out were so damaging to the operations of the company that the tax claim itself was rendered irrelevant because the company could not survive the measures. That situation, the tribunal found it did violate the BIT because the act amounted to expropriation.

In terms of substance, one can observe that four key substantive provisions have been important to conclude a breach of the relevant treaty has occurred, namely, the expropriation clause, the FET clause, the full protection and security (FPS) standard, and the national treatment (NT) provision. Each of these four provisions will be further analyzed.

IV. THE EFFECTIVE BREACHES OF INVESTMENT TREATY BY TAX MEASURES

Investment agreements enshrine a series of obligations on the parties aimed at ensuring a stable and favorable business environment for foreign investors.[71] These obligations pertain to the treatment that foreign investors and their investments are to be afforded in the host country by the domestic authorities; they also ensure that foreign investors have the ability to perform certain key actions related to their investments.[72] The "treatment" granted to investors encompasses all types of laws, regulations and practices of government entities that apply to or affect foreign investors or

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[70] *See* Señor Tza Yap Shum v. The Republic of Peru, ICSID Case No. ARB/07/6, Decision on Jurisdiction and Competence, (June 19, 2009) [Spanish].

[71] *See e.g.*, Mark S. Bergman, *Bilateral Investment Protection Treaties: An Examination of the Evolution and Significance of the US Prototype Treaty*, 16 N.Y.U. J. INT'L L. & POL. 1 (1983). *See generally* KENNETH J. VANDEVELDE, U.S. INTERNATIONAL INVESTMENT AGREEMENTS (2009).

[72] *See generally* Caroline Henckels, *Indirect Expropriation and the Right to Regulate: Revising Proportionality Analysis and the Standard of Review in Investor-State Arbitration*, 15 J. INT'L ECON. L. 223 (2014).

their investments.[73] All public entities, including, where applicable, federal and sub-federal governments, local authorities, regulatory bodies, and entities that exercise delegated public powers, are bound by the international obligations.[74] Measures adopted by private actors can also – although rather exceptionally – fall under the scope of international agreements when such measures can ultimately be attributed to a governmental entity. The set of obligations is rather consistent amongst the great majority of IIAs.[75]

The core provisions found in an investment agreement typically include (1) a most-favored-nation (MFN) treatment obligation, (2) the granting of NT, (3) an obligation to provide FET and protection and security to foreign investors, and (4) an obligation to allow international transfers of funds.[76] However, while the substance of these principles remains the same throughout most investment agreements, the scope and reach of each obligation depends on the precise wording featured in each one.[77] These diverse provisions help to reassure foreign investors that they will be able to reap the benefits of their investments. Even if the presence of these principles in IIAs is consistently found over the years and throughout countries, the evidence on the extent to which investment decisions are influenced by investment treaties is mixed.[78]

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[73] *See generally* Heather L. Bray, Note*, ISCID and The Right to Water: An Ingredient in the Stone Soup,* 29 ICSID REV. 474 (2014).

[74] *See generally* Yas Banifatemi, *The Law Applicable in Investment Treaty Arbitration*, *in* ARBITRATION UNDER INTERNATIONAL INVESTMENT AGREEMENTS: A GUIDE TO THE KEY ISSUES 192, 200 (2010).

[75] Doak Bishop, *Combatting Arbitral Terrorism* (July 16, 2015), http://www.kslaw.com/library/pdf/bishop7.pdf; *see also* Stephen M. Schwebel, *Anti-suit Injunctions In International Arbitration—An Overview*, *in* ANTI-SUIT INJUNCTIONS IN INTERNATIONAL ARBITRATION 5–14 (Emmanuel Gaillard, Juris Publishing Inc., 2003).

[76] *See generally* Kenneth J. Vandevelde, *Treaty Interpretation from a Negotiator's Perspective*, 21 VAND. J. TRANSNAT'L L. 281, 296 (1988).

[77] *See* Anthea Roberts, *Power and Persuasion in Investment Treaty Interpretation: The Dual Role of States*, 104 AM. J. INT'L L. 179, 193 (2010) (explaining the notion of dialogue as an instrument for parties to the treaty and tribunals to influence interpretation through repeated interactions).

[78] The extent to which BITs actually attract increased flows of foreign direct investment is disputed. According to Salacuse and Sullivan, entering into a BIT with the United States would nearly double a country's FDI inflows. However, entering into BITs with other OECD countries had no significant effect on FDI. *See* Jeswald W. Salacuse & Nicholas P. Sullivan, *Do BITs Really Work?: An Evaluation of Bilateral Investment Treaties and Their Grand Bargain*, 46 HARV. INT'L L. J. 67, 105–111 (2005). Another important study concludes that there is "little evidence that BITs have stimulated additional investment." Mary Hallward-Driemeier, *Do Bilateral Investment Treaties Attract FDI? Only a Bit . . . and They Could Bite*, 22 (WORLD BANK DEV. RESEARCH GRP., Policy Research Working Paper No. 3121) http://elibrary.worldbank.org/content/workingpaper/10.1596/

A. The Protection of Investment against Expropriation

The protection of foreign investors has historically been the main goal of IIAs as an attempt to discipline governments inclination to expropriate foreign assets.[79] Hence, the inclusion of safeguards against the nationalization or expropriation of foreign investment constitutes a pivotal guarantee for foreign investors.

1. The Regulation of Expropriation

There are significant discrepancies in the way the FET is defined in investment treaties and in different countries' practices; this is because some IIAs will cover both direct and indirect expropriation, whereas some will not address indirect expropriation.[80] The choice is important, because if a treaty covers indirect expropriation it means that the IIA grants protection to foreign investors who may face serious alterations of the investment climate that they could not have reasonably anticipated. There is, however, no clear definition of indirect expropriation. Despite a number of decisions by international tribunals, the line between indirect expropriation and governmental regulatory measures not requiring compensation has not been clearly articulated and depends on the specific facts and circumstances of the case.[81] In recent years, a new generation of U.S. and Canadian investment agreements, including the investment chapters of FTAs, has introduced specific language[82] and established criteria to assist in determining whether an indirect expropriation requiring compensation has occurred. During the last decade, jurisprudence has developed such that indirect expropriation need not involve the actual physical taking of property but rather may result from the effective loss of management, use,

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1813-9450-3121.

[79] Christopher Hajzler provides a detailed account of the expropriation phenomenon over the years and continents. According to his study, published in 2012, the number of direct expropriation acts was 136 in the 1960s and 423 in the 1970s, but has since declined to only 17 in the 1980s, 22 in the 1990s, and 27 instances in the 2000s, through 2006. *See* Christopher Hajzler, *Expropriation of Foreign Direct Investments: Sectoral Patterns from 1993 to 2006*, 148 REV. WORLD ECON. 119, 127–28 (2012).

[80] *See generally* Julien Chaisse, *Promises and Pitfalls of the European Union Policy on Foreign Investment — How Will the New EU Competence on FDI Affect the Emerging Global Regime*, 15 J. INT'L ECON. L. 51, 57–58 (2012) (discussing the fact that, for instance, not all BITs involving at least one European country, covers indirect expropriation).

[81] *See* Anne Van Aaken, *International Investment Law Between Commitment and Flexibility: a Contract Theory Analysis*, 12 J. INT'L ECON. L. 507, 510–12 (2009).

[82] *See* Rachel D. Edsall, *Indirect Expropriation Under NAFTA and DR–CAFTA: Potential Inconsistencies in the Treatment of State Public Welfare Regulations*, 86 B.U.L. REV. 931, 953–61 (2006).

control, or a significant depreciation of the value, of the assets of a foreign investor.[83]

Another kind of indirect expropriation is regulatory taking, which refers to "those takings of property that fall within the police powers of a State, or otherwise arise from State measures like those pertaining to the regulation of the environment, health, morals, culture, or economy of a host country."[84] The *Tecmed v. Mexico* Award notes that although formally expropriation means a forcible taking by the State, the term also covers a number of situations defined as de facto expropriation.[85] However, in essence, a taking must be a substantially complete deprivation of the economic use and enjoyment of the rights to the property or of identifiable distinct parts thereof (i.e., it approaches total impairment).[86]

Despite a number of decisions by tribunals, the line between indirect expropriation and governmental regulatory measures not requiring compensation has not been clearly articulated. The determination of indirect expropriation very much depends on the specific facts and circumstances of the case.[87] In general terms, the *Electrabel v. Hungary* Decision on

[83] As stated by Gemplus Arbitral Tribunal, "an indirect expropriation occurs if the state deliberately deprives the investor of the ability to use its investment in any meaningful way." *See* Gemplus, S.A., SLP, S.A. & Gemplus Industrial, S.A. de C.V. v. United Mexican States, ICSID Case No. ARB(AF)/04/3 & ARB(AF)/04/4, Award, Part VIII, ¶ 23 (June 16, 2010).

[84] United Nations Conference on Trade and Development, *Taking of Property*, 12, U.N. Doc. UNCTAD/ITE/IIT/15 (2000).

[85] See Técnicas Medioambientales Tecmed, S.A. v. United Mexican States, ICSID Case No. ARB (AF)/00/2, Award, ¶ 113–114 (May 29, 2003).

[86] For instance, the *PSEG v. Turkey* Award finds a requirement for some form of the following in order to find an indirect expropriation: deprivation of the investor in the control of the investment, the management of day-to day-operations of the company, interfering in the administration, impeding the distribution of dividends, interfering in the appointment of officials and managers, or depriving the company of its property or control in total or in part. *See* PSEG Global Inc. v. Republic of Turkey, ICSID Case No. ARB/02/5, Award, ¶ 278 (Jan. 19, 2007). Also, the *AWG v. Argentina* Decision on Liability holds that in an indirect expropriation, sometimes referred to as a "regulatory taking," host states invoke their legislative and regulatory powers to enact measures that reduce the benefits investors derive from their investments, but without actually changing or cancelling investors' legal title to their assets or diminishing their control over them. *See* AWG Group Ltd. v. Argentine Republic, ICSID Case No. ARB/03/19, Decision on Liability, ¶ 132 (July 30, 2010).

[87] Of course, although there are some variations "in the way some arbitral tribunals have distinguished legitimate non-compensable regulations having an effect on the economic value of foreign investments and indirect expropriation requiring compensation, a careful examination reveals that, in broad terms, they have identified the following criteria which look very similar to the ones laid out by the recent agreements: i) the degree of interference with the property right; ii) the character of governmental measures, i.e., the purpose and the context of the governmental measure; and iii) the interference of the measure with reasonable and investment-backed expectations." Catherine Yannaca-Small, *OECD,*

Jurisdiction, Applicable Law and Liability considers that the accumulated mass of international legal materials, comprising both arbitral decisions and doctrinal writings, describes for both direct and indirect expropriation, consistently, albeit in different terms, the requirement under international law for the investor to establish the substantial, radical, severe, devastating or fundamental deprivation of its rights or the virtual annihilation, effective neutralization or factual destruction of its investment, its value or enjoyment.[88]

There are however, three main criteria that arbitrators are likely to consider in evaluating a measure, as recently summarized in the *Burlington Resources v. Ecuador* Decision on Liability.[89] This decision notes that the following requirements must be met in order to find indirect expropriation: "(i) a substantial deprivation of the value of the whole investment" (i.e., the degree of interference with the property rights (including interference with the investor's reasonable investment-backed expectations)); "(ii) a permanent measure" (i.e., the duration of the measure); and "(iii) a measure not justified under the police power doctrine" (which basically is a review of the measure's purpose).[90]

2. Impact in the Regime of Tax

At the outset, it is important to remember that the *Telenor v. Hungary* Award held that the "exercise by government of regulatory powers that create impediments to business or entail the payment of taxes or other levies does not of itself constitute expropriation."[91] Also, the *Link-Trading*

"Indirect Expropriation" and the "Right to Regulate" in International Investment Law, *in* INTERNATIONAL INVESTMENT LAW: A CHANGING LANDSCAPE 54 (Hans Christiansen ed., 2005), http:// browse.oecdbookshop.org/oecd/pdfs/product/2005141e.pdf. *See also* Anne Van Aaken, *International Investment Law Between Commitment and Flexibility: A Contract Theory Analysis*, 12 J. INT'L ECON. L. 507, 510–12 (2009).

[88] Electrabel S.A. v. Republic of Hungary, ICSID Case No. ARB/07/19, Decision on Jurisdiction, Applicable Law and Liability, ¶ 6.62 (Nov. 30, 2012).

[89] *See* Burlington Resources Inc. v. Republic of Ecuador, ICSID Case No. ARB/08/5, Decision on Liability, ¶ 471 (Dec. 14, 2012).

[90] *Id.*

[91] "It is well established that the mere exercise by government of regulatory powers that create impediments to business or entail the payment of taxes or other levies does not of itself constitute expropriation. Any investor entering into a concession agreement must be aware that investment involves risks and that in some degree the investor's activities are likely to be regulated and payments made for which the investor will not receive compensating advantages. These are all part of the price the investor has to pay for securing the concession. Similarly, unreasonable behavior on the part of officials and breaches of contract, even if serious, do not by themselves constitute acts of expropriation. The conduct complained of must be such as to have a major adverse impact on the economic value of the investment." Telenor Mobile Communications A.S. v. Republic of Hungary, ICSID Case

v. Moldova Award found that "tax measures may also become expropriatory without necessarily being arbitrary or discriminatory, when their application violates a specific obligation that the state has previously undertaken in favor of a particular person or class of persons, such as an investor protected under a treaty."[92] In the same vein, the *EnCana v. Ecuador* Award held that "in the absence of a specific commitment from the host state, the foreign investor has neither the right nor any legitimate expectation that the tax regime will not change, perhaps to its disadvantage, during the period of the investment . . . it will only be in an extreme case that a tax which is general in its incidence could be judged as equivalent in its effect to an expropriation of the enterprise which is taxed."[93] As a result, the *Tza Yap Shum v. Peru* Award notes that there is a "remarkable consensus" around the fact that taxation and the enforcement of tax measures can acquire an expropriatory nature if they are confiscatory, arbitrary, abusive or discriminatory.[94]

Disputes between tax authorities and taxpayers about the valuation of goods and services for tax purposes are common in administrative appeals and tax courts. It is not so common to find such disputes before an international arbitration tribunal. That is, however, exactly what happened in six disputes between a foreign investor and host state, which were decided via arbitration. The majority of cases (exactly nine awards) concluded with a finding of expropriation.[95] An important case, however, is

No. ARB/04/15, Award, ¶ 64 (Sept. 13, 2006).

