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**REVISITING THE NECESSITY DEFENSE:  
CONTINENTAL CASUALTY V. ARGENTINA**

**José E. Alvarez**

NYU School of Law

**Tegan Brink**

Columbia University School of Law

**Faculty Director:** Robert Howse

**Co-Directors:** Philip Alston and J.H.H. Weiler

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**Institute for International Law and Justice**

New York University School of Law  
40 Washington Square South, VH 314  
New York, NY 10012

Website: [www.iilj.org](http://www.iilj.org)

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New York University School of Law  
New York, NY 10012  
U.S.A.



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***Revisiting the Necessity Defense: Continental Casualty v. Argentina***  
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José E. Alvarez<sup>\*</sup> and Tegan Brink<sup>†</sup>

**ABSTRACT**

A series of recent ICSID decisions have dealt with claims against Argentina arising out of that country's economic crisis in 2001-2002. Several of these cases have involved U.S. investors' claims under the US-Argentina bilateral investment treaty (BIT). Divergent interpretations of the relationship between "essential security" exceptions contained in Art. XI of that treaty and the customary international law defense of necessity have attracted considerable scholarly attention and have raised broader concerns about the legitimacy of the international investment regime. A recent ICSID decision, *Continental Casualty v. Argentina*, interpreted Art. XI of the treaty in a manner notably different from preceding decisions on point. That tribunal, led by an arbitrator who had previously served on the WTO Appellate Body, was guided by the WTO's approach under GATT Art. XX. This paper considers the justification for this approach advanced by the tribunal and the legal and systemic issues it raises. It critiques this aspect of the *Continental Casualty* decision, finding its approach deeply flawed. Focusing on the textual discrepancies between the BIT and WTO rules, as well as the different object and purpose of the two regimes, the paper argues that it was an interpretative error to extrapolate from the GATT on this question. More generally, this paper finds that while the inclination towards undertaking "systemic integration" of the trade and investment regimes is understandable, there are limits on the extent that WTO jurisprudence can be legitimately brought into investment treaty arbitration, at least if both trade and investment arbitrators are seeking to adhere to the fundamental rules that truly unite these disparate legal regimes, namely the traditional interpretative rules of treaty interpretation that both sets of adjudicators are supposed to apply. While our criticisms of *Continental Casualty* do not necessarily mean that the arbitrators reached an erroneous result in that case, we believe that *how* investment arbitrators reach their conclusions is as (or even more) important to the legitimacy of their decisions (and the regime). The paper concludes with suggestions about alternative legal methodologies that the arbitrators should have considered that would have done considerable less harm to the principles of treaty interpretation.

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<sup>\*</sup> Herbert and Rose Rubin Professor of Law, New York University School of Law: [jose.alvarez@nyu.edu](mailto:jose.alvarez@nyu.edu). In the interests of full disclosure, Professor Alvarez testified as an expert witness in several of the Argentina cases discussed in this paper but was not involved in any capacity in *Continental Casualty v. Argentina*.

<sup>†</sup> LL.M, Columbia University School of Law, 2009. The author is on leave from the Australian Department of Foreign Affairs and Trade (DFAT). The views expressed in this paper are the author's own and do not necessarily reflect those of the Australian Government.

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*“The Tribunal is thus faced with the task of determining the content of the concept of necessity in Art. XI... Since the text of Art. XI derives from the parallel model clause of the U.S. FCN treaties and these treaties in turn reflect the formulation of Art. XX of GATT 1947, the Tribunal finds it more appropriate to refer to the GATT and WTO case law which has extensively dealt with the concept and requirements of necessity..., rather than to refer to the requirement of necessity under customary international law.”<sup>1</sup>*

## I. INTRODUCTION

A series of recent arbitral decisions under the auspices of the World Bank’s International Center for the Settlement of Investment Disputes (ICSID) have dealt with claims against Argentina arising out of its economic crisis in 2001-2002. In five cases under the US-Argentina bilateral investment treaty (BIT),<sup>2</sup> divergent interpretations of the relationship between Art. XI of the BIT and the customary international law (CIL) defense of necessity, including by an ICSID annulment committee, have attracted considerable academic attention<sup>3</sup> and raised

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<sup>1</sup> *Continental Casualty v. Argentine Republic*, ICSID Case no. ARB/03/9, Award (Sept. 5, 2008), para. 192, full award available at <http://www.investmenttreatynews.org/documents/p/24.aspx>.

