School of Economics and Business Administration
LLM. in Transnational and European Commercial Law
and Alternative Dispute Resolution
Student ID: 1104120012

"Operationalizing the proportionality principle in investment treaty arbitration along with a comparability study on techniques of balancing interests by international courts"

by:

THEODORA I. KIOSEOGLOU
Supervisor : Dr. George Christodakis

Dissertation submitted to the International Hellenic University (IHU) in partial fulfillment of the requirements for the degree of:

"LLM in Transnational and European Commercial Law and Alternative Dispute Resolution"

January 15, 2014
ACKNOWLEDGEMENT

This dissertation thesis would not have been possible without the guidance and the help of several individuals who in one way or another contributed and extended their valuable assistance in the preparation and completion of this study.

First and foremost, my utmost gratitude to my supervisor Dr. iur. Giorgos Christonakis, Professor at the Berlin School of Economics & Law, who has been a truly outstanding guide during my study. His availability, his response time and the quality of his feedback have been incredible. He was always approachable and ready to discuss difficult points and I am extremely grateful to him for his constant support.

Prof. Dr. Athanassios Kaissis, member of the Governing Board of the International Hellenic University for his advice, guidance and encouragement throughout the Programme.

My mentor Dr. Komninos G. Komnios and academic assistance Stavroula I. Angoura for their support.

The academic and library staff for their kind assistance.

A special thanks to the authors mentioned in the bibliography page.

Most especially I wish to thank my parents and Niki Lolou for their personal support and help.
Abstract

This study begins by examining the origins of the proportionality principle. I describe the structure of the proportionality principle and fundamentals of proportionality analysis, and the problems attendant on weighing the value of the interests involved. There follows an analysis of the application of the principal to a range of rights and interests and comparative analysis of proportionality test and method of balancing in international jurisprudence. The second part focuses on the proportionality principle analysis in the field of investment treaty arbitration which is providing arbitrators with the appropriate analytical procedure currently available for adjudicating disputes. Investor–State arbitration as a mechanism to settle disputes but also a form of exercising power by the arbitral tribunals in setting standards of review. Comparability to system building contribution of precedents and the system building effect. This paper argues that proportionality analysis is a precondition for the encapsulation of the notion of public interest in customary international law.

Keywords: Construction and fundamentals of proportionality principle, scope in comparison, doctrinal structure, investment treaty arbitration, judicialization, fair and equitable treatment, balancing.
## Contents

**Introduction** ................................................................................................................................................. 6

**Chapter 1**

**Fundamentals of the proportionality principle** ......................................................................................... 8
   A. Origins of proportionality .......................................................................................................................... 8
   B. Doctrinal Structure ..................................................................................................................................... 11
   C. Criticism on the concept of proportionality .............................................................................................. 15

**Chapter 2**

**Proportionality in investment treaty arbitration** ..................................................................................... 17
   A. Developments in instrumentalizing proportionality by international investment tribunals:
      Proportionality as a regulative of the relationship between equal dispute parties .................. 17
         1. Particularities of the evolving international investment arbitration system and its
            signiﬁcance for any operation with the proportionality principle ............................................. 17
         2. Proportionality as a tool for balancing investor rights and the public interest .......... 20
         3. Proportionality analysis in indirect expropriation claims ....................................................... 23
         4. Proportionality analysis and FET standard .............................................................................. 27
   B. Methodology of legal reasoning and rationales for determining standards of review in the
      application of proportionality test ............................................................................................................. 30
   C. Scope of the proportionality analysis by investment arbitral tribunals in comparison to
      international courts and tribunals ............................................................................................................ 31
   D. Encapsulation of the notion of public interest in customary international law as the
      precondition for developing operability of proportionality ................................................................. 34
         1. Doctrinal necessity to operate with proportionality and structural transformation of
            proportionality into the field of international investment disputes ........................................ 34
         2. The need to structurally transpose the proportionality doctrine ............................................. 35
         3. The need to introduce a formal principle in the balancing process ........................................ 35

**Chapter 3**
Personal statements and proposals: Improvement of arbitral decision making by elaborating proportionality analysis .................................................................37

A........ Methodological advantages in decision making - comparability to system building contribution of precedents (system building effect) .................................................................37

B. Potentials of Proportionality to contribute for legitimating investment tribunal decisions – Allocation of authority in a fragmented international investment arbitration system...... 40

Conclusions ..................................................................................................................................................................................43
Introduction

Proportionality is the dominant judicial standard for resolving disputes engaging the competing values governing the protection of rights or protection of the legal regime’s primary interest and the public interest embodied in new laws or other government conduct; in other words, a method of legal interpretation and decision-making in situations of collisions or conflicts of different principles and legitimate public policy objectives.

This study begins by examining the origins of proportionality followed by an analysis of the doctrinal structure and a brief overview to critical voices regarding the usefulness and rationality of the principle.

The search for balancing the general interest of the community and the individual’s fundamental rights is a basic requirement in adjudication and it has emerged in recent times to the arbitral decision-making over international investment disputes as well. The significance of any advantages offered by a systematic instrumentalization of proportionality in this area have been rightly highlighted by some influential scholars; not all the theoretical aspects on any rationality gains have been, however, sufficiently discussed.

The paper is organized as follows: Chapter 1 gives the fundamentals of the proportionality principle. In Chapter 2 I emphasize on the developments in instrumentalizing proportionality by international investment tribunals: proportionality as a regulative of the relationship between equal dispute parties. I make an effort – under comparative examination of the approaches of the ECJ and ECtHR and WTO related jurisprudence - to assess the methodology of legal reasoning and rationales for determining standards of review in the application of proportionality test by investment arbitral tribunals. The selective-reading of case law with predisposition for proportionality is due to the distinctive features (three tier test) of the principle which distinguish it and place it at the center not only of scholarly debate but also in legal, economic and political developments. To my view, it furthers the present survey to define the balance of public and private interest especially in investment treaty arbitration where there is usually an enunciation in the respective investment treaty due to the importance of the interests involved. Investment tribunals’ tentative moves to proportionality analysis in the context of indirect expropriation indicates that proportionality may be crystallizing as a norm in relation to when the police powers doctrine applies to defeat a claim of expropriation.
In Chapter 3 through analyzing personal statements and proposals I focus to the methodological advantages in decision making and I plead for a system building contribution of proportionality (system building effect). Furthermore, I represent the opinion that proportionality analysis has the potential to become a tool to enhance accountability and justification for governmental action and the activity of arbitral tribunals.
Chapter 1

Fundamentals of the proportionality principle

A. Origins of proportionality

Proportionality is a common feature of decision-making in constitutional and human rights contexts. It is a doctrine, a principle of law that seeks to police the justification of state interference with constitutional and human rights, ensuring that the state places no greater limitation on rights than necessary. The doctrine has become a familiar part of the reasoning process of the European Court of Justice, the European Court of Human Rights (ECtHR) and is increasingly familiar in the context of WTO dispute settlement and the International Court of Justice. Investment treaty tribunals have already begun conducting some forms of proportionality analysis as well.

The concept of proportionality did not begin as a legal concept but rather its origins can be traced to ethical discourse. Proportionality as a principle of law arose out of the Aristotelian concept of

---

1 Regarding the differentiation between principals and rules see footnote 20.


6 See e.g. LG&E v. Argentina, ICSID (United States/Argentina BIT), Decision on Liability, 3 October 2006, para. 158; BG Group Plc v. Argentina, UNCITRAL (UK/Argentina BIT), Award, 24 December 2007 para. 339 et seq; EDF v. Romania ICSID (UK/Romania BIT), Decision and Partial Dissent, 9 October 2009, para. 302 et seq. Also E.g. Saluka Investments BV v. The Czech Republic, UNCITRAL, (Dutch/Czech BIT), Partial award, 17 March 2006, para. 306; AWG Group Ltd. v. Argentina, UNCITRAL (UK/Argentina BIT), Decision on Liability 30 July 2010, para 236
Operationalizing the proportionality principle in investment treaty arbitration

Theodora I. Kioseoglou

In German constitutional law, it is a key principle. The concept appeared as a prohibition of disproportionality - the state must by activities of its powers use proportional means to legitimate ends - and evolved to a clearly defined principle. The concept of proportionality is most fully developed within German law. The first detailed explanation of the context of the principle of proportionality appeared in a landmark case the Pharmacy Case (Apothekenurteil) of the year 1958 which required a highly differentiated complex of scrutiny mechanisms. It is controversial, whether this principle stems from a rule of law or it is connected with the fundamental rights. As stated in the case that involved a challenge to a Bavarian law regulating drug stores based on the freedom of occupation provision of Article 12 1 of the GG:

«The [purpose of] constitutional right should be to protect the freedom of the individual [while the purpose of] the regulation should be to ensure sufficient protection of societal interests. The individual's claim to freedom will have a stronger effect... the more his right to free choice of a profession is put into question; the protection of the public will become more urgent, the greater the disadvantages that arise from the free practicing of professions. When one seeks to maximize both... demands in the most effective way, then the solution can only lie in a careful balancing [Abwägung] of the meaning of the two opposed and perhaps conflicting interests.»

With the Apotheke decision - a movement began on the part of increasing numbers of courts around the world to adopt the language of judicial balancing to justify their decisions on constitutional rights.

The doctrine of proportionality in WTO and investment tribunals does not have any clear connection with the older concept of proportionality in ethics discourse. Instead, proportionality in

9 Apothekenurteil Case, Entscheidungen des Bundesverfassungsgerichts Vol. 7, pp. 377 ff..
10 A 1958 case in which a provision in the Bavarian Apothecary Act was struck down as unconstitutional. The act provided that an admitted apothecary could only be allowed to open a pharmacy if the new pharmacy was commercially viable and causes no economic harm to nearby competitors. The Constitutional Court held that, although the wording of Article 12 of the Basic Law seemed to protect a number of rights (choice of occupation, profession, place of work, place of training, practice of an occupation), in fact, it only protected the free choice and exercise of the occupation, from education to retirement. The Court held that occupation has to be understood in the largest possible sense, as a legal activity with a certain duration serving the creation or support of one's welfare, i.e. not just a hobby. The protection covers all aspects of such an activity. It was agreed upon the first appearance of this principle as an underlying rationale of the German constitutional system, that government action limiting upon those fundamental rights could only be justified on the basis of a highly differentiated scrutiny mechanism.
12 Arnauld A., Die normtheoretische Begründung des Verhältnismäßigkeitsgrundsatzes, Juristenzeitung 2000, pp. 276 ff. Many in the academic world in Germany - as well as the courts - are of the opinion that the concept of proportionality should be derived from the notion of the constitutional state under the rule of law (Rechtsstaat), Barak A., Proportionality: Constitutional Rights and Their Limitations, 2012,
international human rights law has developed as a legal principle\textsuperscript{13}. This will be further analyzed below (Chapter 2).