[92] Link-Trading Joint Stock Company v. Republic of Moldova, UNCITRAL, Final Award, ¶ 73 (Apr. 18, 2002).

[93] EnCana Corporation v. Republic of Ecuador, LCIA Case No. UN3481, Award, ¶ 173 (Feb. 3, 2006). Recently, the *Perenco v. Ecuador* Decision on the Remaining Issues of Jurisdiction and on Liability, citing EnCana, finds that when determining whether a measure should be characterized as a tax for the purposes of international law, the focus is on the law's substantive effect. Perenco Ecuador Limited v. Republic of Ecuador & Empresa Estatal Petróleos del Ecuador, ICSID Case No. ARB/08/6, Decision on Remaining Issues of Jurisdiction and on Liability, ¶ 585 (Sept. 12, 2014).

[94] Tza Yap Shum v. Republic of Peru, ICSID Case No. ARB/07/6, Award, ¶ 181 (July 7, 2011) [Spanish].

[95] Antoine Goetz et consorts v. République du Burundi, ICSID Case No. ARB/95/3, Award, (Feb. 10, 1999) [French Only]; RosInvestCo UK Ltd. v. The Russian Federation, SCC Case No. V079/2005, Final Award, (Sep. 12, 2010); Señor Tza Yap Shum v. The Republic of Peru, ICSID Case No. ARB/07/6, Award, (Jul. 7, 2011) [Spanish]; Renta 4 S.V.S.A, Ahorro Corporación Emergentes F.I., Ahorro Corporación Eurofondo F.I., Rovime Inversiones SICAV S.A., Quasar de Valors SICAV S.A., Orgor de Valores SICAV S.A., GBI 9000 SICAV S.A. v. The Russian Federation, SCC No. 24/2007, Award, (Jul. 20, 2012); Mobil Corporation, Venezuela Holdings, B.V., Mobil Cerro Negro Holding, Ltd., Mobil Venezolana de Petróleos Holdings, Inc., Mobil Cerro Negro, Ltd., and Mobil Venezolana de Petróleos, Inc. v. Bolivarian Republic of Venezuela, ICSID Case No. ARB/07/27, Award of the Tribunal, (Oct. 9, 2014); Hulley Enterprises Ltd. (Cyprus) v. The

the *Occidental Exploration v. Ecuador* Final Award, which sets out a series of applicable principles and definitions and finds that, even under the broadest definition applied, there was no expropriation of tax refunds.[96] Also, the *Feldman v. Mexico* Award is important as the reasoning distinguishes between the activities of taxation authorities (which are not always consistent and predictable) and expropriatory activity (which encapsulated the idea of economic severity).[97] Although we cannot review each of these nine awards in the present article, we focus on the recent awards rendered in the *Yukos* case, which is arguably one of the most important disputes under investment treaties.

After taking control over Yukos, Mikhail Khodorkovsky (and his business associates) carried out massive financial engineering to reduce tax liabilities of the oil company. They used shell companies registered in offshore tax havens (such as Gibraltar, Cyprus, Isle of Man, and Switzerland) to transfer highly profitable operations to such low-tax jurisdictions. Under this arrangement, Yukos would sell crude oil to these offshore shell companies (with no assets or employees) at below-market rates and the shell companies would sell oil to domestic and foreign buyers at market rates.[98] Through such manipulative transfer pricing strategies, Yukos avoided paying taxes in Russia while the shell companies earned the

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Russian Federation, UNCITRAL, PCA Case No. AA 226, Final Award, (Jul. 18, 2014); Yukos Universal Ltd. (Isle of Man) v. The Russian Federation, UNCITRAL, PCA Case No. AA 227, Final Award, (Jul. 18, 2014); Veteran Petroleum Limited (Cyprus) v. The Russian Federation, UNCITRAL, PCA Case No. AA 228, Final Award, (Jul. 18, 2014). One can however note that two claims were consolidated into a single case for Renta 4 and Quasar de Valores v. Russia. Also, as part of the Yukos case, three separate lawsuits by former Yukos shareholders were filed by Hulley Enterprises Limited (Cyprus), Yukos Universal Limited (Isle of Man) and Veteran Petroleum Limited (Cyprus). As a result, there are only six truly different tax disputes that resulted in a finding of expropriation.

[96] Occidental Exploration & Production Company v. Republic of Ecuador, Final Award – London Court of International Arbitration Case No. UN 3467, ¶¶ 84–89 (Jul. 1, 2004).

[97] As noted, "[h]ere, it is undeniable that the Claimant has experienced great difficulties in dealing with SHCP officials, and in some respects has been treated in a less than reasonable manner, but that treatment under the circumstances of this case does not rise to the level of a violation of international law under Article 1110. Unfortunately, tax authorities in most countries do not always act in a consistent and predictable way. The IEPS law on its face (although not necessarily as applied) is undeniably a measure of general taxation of the kind envisaged by Restatement Comment g (see *supra*, paras. 105, 106). As in most tax regimes, the tax laws are used as instruments of public policy as well as fiscal policy, and certain taxpayers are inevitably favored, with others less favored or even disadvantaged." Marvin Roy Feldman Karpa v. United Mexican States, ICSID Case No. ARB(AF)/99/1, Award, ¶ 113 (Dec. 16, 2002).

[98] See Yukos Universal Ltd. (Isle of Man) v. The Russian Federation, UNCITRAL, PCA Case No. AA 227, Final Award, (Jul. 18, 2014)

bulk of the profits. The shell companies were wholly owned by Khodorkovsky and his close business associates. However, the rules of the game changed when Vladimir Putin was elected president in 2000, and one of his first steps was to crack down on tax evasion by big firms owned by oligarchs.

The Permanent Court of Arbitration (PCA) has recently decided a decade-long case brought by shareholders in the defunct Yukos oil company and ordered Russia to pay about $50 billion in damages. As part of the case, three separate lawsuits by former Yukos shareholders were filed by Hulley Enterprises Limited (HEL), Yukos Universal Limited (YUL), and Veteran Petroleum Limited (VLP). The court ruled that $39.97 billion of the compensation should go to Hulley Enterprises, $1.85 billion to Yukos Universal, and $8.2 billion to Veteran Petroleum Limited.

The three awards come to the same conclusion: Russia violated the EU Energy Charter when it redistributed the company's assets and through "the measures that Respondent [Russia] has taken in response to nationalization or expropriation."[99] Hulley, YUL and VPL were the controlling shareholders of the OAO Yukos Oil Company, referred to as "Yukos," and collectively held up to 70.5% share therein. Yukos was engaged in the exploration, production, refining, marketing and distribution of crude oil, natural gas and petroleum products. It was established in 1993 and was fully privatized by 1996. Yukos was set to become the fourth largest private oil producer in the world after its projected merger with Russia's fifth largest company, Sibneft, in 2003. However, between July 2003 and November 2007 a number of measures were taken by the Russian Federation that devastated Yukos, leading to its bankruptcy in 2006 and being struck from the register of companies in November 2007.[100]

Measures taken by the Russian Federation included criminal prosecution of Yukos, its employees, and persons related to the company. The measures related to taxation included massive tax re-assessments for the years 2000-2004 totaling more than $24 billion. The reassessment of the taxes by the Russian authorities was taken in light of the questioned legitimacy of the "Tax Optimization Strategy" undertaken by Yukos in the "ow-tax regions," which consisted of using "trading companies" located in

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[99] *Hulley Enterprises v. Russia* ¶ 1580*, Yukos v. Russia, Veteran Petroleum v. Russia* Final Awards note that Article 13 of the ECT could be violated through a *bona fide* taxation measure that was aimed at raising State revenue whose effect was expropriatory. Veteran Petroleum Ltd. (Cyprus) v. Russian Federation, PCA Case No. AA 228, Final Award, 1434 (Jul. 18, 2014); Yukos Universal Ltd. (Isle of Man) v. Russian Federation, PCA Case No. AA 227, Final Award, 1434 (Jul. 18, 2014); Hulley Enterprises Ltd. (Cyprus) v. Russian Federation, PCA Case No. AA 226, Final Award, 1434 (Jul. 18, 2014).

[100] See the full Factual Background in Veteran Petroleum Limited (Cyprus) v. Russia, PCA Case No. AA 228, Final Award, ¶¶ 63–105 (Jul. 18, 2014).

the low-tax regions as intermediaries in the chain of transactions between Yukos's core oil-producing entities and consumers. The central issue was whether Yukos was taking advantage of existing legislative arrangements to minimize the incidence of taxes or if there was an element of abuse in its "tax optimization scheme."[101]

However, equally questionable was the re-assessment performed by the Russian authorities, as concerns were raised as to whether the Russian Federation was merely enforcing its tax laws or carrying out a punitive campaign against Yukos. Further, specifically with reference to value-added tax (VAT), Russian authorities determined Yukos to be an exporter, where in fact it was the trading companies in the Yukos tax optimization structure that exported oil and oil products and filed VAT returns to claim exemption (not Yukos itself). According to Russian authorities, Yukos failed to file VAT returns and claim exemption, and this position was affirmed by the decision of the Moscow Arbitrazh Court. That decision was followed by asset freezes and other punitive measures taken against Yukos to enforce tax reassessments, including the forced sale of Yukos's core oil production asset, which was the largest State-owned oil company, Rosneft. Accordingly, claims were brought against the Russian Federation for the failure to provide fair and equitable and non-discriminatory treatment, constituting a breach of Article 10(1) and expropriation in breach of Article 13(1) of the Energy Charter Treaty (ECT).[102]

TABLE 4. TIMELINE OF THE YUKOS SAGA (2003–2015)

- October 2003: Mikhail Khodorkovsky is arrested on charges of massive tax evasion and fraud.
- April 2004: Yukos is hit with a bill for $3.5 billion for tax allegedly unpaid in 2000. The Russian government freezes its assets.
- November 2014: The Russian tax authorities examine the accounts of Yukos for the year 2002 and issue another multi-billion-dollar tax bill. All top executives of Yukos leave Russia, fearing imminent arrest.
- December 2004: Russia auctions Yuganskneftegas, Yukos's main production unit, which is later sold for $9.3 billion.
- May 2005: Khodorkovsky is convicted of fraud and sentenced to nine years in prison.
- 2006–2007: Russia declares Yukos bankrupt and sells its remaining assets to Rosneft.
- November 2009: An arbitral tribunal constituted under the auspices of

101 *Id.*
102 *Id.*

the PCA decides that Russia is bound by the ECT and that the claims by majority shareholders are admissible under the Treaty.

- October–November 2012: The arbitration case is tried over five weeks at the PCA in The Hague.
- December 2013: Khodorkovsky is pardoned by President Putin and released after a decade in custody.
- July 2014: The arbitral tribunal gives a Final Award of $50 billion to the majority shareholders of Yukos.
- June 2015: Yukos shareholders announce they are initiating enforcement proceedings against Russian state assets in the UK, France and the USA.

Source: Compiled by the author

The ECT provides protection against not merely outright nationalization by member-states but also against measures having an effect equivalent to nationalization or expropriation, including regulatory and tax policies.[103]

On July 28, 2014, an international arbitration tribunal under the auspices of the PCA announced that Russia must pay $50 billion in damages to former shareholders of the now defunct oil giant, Yukos Oil Company. First, *Hulley Enterprises v. Russia, Yukos v. Russia,* and the *Veteran Petroleum v. Russia* Final Awards hold that the exclusion of taxation measures does not apply in the present dispute.[104] Second, the three-member tribunal unanimously declared that Russia breached its

[103] The Article 13(1) of the ECT clearly states: "Investments of Investors of a Contracting Party in the Area of any other Contracting Party shall not be nationalized, expropriated or subjected to a measure or measures having effect equivalent to nationalization or expropriation (hereinafter referred to as 'Expropriation') except where such Expropriation is: (a) for a purpose which is in the public interest; (b) not discriminatory; (c) carried out under due process of law; and (d) accompanied by the payment of prompt, adequate and effective compensation. Such compensation shall amount to the fair market value of the Investment expropriated at the time immediately before the Expropriation or impending Expropriation became known in such a way as to affect the value of the Investment (hereinafter referred to as the 'Valuation Date'). . . . Such fair market value shall at the request of the Investor be expressed in a Freely Convertible Currency on the basis of the market rate of exchange existing for that currency on the Valuation Date. Compensation shall also include interest at a commercial rate established on a market basis from the date of Expropriation until the date of payment." Energy Charter Treaty, art. 13, Dec. 7, 1994, 33 I.L.M. 260 (1995).