<sup>2</sup> *CMS Transmission Co. v. Argentine Republic*, ICSID Case No. ARB/01/8, Award (May 12, 2005); *LG&E Energy Corp. v. Argentine Republic*, ICSID Case No. ARB/02/1, Decision on Liability (Oct. 3, 2006); *Enron Corp., Ponderosa Assets, L.P. v. Argentine Republic*, ICSID Case No. ARB/01/3, Award (May 22, 2007) ; *CMS Gas Transmission Company v. Argentine Republic* (ICSID Case No. ARB/01/8) (Annulment Proceeding), Decision of the Ad Hoc Committee on the Application for Annulment of the Argentine Republic (Sept. 25, 2007); *Sempra Energy Int’l v. Argentine Republic*, ICSID Case No. ARB/02/16, Award (Sept. 28, 2007); and *Continental*.

<sup>3</sup> José E Alvarez and Kathryn Khamsi, ‘The Argentine Crisis And Foreign Investors: A Glimpse Into The Heart Of The Investment Regime’, Yearbook on International Investment Law and Policy 2008/2009, 379, available at [http://www.vcc.columbia.edu/pubs/documents/Alvarez-final\\_000.pdf](http://www.vcc.columbia.edu/pubs/documents/Alvarez-final_000.pdf).

IIJ Working Paper 2008/5; William W Burke-White, ‘The Argentine Financial Crisis: State Liability under BITs and the Legitimacy of the ICSID System (2008) 3 *Asian Journal of International Health Law and Policy* 199; William W Burke-White and Andreas Von Staden, ‘Investment Protection in Extraordinary Times: The Interpretation and Application of Non-Precluded Measures Provisions in Bilateral Investment Treaties’ (2008) 48 *Virginia Journal of International Law* 307; Michael Waibel, ‘Two Worlds of Necessity in ICSID Arbitration: CMS and LG&E’ (2007) 20 *Leiden Journal of International Law* 637; Sarah Hill, ‘The ‘Necessity Defense’ and the Emerging Arbitral Conflict in its Application to the U.S-Argentina Bilateral Investment Treaty’ (2007) 13 *Law and Business Review of the Americas* 547; Stephen W. Schill, ‘International Investment Law and Host State’s Power to Handle Economic Crises – Comment on the ICSID decision in LG&E v. Argentina’ (2007) 24(3) *Journal of*

questions about the implications of these discrepancies for the legitimacy of the international investment regime.<sup>4</sup> The most recent of these decisions, *Continental Casualty v. Argentina*, has raised a more specific issue, however, that has only begun to draw scholarly attention.<sup>5</sup> In this case, the tribunal, inspired by the Annulment Committee's decision in *CMS v. Argentina*, took the controversial path of importing the WTO's approach to necessity under GATT Art. XX into its interpretation of the United States-Argentina BIT. It used WTO law in a manner that largely excused Argentina from liability. *Continental* is only one of a growing number of investor-state arbitral decisions that have turned to WTO law to interpret one of the nearly 3000 BITs or investment chapters of free trade agreement agreements now in existence.<sup>6</sup>

This paper considers the propriety of *Continental's* approach. After summarizing the decision in *Continental* in the context of other Argentina cases on point (Part II), we consider the justification advanced by the tribunal for its approach and the resulting methodological difficulties that it poses (Part III). Part IV presents alternatives more faithful to the traditional rules of treaty interpretation that possibly would have yielded comparable results to those reached in *Continental*. In Part V we identify potential lessons both about the interpretation of the necessity defense in investor-state arbitration and about the possible resort to WTO law generally within the investment regime.

## II. CONTINENTAL CASUALTY IN CONTEXT

### A. Context: The Argentina Crisis Cases

*Continental* is one of a number of recent ICSID decisions dealing with claims against Argentina arising out of its economic crisis in 2001-2002. It is one of five recent cases brought by U.S. investors under the 1991 U.S.-Argentina BIT,<sup>7</sup> the others being: *CMS*, *Sempra*, *Enron*

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*International Arbitration* 265; and David Foster, 'Necessity knows no Law! – LG&E v. Argentina' (2006) 9(6) *International Arbitration Law Review* 149.

<sup>4</sup> Alvarez and Khamsi, above n 3 at 381-86; 460-78.

<sup>5</sup> See, e.g., Sarah Vasani, 'Bowling to the Queen: Rejecting the Margin of Appreciation Doctrine in International Investment Arbitration' presentation to the Third Annual Investment Treaty Arbitration Conference: A Debate and Discussion - Interpretation In Investment Arbitration, Washington, D.C. (Apr. 30, 2009)(critiquing *Continental's* application of a margin of appreciation standard of review but not specifically addressing the merits of the tribunal's decision to apply the WTO's approach to necessity).