Domestic courts and international courts and tribunals\textsuperscript{14}, such as the European Court of Human Rights and the World Trade Organization (WTO) Appellate Body, routinely exercise deferential review whilst still finding government agencies or states liable in appropriate cases. How strictly will tribunals scrutinize governmental conduct which aims to furthering the public interest and how readily they will substitute their own views for those of respondent States? For example:

- If a State regulatory agency decides that a chemical is harmful and should be banned, despite the negative impact that this will have on foreign investors, when should arbitral tribunals second-guess these questions of science and policy?

- If a State legislature decides to enact measures to protect the environment or its economy, even though these measures will harm foreign investors, when should arbitral tribunals sit in judgment of the appropriateness of these policy goals or the measures enacted to achieve them?

- If a national court has made certain determinations of fact or given certain interpretations of national law, should arbitral tribunals consider these issues afresh if they are implicated in an investor-State dispute?\textsuperscript{15}

\textsuperscript{13} What is a principle? As a starting point, it may be said that a principle is a general proposition of law of some importance from which concrete legal rules derive. Principles are generally unwritten and are derived from the legal system as a whole. Alexy R., \textit{A Theory of Constitutional Rights}, 1985 (first edition in german)/2010 has developed the theory that constitutional rights are principles and that principles are optimization requirements. Rules are definitive requirements, while principles are prima facie requirements. For Alexy “the decisive point in distinguishing rules from principles is that principles are norms which require that something be realized to the greatest extent possible given the legal and factual possibilities. Principles are optimization requirements, characterized by the fact that they can be satisfied to varying degrees, and that the appropriate degree of satisfaction depends not only on what is factually possible but also on what is legally possible. The scope of the legally possible is determined by opposing principles and rules. By contrast, rules are norms which are always either fulfilled or not. If a rule validly applies, then the requirement is to do exactly what it says, neither more nor less. In this way rules contain fixed points in the field of the factually and legally possible. This means that the distinction between rules and principles is a qualitative one and not one of degree. Every norm is either a rule or a principle.”

\textsuperscript{14} International commercial arbitration is a form of private dispute resolution between private parties concerning their private rights and obligations only. The disputing parties are treated as equals – both substantively in terms of their contractual relations (equal contracting parties) and procedurally in terms of their dispute resolution status (equal disputing parties). This is true even when one party is a State as States are generally considered to be acting in their private capacities when they enter into and breach commercial contracts. International commercial arbitral tribunals are thus called upon to resolve private contractual disputes rather than to adjudicate upon public governance functions. Their awards tend to remain confidential and thus are unlikely to form a body of persuasive precedents as to the meaning of common obligations. As a result, international commercial arbitrations generally have a relatively contained effect, directly impacting upon the disputing parties but rarely having significant broader consequences.

\textsuperscript{15} See Anthea Roberts in \textit{The Present – Investment Arbitration as a Governance Tool for Economic International Relations? The Next Battleground: Standards of Review in Investment Treaty Arbitration} in Albert Jan van den Berg
– If a national court has made certain determinations of fact or given certain interpretations of national law, should arbitral tribunals consider these issues afresh if they are implicated in an investor-State dispute?16

B. Doctrinal Structure

The doctrine of proportionality assesses both the means and the side effects of state action. The structure of proportionality reasoning applies can be used to assess the legitimacy of the state’s aim. Normally, this will not happen, because the applicant will not argue that the aim itself is illegitimate. For example, if a highway is to be built over the applicant’s land, the argument will not be about whether the state has a legitimate aim in building highways.17

Proportionality analysis is a device used to adjudicate disputes engaging the competing values of the protection of rights (or protection of the legal regime’s primary interest, such as free movement of goods) and the public interest embodied in new laws or other government conduct or even legislative measures;18 in other words, a method of legal interpretation and decision-making in situations of collisions or conflicts of different principles and legitimate public policy objectives.

In several constitutional systems across the globe, most notably, besides Germany, in South Africa19, Canada20 and Israel21, proportionality balancing today constitutes the dominant, judicial standard for resolving disputes that involve an alleged conflict between two legally protected interests or rights, between a provision of rights and a state or public interest (constitutional law), or between a private interest and a state or public interest (administrative law).22 In the latter,


19 Saurer J., Die Globalisierung des Verhältnismäßigkeitsgrundsatzes, Der Staat 51 (2012), pp. 1 (16 f.).

20 Jackson C. V., Being Proportional about Proportionality, Constitutional Commentary (2004), pp. 803 ff Being Proportional about Proportionality


22 The principle of proportionality may emerge as determinative in at least six different settings when the tribunals assess and determine their decisions,
paradigmatic situation, the analysis proceeds step by step, as follows. In a preliminary phase, the judge considers whether a prima facie case has been made to the effect that a government act burdens the exercise of a right. Proportionality analysis as a framework clearly indicates to litigating parties the type and sequence of arguments that can and must be made, and the path through which the judges will reason to their decision. It provides ample occasion for the balancing court to express its respect, even reverence, for the relative positions of each of the parties. This latter point is crucial. In situations where the judges cannot avoid declaring a winner, they can at least make a series of ritual bows to the losing party. Indeed, the court that moves to balancing stricto sensu is stating, in effect, that each side has some significant legal arguments on its side, but that the court must, nevertheless, take a decision.\(^{23}\)

Proportionality analysis proceeds through a sequence of three tests. A government measure that fails any one of these tests violates the proportionality principle and is therefore unlawful.\(^{24}\)

The first stage of proportionality analysis mandates inquiry into the "suitability" of the measure under review. The government must demonstrate that the relationship between the means chosen and the ends pursued is rational and appropriate, given a stated policy purpose.\(^{25}\) The suitability test, or appropriateness test, refers to the relationship between the means and the end. The question to be

---


answered is whether the measure to be considered is suitable or appropriate in order to achieve the given aim by using the chosen measure.

The second step is "necessity". Necessity analysis requires a court or tribunal to consider possible alternative measures that impact less on the right or interest at stake. The assessment of necessity involves the making of (rather difficult) predictions concerning the likely efficacy and impact of alternative measures, which may be a matter of fine distinctions, particularly where a decision involves the consideration and balancing of a number of divergent interests or engages economic policy.26 The necessity test is conducted when the court assesses whether the chosen measure is necessary to achieve the proposed goal, in the meaning that the measure should be chosen which is least restrictive on the given norm.

In the ECtHR context, the effect of the reasonable necessity approach is that generally a measure interfering with property will not fail the necessity test unless the measure pursued is clearly inappropriate or disproportionate. As Stone Sweet27 states the ECtHR prefers a broader balancing approach, which it use, among other things, to define the scope of the State’s discretion in an executive or legislative framework which the ECtHR calls a “margin of appreciation”28 having been shaped by the jurisprudence of the Court in view of the closer proximity of domestic decision makers to the social realities of the community, to make the initial assessment of the reality of the pressing social need. The margin of appreciation as a standard of review recognizes that some national determinations restricting Convention rights may be necessary for the protection of other values and permissible objectives, such as national security, public order, health, or morals.29 So far, the margin of appreciation relativates the level of review within the proportionality examination30 but, contrary to proportionality, it seems to be more an interpretation instrument than a balancing method.

The ECJ’s review of national measures is conducted with more stringency, the ECJ will be more inclined to accept authorities’ arguments as to necessity where the measure is sensitive and relates to

28 This wide margin in the pursuit of social and economic policies notwithstanding, any measure adopted by a state must also meet the requirements of lawfulness and proportionality
social policy or to areas in which national authorities have exclusive competence. The ECJ has also held that administrative complexity and the desirability of general and simple rules may justify a reasonable necessity approach.

In relation to the WTO agreements’ general exceptions provisions with a nexus requirement of necessity, WTO tribunals demonstrate a form of reasonable necessity by permitting the responding state to demonstrate that an alternative measure is inappropriate where the state is not capable of taking it, where it imposes an undue burden on the state such as prohibitive costs or substantial technical difficulties, or where the alternative measure does not achieve the state’s chosen level of protection against the harm pursued with respect to regulatory objective. WTO tribunals are generally deferential with respect to the analysis of the existence of prohibitive costs or technical difficulties in recognition of their comparative lack of expertise and resources.

The third step-balancing stricto sensu is also known as "proportionality in the narrow sense. In the balancing phase, the judge weighs, in light of the facts, the benefits of the act (already found to have been narrowly tailored) against the costs incurred by infringement of the right, in order to decide which side shall prevail. A court that strikes down a law as unconstitutional in the third stage of proportionality analysis will typically use the first two steps to pay its respects to the importance of the purposes pursued by the government and to the quality of the government's own deliberations on the proportionality of the law. The legal possibilities are weighed by proportionality stricto sensu, which conducts the balance between the conflicting principles. We come up to this final stage of assessment once a measure has been found suitable and necessary to achieve a particular

---

31 In Case 11/70, Internationale Handelsgesellschaft v Einfuhr- und Vorratsstelle Getreide [1970] ECR 1125 at 1147, the court held that ‘the individual should not have his freedom of action limited beyond the degree necessary in the public interest’.

32 Criticism on some operational modalities of proportionality in the jurisprudence of the ECJ by Christonakis G., Effective adjudication v. jurisprudential absolutism at supranational level. How is criticism on developments in recent case law of the Court of Justice of the European Union pacifiable?, Ceremonial address in the Danubius University in October 2013, in publication process.