[104] Veteran Petroleum Ltd. (Cyprus) v. Russian Federation, PCA Case No. AA 228, Final Award, 1406-1407 (Jul. 18, 2014); Yukos Universal Ltd. (Isle of Man) v. Russian Federation, PCA Case No. AA 227, Final Award, 1406-1407 (Jul. 18, 2014); Hulley Enterprises Ltd. (Cyprus) v. Russian Federation, PCA Case No. AA 226, Final Award, 1406-1407 (Jul. 18, 2014).

obligations under Article 13(1) of the Energy Charter Treaty when it took steps equivalent to the expropriation of the claimants' investment in Yukos. In its award, the tribunal said, "Yukos was the object of a series of politically motivated attacks by the Russian authorities that eventually led to its destruction . . . . The primary objective of the Russian Federation was not to collect taxes but rather to bankrupt Yukos and appropriate its valuable assets."[105]

This award is important as the Tribunal held that the primary objective of the Russian Federation was not to collect taxes but rather to bankrupt Yukos and appropriate its valuable assets, and that if the true objective was tax collection, Yukos, its officers, employees, properties and facilities would not have been mistreated the way they were. Also, the Tribunal held that the fines imposed by the Russian Federation after finding Yukos liable for the payment of VAT on the export of the oil and oil products by its trading companies rendered Yukos bankrupt. In substance, the actions taken by the Russian Federation had an effect equivalent to nationalization or expropriation, as:

(a) The destruction of Russia's leading oil company and largest taxpayer was not in public interest;

(b) No due process was followed as evidenced by the harsh treatment accorded to Mikhail Khodorkovsky and Platon Lebedev (remotely jailed and caged in court), the mistreatment of counsel of Yukos, the difficulties counsel encountered in reading the record and conferring with Messrs. Khodorkovsky and Lebedev, the very pace of the legal proceedings, etc.; and

(c) No payment of prompt, adequate and effective compensation, or any kind of compensation was made.

The treatment of Yukos vis-à-vis other Russian oil companies that also took advantage of investing in low tax jurisdictions may have been discriminatory. (The question was not decided by the Tribunal as it was inconclusively argued.) Having found the Russian Federation in violation of Article 13(1) of the ECT for expropriating Yukos, the Tribunal did not consider it necessary to venture into the issue of Fair and Equitable treatment under Article 10(1) of the ECT.[106]

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[105] Yukos Universal Ltd. (Isle of Man) v. Russian Federation, PCA Case No. AA 227, Final Award, 1253 and 756 (Jul. 18, 2014).

[106] The Tribunal also found Yukos liable for contributory fault due to its abuse of tax avoidance arrangements in some of the low-tax regions and the Cyprus–Russia DTAA. See Yukos Universal Ltd. (Isle of Man) v. The Russian Federation, UNCITRAL, PCA Case No. AA 227, Final Award, (Jul. 18, 2014)

B. The Fair and Equitable Treatment of Foreign Investors

Comparative standards of treatment, like the MFN and NT principles, operate through the extension of rights already afforded to some investors and the investments of the contracting party. They do not, however, provide an objective guarantee of "good" treatment towards foreign investors. Indeed, the MFN and NT obligations would be of little help in the case that *all* investors were subject to equally egregious treatment. Absolute standards of treatment, such as the fair and equitable treatment, are meant to ensure that foreign investors are granted adequate treatment, independent of the treatment that the host country affords to its own investors or to investors from other countries.[107] Several formulations are found in BITs that are intended to express the obligation of the host state to provide a certain minimum standard of "good" treatment to foreign investors.[108] Most of these formulations relate to the most common requirement of ensuring FET to foreign investors.[109]

1. The Standard of Fair and Equitable Treatment

To the extent an investment treaty does not exclude taxation from the scope of the FET standard, it is possible for tribunal to review the legality of national tax measures in light of the FET principle. Actually, some treaties even explicitly call for such a possibility, as does the Lithuania-U.S. BIT: "With respect to its tax policies, each Party should strive to accord fairness and equity in the treatment of investment nationals and companies of the other Party."[110]

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[107] *See* generally Ronald Kläger, *Fair and Equitable Treatment*, *in* INTERNATIONAL INVESTMENT LAW 15–20 (2011). See also Stephan W. Schill, *General Principles of Law and Investment Law*, *in* INTERNATIONAL INVESTMENT LAW: THE SOURCES OF RIGHTS AND OBLIGATIONS 133, 134 (Tarcisio Gazzini & Eric de Brabandere eds., 2012).

[108] *See, e.g.*, UNCTAD, Fair and Equitable Treatment: UNCTAD Series on Issues in International Investment Agreements II, 1–12, U.N. Doc. UNCTAD/DIA/IA/2011/5 (2012) ("[T]he vague and broad wording of the obligation carries a risk of an overreach in its application"; "The vagueness of the FET standard is at the core of the problem"; "the legal building blocks for the analysis of the international minimum standard and its role in international investment law are precarious and often incomplete, vague and contested"; "It has even been suggested that due to its extreme vagueness the FET obligation lacks legitimacy as a legal norm").

[109] *See* Todd J. Grierson-Weiler & Ian A. Laird, *Standards of Treatment*, *in* THE OXFORD HANDBOOK OF INTERNATIONAL INVESTMENT LAW 272–77 (2008) (discussing requirements of good faith and its corollary of detrimental reliance on legitimate expectations in the context of international investment law generally and FET claims specifically).

[110] *See* Treaty Between the Government of the United States of America and the Government of the Republic of Lithuania for the Encouragement and Reciprocal Protection

Tribunals, in fact, have avoided grand theories about the meaning of the FET standard. Some authors, like Ioana Tudor, have endorsed such an approach, stating that "FET has only one content which [operates] at different thresholds, depending on the context".[111] However, these different formulations may lead to different interpretative outcomes.[112] Most commonly, any theoretical discussion is limited to a list of examples of the kinds of behavior that violate the standard.[113] In this respect, illustrative is the North American Free Trade Agreement (NAFTA) award in *Waste Management v. Mexico*, in which the tribunal held that FET is violated by conduct that is:

> [A]rbitrary, grossly unfair, unjust or idiosyncratic, is discriminatory and exposes the claimant to sectional or racial prejudice, or involves a lack of due process leading to an outcome which offends judicial propriety – as might be the case with a manifest failure of natural justice in judicial proceedings or a complete lack of transparency and candor in an administrative process. In applying this standard, it is relevant that the treatment is in breach of representations made by the host State which were reasonably relied on by the claimant.[114]

In this connection, the *Roussalis v. Romania* Award found that the scope of

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of Investment, Lith-U.S., art. X, Jan. 14, 1998, 2358 U.N.T.S. 9.

[111] *See* IOANA TUDOR, THE FET STANDARD IN THE INTERNATIONAL LAW OF FOREIGN INVESTMENT 154 (Oxford University Press, 2008). See also Ronald Kläger, *Fair and Equitable Treatment*, *in* INTERNATIONAL INVESTMENT LAW 15–20 (2011) (discussing the use of various international law sources in determining the nature of the fair and equitable treatment standard).

[112] The FET standard is expressed in different ways. Some treaties contain a bare reference to FET; others link FET to international law or to customary international law. Still others include the standard in a clause that also contains prohibitions against arbitrary and discriminatory acts and/or a "non-impairment" obligation. In this regard, the *Sempra v. Argentina* Award notes that FET is not a clear and precise standard and that it has evolved by case-by-case determinations. *See* Sempra Energy International v. Argentine Republic, ICSID Case No. ARB/02/16, Award, ¶ 296 (Sept. 28, 2007). Recently, the *El Paso v. Argentina Award*, citing the CMS Annulment Decision, agrees that there is variation in the practice of arbitral tribunals in relation to the fair and equitable standard. See El Paso Energy International Co. v. Argentine Republic, ICSID Case No. ARB/03/15, Award, ¶ 338 (Oct. 31, 2011).

[113] *Mondev v. United States* observed that the minimum standard of treatment "applies to a wide range of factual situations, whether in peace or in civil strife, and to conduct by a wide range of state organs and agencies," Mondev International Ltd. v. United States of America, ICSID Case No. ARB(AF)/99/2, Award, ¶ 95 (Oct. 11, 2002).

[114] Waste Mgmt., Inc. v. United Mexican States, ICSID Case No. ARB(AF)/00/3, Award, ¶ 98 (Apr. 30, 2004).

the fair and equitable treatment standard is not precisely defined beyond general principles (i.e., transparency, good faith, etc.).[115] The broad meaning given to the FET allows claimants to often use it in their dispute with host states. As such, the FET has become a pillar of the investment regime.[116] For this reason, many tribunals, such as the one in the *Sempra v. Argentina* Award, have highlighted the central role of fair and equitable treatment in investment treaties.[117]

2. Impact in the Regime of Tax

The *Toto Costruzioni v. Lebanon* Decision on Jurisdiction found that treaty provisions requiring the state to create and maintain "favourable economic and legal conditions" do not prohibit an increase in customs duties and taxes.[118] In this respect, at present there have been four investment disputes which have resulted in a finding that national tax measures violated the obligation of FET enshrined in the relevant IIAs.[119]

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[115] Spyridon Roussalis v. Romania, ICSID Case No. ARB/06/1, Award, ¶ 318 (Dec. 1 2011). In the same vein, the *Hochtief v. Argentina* Decision on Liability notes that the tribunal is mindful of the controversy concerning the precise definition and content of the FET standard; the treaty does not define the FET standard, and the decisions of other tribunals are not in themselves binding sources of international law; however, the tribunal notes that the threshold for a treaty breach set by Waste Management II is representative of the approach taken by investment tribunals to this question, and agrees that this is the proper approach to the interpretation of the FET obligation. HOCHTIEF Aktiengesellschaft v. Argentine Republic, ICSID Case No. ARB/07/31, Decision on Liability, ¶ 219 (Dec. 29, 2014).

[116] *See, e.g.*, Ole Kristian Fauchald, *The Legal Reasoning of ICSID Tribunals - An Empirical Analysis*, 19 EUR. J. INT'L. L. 301, 312 (2008).

[117] *See* Sempra Energy International v. Argentine Republic, ICSID Case No. ARB/02/16, Award, ¶ 300 (Sept. 28, 2007). Also the *Continental Casualty v. Argentina* Award finds that fair and equitable treatment is especially important for direct investments which are usually made for a considerable duration and whose profitability and economic contribution to the host country's economy are dependent on them being treated by local authorities in a way which is coherent with the ordinary conduct of business activity. Continental Casualty Company v. Argentine Republic, ICSID Case No. ARB/03/9, Award, ¶ 254 (Sept. 5, 2008).

[118] "The Tribunal finds that the Treaty does not sanction changes in legislation. It rather obliges Lebanon to create and maintain favorable economic and legal conditions. The Tribunal does not regard a mere increase in customs duties and taxes as prima facie evidence of failure to maintain "favorable economic and legal conditions" of the investment." Toto Costruzioni Generali S.p.A. v. Republic of Lebanon, ICSID Case No. ARB/07/12, Decision on Jurisdiction, 129 (Sept. 11, 2009).

[119] Occidental Exploration and Production Company v. The Republic of Ecuador, LCIA Case No. UN3467, Final Award, (Jul. 1, 2004); Enron Corporation and Ponderosa Assets, L.P. v. Argentine Republic, ICSID Case No. ARB/01/3, Award, (May 22, 2007) (also known as: Enron Creditors Recovery Corp. and Ponderosa Assets, L.P. v. The Argentine Republic);

This Article focuses on the first investment award which identified a FET breach due to tax measures. The *Occidental Exploration v. Ecuador* Final Award highlighted that various tribunals have insisted on the need for a stable legal and business framework.[120]

In the *Occidental v. Ecuador* Award of 2004, the claimant had a long-standing commercial relationship with Petroecuador and its predecessor.[121] Until 1999 the Occidental Exploration & Production Company (OEPC) was a mere service provider to Ecuador; it received a fee and was reimbursed for the purchases it made on Ecuador's behalf for the provision of exploitation activity. In 1999, however, OEPC obtained the exclusive right to carry out the exploration and exploitation of hydrocarbons in Block 15 and assumed virtually all of the costs of doing so. It also had to pay VAT on any expenses it incurred. In return for its obligations under the contract, it received a percentage of the oil, which it was permitted to export.[122]

In 2001, the Ecuadorian authorities took the position that OEPC's contract took account of the paid VAT, in effect compensating OEPC with respect to its VAT liability. Therefore, OEPC was not entitled to VAT refunds. Resolutions were issued denying the right to refunds. OECP disagreed with such an interpretation. According to the applicable BIT, a breach of the expropriation article occurs only if deprivation arises to a level that represents a significant part of the investment. In this case, the tribunal did not find that substantial economic deprivation had occurred.

Duke Energy Electroquil Partners & Electroquil S.A. v. Republic of Ecuador, ICSID Case No. ARB/04/19, Award, (Aug. 18, 2008); El Paso Energy International Company v. The Argentine Republic, ICSID Case No. ARB/03/15, Award, (Oct. 31, 2011).

120 Occidental Exploration & Production Company v. Republic of Ecuador, LCIA Case No. UN3467, Final Award, ¶ 184–85 (Jul. 1, 2004). Such an idea was further confirmed by other tribunals. For instance, *Total v. Argentina*, Decision on Liability noted that the applicable BIT does not contain any reference to "a stable framework for investments," holds that this indicates at a minimum that stability of the legal domestic framework was not envisaged as a specific element of the domestic legal regime that the Contracting Parties undertook to grant to their respective investors. *Total S.A. v. Argentine Republic*, ICSID Case No. ARB/04/01, Decision on Liability, 113–117, 122, 146, 309, 312, 435 (Dec. 27, 2010). Also, *LESI and Astaldi v. Algeria* Award cites *MTD v. Chile* and *Tecmed v. Mexico* in concluding that a State's obligation to undertake "fair and equitable treatment" means that the state must act in a coherent, non-ambiguous, and transparent manner, whilst maintaining a sufficiently stable investment climate so as to allow a reasonably diligent investor the opportunity to adopt, then implement, their commercial strategy; moreover, the state must also act in a non-arbitrary and non-discriminatory manner, and refrain from any abuse of power while executing its contractual undertakings. LESI, S.p.A. and Astaldi, S.p.A. v. People's Democratic Republic of Algeria, ICSID Case No. ARB/05/3, Award, ¶ 151 (Nov. 12, 2008) [French].