<sup>6</sup>

<sup>7</sup> For the text of the U.S.-Argentina BIT of 1991, see Annex A.

and *LG&E*.<sup>8</sup> The U.S. investments in question were all made during the wave of privatizations undertaken by the Argentine government in the early 1990s as part of its economic reform efforts. As is well known, by the late 1990s, Argentina's economy and its fixed exchange rate between the peso and the U.S. dollar, was under severe strain.<sup>9</sup> In December 2001, Argentina enacted a series of decrees and resolutions that sought to address the worsening economic situation which had led to social and political instability. Known collectively as 'Argentina's Capital Control Regime,' key measures included bank freezes and prohibitions on international currency transfers (the *Corralito*), an end to the convertibility regime with the U.S. dollar, 'pesification' of U.S. dollar deposits, rescheduling of term deposits (the *Corralon*), and default on debt obligations.

These measures had grave impacts on the value and legal security of investments in Argentina and gave rise to the greatest number of investor-state claims filed against a single state in history. In the cases considered here, the investors claimed multiple breaches of the BIT, including the umbrella clause,<sup>10</sup> the requirement to provide treatment in accordance with international law, including fair and equitable treatment and full protection or security,<sup>11</sup> and the requirement to pay compensation upon acts of expropriation.<sup>12</sup> In *Continental*, the claimant argued, in addition, violation of the BIT's free transfers guarantee, that is, the treaty's requirement that investors be permitted to make all transfers of capital relating to investments.<sup>13</sup> In all of these instances, the claimants sought compensation equal to the amount of the damages suffered, in ranges from \$46.4 million in the case of *Continental*, to approximately \$500 million in the case of *Enron*.

In all five cases, Argentina was unsuccessful in its jurisdictional challenges, and in the proceedings on the merits, invoked defenses based on Argentine law, the treaty, and customary international law. In particular, Argentina argued that it was excused from all liability by Art. XI of the U.S.-Argentina BIT and by the customary international law (CIL) defense of necessity. In

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<sup>8</sup> See above n 2.

<sup>9</sup> For a detailed assessment of the crisis, see IMF Independent Evaluation Office, *The IMF and Argentina 1991-2001* (Washington D.C.: IMF, 2004).

<sup>10</sup> Art. II(2)(c) BIT, Annex A.

<sup>11</sup> Art. II(2)(b) BIT, Annex A.

<sup>12</sup> Art. IV BIT, Annex A.

<sup>13</sup> Art. V. BIT, Annex A.

each case, Argentina contended that the actions that it took were “necessary” to protect its “essential security” interests and to maintain “public order.”

Art. XI of the US-Argentina BIT provides as follows: “This treaty shall not preclude the application by either Party of measures necessary for the maintenance of public order, the fulfillment of its obligations with respect to the maintenance or restoration of international peace or security, or the protection of its own essential security interests.”

The tribunals in these cases all agreed that the Art. XI non-precluded measures (NPM) clause was not, contrary to Argentina’s claim, “self-judging” or subject to an extremely deferential “good faith” standard of review.<sup>14</sup> They also all agreed that “economic” crises could, in principle, impact on the “maintenance of public order” or affect a state’s “essential security interests” and thus fall within the scope of the provision.<sup>15</sup> However, the tribunals expressed divergent views on the interpretation of Art. XI and, in particular, on the relationship between Art. XI and the CIL defense of necessity as codified in Art. 25 of the ILC *Articles on State Responsibility*.<sup>16</sup>

While the original *CMS* tribunal, and the *Sempra* and *Enron* tribunals concluded that Art. XI reflected the CIL standard of necessity and that Argentina failed to satisfy the requisites of that defense, *LG&E* appeared to treat Art. XI as a distinct defense and concluded that Argentina satisfied it such that it was excused from liability for harms caused during the period of the crisis. The *CMS* annulment committee, while it affirmed the monetary award rendered in the original

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<sup>14</sup> But *LG&E* was more ambiguous concerning the applicable standard of review. See *LG&E* at para. 214 and Alvarez and Khamisi, *supra* note , at 417-26.

<sup>15</sup> Pincites to *CMS*, *Enron*, *Sempra* and *LG&E*. In addition, all the tribunals, with the apparent exception of *Continental Casualty*, appeared to agree that Art. XI of the U.S.-Argentina BIT’s reference to “the maintenance of public order” as its text implies refers to states’ police power, that is, the power of governments to *maintain* internal public order (such as the imposition of martial law, curfews, or other measure to safeguard the security of a state’s citizens). It is not the far broader civil law concept of “*ordre public*” permitting all measures that advance the public interest since otherwise Art. XI would have been phrased differently, e.g., “necessary to protect the public welfare.” Pincites to *CMS*, *Enron*, *Sempra*, *LG&E* but see *Continental Casualty* at para. 174 and discussion *infra* at ..