33 Alternative measures must be reasonable and to take into account technical and economic feasibility and less restrictive to trade. The objective id bring weighed with the effects of the measure, eg objectives concerning environment or health issues cannot be weighed against each other like effects concerning trade restrictions.


37 Banks A., Proportionality: Constitutional Rights and Their Limitations. , Cambridge 2012, p. 236
objective the ECJ – which, notably, does not always practices the third examination level\(^{38}\) - explained the full proportionality test:

“[T]he principle of proportionality [...] requires that measures adopted by Community institutions should not exceed the limits of what is appropriate and necessary in order to attain the legitimate objectives pursued by the legislation in question, and where there is a choice between several appropriate measures, recourse must be had to the least onerous, and the disadvantages caused must not be disproportionate to the aims pursued [...]\(^{39}\) In this context, proportionality stricto sensu involves a “fair balance” between the disadvantages for the person whose rights are restricted and the weight of the legitimate aims pursued by the state.”\(^{40}\)

---

**C. Criticism on the concept of proportionality**

The concept of proportionality is apparently not perfect. There is some skepticism about its effectiveness. It has also been criticized of how adequate is to guarantee the protection of fundamental rights, especially in cases where those rights are in conflict with public interest.\(^{41}\)

Proportionality analysis typically concerns conflicts related to subjective rights as conflicts whose solution requires relating the right at consideration with the public good or some other competing right, and determining whether infringement on the engaged right is legitimated by the benefits achieved on the side of the competing right or public good. In such conflicts we should decide in favor of the alternative that realizes the most the engaged interests, values, or principles. It has also been criticized on the basis that when there is an attempt to evaluate a government measure by reference to some comparison between importance and intensities of interference with rights and the public good, it is not a rational comparison.

It is also contended that proportionality cannot readily be applied in cases that do not concern rights, because it is difficult or impossible to decide on the interests to be balanced and the weight to be ascribed to such interests.\(^{42}\)

---

\(^{38}\) A clear and full exercise of proportionality has taken place for example in Schmidberger case (C-112/00).


\(^{41}\) A systematic overview over the critical voices is offered by Matthias Klatt and Moritz Meister, Verhältnismäßigkeit als universelles Verfassungsprinzip, Der Staat 51 (2012), pp. 159 (163 ff.) who prove these worries unfounded with constructive argumentation.

The debate concerning the respective merits of proportionality a test for judicial review will doubtless continue. For most scholars, the proportionality test has the capacity to deal with problems of unlawful provocation properly. An application of this test in international investment constellations will follow as the main research object of the present study.
Chapter 2

Proportionality in investment treaty arbitration

A. Developments in instrumentalizing proportionality by international investment tribunals: Proportionality as a regulative of the relationship between equal dispute parties

1. Particularities of the evolving international investment arbitration system and its significance for any operation with the proportionality principle

In recent years, there has been much criticism of Bilateral Investment Treaties (BITs), of the investment treaty arbitration process and of the effect of international investment law on regulatory sovereignty, particularly in the case of developing countries. An important facet of this overall debate has been the discussion surrounding the question of whether arbitration constitutes an appropriate adjudication model for investor-state disputes. 43,44

BITs are legal instruments concerning parties to such treaties that are sovereign states, which have a right or duty to regulate in the public interest and that such treaties hinder, to some extent, the ability of the contracting states to regulate. From one aspect we can view international investment law system as a form of ‘public’ law from another we consider each individual treaty as a ‘private’ arrangement between states 45. The tension between regulatory sovereignty and investment protection is of great importance since, although exceptions and reservations are over the years increasingly being incorporated into BITs, the substantive rights conferred on investors largely remain shaped in


45 See the contribution in Schill (ed.), International Investment Law and Comparative Public Law, 2010. International investment law can be deemed a form of public law because it involves the adjudicatory control of the exercise of public authority and operates on the global level by drawing on both domestic and international law and creating a legal regime granting primacy to the former. Furthermore, since most international investment protection treaties set similar standards, these standards harmonize the way investors must be treated on a global level. This is valid in spite of the fact that investment claims are targeted at monetary compensation, and arbitral awards as such cannot amend national law or overhaul a policy.
a broad manner, leading to a continuing lack of certainty as to their scope by the contracting states. Investment treaty tribunals shall balance private and public interests in defining investor-state disputes.

International investment arbitration — pursuant to regional and bilateral investment treaties has four distinctive features as they are depicted in investment treaties: (a) they permit investor claims against the state without exhausting local remedies; (b) they allow claims for damages; (c) they allow investors to directly seek enforcement of awards before domestic courts; and (d) they facilitate forum-shopping, which can lead to parallel proceedings and, consequently, to inconsistent outcomes.

The proportionality principle analysis in the field of investment treaty arbitration is providing arbitrators with the appropriate analytical procedure currently available for adjudicating disputes involving conflicts between two principles (or interests, or values) that possess the same rank in a normative hierarchy. The distinctive example is a conflict between a pleaded right, and a government measure that infringes upon that right, but is nonetheless exceptionally permitted in order to further some public interest exception. Such conflicts—of which the Argentina cases before ICSID tribunals represent one type—are among the most politically controversial cases that judges are asked to resolve in recent times.

Most arbitral tribunals tend to respond by adopting a balancing attitude and they use techniques associated with balancing to mitigate certain strategic dilemmas, the most important of which is the “two against one” problem, which is to be analyzed as follows.

The social legitimacy of third-party dispute resolution rests on the perception of the parties that dispute resolvers will be neutral, vis-à-vis the parties, and will not be biased toward one value being pleaded as opposed to another. Yet each party seeks to prevail over the other. To the extent that the dispute resolver declares a winner, a two-against-one situation is created, which threatens to undermine the legitimacy of the proceeding and of the third party. Ad hoc balancing allows the dispute resolver to take a decision while making it clear, to present and future parties, that probably he might have decided otherwise if the facts had been different. More generally, balancing provides flexibility, enabling tribunals to adapt decisions to facts and to fashion equitable judgments, reducing


the burden of the defeated party as much as possible. Proportionality also provides a semblance of a response to substantive indeterminacy, providing a fixed procedure for managing such disputes, as well as a stable framework for argumentation and justification.49

Investor-State arbitration is not only a method to settle disputes between an investor and a State arising out of an investment,50 it is also a form of global governance that involves the exercise of power by arbitral tribunals in the global administrative space. In setting standards for State conduct vis-à-vis foreign investors, for example in defining what is improper administration or a violation of due process under fair and equitable treatment, tribunals set standards which may influence future conduct by the respondent State and other States, and will very likely influence the decision-making of tribunals in other cases. In settling disputes between investors and States, the tribunals also act as pre-agreed review agencies of a State’s specific actions, in some cases applying proportionality analysis or other tools of public law review when confronted with difficult balances between investor protection and the State’s environmental or economic policy choices in the wider public interest. In these respects, investor-State arbitration forms part of a governance structure, and helps constitute and shape the emerging body of global administrative law. At the same time, this quasi regulatory activity of arbitral tribunals attracts significant criticism, not only of specific decisions but with regard to the legitimacy of the decision-making powers of these tribunals as such.51

Investment treaties typically do not address the relationship between the standards of investment protection (such as indirect expropriation, fair and equitable treatment and national treatment) and the continuing powers of host states to regulate and take other actions in the interest of their populations. They also do not stipulate the applicable standard of review, meaning that tribunals must rely on their inherent powers in the determination of the appropriate degree of deference to the extent that the treaty text does not shed light on the matter.52 Most investment treaties do not explicitly list conditions under which the host state can restrict investors’ rights (as is

49 Arbitration and Judicialization by Alec Stone Sweet, Oñati Socio-Legal Series, v. 1, n. 9 (2011) – Autonomy and Heteronomy of the Judiciary in Europe ISSN: 2079-5971
50 This type of arbitration differs from purely contract-based arbitration, in which the governing law, the host State’s consent to arbitration and the rules of the arbitration are dependent on an investor State contract, not on an international treaty.
52 Arguably, the WTO Appellate Body in EC-Hormones took the view that the determination of the applicable standard of review is an inherent power (Appellate Body Report, European Communities – Measures Affecting Livestock and Meat (Hormones), WT/DS26 & 48/AB/R, 16 January 1998, at paras. 114-117). Investment tribunals have affirmed the existence of inherent powers, although not specifically in relation to the standard of review: see e.g. Libananco Holdings Co. Limited v. Republic of Turkey, ICSID Case No. ARB/06/8, Award, 2 September 2011, para. 78.
done in many human rights treaties); nor do they usually define classes of exceptions to the protection granted to foreign investors.

2. Proportionality as a tool for balancing investor rights and the public interest

When exercising their dispute settlement function, investment treaty tribunals consider public law issues on the merits on the level of compensation and damages. Tribunals do not grant much prominence to public interest considerations and arguments when discussing and measuring the amount of damages. In fact they hardly even mention them.

Two cases that public interests are explicitly mentioned in order to corroborate their argumentation are Himpurna v. PLN\textsuperscript{53} and CME v. Czech Republic\textsuperscript{54}

In Himpurna, PLN, an Indonesian State-owned electricity utility refused to fulfill its contractual obligations owed to the investor, since the 1997 Asian crisis had made the contract economically unviable. According to the investment contract, Himpurna was required to develop a geothermal energy facility in Indonesia by making large investments into the sector and PLN had to purchase electricity generated from the project. Although the issue came before an international commercial arbitration forum, the legal questions involved were essentially those typically to be found in investment arbitration.

In the eyes of the Tribunal, while the crisis could not justify the breach, the investor’s entitlement to lucrum cessans was considerably limited for, so the arbitrators held, claiming the full amount of lost profits would have constituted an abuse of rights:

‘The respondent did not seek actively to dispossess the claimant of valuable contractual rights; it has suffered helplessly from a precipitate deterioration in the macroeconomic value of the project with respect to which it had accepted the entire market risk. [...] the issue of lucrum cessans has so often come up in the context of cases where the defending State entity has acted to evict the foreign investor from a healthy on-going profitable venture. Thus the notion of the victim’s lost profits has gone hand in glove with that of the breaching party’s gain.’\textsuperscript{55}

In contrast to the latter scenario, the Tribunal found that in the present case Indonesia – through PLN – did not intend to enrich itself by appropriating Himpurna’s benefits and hence the Tribunal concluded that this fact must have a ‘moderating effect’ on the recovery of lucrum cessans. In other


\textsuperscript{54} CME Czech Republic B.V. (The Netherlands) v. Czech Republic, UNCITRAL, Final Award, Separate Opinion by Ian Brownlie, 14 Mar. 2003 (hereinafter: CME v. Czech Republic, Separate Opinion Brownlie).