121 Occidental Exploration & Production Company v. Republic of Ecuador, Final Award, London Court of International Arbitration Case No. UN3467 (Jul. 1, 2004).

122 *Id*. at ¶¶ 3–4, 26–30, 45, 88–89, 127, 168–200 (Jul. 1, 2004).

However, there was a violation of NT because the claimant had been treated in a less favorable manner than other exporters (e.g., banana and palm oil exporters). There was also a violation of FET, because, even if there is not a VAT obligation under international law, there is an obligation not to alter the legal and business framework of an investment.[123]

The tribunal interpreted the FET standard to require the "stability of [the] legal and business framework,"[124] and it emphasized that "the relevant legal question under international law was not whether there was an obligation to refund VAT . . . but whether the legal and business framework met the requirements of stability and predictability."[125] The tribunal also noted that the FET standard is objective and does not depend on whether or not the respondent acts in good faith.[126] The tribunal concluded that "the framework, under which the investment was made and operates, has been changed in an important manner by the actions adopted by the Servicio de Rentas Internas, an Ecuadorian tax authority, and "[t]he tax law was changed without providing any clarity about its meaning and extent, and the practice and regulations were also inconsistent with such changes."[127] The tribunal thus concluded that Ecuador breached its obligation to accord FET.

C. Full Protection and Security Guaranteed to Foreign Investors

The full protection and security standard was originally perceived as a very minor provision in IIAs. However, over the last few years it has become increasingly important. Indeed, one of the key substantive provisions commonly included in investment treaty texts is the obligation to provide "full protection and security."[128] Different formulations are also

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[123] *Id.* at ¶ 191.

[124] Occidental Exploration & Production Company v. Republic of Ecuador, Final Award, London Court of International Arbitration Case No. UN 3467, ¶ 183 (Jul. 1, 2004).

[125] *Id.* at ¶ 191.

[126] *Id.* at ¶ 186.

[127] *Id.* at ¶ 184.

[128] NAFTA: Legal Text and Interpretive Materials § 20:24 art. 1105(1), (Sept. 1, 1992) which provides that "[e]ach party shall accord to investments of investors of another party treatment in accordance with international law, including fair and equitable treatment and full protection and security." *See also* NAFTA: Legal Text and Interpretive Materials § 18:1 (July 31, 2001) (documenting the interpretation of this provision adopted by the Free Trade Commission on July 31, 2001. The Commission took the view that "[a]rticle 1105(1) prescribes the customary international law minimum standard of treatment of aliens as the minimum standard of treatment to be afforded to investments of another Party," and that "[t]he concepts of 'fair and equitable treatment' and 'full protection and security' do not require treatment in addition to or beyond that which is required by the customary international law minimum standard of treatment of aliens."). For further discussion, see *The Loewen Group, Inc. & Raymond L. Loewen v. United States*, ICSID Case No.

found, such as "full protection and full security,"[129] "constant protection and security,"[130] "protection and security,"[131] and "physical protection and security,"[132] but these variations do not have much impact on the way the standard is applied.[133] This Article will present the concept of FPS before looking at the way it may be applied in tax-services-related disputes.

ARB(AF)/98/3, Award, ¶¶ 35–39 (June 26, 2003). The *Frontier Petroleum v. Czech Republic* Final Award holds that where the acts of the host State's judiciary are at stake, "full protection and security" means that the State is under an obligation to make a functioning system of courts and legal remedies available to the investor; on the other hand, not every failure to obtain redress is a violation of the principle of full protection and security and even a decision that in the eyes of an outside observer, such as an international tribunal, is "wrong" would not automatically lead to State responsibility as long as the courts have acted in good faith and have reached decisions that are reasonably tenable. *See* Frontier Petroleum Services Ltd. v. Czech Republic, UNCITRAL, Final Award, ¶ 273 (Nov. 12, 2010).

[129] This is incorporated in NAFTA as well. Article 1105 of NAFTA states, "Each Party shall accord to investments of investors of another Party treatment in accordance with international law, including fair and equitable treatment and full protection and security." North American Free Trade Agreement, U.S.-Can.-Mex., art. 1105, Dec. 17, 1992, § 1, 32 I.L.M. 612, 639 (1993). *See, e.g.,* ADF Group Inc. v. United States, 6 ICSID (W. Bank) 499, 530 ¶ 184 (Jan. 9, 2003) (holding "fair and equitable treatment" and "full protection and security" to be based on "State practice and judicial or arbitral case law or other sources of customary or general international law."); *see also* Noble Ventures Inc. v. Romania, ICSID Case No. ARB/01/11 ¶ 164 (Oct. 12, 2005) (holding similarly that it is doubtful the clause in the U.S.-Romanian BIT could be "understood as being wider in scope than the general duty to provide for protection and security of foreign nationals found in the customary international law of aliens").

[130] *See e.g.,* Agreement Between the Government of the People's Republic of China and The Government of Côte d'Ivoire on the Promotion and Protection of Investments, China-Côte d'Ivoire, art. 2(2), Sept. 23, 2002, http:// www.unctad.org/sections/dite/iia/docs/ bits/china_cotedivoire.pdf ("Investments of the investors of either Contracting Party shall enjoy the constant protection and security in the territory of the other Contracting Party. 3. Without prejudice to its laws and regulations, neither Contracting Party shall take any unreasonable or discriminatory measures against the management, maintenance, use, enjoyment and disposal of the investments by the investors of the other Contracting Party"); *see* RUDOLF DOLZER & CHRISTOPH SCHREUER, PRINCIPLES OF INTERNATIONAL INVESTMENT LAW 132 (2d ed. 2012) 160–162.

[131] *Id.*

[132] *Id.*

[133] The *Parkerings v. Lithuania* Award found that it is generally accepted that the variation of language between the formulation of "protection" and "full protection and security" does not make a significant difference in the level of protection a host state is to provide. *See* Parkerings-Compagniet AS v. Republic of Lithuania, ICSID Case No. ARB/05/8, Award, ¶ 354 (Sept. 11, 2007), http://www.italaw.com/sites/default/ files/case-documents/ita0619.pdf.

1. The Principle of Full Protection and Security

The extent of the protection was detailed in the *Saluka v. Czech Republic* Award, which noted that the "'full protection and security' standard applies especially when the foreign investment has been affected by civil strife and physical violence."[134] It is clear that tribunals are in agreement that the standard "applies at least in situations where actions of third parties involving either physical violence or the disregard of legal rights occur, and requires that the state exercise due diligence to prevent harm to the investor."[135]

It is "understood that the FPS standard does not grant the investor an 'insurance against all and every risk,'" as noted recently in the *Vanessa Ventures v. Venezuela* Award.[136] International law generally holds that "although the host state is required to exercise an objective minimum standard of due diligence, the standard of due diligence is that of a host state in the circumstances and with the resources of the state in question" (a modified objective standard).[137] This view has been endorsed by subsequent tribunals.[138] More recently, the scope of the full protection and security concept has been extended to "provide a legal framework that offers legal protection to investors – including both substantive provisions to protect investments and appropriate procedures that enable investors to vindicate their rights."[139]

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[134] Saluka. Invs. BV (Netherlands) v. Czech Republic, Partial Award, UNCITRAL, ¶ 483 (Mar. 17, 2006). Technically, it was *Asian Agricultural Products Ltd. v. Democratic Socialist Republic of Sri Lanka*, ICSID Case No. ARB/87/3, Final Award on Merits and Damages, 30 I.L.M. 577 (Jun. 21, 1990) where the FPS standard was discussed first.

[135] *See Parkerings-Compagniet AS.*, ICSID Case No. ARB/05/8, Award.

[136] Vanessa Ventures Ltd. v. Bolivarian Republic of Venezuela, ICSID Case No. ARB(AF)/04/6, Award, ¶ 223 (Jan. 16, 2013).

[137] Pantechniki v. Albania Award, ICSID Case No. ARB/07/21, Award, ¶ 81 (Jul. 30, 2009), citing ANDREW NEWCOMBE & LLUÍS PARADELL, LAW AND PRACTICE OF INVESTMENT TREATIES 233 (2009). *See* Parkerings-Compagniet AS v. Republic of Lithuania*,* ICSID Case No. ARB/05/8, Award, ¶¶ 81–84 (Sept. 11, 2007).

[138] For instance, *Paushok v. Mongolia* notes that "[t]he 'legal protection' clause has been raised in a number of BIT cases and it has sometimes been interpreted, as a stand-alone clause, as aiming at the physical protection of persons or assets against illegal actions by third parties"; in the case before the tribunal "the treaty provides clearly for 'full legal protection to investments of investors of the other Contracting Party'" and "there is therefore no reason to limit the protection guaranteed to mere physical protection." Sergei Paushok, CJSC Golden East Co. & CJSC Vostokneftegaz Co. v. Mongolia, Award on Jurisdiction and Liability, ¶ 326 (Apr. 28, 2011). See also *Reinhard Unglaube and Marion Unglaube v. Costa Rica* Award, which accepted that "full protection" may, in appropriate circumstances, extend beyond the traditional standard focused on physical security. Unglaube v. Republic of Costa Rica, ICSID Case No. ARB/09/20, Award, ¶ 281 (May 16, 2012).

[139] Frontier Petroleum.Servs. Ltd v. Czech Republic, UNCITRAL, Final Award, ¶ 263

2. Impact in the Regime of Tax

So far, the standard of full protection and security has never been directly applied in a tax-related dispute. Of course, in the *Occidental v. Ecuador* Award of 2004, the tribunal found a breach of FPS, but it was as a consequence of the FET violation. Having found that Ecuador was in breach of the FET standard, the tribunal held that this had the effect of also constituting a breach of the related BIT guarantee of Full Protection and Security.[140]

This does not, however, mean that such a provision is irrelevant. On the contrary, the FPS has been increasingly applied in recent disputes, which shows that its potential has been only partly explored. The FPS standard is likely to be applied in future disputes. Indeed the *Burlington Resources v. Ecuador* Decision on Jurisdiction held that a full protection and security claim, rooted in the respondent's purported failure to provide legal and commercial security, challenges taxation law and thus raises "matters of taxation" under Article X of the BIT.[141]

D. The Non-Discrimination Principle

Countries conclude IIAs primarily for the protection and, indirectly, promotion of foreign investment. IIAs offer contracting parties increased security and certainty under international law when they invest or set up a business in other countries which are parties to the agreement. The reduction of investment risk flowing from an IIA is meant to encourage companies and individuals to invest in the country that entered into the IIA. Allowing foreign investors to settle disputes with the host country through international arbitration, rather than only through the host country's domestic courts, is an important aspect of the construct. Non-discrimination, in the broadest sense, means that the host country must refrain from taking discriminatory actions against either specific foreign investors or foreign investors in general. BITs use two different terms to

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(Nov. 12, 2010).

140 Occidental Exploration & Production Company v. Republic of Ecuador, London Court of International Arbitration Case No. UN3467, Final Award, ¶ 187 (Jul. 1, 2004).

141 The Burlington Tribunal stated that "[o]n the basis of these allegations, the Tribunal deems that Claimant's full protection and security claim, rooted in Ecuador's purported failure to provide legal and commercial security in Blocks 7, 21, 23, and 24, challenges Law 42 and thus raises 'matters of taxation' under Article X. Accordingly, as is the case with the FET claims and the arbitrary impairment claim, which also involve taxation matters, the tribunal must ascertain whether this claim relates to the observance and enforcement of the terms of an 'investment agreement' in order to determine its jurisdiction over this claim." Burlington Resources Inc. v. Republic of Ecuador, ICSID Case No. ARB/08/5, Decision on Jurisdiction, ¶ 215 (Jun. 2, 2010).

prevent the discriminatory treatment of investments: the MFN clause and the NT standard.

1. The Principles of National Treatment and Most-Favored-Nation Treatment

The *Asian Agricultural Products v. Sri Lanka* Dissenting Opinion of Samuel K.B. Asante, citing various publicists, noted that NT does not derive from customary law.[142] According to investment treaties, NT requires that foreign investors are accorded treatment that is no less favorable than that accorded to investors from the host state.[143] Essentially, NT requires that countries do not discriminate against foreign investors in favor of domestic investors.[144] The promise of NT in an IIA is appealing to foreign investors. On the other hand, some IIAs allow the contracting states to have exceptions to NT in their respective legislation.[145]

"No less favorable" treatment does not necessarily mean "the same" treatment. NT prohibits both discriminatory treatment expressed in law (*de jure*) as well as discriminatory treatment resulting from the application of the law in fact (*de facto*). The *Bogdanov v. Moldova III* Final Award noted that although "discrimination can take many different forms in the context of the treatment of foreign investments a very frequent problem . . . is discrimination on the basis of nationality."[146] The benefit of NT to an investor is that it offers the investor a level playing field and protects the investor against discrimination.

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[142] Asian Agricultural Products Ltd. v. Democratic Socialist Republic of Sri Lanka, ICSID Case No. ARB/87/3, Final Award on Merits and Damages (1991), ¶¶ 40–41, 30 I.L.M. 577 (Jun. 21, 1990) (Samuel K.B. Asante, dissenting) (Jun. 27, 1990).

[143] *Champion v. Egypt* Award states that national treatment prohibits discrimination on the grounds of nationality. Champion Trading Company & Ameritrade International, Inc. v. Arab Republic of Egypt, ICSID Case No. ARB/02/9, Award, ¶¶ 128, 156 (Oct. 27, 2006).

[144] The standard of treatment can be defined in two ways: "same" or "as favorable as" treatment or "no less favorable" treatment than the treatment they grant to investments of their own investors. The difference is subtle, but the "no less favorable" formulation leaves open the possibility that investors may be entitled to treatment that is more favorable than that accorded domestic investors, in accordance with international standards. Often the definition of NT is qualified by the inclusion of the provision that it only applies in "like circumstances" or "similar circumstances.". With the situations of foreign and domestic investors often not being identical, this language obviously leaves room for interpretation.