<sup>16</sup> International Law Commission, *Draft Articles on the Responsibility of States for Internationally Wrongful Acts with Commentaries*, UN GA Doc A/56/10 (2001). Article 25, entitled “Necessity” provides:

1. Necessity may not be invoked by a State as a ground for precluding the wrongfulness of an act not in conformity with an international obligation of that State unless the act:
  - (a) is the only way for the State to safeguard an essential interest against a grave and imminent peril; and
  - (b) does not seriously impair an essential interest of the State or States towards which the obligation exists, or of the international community as a whole;
2. In any case, necessity may not be invoked by a State as a ground for precluding wrongfulness if:
  - (a) the international obligation in question excludes the possibility of invoking necessity; or
  - (b) the State has contributed to the situation of necessity.



*CMS* award, severely criticized the earlier tribunal’s reliance on the CIL defense of necessity, suggesting that the arbitrators should have considered Art. XI a distinct treaty defense.<sup>17</sup> As is further discussed *infra*, the *Continental* tribunal, citing the *CMS* annulment decision, treated Art. XI as a distinct defense. It found that in light of the commonalities between BITs, the preceding network of friendship, commerce and navigation treaties (FCNs), and the GATT, WTO jurisprudence relating to the GATT’s Art. XX exceptions was “more appropriate” to making the determination of necessity called for by Art. XI of the U.S.-Argentina BIT than was the customary law defense of necessity.<sup>18</sup>

These tribunals, including the *CMS* annulment committee, also diverged with respect to the implications for liability should the defense in Art. XI be found applicable. Consistent with their determinations that Art. XI and the CIL defense of necessity were functionally equivalent, the original tribunal in *CMS*, and the *Sempra* and *Enron* tribunals opined, in dicta, that while a demonstration of “necessity” precludes wrongfulness, it would not exclude any duty to compensate investors that exist under international law, including the substantive rights in a BIT.<sup>19</sup> The tribunals in *LG&E* and *Continental*, to the extent they found that Argentina had a valid defense under Art. XI, found, on the contrary, that Argentina’s financial liability was excused for any breach of BIT obligations occurring during its state of emergency.<sup>20</sup> The *CMS* annulment committee appeared to agree with this result as it opined that Art. XI, unlike the CIL defense of necessity which was only a “secondary” rule, was a “primary” rule that excludes all liability under the BIT.<sup>21</sup> Apart from *CMS*, all these cases remain subject to annulment proceedings.

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<sup>18</sup> *Continental*, para. 192. But, as noted below, *Continental* also suggested that the customary defense of necessity remained “relevant” but did not explain precisely how. *Continental*, para. 168 and see discussion *infra* at .

<sup>19</sup> *CMS*, para. 388; *Enron*, para. 260; *Sempra*, para. 303 .

<sup>20</sup> *Continental*, para. 199; *LG&E*, para. 124 .

<sup>21</sup> It set aside the finding on the umbrella clause but this did not have implications for the quantum of damages awarded. See *CMS Annulment*, para. 160.

## Continental Casualty's Treatment of the Necessity Defense

Unlike the other four cases which involved gas utilities, *Continental Casualty* concerned an insurance business. Continental was the U.S. subsidiary of CNA Financial Inc. (CNA), a leading financial services provider, headquartered in Chicago. Continental, in turn, owned and controlled CNA ART, one of Argentina's leading providers of workers' compensation insurance. Like other insurance companies, CNA ART maintained a portfolio of investments consisting mainly of low-risk assets, such as cash deposits, treasury bills and government bonds. Continental claimed that as a result of the measures introduced as part of Argentina's Capital Control Regime, it had suffered losses in value of its assets in the amount of \$46.4 million.<sup>22</sup>

In a departure from the preceding cases, the *Continental* tribunal did not begin by assessing Continental's specific claims of treaty breaches. Taking its clue from the *CMS* annulment committee's contention that Art. XI stated a "primary" rule or a "threshold requirement" that derogates from the substantial obligations undertaken by BIT in so far as the conditions for its invocation are satisfied,<sup>23</sup> it began instead with Argentina's necessity defense, noting the "pervasive nature of these general [necessity] exceptions" which "might be such to absolve Argentina...from the alleged breaches."<sup>24</sup>