\textsuperscript{55} Himpurna v. PLN, p. 93, para. 332 and p. 94, para. 335.
words, the Himpurna Tribunal emphasized the limiting influence of the crisis and the pressure that thus was put on the host State on the calculation of compensation and damages.

In an opinion of in Azurix v. Argentina case, one aspect that is of particular importance and is the tribunal’s conclusions regarding fair and equitable treatment. That doctrine, embedded in numerous bilateral investment treaties, is becoming extraordinarily important in the legal analysis of foreign investment claims. It is sometimes used not unlike a due process claim by foreign investors for any unfair treatment by host governments. Here is how the tribunal put it in the Azurix case:

“It follows from the ordinary meaning of the terms fair and equitable and the purpose and object of the BIT that fair and equitable should be understood to be treatment in an even-handed and just manner, conducive to fostering the promotion of foreign investment [...].”

The principle of proportionality has been applied in the case of Tecmed v. Mexico.

56 Along those lines, in CME v. Czech Republic Professor Ian Brownlie acknowledged the distinct challenges that a modern welfare State has to face, which owes myriads of obligations to its citizens in this regard. In his Separate Opinion Ian Brownlie argued that: ‘[a]ny assessment of the commercial approach to compensation in these proceedings must involve an adequate appreciation of the character of a bilateral investment treaty. [...]’

In this context, it is simply unacceptable to insist that the subject-matter is exclusively commercial in character or that the interests at issue are, more or less, those of the investor. Such an approach involves setting aside a number of essential elements in a Treaty relation. The first element is the significance of the fact that the Respondent is a sovereign State, which is responsible for the well-being of its people. This is not to confer a privilege on the Czech Republic but only to recognize its special character and responsibilities. The Czech Republic is not a commercial entity.[...]

The resources of a corporation entail considerable flexibility in changing the location of assets and in changing the organization of assets. The resources of a country, its human and natural resources, are a given: they are necessarily fixed.’

57 CME v. Czech Republic, Separate Opinion Brownlie, para. 73, 74 and 76.

58 Azurix Corp v. Argentina, ICSID Case No. ARB/01/12, Award, 14 Jul. 2006 (hereinafter: Azurix v. Argentina). The dispute stretches over a considerable time period resulting in an (however, dismissed) application on annulment of the original award, see Azurix Corp v. Argentina, ICSID Case No. ARB/01/12, Decision on the Application for Annulment of the Argentine Republic, 1 Sep. 2009. However, the ad hoc Committee’s decision deals with issues not particularly relevant to our analysis beforehand and thus I consider it a venial sin not to further elaborate on the Azurix annulment award.

59 Para. 360.

60 Técnicas Medioambientales Tecmed, S.A. v. United Mexican States (Case No. ARB(AF)/00/2) In August 2000, Técnicas Medioambientales Tecmed, S.A. (TECMED), a company incorporated in Spain, submitted before the Centre a request for arbitration against the United Mexican States (Mexico). The request invoked the dispute settlement clause contained in the bilateral invest ment treaty (BIT) between Mexico and Spain and was administered under the ICSID Arbitration (Additional Facility) Rules. The Arbitral Tribunal noted and considered economic impacts and burdens that the measure imposed on the investor, the host country's power of regulating investment, public interests that the host country wanted to protect and the protection by law of the investor and compensation. Furthermore, the Arbitral Tribunal took into account the absence of foreign investors in the management of the host authorities in charge of investment and also demanded existence of a reasonable relationship between the burden imposed on the foreign investor and the interest that expropriation measures wanted to achieve. The Arbitral Tribunal considered the reasons for the non-renewal and whether such reasons as a whole can determine if the measures were proportional to the deprivation of rights sustained by Cytar and the negative economic impact on the Claimant arising from such deprivation. The Arbitral Tribunal held that the economic and commercial operations in the landfill after the non-renewal of the permit had been fully and
Analysis indicates that its application will be expanded further. The principle of proportionality demands more than the non-discrimination treatment principle and is even regarded as an important principle included in the fair and equitable treatment principle.61

Under explicit reference to the doctrinal structure of fundamental rights reasoning in the EctHR jurisprudence 62, the Tribunal then engaged in a comprehensive proportionality test that weighed and balanced the competing interests in order to determine when legitimate regulation flipped over into indirect expropriation. In doing so, the tribunal essentially aimed at achieving reconciliation63 between the various rights and interests affected. From this perspective, a compensable indirect expropriation occurs only when state measures lead to disproportional restrictions of the right to property.

After establishing the rules that regulatory actions and measures will not be initially excluded from the definition of expropriation acts in addition to the negative financial impact of such actions or measures, the arbitral Tribunal considered, in order to determine if they were to be characterized as expropriation, whether such actions or measures were

"Proportionate to the public interest presumably protected thereby and to the protection legally granted to investments, taking into account that the significance of such impact had a key role upon deciding proportionality."64

The arbitral Tribunal confirmed its competence to examine

"the actions of the State in the light of Article 5(1) of the Agreement to determine whether such measures were reasonable with respect to their goals, the deprivation of economic rights and the legitimate expectations of those who suffered such deprivation. There must be a reasonable

irrevocably destroyed, and means was disproportionate to end. The arbitration was conducted under the auspices of the International Center for Settlement of Investment Disputes

61 As Xiuli H. argues that “this case seems to indicate that the principle of proportionality is to be applied more in future ICSID arbitrations, and this will be a huge challenge that the host country must confront.”

62 Para 122.

63 Kingsbury/Schill, Investor-State Arbitration as Governance: Fair and Equitable Treatment, Proportionality and the Emerging Global Administrative Law, 2009, p. 34 and A. Kulick, Global Public Interest In International Investment, 2012, p. 190. These scholars use the term “Konkordanz” or “praktische Konkordanz” was coined by the German constitutional law scholar and Federal Constitutional Judge Konrad Hesse, Grundzuge des Verfassungsrechts der Bundesrepublik Deutsch land (20th edn, 1995) para 72 and refers to a concept or method of reconciliation and balancing of competing fundamental rights. In a differentiated manner, a task that is achieved in the fundamental rights context by balancing the different rights and interests under a comprehensive proportionality methodology while aiming at a solution that gives both rights effective protection to the possible extent. ( The term 'Konkordanz or ‘praktische Konkordanz was coined by the German constitutional law scholar Konrad Hesse and refers to a concept or method of reconciliation and balancing of competing fundamental rights. In a case where two fundamental rights collide, Konkordanz’ requires that both rights be reconciled without giving up either one of them. W h a t this concept primarily excludes is perceiving one of the fundamental rights as superior to any other such right. Instead both rights have to be reconciled.

64 Para 122.
The relationship of proportionality between the charge of weight imposed on the foreign investor and the end sought to be realized by any expropriation measure. To value such charge or weight, it is very important to measure the size of the ownership deprivation caused by the actions of the State and whether such deprivation was compensated or not.  

On the basis of a number of legal and practical factors, it should be also considered that the foreign investor has a reduced or no participation in the taking of the decisions that affect it, partly because the investors are not entitled to exercise political rights reserved to the nationals of the State, such as voting for the authorities that will issue the decisions that affect such investor.

We notice that the tribunal considered the economic impact that the measure imposed on the investor, the host country's power of regulating investment, public interests that the host country wanted to protect and the protection by law of the investor and compensation. Furthermore, the Arbitral Tribunal took into account the absence of foreign investors in the management of the host authorities in charge of investment and also demanded existence of a reasonable relationship between the burden imposed on the foreign investor and the interest that expropriation measures wanted to achieve. It concluded that the economic and commercial operations in the landfill after the non-renewal of the permit had been fully and irrevocably destroyed, and means was disproportionate to end.

Following the above we conclude that the application of the principle of proportionality is to protect regulatory measures enacted in good faith and aimed at the public interest. Therefore, it is a beneficial contribution to the development of ICSID case law. Some scholar observes that “the principle of proportionality is perhaps the only reasonable means if we are dealing with an issue which concerns both public and private interests and which may take place in innumerable circumstances”.

3. Proportionality analysis in indirect expropriation claims

When tribunals in investor-state arbitration are considering the standards of review they are applying means by which they reconcile the power between host states and foreign investors in international investment law, and are a critical factor in determining whether host states may

---

65 Para 122.
permissibly regulate or take other actions in the public interest without being liable to compensate foreign investors. Bearing in mind the importance of either interest, the importance of protecting investor rights for the promotion of the economic development through foreign direct investment proportionality analysis is trying to reconcile conflicting interests and provide the optimal solution for both of them.

Not any such domestic public purpose will qualify as a public interest, vice versa, any public interest can be regarded as public purpose. Investment tribunals’ tentative moves to proportionality analysis in the context of indirect expropriation indicates that proportionality may be crystallizing as a norm in relation to when the police powers doctrine applies to defeat a claim of expropriation. Similar developments can be seen in relation to fair and equitable treatment. These decisions evidence an increasing understanding of the need for international investment law to accommodate greater space for host states to regulate in pursuit of the public interest.

The protection of the investor’s legitimate expectations does not make the domestic legal framework unchangeable or subject every change in the regulatory framework to a compensation requirement. Rather a balancing test is sometimes needed in order to apply this, and potentially other, aspects of fair and equitable treatment.

Expropriation is not necessarily confined to direct expropriations or nationalizations that involve the transfer of title from the foreign investor to the state or a third party. Depending on the treaty provision or other controlling standards (such as customary international law), it may also cover so-called indirect, creeping, or de facto expropriations, involving state measures that do not interfere with the owner’s title, but negatively affect the property’s substance or void the owners control over it.