[145] Agreement Between the Government of the Kingdom of Sweden and the Government of the Russian Federation on the Promotion and Reciprocal Protection of Investments, article 3.3, Sweden-Russia, Apr. 19, 1991 (entered into force Sept. 28, 1992) ("Each Contracting Party may have in its legislation limited exceptions to national treatment provided for in Para. (2) of this Article.").

[146] Bogdanov & Bogdanov v. Moldova (Russ. v. Mold.), Final Award, SCC Case No. V091/2012, ¶¶ 215–16 (Apr. 16, 2013).

The *Occidental Exploration v. Ecuador* Final Award stated that "the purpose of NT is to protect investors as compared to local producers, and this cannot be done by addressing exclusively the sector in which the particular activity is undertaken."[147] However, for host states, NT reduces the possibility of favoring domestic firms, unless exceptions or reservations are expressly introduced into agreements to allow discrimination such as is commonly done in the case of government procurement, domestic subsidies to local business, etc.[148] The U.S. Model BIT creates exclusions from MFN and NT for these kinds of government actions in addition to a general exception for security.[149] Host states could also use a positive list, such that NT is applicable only to sectors covered in the list and not common to all. The scope of NT in this kind of provision is limited, although quite broad. It is applicable only to the "establishment, acquisition, expansion, management, conduct, operation and sale or other disposition"[150] of investments.

Under international law, the usual rule, derived from the principle of territorial sovereignty, allows a state to prohibit the admission of foreigners and to deny the right to settle within its territory. This principle is reflected in many international agreements.[151] In other words, under the classic BIT the host country has the exclusive authority to decide whether an investment may be allowed within its territory.

The *Parkerings v. Lithuani*a Award discussed the relationship between MFN, NT and discrimination, noting that differentiated treatment must be

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[147] Occidental Exploration & Prod. Co. v. Ecuador (U.S. v. Ecuador), Final Award, LCIA Case No. UN3467, ¶ 173 (Jul. 1, 2004).

[148] *See* generally CARIN SMALLER & HOWARD MANN, A THIRST FOR DISTANT LANDS: FOREIGN INVESTMENT IN AGRICULTURAL LAND AND WATER, INST. FOR SUSTAINABLE DEV. 14 (2009) at 11.

[149] *See* Catherine H. Gibson, *Beyond Self-Judgment: Exceptions Clauses in US BITs*, 38 FORDHAM INT'L L.J. 1 (2015).

[150] For an analysis of U.S. BITs approach of national treatment, see Kenneth J. Vandevelde, *A Comparison of the 2004 and 1994 US Model BITs: Rebalancing Investor and Host State Interests, in* YEARBOOK ON INTERNATIONAL INVESTMENT LAW AND POLICY 283 (Karl P. Sauvant, ed., 2009).

[151] Most countries are reluctant to grant to nationals and foreign companies an unqualified right to make investments in their territories and for various reasons. Countries are often reluctant to allow foreign control of the most important means of production. Some countries may be concerned about the issue of foreign ownership in industries that are essential to national security, while others countries may be interested in foreign ownership of industries of particular importance to the development effort or ones that have a value and a special cultural significance. In other cases, domestic firms may require protection against foreign competition. The result is that many countries impose restrictions or conditions on the entry of foreign direct investment in specific industries. For these reasons, in general, a BIT does not give investors the absolute right to make investments in the territory of the other contracting party.

objectively justified.[152] The MFN standard establishes, at least in principle, a level playing field between all foreign investors. MFN treatment requires that a government does not discriminate between foreign investors from different countries. Unlike NT, virtually all IIAs include the MFN standard.[153] The MFN standard does not require the host country to treat enterprises in different sectors or in different "situations" or "circumstances" in the same way; however, there is difficulty in determining what constitutes a "like circumstance."[154]

2. Impact in the Regime of Tax

The NT standard under investment treaties is a protection against discrimination which extends far beyond the NT found in tax treaties. In order to assess the added value of the investment standard with regard to foreign investors operations, one can look at the investment disputes lost by host-states on the ground of NT. The NT clause was violated by tax measures in three different disputed matters, namely *Marvin Feldman v. Mexico; Occidental Exploration & Prod. Co. v. Ecuador;* and *Archer Daniels Midland Co. & Tate & Lyle Ingredients Americas, Inc. v. Mexico*.[155] The *Marvin Feldman v. Mexico* Award is of great importance because it held that "tax law and policy changes are intended to be given relatively broad leeway under NAFTA, even if their effect is to make it

[152] Parkerings-Compagniet AS v. Lithuania, (Nor. v. Lith.), ICSID Case No. ARB/05/8, Award, ¶¶ 366–371 (Sep. 11, 2007).

[153] BITs commonly provide that MFN treatment shall not apply so as to require that investors be given the same benefits as may be given to investors under the terms of customs unions, free trade zones, economic unions and the like. That provision ensures that the BIT does not become an impediment to regional economic integration. *See* Agreement Between the Government of Hong Kong and the Government of the Republic of Austria for the Promotion and Protection of Investments H.K.-Austria, art. 4, Oct. 11, 1996 which provides that MFN obligations shall not apply so as to require the host state to match any benefits resulting from any arrangements "designed to lead in future" to a regional customs, monetary, tariff or trade arrangement, or from any arrangement with any third state in the region "designed to promote regional cooperation in the economic, social, labor, industrial or monetary fields within the framework of specific projects."

[154] On the difficulties and controversies provoked by the extension of jurisdiction via MFN clauses, see generally Julie A. Maupin, *MFN-Based Jurisdiction in Investor-State Arbitration: Is There Any Hope for a Consistent Approach*?, 14 J. INT'L ECON. L. 157, 157–162 (2011).

[155] Marvin Feldman v. Mexico, ICSID Case No. ARB(AF)/99/1, Award, ¶¶ 1, 165, 188 (Dec. 16, 2002) (also known as *Marvin Feldman v. Mexico*); Occidental Exploration & Prod. Co. v. Ecuador, LCIA Case No. UN3467, Final Award, ¶¶ 173–74 (Jul. 1, 2004); Archer Daniels Midland Co. & Tate & Lyle Ingredients Americas, Inc. v. Mexico, ICSID Case No. ARB (AF)/04/5, Award, ¶¶ 3, 304(Nov. 21, 2007).

impractical for certain business activities to continue."[156]

The 2002 NAFTA case of *Feldman v. Mexico* concerned tax rebates which may be available when cigarettes are exported. [157] In most instances, when cigarettes were purchased in Mexico at a price that included the tax and then subsequently exported, the tax amounts initially paid could be rebated. Due to a 1991 legislative amendment, cigarette resellers who were not also producers, such as Corporación de Exportaciones Mexicanas, S.A. (CEMSA), were subject to certain requirements in order to be eligible for rebates. CEMSA won an Amparo action[158] to challenge the constitutionality of the amendment. In 1992, while the Amparo action was still pending, the legislature amended the law, effectively reverting to the former system. In 1993, CEMSA was shut down because it was not able to meet the other requirements of the Impuesto Especial Sobre Producción y Servicios (IESP) law (a special or excise tax on products and services). CEMSA was required to obtain invoices separating tax from product price. However, CEMSA was not able to do so because it was a reseller, not a producer. The Mexican Supreme Court found this regulation unconstitutional. Nevertheless, the Mexican tax authority still asked CEMSA for such invoices.

CEMSA claimed that an oral agreement was reached in 1995 and it was paid a rebate for over a year. However, CEMSA was audited and was asked to repay $25 million for tax rebates for the 1993 through 1995 period. In this case, there was no expropriation, because not every business problem experienced by a foreign investor is an expropriation under NAFTA Article 1110: states are not required to permit the export of cigarettes; the claimant had no right to export cigarettes; and the claimant had not lost control of its investment.[159]

Interestingly, the *Feldman v. Mexico* Decision on Jurisdiction notes that NAFTA in principle does not apply to taxation measures (due to its exclusion under Article 2103), but there are several exceptions – such as the article on expropriation – to that exclusion.[160]

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[156] Karpa v. Mexico, Interim Decision on Preliminary Jurisdictional Issues, ICSID Case No. ARB(AF)/99/1, ¶ 116 (Dec. 6, 2000).

[157] *Id.* at ¶ 1.

[158] In Mexico, the Amparo remedy or action is an effective and inexpensive instrument for the protection of individual rights. *See* Orlando Federico Cabrera Colorado, *Telecommunications Reform and Other Policies That Impact on both the Internet and ICTs for the Economic Development of Mexico*, C.T.L.R. 20(5), 134–138 at n.10 (2014).

[159] The *Karpa v. Mexico* Award rejects an expropriation claim based on officials' alleged failure to comply with an oral agreement alleged to have waived an explicit requirement of a tax law. Karpa v. Mexico, Interim Decision on Preliminary Jurisdictional Issues, ICSID Case No. ARB(AF)/99/1, ¶ 128 (Dec. 6, 2000).

[160] The tribunal opined as follows: "On the other hand, NAFTA itself provides several

Although the tribunal found that there had been no expropriation, it did find that a violation of the NT standard had occurred. The limited facts made available demonstrated to a majority of the tribunal that CEMSA had been treated in a less favorable manner than domestically owned resellers/exporters of cigarettes, a *de facto* discrimination by the Mexican Ministry of Finance and Public Credit (Secretaría de Hacienda y Crédito Público, hereinafter SHCP), which is inconsistent with Mexico's obligations under Article 1102 of NAFTA. The only confirmed cigarette exporters on the limited record before the tribunal were CEMSA (owned by US citizen Feldman) and the Mexican corporate members of the Poblano Group (Mercados I and Mercados II). According to the available evidence, CEMSA had been denied the rebates for October–November 1997 and subsequently in the 1998–2000 period; SHCP had also demanded that CEMSA repay rebate amounts initially allowed from June 1996 through September 1997. Thus, CEMSA was denied IEPS rebates during the periods when members of the Poblano Group were receiving them.[161]

In addition, the tribunal found that CEMSA had been denied registration as an export trading company, even though three other cigarette-export trading companies (including the Poblano Group) had been swiftly granted registration.[162] While it recognized the limited extent of the evidence of discrimination on the record, the tribunal's holding was based, first, on the burden of proof being shifted from the claimant to the respondent (with the respondent then failing to meet its new burden), and, second, on a very simple two-pronged conclusion which was not effectively challenged by the respondent:

(a) no cigarette reseller-exporter could legally have qualified for

other time-related constraints in order to allow arbitration to proceed. Thus, under Article 1118, '[t]he disputing parties should first attempt to settle a claim through consultation or negotiation'; no time indication is provided here. In addition, under Article 1119, the notice of intent to submit a claim to arbitration shall be delivered to the disputing Party 'at least 90 days before the claim is submitted.' Moreover, under Article 1120 (1) a disputing investor may submit a claim to arbitration only after 'six months have elapsed since the events giving rise to [the] claim.' Finally, while NAFTA in principle does not apply to taxation measures (Art. 2103(1)), there are several exceptions. Among them, Article 1110 on expropriation and compensation shall apply to taxation measures and arbitration may proceed unless it has been determined that the measure is not an expropriation. If the competent authorities fail to agree that the measure is not an expropriation within a period of six months after this issue was referred to them, the claim pertaining to taxation measures alleged to be an expropriation may be submitted to arbitration (Art. 2103(6))." Karpa v. Mexico*,* Interim Decision on Preliminary Jurisdictional Issues, ICSID Case No. ARB(AF)/99/1, ¶ 42 (Dec. 6, 2000).

[161] Karpa v. Mexico, ICSID Case No. ARB(AF)/99/1, Award, ¶ 173 (Dec. 16, 2002).

[162] *Id.* at ¶ 175.

> the IEPS rebates, since none under the facts established in this case would have been able to obtain the necessary invoices stating the tax amounts separately, and (b) the claimant was denied the rebates at a time when at least three other companies in like circumstances, *i.e*., resellers and exporters apparently including at least two members of the Poblano Group, were granted them.[163]

On the other hand, one dissenting member of the tribunal believed that the evidence on the record was insufficient to prove discrimination.[164] Although the tribunal noted that there is no requirement in Article 1102 that any departure from NT must be explicitly shown to be a result of the investor's nationality, it nonetheless found that in the present case there was "evidence of a nexus between the discrimination and the claimant's status as a foreign investor."[165]

E. The Umbrella Clause

The "umbrella clauses," also known as "observance of undertakings"[166] clauses, play a key role in investment protection by providing a further guarantee to foreign investors.[167] In terms of drafting, the umbrella clauses are common to investment treaties and exist in numerous formulations.[168] Under a more expansive version, each state

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[163] *Id.* at ¶ 176 (internal citations omitted).

[164] Marvin Roy Feldman Karpa v. United Mexican States, ICSID Case No. ARB(AF)/99/1 (Dissenting Opinion of Jorge Covarrubias Bravo) (December 3, 2002) (also known as *Marvin Feldman v. Mexico*).

[165] Karpa v. Mexico, ICSID Case No. ARB(AF)/99/1, Award, ¶ 182 (Dec. 16, 2002).

[166] *See* Andrey V. Kuznetsov, *The Limits of Contractual Stabilization Clauses for Protecting International Oil and Gas Investments Examined Through the Prism of the Sakhalin-2 Psa: Mandatory Law, The Umbrella Clause, And The Fair And Equitable Treatment Standard*, 22 WILLAMETTE J. INT'L L. & DISP. RESOL. 223 (2015). For a discussion by tribunals, *see, e.g.*, Eureko B.V. v. Republic of Pol., Ad Hoc Arbitration under the Agreement Between the Kingdom of the Netherlands and the Republic of Poland on Encouragement and Reciprocal Protection of Investment, Partial Award, ¶¶ 251–56 (Aug. 19, 2005).