*Continental* rejected the claimant's contentions that "necessary" in Art. XI should be interpreted in accordance with its "ordinary meaning," that is, that it was something that "cannot be dispensed with or done without" or, in other words, was "indispensable."<sup>25</sup> The claimants had argued for this high standard not only on the basis of the plain meaning of Art. XI but also because of the underlying CIL defense of necessity as well as the object and purpose of the treaty which, they argued, was to provide a stable framework for investment and to encourage and protect investments.<sup>26</sup> Taking their clue from dicta in the *CMS* annulment committee, the arbitrators in *Continental* rejected the suggested equivalence between Art. XI and the CIL

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<sup>22</sup> Id at para 19. These claims included complaints that Argentina had violated specific government commitments made in connection with government bonds and government loans (GGLs) held by Continental in its portfolio. Continental also complained about Argentina's decision of Dec. 9, 2004 to restructure Treasury bills (LETE) that it held.

<sup>23</sup> *CMS Annulment*, para. 129.

<sup>24</sup> Id at para. 161.

<sup>25</sup> Id at para. 190.

<sup>26</sup> Id at paras. 191-2.

defense of necessity.<sup>27</sup> They decided that the CIL defense of necessity's stricter standards, specifically its requirement that a state seeking to invoke the defense prove that the measures that it took were the "only means" to address the crisis, was inapplicable.<sup>28</sup> Confronted with the need to come up with a distinct interpretation of the requisites of the Art. XI defense, that is, a distinct interpretation of the word "necessary," they accepted Argentina's contention that the term should be interpreted in line with GATT and WTO case law, under which "necessary" was not synonymous with "indispensable."<sup>29</sup>

That tribunal's rationale for reaching to trade law consisted of a single sentence indicating merely that Art. XI derived from "the parallel model clause of the U.S. FCN treaties and these treaties in turn reflect the formulation of Art. XX of GATT 1947."<sup>30</sup> *Continental* did not explore this justification any further, but simply proceeded to set out the GATT/WTO approach and apply it to the facts at hand. Citing the test in *Korea – Beef*,<sup>31</sup> it noted that the term "necessary" referred to a range of degrees of connection, from "making a contribution to" at the one end, to "indispensable," at the other.<sup>32</sup> In order to determine whether a measure which was *not* indispensable, may nonetheless be "necessary," the tribunal identified the "weighing and balancing" exercise set out in *Korea – Beef* and followed in subsequent WTO cases, requiring consideration of the relative importance of the end pursued, the contribution of the means to that end and the restrictive impact on international trade.<sup>33</sup> The tribunal recalled that a measure would nevertheless *not* be necessary under GATT Art. XX if a "less inconsistent alternative" was reasonably available. On this latter point, it cited *US – Gambling*<sup>34</sup>:

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<sup>27</sup> Nevertheless, they were less than clear on whether they regarded Art. XI as *lex specialis*. In a loose approach reminiscent of the *LG&E* tribunal, the arbitrators in *Continental* conceded that there may be a "link" between the treaty and customary law defenses. They "focus[ed] on the analysis of Art. XI and the conditions of its application, referring to the customary rule on [the] State of Necessity only insofar as the concept there used assists in the interpretation of Art. XI itself." *Id.* at para. 168.

<sup>28</sup> *Continental*, para. 192. On the customary defense of necessity, see the ILC Articles of State Responsibility, Art. 25. *Continental* also appeared to reject the second element of that defense, namely that the state be shown not to have contributed to the state of necessity, *id.*, at 234, but did conclude that given the conflicting economic advice that Argentina received it could not be said to have been barred by its own conduct from invoking the defense. *Id.* at para. 236.

<sup>29</sup> *Continental*, para. 85.

<sup>30</sup> *Id.* at para. 192, internal references omitted.

<sup>31</sup> Appellate Body Report, *Korea – Measures Affecting Imports of Fresh, Chilled and Frozen Beef*, WT/DS161/Appellate Body/R, WT/DS169/Appellate Body/R, adopted 10 January 2001.

<sup>32</sup> *Id.* at para. 193.

<sup>33</sup> *Continental*, para. 194.

<sup>34</sup> Appellate Body Report, *United States – Measures Affecting the Cross-Border Supply of Gambling and Betting Services*, WT/DS285/Appellate Body/R, adopted 20 April 2005.