International investment tribunals when they have the opportunity to elaborate claims of indirect expropriation have increasingly taken into account the host state’s regulatory purpose in their analysis, implying the need for measures to achieve a balance between host state and investor interests. Some tribunals have attempted to adopt proportionality analysis in their determination of claims, but their reasoning has been rather problematic and characterized by a rather rigorous

---

70 See in Benedict Kingsbury/Stephan W Schill, Public Law Concepts to Balance Investor’s rights with State Regulatory Actions in the Public Interest- The Concept of Proportionality
standard of review. The turn to proportionality analysis in indirect expropriation cases has its origins in the early NAFTA cases of S.D. Myers v. Canada and Feldman v. Mexico.\footnote{Marvin Feldman v. Mexico case no. arb(AF)/99/1 This case concerns a dispute regarding the application of certain tax laws by the United Mexican States to the export of tobacco products by Corporación de Exportaciones Mexicanas, S.A. de C.V. (“CEMSA”), a company organized under the laws of Mexico and owned and controlled by Mr. Marvin Roy Feldman Karpa, a citizen of the USA. The Claimant, who is suing as the sole investor on behalf of CEMSA, alleges that Mexico’s refusal to rebate excise taxes applied to cigarettes exported by CEMSA and Mexico’s continuing refusal to recognize CEMSA’s right to a rebate of such taxes regarding prospective cigarette exports constitute a breach of Mexico’s obligations under the Chapter 11 of the NAFTA”. In particular, Mr. Feldman alleges violations of NAFTA Articles 1102 (National Treatment), 1105 (Minimum Level of Treatment), and 1110 (Expropriation and Indemnification). Mexico denies these allegations.}

Proportionality analysis thus facilitates balancing between interests of foreign investors, or more generally property rights, and conflicting public interests. When proportionality is used by sophisticated courts and tribunals in national and international jurisprudence to deal with open-ended concepts and difficult balancing analysis it has proved to be methodologically more efficient and workable than the kinds of reasoning applied by many tribunals to fair and equitable treatment clauses or to the concept of indirect expropriation.\footnote{A. Stone Sweet, Investor-State Arbitration: Proportionality’s New Frontier, 4 Law & Ethics of Human Rights (2010), 47 ff.; Kingsbury/Schill, Investor-State Arbitration as Governance: Fair and Equitable Treatment, Proportionality and the Emerging Global Administrative Law, 2009.}

The majority of the tribunals, however, takes into account the purpose of a state’s measure and adopts the so-called police power doctrine in deciding whether a general measure entitles an investor to compensation under the concept of indirect expropriation. The police power doctrine recognizes that a state has the power to restrict private property rights without compensation in pursuance of a legitimate purpose (\textit{under this approach, it is not sufficient to determine the effect of a state measure; instead, the measure’s effect has to be balanced in relation to the object and purpose of the interference}).\footnote{See B. Kingsbury/S. W. Schill, Public Law Concepts to Balance Investor’s Rights with State Regulatory Actions in the Public Interest-The Concept of Proportionality, in Schill (sd.), International Investment Law and Comparative Public Law, 2009, p. 90.}

The notions of proportionality and reasonableness appear in various instances of arbitral jurisprudence on fair and equitable treatment, usually without further explanation of their meaning. In the case of S.D, Myers Inc. v. Canada\footnote{S.D. Myers, Inc. v. Government of Canada, UNCITRAL 2000-2002,} applied a test that adhered to a common proportionality analysis. According to the facts of the case S.D. Myers, Inc., an Ohio corporation that processes and disposes of PCB waste, filed in 1998 a claim alleging that Canada's ban on the export of PCB wastes from Canada to the United States in late 1995 breached Canada's obligations under Chapter Eleven of the North American Free Trade Agreement. The Tribunal released its Award on liability which
ruled that Canada's actions had breached two of the four obligations under Chapter 11 that were subject to the claim. Subsequently, Canada filed an application with the Federal Court of Canada seeking review of the tribunal's decision, on the grounds that elements of the decision exceeded the tribunal's jurisdiction and were made in conflict with Canada's public policy. The judge dismissed Canada's application. The tribunal held:

“Canada was concerned to ensure the economic strength of the Canadian industry, in part, because it wanted to maintain the ability to process PCBs within Canada in the future. This was a legitimate goal, consistent with the policy objectives of the Basel Convention [on the Control of Transboundary Movements of Hazardous Wastes and Their Disposal], There were a number of legitimate ways by which Canada could have achieved it, but preventing [the investor] from exporting PCBs for processing in the USA by the use of the interim order and the final order was not one of them. The indirect motive was understandable, but the method contravened Canada’s international commitments under the NAFTA. Canada’s right to source all government requirements and to grant subsidies to the Canadian industry are but two examples of legitimate alternative measures. The fact that the matter was addressed subsequently and the border re-opened also shows that Canada was not constrained in its ability to deal effectively with the situation”.

The tribunal in this case assessed the legitimacy of the goal pursued by Canada, especially because it also deliberately emphasized the ‘high measure of deference that international law generally extends’ to matters of domestic regulation. The reasoning for the tribunal to adopt regulatory objectives emerged not only from the sovereignty of Canada, but was in this case also sustained by the principle of sustainable development, as the objectives also complied with the Basel Convention. The suitability of the export ban in relation to that goal was obvious and therefore probably not worth mentioning for the tribunal. Difficulties arose with regard to the necessity of the measure, which was explicitly scrutinized by the tribunal. It found that at least two other alternative, and arguably less restrictive, measures existed. Because the necessity of the export ban was denied, a balancing at the stage of proportionality stricto sensu did not take place. Without expressly referring to the notion of proportionality, the tribunal thus carried out a structured proportionality analysis. 76

While the Tecmed77 tribunal’s analysis was methodologically problematic, its attempt to reconcile host state and investor interests through proportionality analysis nevertheless shows

76 See ‘Fair and Equitable Treatment ‘in International Investment Law, by Roland Klager, Cambridge university Press, p.241
77 As well as its approach to expropriation, the decision is also notable (or notorious) for its expansive interpretation of the fair and equitable treatment standard: ‘the foreign investor expects the host State to act in a consistent manner, free from ambiguity and totally transparently . . . so that it may know beforehand any and all rules and regulations that will govern its investments, as well as the goals of the relevant policies and administrative practices or directives. Any and all State actions conforming to such criteria should relate not only to the guidelines, directives or requirements issued, or the resolutions approved thereunder, but also to the goals underlying such regulations. The foreign investor also expects the host State to act consistently, i.e. without arbitrarily revoking any preexisting decisions or permits issued by the State
potential for the technique to be used to assist in delimiting non-compensable measures from indirect expropriations.\(^\text{78}\)

Such decisions are an important first step towards the development of a jurisprudence of indirect expropriation that gives broader scope for justifying measures interfering with investment without a requirement to pay compensation, where such measures reflect sound public policy objectives. Several other tribunals (\textit{Azurix v Argentina,\(^\text{79}\) Suez and InterAgua v Argentina,\(^\text{80}\) Archer Daniels v Mexico\(^\text{81}\) and Fireman’s Fund v Mexico\(^\text{82}\)}) either approved the Tecmed approach or referred to the concepts of proportionality or balancing.

4. \textit{Proportionality analysis and FET standard}

When Tribunals set standards for State conduct vis-à-vis foreign investors, they have to decide whether to apply proportionality analysis or other standards of public law review when they deal with disputes concerning difficult balances between investor protection and the State’s environmental or economic policy choices. Proportionality analysis can also apply in some contexts and with regard to some sub-elements of the fair and equitable treatment (FET) standard.

\(^{78}\) The claimant in \textit{Tecmed v. Mexico} was a Spanish concern Tecmed, which, by public auction, acquired a hazardous waste landfill in Mexico in 1996 through its subsidiary, the Mexican Cytrar. The official 1994 authorization to operate the landfill and the subsequent permits granted by Mexican environmental authorities had projected that the landfill would have a ten-year life. Cytrar’s acquisition included the landfill’s tangible assets and permits. In 1996, the Hazardous Materials, Waste and Activities Division of the National Ecology Institute of Mexico (hereinafter referred to as “INE”), which is in charge of Mexico’s national policy on ecology and environmental protection and is also the regulatory body on environmental issues, issued a one-year permit to Cytrar, which could be extended every year at the applicant’s request 30 days prior to its expiration. It was extended for an additional year, but Cytrar was refused when it required the INE to extend the permit in 1998. The claimant argued that the refusal of Mexican authority (respondent) constituted indirect expropriation of its assets and breached the Bilateral Investment Treaty between Spain and Mexico. Therefore, the claimant applied for arbitration to the ICSID on 28 July 2000.

\(^{79}\) Azurix Corporation v The Argentine Republic (Azurix v Argentina), ICSID Case No. ARB/01/12, Award, 14 July 2006, at paras 310–12, simply citing relevant passages from James v U.K. and Tecmed v Mexico and holding that the factors referred to would provide useful ‘guidance’ on the question of expropriation.

\(^{80}\) Suez, Sociedad General de Aguas de Barcelona S.A., and InterAgua Servicios Integrales del Agua S.A. v Argentina, (InterAgua v Argentina) ICSID Case No. ARB/03/17, Decision on Liability, 30 July 2010, at paras 147–48: ‘States have a reasonable right to regulate foreign investments in their territories even if such regulation affects investor property rights. In effect, the [police powers] doctrine seeks to strike a balance between a State’s right to regulate and the property rights of foreign investors in their territory.

\(^{81}\) Archer Daniels Midland Company and Tate & Lyle Ingredients Americas, Inc. v United Mexican States (Archer Daniels v Mexico), ICSID Case No. ARB (AF)/04/5, Award, 21 November 2007, concerning taxes levied on soft drinks and syrups.