[167] *See* OECD, *Interpretation of the Umbrella Clause in Investment Agreements*, *in* INTERNATIONAL INVESTMENT LAW: UNDERSTANDING CONCEPTS AND TRACKING INNOVATIONS (2008).

[168] In the literature, these clauses are also referred to as 'elevator,' 'mirror' or 'parallel' clauses, among other names. *See* Thomas W. Wälde, *The "Umbrella" Clause in Investment Arbitration: A Comment on Original Intentions and Recent Cases*, 6 J. WORLD INVESTMENT & TRADE 183, 185 (2005); Anthony C. Sinclair, *The Origins of the Umbrella Clause in the International Law of Investment Protection*, 20 ARB. INT'L 411, 412 (2004). For a comprehensive study on the subject, see KATIA YANNACA-SMALL, INTERPRETATION OF THE UMBRELLA CLAUSE IN INVESTMENT AGREEMENTS (2006).

commits to "observe any obligation it may have entered into with regard to investments."[169]

1. The Notion of Umbrella Clause

Some IIAs cover only those disputes which relate to an "obligation under this agreement," i.e., only for claims of BIT violations.[170] Others extend the scope to ''any dispute relating to investments."[171] Still others create an international law obligation that a host state shall, for example, "observe any obligation it may have entered [in]to," "constantly guarantee the observance of the commitments it has entered into," "observe any other obligation it has assumed," or use yet even other formulations, with respect to investments.[172] These provisions are commonly called "*umbrella clauses*."[173]

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169 *See* Yuval Shany, *Contract Claims vs. Treaty Claims: Mapping Conflicts Between ICSID Decisions on Multisourced Investment Claims*, 99 AM. J. INT'L L. 835, 844–45 (attributing the difference in outcomes not to textual interpretation, but rather to a divide between "disintegrationist" and "integrationist" ideologies toward municipal and international law).

170 *See* UNCTAD, Bilateral Investment Treaties 1995-2006: Trends in Investment Rulemaking, 73, UNCTAD/ITE/IIT/2006/5 (Feb. 1, 2007) (stating that approximately forty percent of the existing BITs in 2006 contain such an umbrella clause). *See also* Jarrod Wong, *Umbrella Clauses in Bilateral Investment Treaties: Of Breaches of Contract, Treaty Violations, and the Divide Between Developing and Developed Countries in Foreign Investment Disputes*, 14 GEO. MASON L. REV. 135, 138 (2006).

171 *See, e.g.*, Agreement Concerning the Promotion and Reciprocal Protection of Investments, Chile-Den., art. 3(1), May 28, 1993, WIPO Lex No. TRT/CL-DK/001 (entered into force Nov. 30 1995); and Agreement between the Government of Hong Kong and the Government of Japan for the Promotion and Protection of Investment, H.K-Japan, art. 2(3), May 15 1997.

172 *See* Stephan W. Schill, *Enabling Private Ordering: Function, Scope and Effect of Umbrella Clauses in International Investment Treaties*, 18 MINN. J. INT'L. L. 1, 4 (2009). For a comprehensive study on the subject, see also KATIA YANNACA-SMALL, INTERPRETATION OF THE UMBRELLA CLAUSE IN INVESTMENT AGREEMENTS (2006) at 147.

173 An umbrella clause can be drafted in different ways. Under the Germany–Pakistan BIT, article 7: "Either Party shall observe any other obligation it may have entered into with regard to investments by nationals or companies of the other party." Treaty for the Promotion and Protection of Investments, Pak.-Ger., art. 7, Nov. 25, 1959, 457 U.N.T.S. 6575. In Australia–Poland 1991, article 10: "A Contracting Party shall, subject to its law, do all in its power to ensure that a written undertaking given by a competent authority to a national of the other Contracting Party with regard to an investment is respected." Reciprocal Promotion and Protection of Investments, Austl.-Pol., art. 10, May 7, 1991, ATS 10. In Singapore–Czech Republic 1995, article 15: "Each Contracting Party shall observe commitments, additional to those specified in this Agreement it has entered in to with respect to investments of the investors of the other Contracting Party. Each Contracting Party shall not interfere with any commitments, additional to those specified in this Agreement, entered into by nationals or companies with the nationals or companies of the other

In essence, an umbrella clause extends the scope of the application of a BIT and offers greater protection to the investor. The 2015 *OI European Group v. Venezuela* Award held that the broad language of the BIT's umbrella clause obligates the respondent State to comply with domestic laws and regulations.[174] If a BIT contains an umbrella clause a foreign investor should have an incremental incentive to invest in the host country. Conversely, if there is no umbrella clause, an investor will likely have relatively less interest in relying upon a BIT to invest.

The *CMS Gas Transmission v. Argentina* Decision of the ad hoc Committee on the Application for Annulment of the Argentine Republic had to elucidate the meaning of such a clause and held that the umbrella clause could only concern consensual obligations arising independently of the BIT, not general obligations; a contractual obligation towards a non-protected investor cannot be transformed by the magic of the so-called umbrella clause into a treaty obligation to a protected investor; its effect is not to transform the obligation which is relied upon into something else.[175] As for the obligations covered by the clause, the *Continental Casualty v. Argentina* Award found that obligations include contracts and unilateral commitments addressed specifically to foreign investors in relation to their investments; they can include unilateral commitments arising from provisions of the law of the host State regulating a particular business sector and addressed specifically to the foreign investors in relation to their investments therein.[176] What is essential is, as clarified by the *Al-Bahloul v.*

Contracting Party as regards their investments." Agreement Between the Government of the Czech Republic and the Government of the Republic of Singapore on the Promotion and Protection of Investment, Czech-Sing., art. 15, Apr. 8, 1995, *available at* http:// investment policyhub.unctad.org/Download/TreatyFile/981. For a discussion of the role of stabilization clauses in this respect, see generally Sam Foster Halabi, *Efficient Contracting Between Foreign Investors and Host States: Evidence from Stabilization Clauses*, 31 NW. J. INT'L. L. & BUS., 261, 265–66, 270–71, 291, 292, 293–94 (2011).

[174] OI European Group B.V. v. Bolivarian Republic of Venezuela, ICSID Case No. ARB/11/25, Award, ¶ 624 (Mar. 10, 2015). In the same vein, the Micula v. Romania Award notes that the tribunal does not need to decide whether a general entitlement, in a law or regulation, could give rise to an obligation subject to the umbrella clause; here the general obligation was converted into a specific commitment; however, the majority of the tribunal does not find that the claimants have provided sufficient evidence and legal arguments on the content of Romanian law for the tribunal to find the existence of an obligation protected by the umbrella clause. Ioan Micula, Viorel Micula and others v. Romania, ICSID Case No. ARB/05/20, Award, ¶¶ 422, 447, 459 (Dec. 11 2013).

[175] CMS Gas Transmission Company v. Argentine Republic, ICSID Case No. ARB/01/8, Decision of the Ad Hoc Committee on the Application for Annulment of the Argentine Republic, ¶ 95 (Sept. 25, 2007).

[176] Continental Casualty Company v. Argentine Republic, ICSID Case No. ARB/03/9, Award, 298–301 (Sept. 5, 2008). In this respect, *Burlington Resources v. Ecuador* Decision on Jurisdiction considered that a claimant may rely upon the treaty's umbrella clause even if

Tajikistan Partial Award on Jurisdiction and Liability, that as the obligation must have been entered into "with" an investor or an investment of an investor, the provision does not refer to general obligations of the State arising as a matter of law.[177]

2. Impact in the Regime of Tax

The impact of the "umbrella clause" on tax matters can be assessed in light of the investment disputes lost by host states on the grounds of such a clause. There have been two disputes involving tax matters that have resulted in a breach of the umbrella clause.[178] This Article first focuses on the 2007 *Enron Corporation v. Argentina* Award.[179] In the 1990's, the Government of Argentina undertook a vast program of privatization of State-owned companies, including, *inter alia*, key sectors of economy, gas transportation and distribution.[180] The Currency Convertibility Law was enacted and several other measures directed at integrating the economy with global trade and business were undertaken. TGS, a major gas transportation company, was created in 1991. Enron began making an investment in TGS by means of a number of complex transactions and eventually held up to 35.5% of the company.[181] However, the Argentine Government asserted

no exercise of sovereign power is involved. Burlington Resources Inc. v. Republic of Ecuador, ICSID Case No. ARB/08/5, Decision on Jurisdiction, ¶ 190(June 2, 2010). However, there must be an obligation. Otherwise, as explained in the *Invesmart v. Czech Republic* Award, the tribunal may find that the investor has not established that there was any firm, unconditional undertaking, whether contractual or not, to provide State aid; an "obligation" to provide aid would require the establishment of a clear, unconditional commitment which would specify its essential terms including the amount of aid, the date to be provided and so on; an encouragement by the State to an investor to apply for aid or an expectation by an investor that aid will be provided is not sufficient by itself to constitute an "obligation" to provide aid. Invesmart, B.V. v. Czech Republic, UNCITRAL, Award (Redacted), ¶ 526 (June 26, 2009).

[177] Mohammad Ammar Al-Bahloul v. Republic of Tajikistan, SCC Case No. V064/2008, Partial Award on Jurisdiction and Liability, ¶ 257 (Sept. 2 2009).

[178] *Enron Corp.& Ponderosa Assets, L.P. v. Argentine Republic*, ICSID Case No. ARB/01/3, Award, (May 22, 2007) (also known as: *Enron Creditors Recovery Corp. & Ponderosa Assets, L.P. v. The Argentine Republic*), http://www.italaw.com/sites/default/files/case-documents/ita0293.pdf; *Duke Energy Electroquil Partners & Electroquil S.A. v. Republic of Ecuador*, ICSID Case No. ARB/04/19, Award, (Aug. 18, 2008), http://www.italaw.com/sites/default/files/case-documents/ita0256.pdf.

[179] *Enron Corp. & Ponderosa Assets, L.P. v. Argentine Republic*, ICSID Case No. ARB/01/3, Award, (May 22, 2007) (also known as: *Enron Creditors Recovery Corp. & Ponderosa Assets, L.P. v. Argentine Republic*) http://www.italaw.com/sites/default/files/case-documents/ita0293.pdf.

[180] *See id.* at ¶ 41.

[181] *Id.* at ¶ 53.

that Enron could claim only a 19.5% indirect interest in TGS, because its investment was partially financed by loan.

Several important terms upon which Enron relied when it made its decision to invest included measures such as:

> The calculation of tariffs in US dollars; their semiannual adjustment according to changes in the US Producer Price Index ('PPI'); the commitment that there would be no price freeze applicable to the tariff system and, if one was imposed, the licensee had a right to compensation; the commitment that the license would not be amended by the Government, in full or in part, except with the prior consent of the licensee [etc.].[182]

However, due to socio-economic and political crises, the environment in Argentina became unsympathetic to foreign investors in utility companies. No PPI adjustments were made after 1999 and all PPI adjustments were subsequently abolished by the Argentine authorities. Further, in 2001, according to an Emergency Law, the right to calculate tariffs in U.S Dollars was eliminated and tariff convertibility was fixed at one dollar to one peso.

Aggrieved by these measures, the claimants initiated arbitration and claimed damages suffered due to them. However, in 2001 the claimants had filed a request for arbitration against the Argentine Republic concerning certain tax assessments (referred to as the Stamp Tax Claim) imposed by some Argentinian provinces with respect to TGS under the Argentina-U.S BIT.[183] Then, in 2003, while the first request for arbitration concerning tax was pending, a new request came with respect to the measures related to PPI adjustments and the freezing of tariffs as discussed above. The Stamp Tax claim was suspended until December 2005 and was eventually discontinued without prejudice on the agreement of both parties. Therefore, the right of each party to proceed with the Stamp Tax Claim at the ICSID was protected.[184]

Because the Stamp Tax claim was discontinued, there was no discussion of the merits of the tax claim. However, other claims, including those related to PPI indexing, the calculation of tariffs in U.S Dollars, the stability of contracts and licensing under Argentine Law, were decided on the merits. The Tribunal held that there was breach of the fair and equitable treatment standard, because "a stable legal framework" that induced the investment was no longer in place and a definitive framework was not made available almost for five years.[185] The tribunal did not find the claim of

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182 *Id.* at ¶ 44.

183 *Id.* ¶ 3.

184 *Id.* at ¶¶ 41–44, 53–55, 63–72, 276.

185 Id. at ¶¶ 28, 127–28, 210–212, 267.

expropriation substantiated, because it did not find that there had been any capricious, irrational or absurd differentiation in the treatment accorded to the claimants compared to investors in other entities or sectors; neither was there a breach of the FPS obligation. The Tribunal held that the breach of Argentina's obligations under both the contract and the law with respect to the investment constituted a breach of protection under the umbrella clause of the BIT.

The umbrella clause also played a prominent role in a second dispute – the 2008 *Duke Energy v. Republic of Ecuador* Award. This award is interesting because it references *Encana v. Ecuador* for the view that it is in the nature of a tax that it is imposed by law on classes of persons to pay money to the state for public purposes.[186] *Duke Energy v. Ecuador* also approves of the approach taken in *Encana v. Canada*, finding that a claim for customs duties relates to matters of taxation.[187]

The *Duke Energy v. Ecuador* dispute, filed with ICSID in 2004, arose out of agreements between Electroquil, an Ecuadorian company in which Delaware-based Duke Energy acquired an ownership interest in 1998, and INECEL, a state-owned power company.[188] Electroquil was to receive a guaranteed price for the electricity it supplied to INECEL, and in return INECEL would guarantee the delivery of certain amounts of power. Should Electroquil fail to meet its obligations, INECEL was permitted to penalize the company.[189]

A year into the agreement, INECEL began fining Electroquil; by 2002 these fines totaled over $8 million.[190] The fines, which Electroquil argued

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[186] *Duke Energy Electroquil Partners & Electroquil S.A. v. Republic of Ecuador*, ICSID Case No. ARB/04/19, Award, ¶ 174 (Aug. 18, 2008).