[...] an alternative measure may be found not to be “reasonable available,” however, where it is merely theoretical in nature, for instance, where the Responding Member is not capable of taking it, or where the measure imposes an undue burden on that Member, such as prohibitive costs or substantial technical difficulties. Moreover a “reasonable available” alternative measure must be a measure that would preserve for the responding Member its right to achieve its desired level of protection with respect to the objective pursued under paragraph (a) of Article XIV.<sup>35</sup>

In applying the WTO approach to the facts in *Continental*, the tribunal therefore considered whether Argentina’s measures made a “material or decisive contribution” to protect the essential security interests of Argentina. It found that they did, in particular, that they were:

...in part inevitable, or unavoidable, in part indispensable and in any case material or decisive in order to react positively to the crisis, to prevent the complete breakdown of the financial system, the implosion of the economy and the growing threat to the fabric of Argentinean society and generally to assist in overcoming the crisis. In the Tribunal’s view, there was undoubtedly “a genuine relationship of end and means in this respect.”<sup>36</sup>

In considering the question of reasonably available alternative measures, the tribunal asked itself two questions: (i) whether alternatives to the measures, not in breach of the BIT, might have been available when the measures challenged were taken that would have yielded equivalent results/relief; and (ii) whether Argentina could have adopted different policies at some earlier time, that would have avoided or prevented the situation that brought about the adoption of the challenged measures.<sup>37</sup>

In seeking to answer these questions the tribunal emphasized that its mandate was not to pass judgment on Argentina’s economic policy or its “sovereign choices.”<sup>38</sup> It noted that the claimant had put forward a number of arguments as to why the measures were not necessary,

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<sup>35</sup> *Continental*, para. 195.

<sup>36</sup> *Id.* at para. 196, internal references omitted.

<sup>37</sup> *Id.* at para. 198. The second inquiry, however, is not part of the WTO’s approach to necessity. Interestingly, the second inquiry is also not exactly the same as that demanded by the CIL defense of necessity – which requires that a state claiming necessity prove that it did not substantially contribute to the underlying state of necessity. *Continental* appears to recognize that its approach does not replicate even this aspect of the CIL defense of necessity. See *Continental*, para. 234 (rejecting this element of the CIL defense).

<sup>38</sup> *Id.* at para. 199.

either because they were counterproductive or alternatives existed to them, such as renegotiation of debts, full dollarization of the economy, and shielding dollar-denominated contracts from pesification. The tribunal was, however, not convinced. It concluded that *the claimant* had failed to demonstrate reasonable alternatives available to Argentina.<sup>39</sup> Drawing on economic studies and testimony and its own appraisal of the facts, it found that the bank freezes were necessary to prevent further capital flight that risked bankrupting the banks and exhausting the country's currency reserves;<sup>40</sup> devaluation of the peso was inevitable in view of the "economic unsustainability" of parity with the US dollar;<sup>41</sup> de-dollarization of contracts and deposits was necessary to "avoid unbearable asymmetries" in the allocation of the burden of devaluation;<sup>42</sup> and the suspension of payments and default and rescheduling of government financial instruments was necessary given the perilous state of Argentina's finances and the need to stabilize the banks and progressively reinstate the rights of depositors.<sup>43</sup>

With respect to the treasury bills, the tribunal found that Argentina could *not* avail itself of the necessity defense, however, under Art. XI *or* CIL, because "Argentina's financial conditions were evolving towards normality" at the end of 2004 when Argentina undertook to restructure those bills.<sup>44</sup> The latter finding was not made in the context of alternative actions that Argentina could have taken or a balancing of investors versus state interests but was based on the arbitrators' conclusion that the defense of necessity was no longer applicable once the crisis was over.<sup>45</sup>

With respect to the bulk of the claims, the tribunal also rejected claimant's contention that Argentina could have adopted different policies at an earlier time that would have avoided the situation that gave rise to the crisis but did so cautiously. It noted that Argentina did fail to fully carry out IMF recommendations, but that the IMF remained supportive of Argentina's efforts and had noted exogenous factors that had worsened the economic situation. The tribunal concluded that "even *ex post facto*...qualified observers remain in disagreement as to the exact

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<sup>39</sup> Id., at paras. 200-19.

<sup>40</sup> Id at para 205.

<sup>41</sup> Id at para 210.

<sup>42</sup> Id at para 213.

<sup>43</sup> Id at para 219.

<sup>44</sup> Id at para 221.