\(^{82}\) Fireman’s Fund Insurance Company v United Mexican States, ICSID Case No. ARB(AF)/02/01, Award, 17 July 2006, at para 176(j), concerning Mexican financial regulations adopted in response to its 1990’s economic crisis.
Investment treaties require the parties to provide a certain level of protection to investors and investments from the other party by requiring the host State to provide national and most-favoured nation treatment; that is, the treaties require the host State to treat investors and investments from the other party no less favourable than the host State treats its own investors and investments, or investors and investments from third parties, which are in like circumstances. Also most investment treaties do impose a more general obligation of 'fair and equitable treatment'. Many attempts have been made to define exactly 'fair and equitable treatment'. For instance the tribunal in *Tecmed v. Mexico* stated that the fair and equitable treatment standard *requires the Contracting Parties to provide to international investments treatment that does not affect the basic expectations that were taken into account by the foreign investor to make the investment*. International investment treaty tribunals have repeatedly associated fair and equitable treatment with five elements, principles:

1. The requirement of stability, predictability and consistency of the legal framework,
2. The protection of legitimate expectations,
3. The requirement to grant procedural and administrative due process and the prohibition of denial of justice,
4. The requirement of transparency, and
5. The requirement of reasonableness and proportionality.

---

---

---

---

---

---

---

---

---
The above analyzed gradual development in the indirect expropriation case law is cognate with trends in relation to the fair and equitable treatment standard, particularly in relation to regulatory changes affecting investors and the doctrine of legitimate expectations.96

B. Methodology of legal reasoning and rationales for determining standards of review in the application of proportionality test

Typically, investment treaties do not indicate the standard of review to be applied in considering expropriation claims, meaning a tribunal must itself determine whether it is the more competent institution to decide the particular matter.97

The suitability criterion in proportionality analysis is generally regarded as relatively undemanding, requiring only that a measure be capable of advancing its objective or rationally connected to it.98

Necessity analysis requires a court or tribunal to consider hypothetical alternative measures that impact less on the right or interest at stake. Further, the assessment of necessity involves the making of (sometimes difficult) predictions concerning the likely efficacy and impact of alternative measures, which may be a matter of fine distinctions, particularly where a decision is polycentric (involving the consideration and balancing of a number of divergent interests) or engages (for example) economic policy.99

Standards of review in the international and supranational context are of particular relevance to investment treaty arbitration. There are several factors that can be influencing the standard of review such as the duration and the intensity of the limitation upon the protected right or interest and the degree of harmonization or consensus among members of a regime with respect to the subject matter of a dispute and democratic legitimacy. States have in general the discretion to enact laws and take other actions to further evolve the application of public interest. But several scholars have made a strong argument that only legislative bodies, rather than adjudicators, should bear primary responsibility for law and policy-making, because decisions about what is in the public interest are primarily political decisions.100

98 Kingsbury and Schill (2009), above n 1, 39; Barak, above n 40, 303, 305. Proportionality, (2012)
100 The concern is that the adjudicatory procedure cannot effectively substitute for deliberative democratic processes and that accordingly, adjudicators should be hesitant to engage in review where a matter engages these concerns. The democracy-based rationale for deference also suggests that greater deference should be afforded to decisions of legislators (i.e., in relation to stability) than to exercises of administrative discretion (consistency). A related issue is the proximity of the court or tribunal to the national setting. Most courts and tribunals adjudicating public law matters are
Courts and tribunals at both the domestic and international levels display a high degree of deference in relation to authorities’ assessments of the importance of the regulatory objective, for reasons of democratic legitimacy and proximity to local conditions.

C. Scope of the proportionality analysis by investment arbitral tribunals in comparison to international courts and tribunals

The ECJ is reluctant to intervene where a measure is in an area in which decision-makers have broad discretionary powers and clear political responsibility, particularly where the exercise of public powers entails political choices and polycentric decision-making (including in relation to economic and social policy, national security or issues of local concern such as morality).

The ECtHR similarly takes the view that democratically legitimate decision-makers may be better placed to appreciate what is in the public interest with respect to measures interfering with property rights, particularly in the context of broad reforms that involve the consideration of political, economic, and social issues on which opinions may differ widely. It has also frequently emphasized the need to show deference to national authorities’ proximity to local conditions.

WTO tribunals appear sensitive to the political nature of many legislative decisions and have been at pains to emphasize WTO members’ autonomy to set their own regulatory objectives and the appropriate level of achievement of them, although they do not express these views in terms of a discourse of deference.
Concerning the adjudicators’ institutional competence and expertise regarding matters at issue both the ECJ and ECtHR take into account the level of expertise or knowledge required to make the relevant decision, and both courts are generally highly deferential in the context of complex, large-scale policy decisions including macroeconomic, budgetary and fiscal policy, planning and the environment and pressing or emergency situations.\(^\text{103}\)

A similar approach may be emerging in the context of indirect expropriation claims, at least in the context of economic crises: the LG&E v Argentina tribunal indicated that deference to the host state should be heightened in the context of the Argentine economic crisis, and the Total v Argentina tribunal referred to the fact that the measure at issue was ‘reasonable in light of Argentina’s economic and monetary emergency and proportionate to the aim of facing such an emergency’.\(^\text{104}\)

WTO tribunals acknowledge the issue of expertise in relation to scientific and technical information by relying on, for example, expert evidence and statements of international bodies, although they have not dealt with these issues systematically in terms of how these factors affect the intensity of review.\(^\text{105}\)

Challenges to the legitimacy of investment tribunals exercising power over States also frequently involve some critique of the open-ended language of the investors’ rights provisions and concerns that these empower tribunals to abridge the role of States as regulators to protect the public interest, whether for environmental protection, human rights, or to meet emergencies, in the sole interest of protecting property rights and economic interests. This is particularly the case as regards the State’s function as a regulator by means of abstract and general regulation.\(^\text{106}\) We must bear in mind that Investor-State arbitration is not only a mechanism to settle disputes between an investor and a State arising out of an investment, it is also a form of global governance that involves the exercise of power by arbitral tribunals in the global administrative space.


International courts rarely deploy proportionality, step-by-step, as systematically as, say, the German and Israeli courts do. The ECtHR prefers a broader balancing approach, which it use, among other things, to define the scope of the State’s discretion (which the ECtHR calls a “margin of appreciation”, siehe Chapter 1).

In contrast, the ECJ and the WTO Appellate Body deploy relatively robust versions of necessity analysis when they adjudicate derogations to trading rules (under Article 30 of the Treaty of Rome and Article XX of GATT, respectively).

The ECJ and the WTO AB will typically rule against a State pleading derogations if they can find one (or preferably several) alternatives that were both less restrictive on trade, and reasonably available to policymakers. Modes of reasoning which Germans constitutional lawyers would associate more with balancing in the strict sense are often incorporated into necessity analysis.

Neither the ECJ nor the ECtHR should be regarded as embodying best practice in relation to a consistently applied and well-articulated approach to proportionality analysis. The ECJ is criticized for applying proportionality analysis and exhibiting deference in an inconsistent and imprecise manner, and the ECtHR’s decisions are sometimes stated summarily without further elaboration of the weight ascribed to the competing considerations. Yet, aspects of the comparative jurisprudence referred to in this article demonstrate a structured approach to proportionality analysis and a principled approach to the standard of review: investment tribunals should be guided by these aspects.

When assessing the legitimacy of a policy objective in relation to national authorities’ interference with free movement, the ECJ as well as ECtHR, will be highly deferential.

We notice the decision of tribunals defer to national authorities where authorities’ expertise or knowledge is superior, and states are generally highly deferential in the context of complex, large-

---

107 Turning to the analysis of necessity, the Tribunal quoted extensively from what is today the leading WTO case, EC-Tyres (Brazil – Measures Affecting Imports of Retreaded Tyres (DS332) (2007) including this passage: “The necessity of a measure should be determined through “a process of weighing and balancing of factors” which usually includes the assessment of the following three factors: the relative importance of interests or values furthered by the challenged measures, the contribution of the measure to the realization of the ends pursued by it and the restrictive impact of the measure on international commerce.” This formulation incorporates, into necessity analysis, considerations typically associated with balancing (proportionality in the strict sense).


109 For instance ECtHR, Lecarpentier v France, Application Number 67847/01, Judgment of 14 February 2006 (unreported) at paras 47–48. French measures that applied retroactively to affect disputes between private parties before national courts, taken ostensibly to safeguard the financial stability of the banking system, were not in the public interest as there was no evidence that the banking sector and economic activity in general were jeopardized, although the ECtHR appeared to accepted that such an objective pursued the public interest in a general sense.
scale policy decisions including macroeconomic budgetary and fiscal policy, as well as in relation to planning and the environment, national security concerns or pressing or emergency situations.\footnote{A similar approach may be emerging in the context of indirect expropriation claims, at least in the context of economic crises: the LG&E v Argentina tribunal indicated that deference to the host state should be heightened in the context of the Argentine economic crisis, and the Total v Argentina tribunal referred to the fact that the measure at issue was ‘reasonable in light of Argentina’s economic and monetary emergency and proportionate to the aim of facing such an emergency’.