[187] *Id.* at ¶¶ 174–175.

[188] *Id.* at ¶ 44.

[189] *Id.* at ¶ 16–36.

[190] *Id.* at ¶ 410. In 1992, a crisis resulting in a national power shortage prompted Ecuador to issue the First Emergency Decree and consequent allocation of funds by the Ministry of Finance to enable INECEL, which was a state owned entity engaged in power generation, transmission and distribution, to purchase energy to meet the shortage. On October 31, 1995, Electroquil S.A., the first private power generation facility in Ecuador, entered into a power purchase agreement (PPA 95) with INECEL, authorized under the Second Emergency Decree of 1995, for the importation, assembly, installation, and operation by Electroquil of two new gas turbine generators (referred to as Units 1 and 2). In 1996, another power purchase agreement (PPA 96) was entered into between aforesaid parties for the establishment of two additional generators (Units 3 and 4). PPAs 95 and 96 provided the basis for the supply of power, warranties, penalties and other terms and conditions. Payment for the supply of energy was to be made through a payment trust established at the Central Bank of Ecuador prior to commencement of the commercial operation of the power generation plants, which did not begin until 1998. Duke Energy acquired 51.5% ownership of the Electroquil, which later increased up to 79.7% in 1998. In

were improperly levied, formed one part of the claim. The claimant also charged that a payment trust envisioned under purchase power agreements (PPAs) was not properly established, invoices were often not paid on time, and interest was not paid on late payments.[191] The claim also consisted of two other complaints which were unsuccessful: that customs duties were levied on two turbines when they should have been tariff-free and that Ecuador failed to entertain the claimant's suits in local arbitration. Electroquil invoked an arbitration agreement as the primary basis for the tribunal's jurisdiction. However, it backed up its claim by also citing the Ecuador–United States bilateral investment agreement.[192]

This could have proved significant, for while the tribunal asserted jurisdiction over some of the claims (those relating to fines and penalties) it found that the arbitration agreement did not extend to claims related to customs duties. Jurisdiction was, however, ultimately declined on the grounds that the arbitration agreement excluded most claims related to taxation, a category that included the contested customs duties.[193]

The tribunal concluded that INECEL and Ecuador were in breach of the PPAs on several counts, including improperly penalizing Electroquil and failing to abide by the payment schedule stipulated in the PPAs. These breaches amounted to monetary damages of just over $5.5 million plus interest. The tribunal then proceeded to weigh Ecuador's conduct against the treaty. The tribunal found that Ecuador was in breach of the treaty's

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1999, INECEL was liquidated per the order of the Ecuadorian Parliament, and its rights and obligations were assumed by the Ministry of Energy and Mines (MEM). Subrogation agreements between MEM and Electroquil transferred the rights and obligations of INECEL under the PPAs to the Ecuadorian State. A number of fines were imposed on Electroquil under the PPAs from 1996 to 2002. Electroquil objected to many of them. Additionally, an issue arose when Electroquil requested an exemption from custom duties on a replacement turbine that was shipped from the United States. The request was refused by the CAE, a public body having exclusive domain over customs-related matters under the Customs Law passed on July 13, 1998. According to the Customs Law of 1998, only public bodies could take advantage of the exemption from customs duties. Private companies, such as Electroquil, could not. Prior to enactment of Customs Law of 1998, the Ministry of Finance had confirmed that the turbines under PPAs 95 and 96 were exempt from tax and duties, because they were required to generate electricity and were therefore a national priority. However, after passage of the Customs Law of 1998, the CAE denied Electroquil's 1999 request for an exemption from the duty. In 2001 and 2002, Electroquil and MEM entered into Liquidation Agreements with respect to PPAs 95 and 96. They also attempted to quash disputes pending between the parties, entering into an arbitration agreement to settle disputes relating to the inappropriate implementation of payment trusts, non-payment of interest on late payments, wrongful imposition of fines and penalties, and the disregarding of customs duties applications.

[191] *Id.* ¶ 49–55; 62–73.

[192] *Id.* ¶ 314.

[193] *Id.* at ¶¶ 43, 65, 99, 100–101.

umbrella clause and the FET clause. The umbrella clause stated that "each party shall observe any obligation it may have entered into with regard to investments."[194] While acknowledging that tribunals have taken divergent paths in interpreting such clauses, the tribunal side-stepped the more contentious details of this debate.

In this case, the tribunal found that Ecuador clearly had an obligation towards Electroquil's investment, which it had breached under the umbrella clause.[195] Given this determination and the broad wording of the umbrella clause, the tribunal concluded that Ecuador's failure to abide by its commitments under the PPAs meant that it had also failed to live up to the treaty. In turning to the FET clause, the tribunal yoked the standard to the "investor's justified expectations."[196] The tribunal determined that Ecuador's failure to guarantee payments under the PPAs contravened the claimant's legitimate expectations, and therefore also breached the FET standard.[197] Notably, however, neither of these two breaches of the treaty resulted in additional monetary damages. According to the tribunal, any damages that resulted from a breach of the umbrella clause were already encompassed in the award granted for the breaches of the arbitration agreement. Nor did the claimant convince the tribunal that INECEL's late payments of its invoices — the basis for the breach of the fair and equitable standard — led to any excess damages.

This initial decision is important because the *Burlington Resources v. Ecuador* Decision on Jurisdiction later approved of the approach taken in *Encana* and *Duke Energy* and found that the respondent's measure is a tax.[198]

F. Performance Requirements

Performance requirements (PRs) are the obligations imposed by host states as a condition of: (i) the admission of an investment; and (ii) permitting the continued operation of an investment. PRs are imposed by host countries in order to seek certain benefits associated with investment, but they have been a matter of controversy because of objections made by investors.[199] Host countries usually argue that PRs may foster national

[194] *Id.* at ¶¶ 313, 479.

[195] *Id.*

[196] *Id.* at ¶ 340.

[197] *Id.*

[198] *Burlington Res. Inc. v. Republic of Ecuador*, ICSID Case No. ARB/08/5, Decision on Jurisdiction, ¶¶ 161–167 (Jun. 2, 2010), http://www.italaw.com/sites/default/ files/case-documents/ita0106.pdf.

[199] *See* Andrew T. Guzman, *Why LDCs Sign Treaties That Hurt Them: Explaining the Popularity of Bilateral Investment Treaties*, 38 VA. J. INT'L L. 639 (1998).

development by requiring foreign investors to export goods, provide training to workers, and transfer technology to domestic facilities. PRs restricting imports help to cover the risks of balance-of-payments problems arising from excessive imports. However, investors consider PRs to be in violation of the basic principle of NT when they are applied to foreigners only.

Examples of PRs are numerous, such as the linking of incentives to employment levels. For example, when a firm invests in a host-country, the foreign investor can be promised three-year property tax exemptions with renewals conditional upon it expanding employment by 10% each three-year period. Other incentives are conditioned upon the location of the investment within a country. For example, firms investing in some areas of a country can have as much as 100% of their worker training paid for by the government (compared to 30% in other areas). In response to concerns over pollution, a national government can offer foreign firms investing in pollution-reduction corporate income tax abatements of 5–20%.[200]

1. The Notion of Performance Requirements

Generally, BITs do not impose restrictions on the use of PRs. However, US and Canadian IIAs prohibit PRs imposed both at the time of admission of investments and after admission. In both models the list of prohibited PRs goes beyond trade-related investment matters (TRIMs); the prohibited PRs include requirements for technology transfer and product mandating, as well as for export performance, domestic content, domestic sourcing, trade balancing, and foreign exchange balancing, all in connection with the establishment, acquisition, expansion, management, conduct, operation or sale of an investment.[201] Due to their wide applicability, these treaties may

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[200] For a review of performance requirements, see Julia Ya Qin, The Impact of WTO Accession on China's Legal System: Trade, Investment and Beyond, 2 SKKU J. SCI. & TECH. L 253 (2008)

[201] Some IIAs prefer to simply incorporate by reference the WTO TRIMs prohibition. In that case, the IIA does not add anything to the existing regulatory framework but allows the foreign investor to file PR related complaint before investment tribunals. See for instance, Malaysia-Pakistan Closer Economic Partnership Agreement, Malay.-Pak., Nov. 8, 2007, http://www.commerce.gov.pk/PMFTA/PAk-Malaysia-FTA(TXT).pdf. Article 92 of the Malaysia–Pakistan Closer Economic Partnership Agreement prohibits performance requirements as envisaged in TRIMS. "1. For the purposes of this Chapter, the Parties reaffirm their commitments to the Agreement on Trade-Related Investment Measures in Annex 1A to the WTO Agreement (hereinafter referred to as 'TRIMS') and hereby incorporate the provisions of the TRIMS, as may be amended, as part of this Chapter. 2. A Party shall, upon notification by the other Party, promptly convene consultations with the other Party on any matter relating to this Article that affects the other Party's investors and their investments." The effect of incorporating TRIMS obligations in an investment treaty is

generate PR disputes. *Merrill & Ring v. Canada* agrees with *SD Myers v. Canada* and *Pope & Talbot v. Canada*, holding that measures that may have an incidentally adverse effect on an investor's exports do not appear to be the kind of PR prohibited by Article 1106 (which are those directly and specifically connected to exports).[202]

The list of prohibited performance requirements in NAFTA (Art. 1106) goes beyond that of the World Trade Organization's TRIMs. Actually, US trade agreements establish, in effect, a "TRIMs plus" set of obligations that includes outright bans on certain performance requirements, including exports, minimum domestic content, domestic sourcing, trade balancing and technology transfer. In addition, these provisions cover both goods and services.

The principle of NAFTA Article 1106 is subject only to the exceptions of Article 1108, and it significantly limits the obligations set out in Section A of Chapter 11.[203]

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that it renders the obligations subject to the dispute resolution provisions in the agreement. Julien Chaisse & Mitsuo Matsushita, *Maintaining the WTO's Supremacy in the International Trade Order—A Proposal to Refine and Revise the Role of the Trade Policy Review Mechanism*, 16 J. INT'L ECON. L. 9, 9–36 (2013).

[202] *Merrill & Ring Forestry LP v. Gov't of Canada*, UNCITRAL, ICSID Administrated, Award, ¶¶ 111, 117–118 (Mar. 31, 2010), http://www.uncitral.org/transparency-registry/registry/data/can/merrill_ring_forestry_l.p.html.

[203] North American Free Trade Agreement art. 1108, Dec. 17, 1992, 32 I.L.M. 289 (2003). NAFTA Article 1108 (Reservations and Exceptions) states:

> 1. Articles 1102, 1103, 1106 and 1107 do not apply to:
> (a) any existing non-conforming measure that is maintained by
> (i) a Party at the federal level, as set out in its Schedule to Annex I or III,
> (ii) a state or province, for two years after the date of entry into force of this Agreement, and thereafter as set out by a Party in its Schedule to Annex I in accordance with paragraph 2, or
> (iii) a local government;
> (b) the continuation or prompt renewal of any non-conforming measure referred to in subparagraph (a); or
> (c) an amendment to any non-conforming measure referred to in subparagraph (a) to the extent that the amendment does not decrease the conformity of the measure, as it existed immediately before the amendment, with Articles 1102, 1103, 1106 and 1107.
> 2. Each Party may set out in its Schedule to Annex I, within two years of the date of entry into force of this Agreement, any existing non-conforming measure maintained by a state or province, not including a local government.
> 3. Articles 1102, 1103, 1106 and 1107 do not apply to any measure that a Party adopts or maintains with respect to sectors, subsectors or activities, as set out in its Schedule to Annex II.
> 4. No Party may, under any measure adopted after the date of entry into force of this Agreement and covered by its Schedule to Annex II, require an investor of another Party, by reason of its nationality, to sell or otherwise dispose of an

Paragraph 1 of Article 1108 provides that any non-conforming measures prior to the implementation of NAFTA, i.e., before January 1, 1994, are exempt from the application of Chapter 11 obligations of NT (Article 1102), MFN treatment (Article 1103), the prohibition of certain performance requirements (Section 1106), and requirements imposed upon executives and directors (Article 1107). Any changes to such measures after the implementation of NAFTA are also exempt as long as they do not decrease the conformity of the measures with those obligations.

2. Impact in the Regime of Tax

There are three cases in which NAFTA tribunals have found a breach of Article 1106. These cases are interesting because they allow us to identify the measures implemented by NAFTA members that are not allowed by NAFTA. This Article will discuss the first of these cases, *Archer Daniels Midland Company v. Mexico*. In November 2007, Archer Daniels Midland (ADM) and Tate & Lyle Ingredients Americas Co. prevailed on certain of their claims in a NAFTA Chapter 11 arbitration with Mexico.[204] In this case, the impermissible advantages took the form of a tax exemption for Mexican bottlers if they used domestic cane sugar, thereby severely penalizing bottlers for using any sweetener other than cane

investment existing at the time the measure becomes effective.
5. Articles 1102 and 1103 do not apply to any measure that is an exception to, or derogation from, the obligations under Article 1703 (Intellectual Property – National Treatment) as specifically provided for in that Article.
6. Article 1103 does not apply to treatment accorded by a Party pursuant to agreements, or with respect to sectors, set out in its Schedule to Annex IV.
7. Articles 1102, 1103 and 1107 do not apply to (a) procurement by a Party or a state enterprise; or (b) subsidies or grants provided by a Party or a state enterprise, including government-supported loans, guarantees and insurance.
8. The provisions of: (a) Article 1106(1)(a), (b) and (c), and (3)(a) and (b) do not apply to qualification requirements for goods or services with respect to export promotion and foreign aid programs; (b) Article 1106(1)(b), (c), (f) and (g), and (3)(a) and (b) do not apply to procurement by a Party or a state enterprise; and (c) Article 1106(3)(a) and (b) do not apply to requirements imposed by an importing Party relating to the content of goods necessary to qualify for preferential tariffs or preferential quotas.'