<sup>45</sup> Id.

causes of the crisis and the mix of measures that might have avoided it.”<sup>46</sup> In this context, it found that Argentina had made reasonable efforts to respect its international obligations and, “in conformity with the principle of necessity...” had struck an “appropriate balance” between that aim and the responsibility of the government towards its population.<sup>47</sup>

Finally, on the implications of a finding of necessity, the tribunal sided with the *CMS* annulment committee as well as *LG&E*. It found that to the extent Art. XI applied, Argentina would “escape any liability” since necessity would “exclude a breach of the BIT’s obligations.”<sup>48</sup> As a result, the bulk of the claimant’s claims were dismissed. The only exception was Argentina’s restructuring of the treasury bills – a measure to which the defense of necessity did not apply. The tribunal concluded that this specific measure violated the fair and equitable treatment standard of protection in Art. II(2)(b) of the BIT and as a result awarded Continental \$2.8 million in compensation.<sup>49</sup> The award fell far short of the \$46.4 million initially sought by the claimant. On March 19, 2009, an ad-hoc committee was constituted by ICSID to hear the parties’ respective applications for annulment.

Given the vociferous criticisms by some scholars and NGOs of the original *CMS* panel and the decisions in *Enron* and *Sempra*, it is likely that the completely different result in *Continental* in which Argentina achieved an even greater victory than in *LG&E*, will win considerable praise in the same circles. Thus, Alec Stone Sweet, for whom evidence of what he calls “proportionality balancing” is an important dimension of the growing “constitutionalization” and “judicialization” of international mechanisms for dispute settlement, lauds *Continental* for undertaking the “mature form of proportionality analysis” developed in the WTO for interpreting GATT Art. XX.<sup>50</sup> According to Stone Sweet, *Continental*’s analysis of Art. XI of the U.S.-Argentina BIT is a striking but welcome departure from the arid, “suicidal” formalism of the preceding Argentina decisions on point.<sup>51</sup> He sees it as a “rich piece of

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<sup>46</sup> Id at para. 224.

<sup>47</sup> Id at para. 227.

<sup>48</sup> Id at para. 199.

<sup>49</sup> *Continental*, paras. 266, 320(B).

<sup>50</sup> Alec Stone Sweet, “Investor-State Arbitration: Proportionality’s New Frontier,” available at [http://works.bepress.com/cgi/viewcontent.cgi?article=1030&context=alec\\_stone\\_sweet](http://works.bepress.com/cgi/viewcontent.cgi?article=1030&context=alec_stone_sweet).

<sup>51</sup> Id., at 24.

jurisprudence” that is “far more sophisticated” than these prior decisions<sup>52</sup> since it reflects what he calls the “best practice standard” that judges use ubiquitously to deal with certain kinds of conflict where “qualified rights” are at stake.<sup>53</sup> Stone Sweet predicts that *Continental’s* proportionality approach to the necessity defense will prevail to become a normal feature of investor-state arbitration because it offers arbitrators “the best available doctrinal framework with which to meet the present challenges to the BIT-ICSID system.”<sup>54</sup>

*Continental’s* approach is also likely to win considerable praise from those who think that the investment regime is skewed in favour of investors and is unfair to capital importing states. Burke-White and Von Staden, for example, consider that the WTO’s “least restrictive alternative” approach “offers perhaps the best middle ground for balancing the legitimate expectations of both states and investors.”<sup>55</sup> Others, such as Brigitte Stern, had suggested, even prior to the *Continental* decision, that any ambiguity in non-precluded measures clauses should be resolved “in favour of state sovereignty.”<sup>56</sup>

As we elaborate in Part III, while we believe that Stone Sweet is correct in his assessment of the likely importance of some forms of what he calls “proportionality balancing” to investor-state dispute settlement, we believe that he is wrong to praise its use as deployed in *Continental* to interpret Art. XI of the U.S.-Argentina BIT. Indeed, we contend that those who care about the legitimacy of investor-state arbitration should also care about the rationales offered for such balancing and where, how, and to what end it is applied.

### **III. A CRITIQUE OF CONTINENTAL’S APPROACH TO ART. XI**

#### **A. Why It Matters**

If the decision in *Continental* is any guide, there are substantial differences between the WTO’s approach to “necessity” for purposes of GATT Art. XX and the CIL customary defense of necessity that the original panel in *CMS, Enron* and *Sempre* applied in the context of Art. XI

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<sup>52</sup> *Id.*, at 22.

<sup>53</sup> *Id.*, at 24.

<sup>54</sup> *Id.*, at 25.

<sup>55</sup> Burke-White and Von Staden, *supra* note , at 349.

<sup>56</sup> Brigitte Stern, *The Future of International Investment Law: a balance between the protection of investors and the States’ capacity to regulate* (draft), cited in Alvarez and Khamsi, *supra* note , at 455.

of the U.S.-Argentina BIT. As is suggested by the results in the cases discussed in Part II, the decision to apply one over the other is likely to be decisive.