\footnote{See the contributions in Schill (ed.), International Investment Law and Comparative Public Law, 2010.}


\footnote{So explicitly in the approach of Kingsbury B./Schill W. S., Public Law Concepts to Balance Investor’s rights with State Regulatory Actions in the Public Interest: The Concept of Proportionality in Schill (ed.), International Investment Law and Comparative Public Law, 2010, pp. 75 ff.}

D. Encapsulation of the notion of public interest in customary international law as the precondition for developing operability of proportionality

1. Doctrinal necessity to operate with proportionality and structural transformation of proportionality into the field of international investment disputes

As impressively demonstrated by several scholars in recent discussions\footnote{See the contributions in Schill (ed.), International Investment Law and Comparative Public Law, 2010.}, comparative public law can have a direct effect on the interpretation of international investment treaties. In particular, comparative public law can be relevant in order to ascertain the ordinary meaning states attribute to certain concepts of the notion of public interest - as it is involved in the performance of their obligations under investment law -, for instance, in determining the meaning of “expropriation” or of “fair and equitable treatment” - and thus serve as an aid to interpretation of host state obligations under investment treaties regarding the protection of investors. The relevance of proportionality in this context is obvious if one seeks after the doctrinal vehicle for the consideration of public interest. Since, on the other hand, proportionality can be considered, by its very nature as general principle of law, also relevant and applicable in the relations between the parties to a BIT as constituting, by virtue of Article 38(1)(c) of the Statute of the International Court of Justice, a source of international law, which must be taken into account in the interpretation and application of investment treaties pursuant to Article 31(3)(c) of the Vienna Convention on the Law of Treaties as part of the “relevant rules of international law applicable in the relations between the parties.”\footnote{Stephan W. Schill, Enhancing International Investment Law’s Legitimacy: Conceptual and Methodological Foundations of a New Public Law Approach, Virginia Journal of International Law, Volume 52 (2011), p. 57.} Consequently, proportionality may well serve as a concept to view international investment law issues through the ‘public law’ lens.\footnote{So explicitly in the approach of Kingsbury B./Schill W. S., Public Law Concepts to Balance Investor’s rights with State Regulatory Actions in the Public Interest: The Concept of Proportionality in Schill (ed.), International Investment Law and Comparative Public Law, 2010, pp. 75 ff.}
Following the stages of proportionality analysis a policy objective’s legitimacy can be assessed in terms of a) deference in the assessment of the legitimacy of the regulatory objective, b) deference in suitability analysis, c) deference in necessity analysis and d) deference in relation to strict proportionality. Deference may be exhibited in relation to strict proportionality analysis by the adjudicator attributing presumptive weight to the decision-maker’s ascription of value to the benefit of the measure and to the infringement of the right or interest, or by holding a measure lawful unless the impact on the protected right or interest is regarded as significantly exceeding the measure’s benefits or where the balance appears to be manifestly disproportionate.114

2. The need to structurally transpose the proportionality doctrine

The State’s tendency to intervene in pursuit of a particular objective will naturally be a decision in respect of which opinions may differ. Some states will understand police power as comprising a range of interventions to promote the public good, whereas other states’ exercise of police powers will be restricted to protecting individuals from harm.115 There should always be an assessment of whether a measure pursues the public interest seeks to identify measures taken in bad faith or for clearly illegitimate purposes.

A deferential approach to the questions of legitimate objective, suitability and necessity will lead to consideration of a measure’s strict proportionality where the measure has satisfied the earlier.

3. The need to introduce a formal principle in the balancing process

Provided that a measure is shown to be suitable and necessary to attain a legitimate objective, the assessment of whether an appropriate balance between a measure taken in the exercise of police powers and the measure’s expropriatory effect should primarily be left to host states. Tribunals should be deferential in their evaluation of the relative importance of the host state’s regulatory objective against the measure’s expropriatory effect, and should ascribe appropriate weight to national authorities’ assessment of the requisite balance. In circumstances where host states appear to have acted in good faith in pursuit of the public interest, review of measures should be limited to


115 The result of this deferential approach is that authorities’ assertion of a need to intervene in the public interest will be treated as prima facie valid unless it appears to be ‘manifestly without reasonable foundation’ (See Caroline Henckels in *Indirect Expropriation and the Right to Regulate: Revisiting Proportionality Analysis and the Standard of Review in Investor State Arbitration*, Journal of International Economic Law 15(1), 2423 doi:10.1093/jiel/jgs012)
assessing whether the proportionality of a measure is manifestly disproportionate in light of its expropriatory effect.\textsuperscript{116}

\textsuperscript{116} Such an approach was indicated by the LG&E tribunal, remarking that the exercise of regulatory power should not be regarded as constituting expropriation except where the measure was ‘obviously disproportionate’ (See Caroline Henckels in Indirect Expropriation and the Right to Regulate: Revisiting Proportionality Analysis and the Standard of Review in Investor State Arbitration, Journal of International Economic Law 15(1), 2423 doi:10.1093/jiel/jgs012, page 253)
Chapter 3

Personal statements and proposals: Improvement of arbitral decision making by elaborating proportionality analysis

A. Methodological advantages in decision making - comparability to system building contribution of precedents (system building effect)

The Argentine cases are illustrative of a partially contradictory jurisprudence in terms of theoretical coherence by some investment arbitral tribunals to date. On the other hand, investment treaty tribunals generate largely coherent decisions regarding the interpretation of the substantive principles of investment protection. References to earlier investment treaty awards and decisions can be found in virtually any of the more recent awards.\(^{117}\) As already mentioned, several tribunals have attempted to flesh out a structured and deferential proportionality-based approach to expropriation claims.\(^{118}\) Moreover, with regard to the exercise of competences which is also subjected to proportionality test, due to a concern for institutional sensitivity which is considered in the balancing processes, proportionality analysis may offer a framework for legal discourse about trade-off problems.\(^{119}\) Proportionality analysis has proven to be methodologically workable and coherent and generalizable by many tribunals to “fair and equitable treatment” clauses or the concept of indirect expropriation.\(^{120}\) The diversity of existing uses of proportionality analysis is stressed out because it

\(^{117}\) In fact, as quantitative citation analyses of investment treaty awards show, “citations to supposedly subsidiary sources, such as judicial decisions, including arbitral awards, predominate, Jeffrey Commission, Precedent in Investment Treaty Arbitration - A Citation Analysis of a Developing Jurisprudence, journal of international arbitration 129, 148 (2007). Unlike in commercial arbitrations between private parties that are held behind closed doors, this development is possible because awards in investment treaty arbitrations are regularly published on the Internet and in print journals and are discussed extensively in the investment law community and general media. The latter is also the view of Stephan W. Schill.

\(^{118}\) Tecnicas Medioambientales Tecmed S.A. v The United Mexican States (Tecmed v Mexico), ICSID Case No. ARB(AF)/00/2, Award, 29 May 2003


\(^{120}\) Fundamental to the application of proportionality analysis (and comparable techniques of balancing) in investment treaty arbitration is the question of the relationship of proportionality analysis to the applicable law, and in particular to the applicable international law while the starting point is the good faith interpretation of the applicable treaty. The texts of these treaty provisions are typically sparse in relation to the tribunals’ governance roles, and their interpretation also calls for consideration of their context, their object and purpose, and other relevant materials. General
makes it possible to undertake wide-ranging and instructive comparative law research and analysis as to what is considered as proportional in various national legal systems and transnational or international tribunals.  

How arbitral tribunals translate the patchwork of international investment treaties into a genuine (sub-) system of international law becomes most obvious in regard of the use of precedent. Although arbitral tribunals are not obligated to follow the past awards reasoning of prior tribunals, through a series of cases, for example the Argentinian cases, they tend to establish a system of precedent not only with respect to the interpretation of the same investment treaty, but across various treaties. As stated in case AES v. Argentine (2005)

“Each tribunal remains sovereign and may retain, as it is confirmed by ICSID practice, a different solution for resolving the same problem; but decisions on jurisdiction dealing with the same or very similar issues may at least indicate some lines of reasoning of real interest; this Tribunal may consider them in order to compare its own position with those already adopted by its predecessors and, if it shares the views already expressed by one or more of these tribunals on a specific point of law, it is free to adopt the same solution”.

principles of law concerning the roles and functions of such juridical decision-making institutions may become relevant. Global administrative law principles on the proper conduct of tribunal processes have obvious relevance, but legal principles of broader ambit, such as proportionality, may also help to give substance to the proper roles and functions of these tribunals in their assessment of State conduct, based on their constitutive treaties See Kingsbury, Benedict and Schill, Stephan, *Investor-State Arbitration as Governance: Fair and Equitable Treatment, Proportionality and the Emerging Global Administrative Law*, 2009, New York University Public Law and Legal Theory Working Papers. Paper 146, p. 23, [http://lsr.nellco.org/nyu_plltwp/146](http://lsr.nellco.org/nyu_plltwp/146).


124 The Common Law tradition adequately reflects this working of precedents on the basis of factual analogies, which is, by contrast, underestimated, e.g., in German constitutional law scholarship, which focuses on the abstract evaluations to be found in the legal reasoning of the Federal Constitutional Court. (See Schill W. S., *System-Building in Investment Treaty Arbitration and Lawmaking*, 12 German Law Journal, (2011), pp. 1083-1110)


127 AES Corporation v. Argentine Republic, ICSID Case No. ARB/02/17, Award, para. 30 (Apr. 26, 2005).
Certainly, the ways in which investment treaty tribunals make use of precedent differ.\textsuperscript{128} But the effect of judicial precedents is concealed by the doctrinal ordering of things in light of Article 38(1)(d) ICJ Statute,\textsuperscript{129} classifying international judicial decisions as “subsidiary means for the determination of rules of law.” Under the impact of understanding of judicial interpretation, decisions are thought of as a source that helps one recognize the law and the influence of precedent. Yet, they all illustrate how investment treaty jurisprudence converges, and forms part of a uniform treaty-overarching regime for international investment relations, and how investment treaty tribunals actively engage in system-building in this field.\textsuperscript{130}

As was noted by Stone Sweet & Mathews\textsuperscript{131}, proportionality balancing constitutes a doctrinal underpinning for the expansion of judicial power globally. Balancing is in way leads arbitrators toward proportionality. In investor-State disputes, we have to acknowledge both the recognition of an investor’s property rights and the State claiming a “public interest” defense. This would justify the infringement of the investor’s rights and also that public good was served. The use of the proportionality framework by arbitral tribunals is the most efficient way to weigh between the burden imposed to the foreign investor and the aim sought to be realized by any expropriatory measure.

The mechanism, according to which the outcomes of judicial balancing function as precedents, is twofold. First, abstract evaluations of certain trade-off problems or inter-regime conflicts may be taken from the reasoning of courts. Second, normative expectations may rest on factual analogies,  

\textsuperscript{128} In ascending order of normative impact on tribunal decision-making, the use of precedent includes the following: (1) precedent as a source of cautious analogizing with earlier decisions; (2) precedent as a means of clarifying treaty provisions; (3) precedent as an abbreviation of reasoning; (4) precedent as a standard-setting device; and (5) precedent as an instrument of system-wide law-making. Finally, precedent is even at play in cases of conflicting decision-making in investment treaty arbitration (6). Precedent, in consequence, becomes the basis for those affected by international investment treaties and investment treaty arbitrations to develop normative expectations about the existence of a system of international investment law and its functioning (7).