Id.

[204] *Archer Daniels Midland Co. and Tate & Lyle Ingredients Americas, Inc. v. Mexico*, ICSID Case No. ARB(AF)/04/5, Award, (Nov. 21, 2007), http://www.italaw.com/sites/default/files/case-documents/ita0037_0.pdf. The release of the award comes as the investors continue to vie for additional compensation, beyond the $33.5 million awarded in the ICSID arbitration. The claimants have asked the ICSID tribunal for a supplementary decision – which would provide further compensation. The claimants have also filed an application with a Canadian court seeking the same. Whatever the outcome of the claimants' bid for a further tranche of damages, the current award stands as the largest known financial award against a government under the terms of NAFTA Chapter 11.

sugar.[205] Under the terms of the 2007 award, Mexico was found to have discriminated against a joint venture, ALMEX, owned by ADM, and to have imposed impermissible "performance requirements" to the detriment of that joint venture.[206] The Tribunal found a breach of PR obligations under Article 1106.3 of NAFTA because the underlying intent of the tax imposed was to confer advantages on the sugar industry in Mexico. It was held that the advantage in the form of exemption from taxes was conditioned on the exclusive use of domestic cane sugar and, accordingly, it was discriminatory against the high-fructose corn syrup industry, in which ADM was an investor. The *Archer Daniels Midland v. Mexico* Award is important because it found a breach of NAFTA due to a tax that

[205] *Id.* at ¶ 2. The claimants and ALMEX manufacture and distribute high fructose corn syrup (HFCS), which is widely used as a sweetener instead of sugar in the beverage industry. Mexico has the world's highest per capita consumption of carbonated soft drinks and in particular of Coca-Cola. ALMEX was involved in selling imported HFCS and also producing the same. HFCS became its most important product. HFCS was cheaper than State supported sugar, and it gradually penetrated the soft drinks sweetener market in Mexico, posing severe competition to cane sugar. In 1998, Mexico imposed anti-dumping duties on HFCS from the United States was challenged by United States at the WTO, and was found to be in violation of the WTO Anti-dumping Agreement by the WTO Panel in February 2000. The anti-dumping measure taken by Mexico was also challenged under Chapter 19 of NAFTA. The Chapter 19 Panel in its Final Decision dated August 3, 2001 required Mexico to terminate anti-dumping duties and refund the duties collected since their imposition. However, the Mexican Congress passed an IEPS Amendment on December 30, 2001, amending Articles 1, 2, 3 and 8 of the Ley del Impuesto Especial sobre Producción y Servicios (IEPS). The amendments imposed a 20% excise tax on soft drinks and syrups and on the services used to transfer and distribute them if they used any sweetener other than cane sugar. The main objective of the tax was to afford protection to domestic sugar industry from severe competition posed by HFCS. The IEPS Amendment was challenged by the United States in the WTO as violating NT obligations under the General Agreement on Tariffs and Trade (GATT). It was so held by the WTO Panel in 2005 and upheld by the Appellate Body in 2006. The tax was repealed as effective from January 1, 2007. Accordingly, the tax imposed by Mexico was challenged by the claimants under Chapter 11 of NAFTA. The claimants alleged, that this imposition had a direct impact on its investment in HFCS production and distribution facilities, causing substantial loss, which amounted to a violation of the NT, PR, and expropriation principles.

[206] *Id.* at ¶ 296. Also, the Tribunal found a breach of the NT standard under Article 1102 of NAFTA, as the IEPS Amendment imposed dissimilar taxation on HFCS and cane sugar, which the tribunal held to be directly competitive products. The tax imposed was held to be discriminatory and to have been applied in a way so as to afford protection to the Mexican domestic cane sugar industry. However, the tribunal did not find any case of expropriation under Article 1110 of NAFTA and the degree of the measure taken (in this case the imposition of the Tax) was not such that it could substantially interfere in the business of the claimant. In the present case, at all times the Claimant was in control of its investment and was producing and distributing HFCS in Mexico. Therefore, the mere loss of benefits, the expectation thereof, and the alleged discriminatory nature of the tax alone, was not sufficient to satisfy the criteria for expropriation.

discriminated between users of sweeteners depending upon the type of sweetener, setting the stage for tribunals to find subsequent breaches of NAFTA in other disputes.[207]

V. CONCLUSION

This Article evidenced an important reality: there are a growing number of international arbitration cases that somehow involve a tax issue. This is not totally surprising. After all, foreign investment decisions and tax regulations are deeply intertwined. However, each was historically regulated by different authorities and agreements and used to belong to different spheres. Today, the spheres are increasingly overlapping.

In the coming year, such a trend will continue to increase. The goal of bilateral tax treaties is to enhance cooperation in tax administration and in the exchange of information to avoid tax evasion. Additionally, the OECD launched the Base Erosion and Profit Shifting (BEPS) Project in 2013.[208] The main purpose of the BEPS project is to effectively prevent double non-taxation and no or low taxation cases associated with artificially segregated taxable income from its revenue-generating activities.[209] It is widely anticipated that there will be an increasing number of tax disputes in the post-BEPS scenario[210] and, because of the shortcomings of tax dispute resolution mechanism, many disputes might end up before investment tribunals.

The early jurisprudence of ICSID has already given a strong indication that tax disputes related to foreign investment are also legal disputes that arise directly out of the investment for which the ICSID tribunal may have jurisdiction. Although none of these early cases directly related to tax

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[207] *Id.* at ¶¶ 221–227.

[208] BEPS attempts to addresses the use of tax planning strategies to exploit gaps and mismatches of tax rules in order to artificially shift income to low or zero tax jurisdictions, where there is little or no economic activity, which results in a substantially decreased tax burden such that little or no taxes are paid.

[209] OECD, *Action Plan on Base Erosion and Profit Shifting*, OECD Publishing (2013) at 13, *http://dx.doi.org/10.1787/9789264202719-en.*

[210] *See* Jeffrey Owens, Jasmin Kollmann & Laura Turcan, *Dispute Resolution in International Tax Law* (Institute for Austrian and International Tax Law, Working paper, Oct. 17, 2014), www.wu.ac.at/taxlaw ("All measures proposed as a result of the BEPS project have a substantial impact on the application of tax treaties, leading to changes in the wording of the articles of the OECD Model Convention and their interpretation. Taxpayers and tax administrations will need time to adjust to the profound changes envisioned. In the interim, there will be a period of very high uncertainty with tax administrations applying a very strict approach and taxpayers challenging this, leading to numerous disputes. The problem will only be compounded by the differences in interpretation between the individual countries.").

matters, tribunals felt it important to warn the parties that it may one day be appropriate to link investment protection to tax law.[211] In *AMCO v. Indonesia*, the tribunal observed that tax matters may well be covered by ICSID's jurisdiction.[212] In *Kaiser Bauxite v. Jamaica*, the government had agreed to a tax-stabilization clause, and the tribunal asserted that a dispute over increased taxes would fall under the scope of Article 25 paragraph 1 of the ICSID Convention, because "the dispute concerning the alleged legal rights and obligations stemming from particular provisions in Kaiser's agreements with the Government is a legal dispute."[213] A similar situation and decision was found in *Alcoa Minerals v. Jamaica*.[214] In this Article, more recent cases have been reviewed. For example, in *Feldman v. Mexico*, the issue was the failure of the tax authorities to refund excise taxes for exported cigarettes, which was held by the international arbitration tribunal to be a violation of the NT provision of the investment treaty. In *Occidental v. Ecuador*, a case in which the investor was victorious, the dispute sprang from the refusal of the Ecuadorian tax authority to refund input VAT to a foreign investor.

It is important to note that an arbitration tribunal in an international investment case does not sit as a court of appeal to the local tax court or administrative body that decides tax cases in that state. Whether a certain tax is applicable under the laws of a state is a matter for the courts and administrative bodies of that state, not for the arbitration tribunal. The arbitration tribunal decides whether the state breached any international obligations as set out in the IIA, in general international law or, perhaps, in the contract between the state and the investor. In other words, it is not the role of the arbitration tribunal to interpret and apply the tax laws of a state to an investor. But the way a state applies its tax laws, even if applied correctly under that state's law, may very well constitute a breach of the obligations of that state under international law. As such, the matter can be both a question for a local tax court (to be decided solely on the tax laws of that state) and for an arbitration tribunal (to be decided on international investment law).

The last decade has witnessed a dramatic surge in investment disputes between foreign investors and host country governments. Arbitral panels have been charged with the task of applying the rules of IIAs in specific

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[211] *See* Mark A. Clodfelter, The Adaptation of States to the Changing Word of Investment Protection through Model BITs, 14 ICSID REV. 166, 175 (2009).

[212] *Amco Asia Co. v. Republic of Indonesia,* ICSID Case No. ARB/81/1, Decision on Jurisdiction, (Sept. 25, 1983), 1 ICSID Rep. 389 (1993).

[213] *Kaiser Bauxite Co. v. Jamaica,* ICSID Case No. ARB/74/3, Decision on Jurisdiction, ¶ 16 (Jul. 6, 1975).

[214] *Alcoa Minerals of Jamaica, Inc. v. Jamaica,* ICSID Case No. ARB/74/2, Decision on Jurisdiction and Competence, (July 6, 1975), *cited in* 5 ICSID Rep. 142 (2002).

cases, a task which is not often straightforward given the broad and sometimes ambiguous terms of these arrangements. The new phenomenon of investment arbitration has brought about a number of decisions from different arbitral fora in the tax sector, contributing to the formation of a jurisprudence that is elucidating the meaning of key provisions and contributing to the emergence of global economic regulation of tax matters. Importantly, fifteen disputes have resulted in significant compensation being paid by host states for breaching investment treaty commitments by imposing tax measures. The details of these fifteen disputes show that there a number of provisions which have proven decisive to justify the claims of the taxpayers, namely, protection against expropriation, FET, FPS, non-discrimination, the umbrella clause, and PR. These six investment provisions indirectly constitute part of the international regime of tax matters, which is increasingly being shaped by investment tribunals' awards and international investment agreements.

ANNEX 1. TAX-RELATED INVESTMENT DISPUTES

CASE NAME	TREATY	AWARD DATE	ARBITRATION RULES
Feldman v. Mexico	NAFTA	December 16, 2002	ICSID AF
Goetz v. Burundi	Belgium–Luxemburg–Burundi BIT	February 10, 1999	ICSID
Enron Corporation & Ponderosa Assets LP v. The Argentine Republic	Argentine-USA BIT	May 22, 2007	ICSID
Occidental Exploration and Production Company v. Ecuador	USA–Ecuador BIT	July 1, 2004	UNCITRAL
Archer Daniels Midland Co. & Tate Lyle Ingredients Americas, Inc. v. United Mexican States	NAFTA	November 21,2007	ICSID AF
El Paso Energy International Company v. Argentina	Argentina–USA BIT	October 31, 2011	ICSID
Duke Energy v. Ecuador	USA–Ecuador BIT	August 18, 2008	ICSID
Hulley v. Russia	ECT	July 18, 2014	UNCITRAL
RosInvestCo v. Russia	UK–USSR BIT	September 12, 2010	SCC
Yukos Universal v. Russia	ECT	July 18, 2014	UNCITRAL

Mobil v. Venezuela	Netherlands–Venezuela BIT	October 9, 2014	ICSID
Quasar de Valores Sicav SA v. The Russian Federation	Spain–USSR BIT	July 20, 2012	SCC
Renta 4 v. Russia	Spain–USSR BIT	March 30, 2009	SCC
Tza Yap Shum v. Republic of Peru	China–Peru BIT	July 7, 2011	ICSID
Veteran Petroleum v. Russia	ECT	July 18, 2014	UNCITRAL
Corn Products International Inc. v. Mexican States	NAFTA	August 18, 2009	ICSID AF
Paushok v. Mongolia	Russia–Mongolia BIT	April 28, 2011	UNCITRAL
Burlington Resources v. Ecuador	USA–ECUADOR BIT	December 14, 2012	ICSID
Phoenix Action v. Czech Republic	Israel–Czech Rep BIT	April 15, 2009	ICSID
Noble Energy v. Ecuador	USA–Ecuador BIT	Settled	ICSID
Gottlieb v. Canada	NAFTA		UNCITRAL
TCW v. Dominican Republic	CAFTA	Consent Award/July 16, 2009	UNCITRAL
Lacich v. Canada	NAFTA	Withdrawn	N.A.
Link-Trading v. Moldova	USA–Moldova BIT	April 18, 2002	UNCITRAL
Tokios Tokeles v. Ukraine	Lithuania–Ukraine BIT	July 26, 2007	ICSID
EnCana v. Ecuador	Canada–Ecuador BIT	February 3, 2006	UNCITRAL
Plama Consortium Limited v. Republic of Bulgaria	ECT	August 27, 2008	ICSID
Grand River v. USA	NAFTA	January 12, 2011	UNCITRAL
Amto LLC. v. Ukraine	ECT	March 26, 2008	SCC
EDF v. Romania	UK–Romania BIT	October 8, 2009	ICSID
The Rompetrol Group N.V. v. Romania	Netherlands–Romania BIT	May 6, 2013	ICSID
Jan Oostergetel and Theodora Laurentius v. The Slovak Republic	Netherlands–Slovak Republic BIT	April 23, 2012	UNCITRAL