\textsuperscript{129} Article 38. (1) The Court, whose function is to decide in accordance with international law such disputes as are submitted to it, shall apply: (a) international conventions, whether general or particular, establishing rules expressly recognized by the Contesting States; (b) international custom, as evidence of a general practice accepted as law; (c) the general principles of law recognized by civilized nations; (d) subject to the provisions of Article 59, judicial decisions and the teachings of the most highly qualified publicists of the various nations, as subsidiary means for the determination of rules of law. (2) This provision shall not prejudice the power of the Court to decide a case ex aequo et bono, if the parties agree thereto.

\textsuperscript{130} See Stephan W. Schill in System-Building in Investment Treaty Arbitration and Lawmaking, [Vol. 12 No. 05 German Law Journal]

\textsuperscript{131} See Stone Sweet A. and Mathews J., Proportionality Balancing and Global Constitutionalism. Faculty Scholarship Series, 2008
which give orientation for future cases with comparable facts. Similarly, although investment tribunals are not bound by earlier decisions and can thus diverge without committing an error of law, they nevertheless ought ordinarily to explain why they diverge from the reasoning of well-known prior decisions on the same point. In most cases of “inconsistent decisions” arbitral tribunals do this\textsuperscript{134}. Overall, the integration of external norms by balancing and other legal techniques leads to a dialectic interaction between norm integration and the assertion of authority over external norms.\textsuperscript{135}

To my view because investment treaty tribunals not only have the function to submit disputes to specific investment treaties they also contribute in a case-law affecting not only the investor-Stet relationship by developing the basic principles of investment protection and proportionality. When standards and principals as proportionality are further developed in investment arbitral decision making they generate a system building effect.

**B. Potentials of Proportionality to contribute for legitimating investment tribunal decisions – Allocation of authority in a fragmented international investment arbitration system**

Proportionality analysis may provide one way to counter risks of clinical isolation of international investment law, and to build some degree of coherence into aspects of an international economic order. It is probable that proportionality analysis, if done well and with due circumspection, could potentially enhance the legitimacy of rule-governed legal institutions that undertake it.\textsuperscript{136}

\textsuperscript{134} The tribunal in *SGS v. Philippines*, for example, extensively engaged in a discussion of the earlier award in *SGS v. Pakistan* that suggested a contrary interpretation and application of umbrella clauses. Likewise, the tribunal in *El Paso Energy v. Argentina* that preferred the solution in *SGS v. Pakistan*, and disapproved of the ruling in *SGS v. Philippines*, engaged in an extensive discussion of why it followed one rather than the other approach. Similarly, decisions on the interpretation of most-favored nation clauses usually discuss in a well-reasoned way inconsistent decisions by other investment tribunals.

\textsuperscript{135} The integration of external norms by balancing and other legal techniques leads to a dialectic interaction between norm integration and the assertion of authority over external norms. First, to integrate norms of another system means to acknowledge the authority of that other system to produce pertinent norms. Conversely, it also means asserting authority over those norms. Consequently, to integrate norms of another system is to introduce the problems of overlapping authority. Finally, these problems of overlapping authority foster authority-integrating solutions (e.g., deference). In the end, specialized international courts will refrain from applying external norms as norms and consider them—in a kind of dualist approach—as factual evidence at best, as has already been shown with regard to the WTO Appellate Body. (see Stephan W. Schill, *System-Building in Investment Treaty Arbitration and Lawmaking*, Vol. 12 German Law Journal).

International investment arbitration raises difficult questions of legitimacy. To address those questions is necessary both for the development of international trade on the one hand and that of democratic governance at national level over issues of fundamental public interests on the other.

The principle of proportionality has the potential to enhance the legitimacy of rule-governed legal institutions that undertake it.

Law governing international investment relations is largely fragmented and unsystematically aggregated. The ‘fragmentation’ of international law is itself is fragmented. Moreover, from one analytical viewpoint, the problems associated with the fragmentation of international law can be seen as falling into two broad categories, reflecting two distinct points of entry. Beyond normative fragmentation, the other category of problems relates to the fragmentation of international authority.

To my view, an appellate mechanism, for instance, would have reduced the severity of this conflict of authority as the investor would be not incented to file in two different proceedings as he would be certain that he would reach the same higher authority at some point. In any case, an appellate mechanism for international investment would prevent inconsistent rulings.

Considering proportionality analysis as the best tool to reconcile conflicting interests on the merits stage raises the question as to how it should be embedded in the overall doctrinal structure of a potential rights violation analysis.

Proportionality analysis reflects the allocation of authority between a legal system’s primary decision-makers and its adjudicators and also the balance between state responsibility and sovereignty. Employing the proportionality principle within the current system of investor-state arbitration, is the best way for international investment law to find a better balance between public

---


139 The concern here is not with the interrelationship between rules, as such, but rather with the distribution of authority and power (in the legal sense of the word) among the plethora of international and national institutions and organizations that produce, interpret, and apply interna-tional law. The question is not what is the law, but rather who decides what it is. We ask, who has the authority to make a determination on a particular question arising under international law?

and private interests. It provides more transparent arrival at a decision to whether the measure’s impact is proportionate to the protected public interest\textsuperscript{141}.

Conclusions

1. The present study examines the operationalization of proportionality analysis by investment treaty tribunals. Proportionality was introduced through the jurisprudence from other international law regimes, mostly WTO and European human rights law. Proportionality is a permissible particular legal technique of resolving conflicts between subjective rights which can be located in the international as well as constitutional legal order and legal contents within areas of collision between individual rights and public interests through a process of balancing.

2. The principle of proportionality in its most common version roots in the German administrative and constitutional law and, more specifically, in the jurisprudence of the Federal Constitutional Court, having been there (as well as in the scholarly literature) developed to a sophisticated concept and recognized as a constitutional principle and a control instrument upon administrative discretion in order to resolve conflicts between the rights of the individuals and interests of the State.

3. The “globalized” application of the proportionality principle in the context of the European Human Rights-, European Union-, World Trade Organisation- and, since recent times, the international investment protection adjudication demonstrate that we are currently witnessing the emergence of a general principle of law. Comparative perspectives can assist in formulating a normative understanding about how investment tribunals should approach the standard of review in their determination of public law-type claims.

4. Similarly to the operationalization of proportionality in European Union and European Human Rights law, the principle can prove to be an important tool for arbitral tribunals in investment arbitration to mainly check the regulatory freedom of governments. It can be deemed the emerging law tool to operationalize for the balancing of (infringed) investor rights - as investment treaties oblige the parties to provide a certain level of protection to investments and investors from the other parties to the treaties - with host state necessity defenses referred to public interest; proportionality analysis in investment arbitration raises in circumstances ensuing from fundamental changes in the political system of the host state or imminent economic or social crisis, as enshrined in general principles of law and customary international law.

5. The structural transformation of proportionality into the field of international investment disputes can be achieved via Article 38 para. 1 of the ICJ Statute which includes general
principles of law as a source of international law: proportionality can be considered, by its very nature as general principles of law, also relevant and applicable in the relations between the parties to a BIT.

6. Due to its formal qualities consisting primarily in uniformity and predictability (stability) in the structure of tribunal decisions, the establishment of proportionality analysis in international investment arbitration can further the required legitimation of arbitral decisions. In addition, it can generate coherence in arbitral jurisprudence and therefore develop a system-building effect in the area of international investment protection. Moreover, as investment treaty arbitration involves the review and exercise of governance functions, more attention needs to be paid to standards of review such as proportionality analysis as a mechanism for the balance of governance powers between States and tribunals. Proportionality analysis thus has the potential to become a tool to enhance accountability and justification for governmental action and the activity of future arbitral tribunals as well in particular due to the new generation of investment treaties.
BIBLIOGRAPHY

Chrstonakis G., Effective adjudication v. jurisprudential absolutism at supranational level. How is criticism on developments in recent case law of the Court of Justice of the European Union pacifiable, Ceremonial address in the Danubius University in October 2013, manuscript in publication process
Craig P., EU Administrative Law, Oxford University Press 2006
v. Danwitz T., Der Grundsatz der Verhältnismäßigkeit im Gemeinschaftsrecht, Europäisches & Wirtschafts- und Steuerrecht 2003

Franck T., Proportionality in International Law, in Rights, Balancing & Proportionality, Law and Ethics oh human rights, (2010), pp. 231-242


Hesse K., Grundzüge des Verfassungsrechts der Bundesrepublik Deutschland, 20th edn, 1995


Jackson C. V., Being Proportional about Proportionality, Constitutional Commentary (2004), pp. 803

Kingsbury B. and Schill W. S., Public Law Concepts to Balance Investor’s rights with State Regulatory Actions in the Public Interest- The Concept of Proportionality in Schill W. S., International Investment Law and Comparative Public Law, Oxford University Press 2010


Kischel U., Die Kontrolle der Verhältnismäßigkeit durch den Europäischen Gerichtshof, Europarecht 2000

Klager R., Fair and Equitable Treatment in International Investment Law, Cambridge university Press 2004

Klatt M. and Meister M., Verhältnismäßigkeit als universelles Verfassungsprinzip, Der Staat 51 (2012), pp. 159


Koch O., Der Grundsatz der Verhältnismäßigkeit in der Rechtsprechung des Gerichtshofs der Europäischen Gemeinschaften, Dunker and Hublot, Berlin 2003


Kulick A., Global Public Interest in International Investment Law, Cambridge University Press 2012


Maduro P. M., We the Court: The European Court of Justice and the European Economic Constitution, Oxford: Hart 1998


Nolte G., Thin or Thick? The Principle of Proportionality and International Humanitarian Law, in Rights, Balancing & Proportionality, Law & Ethics of Human Rights (2010), pp. 244

Pirker B., Proportionality analysis and models of judicial review, Europa Law Publishing, 2013


Saurer J., Die Globalisierung des Verhältnismäßigkeitsgrundsatzes, Der Staat 51 (2012), pp. 1-33


Schill W.S., Fair and Equitable Treatment, the Rule of Law, and Comparative Public Law, in Schill W. S., International Investment Law and Comparative Public Law, Oxford University Press 2010

Shill W. S., The multilateralization of international investment law, 2009