All agree that the CIL defense of necessity approach has been codified in Art. 25 of the ILC's *Articles on State Responsibility*. As indicated in that provision, in order to invoke necessity under CIL, a state must demonstrate first, that it is safeguarding "an essential interest against a grave and imminent peril."<sup>57</sup> The CIL defense of necessity, like the other CIL defenses with which it is historically associated (distress and *force majeure*) address particular government actions taken in rare emergencies; these are not exceptions for any and all measures taken to promote the public welfare.<sup>58</sup> Second, the state claiming necessity must show that its response to the peril that it faces is the "only way" to safeguard its essential interests.<sup>59</sup> Measures do not satisfy this criterion if alternatives exist and these must be invoked instead "even if they may be more costly or less convenient" to the state.<sup>60</sup> Third, the defense of necessity is not applicable where the international obligation in question precludes it or the state has contributed to the situation of necessity.<sup>61</sup>

Moreover, as is suggested by *LG&E* and other cases against Argentina that have considered the necessity defense, the CIL defense of necessity has strict temporal limitations: compliance with the relevant international obligations must resume as soon as the circumstances giving rise to the situation of necessity have passed.<sup>62</sup> And the customary necessity defense even when applicable provides only an excuse from wrongfulness. It is, according to the ILC's Art. 27, "without prejudice to the question of compensation."<sup>63</sup> Finally, it is widely assumed that, as with

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<sup>57</sup> Article 25 (a), supra note 16 (emphasis added).

<sup>58</sup> As is affirmed from the original *CMS*, *Enron*, *Sempra* and *LG&E* decisions, those tribunals that assumed that CIL defenses were applicable turned solely to the defense of necessity since this was the only defense potentially relevant in a situation of a political or economic crisis since the other defenses, distress and force majeure, address situations that lie beyond a state's control altogether, such as a natural disaster in the case of distress (see Article 4, *Articles on State Responsibility*) or, as with force majeure, responds to the "occurrence of an irresistible force or an unforeseen event, beyond the control of the state, making it materially impossible in the circumstances to perform the obligation" (see Article 23 *Articles on State Responsibility*).

<sup>59</sup> Article 25 (a), supra note 16.

<sup>60</sup> Commentary to Art. 25, *ILC Articles*, supra note 16, at 83.

<sup>61</sup> Article 25 (2), supra note 16. But as the ILC's Commentary suggests and as the original *CMS*, *Enron*, *Sempra*, and *LG&E* tribunals confirmed, invocation of the defense remains proper when the state has not "substantially" contributed to the underlying peril that it faces. Commentary to Art. 25, supra note 16, at 84.

<sup>62</sup> See, e.g., *LG&E* (pincite), *Continental Casualty* (pincite).

<sup>63</sup> This is consistent with dicta in the original *CMS* panel, as well as the tribunals in *Enron* and *Sempra*, as well as Art. 27, *Articles on State Responsibility*. The *CMS* Annulment Committee made a point of noting that Article 27 itself was a "without prejudice" clause, not a stipulation. It referred to "the question of compensation" without attempting to specify in which circumstances compensation could be due, notwithstanding the state of emergency. See *CMS Annulment*, para. 147. As Alvarez and Khamsi explain, while the CIL defense of necessity does not



respect to other affirmative defenses, the burden of proving customary defenses such as necessity rests on the state asserting them.<sup>64</sup> Imposing the burden on the state claiming necessity also makes practical sense, particularly in the context of disputes that pit private parties against the state since the latter is in the best position to show that the measures taken were the only way to handle the underlying threat and that it did not contribute to that crisis.

Much of this can be contrasted with the WTO approach under GATT Art. XX. As is suggested by *Continental*, the trade case law on point sees Art. XX as requiring only a demonstration of “the least restrictive and reasonably available measure that makes a material contribution to meeting the legitimate end pursued.” The extensive list of legitimate government ends in Art. XX go far beyond safeguarding an “essential interest against a grave and imminent peril” but includes any government measures deemed necessary to protect public morals, to protect human, animal or plant life or health, or to enforce laws on monopolies or the protection of patents, trade marks, and copyrights, or to prevent deceptive practices . . . .”<sup>65</sup> As interpreted by the WTO’s dispute settlers, Art. XX also accords considerably more deference to government actions not only with respect to the policy reasons for its actions but as to the standard of review once a state advances a legitimate reason. The recent decision in *Brazil – Tyres*<sup>66</sup> confirms that a measure taken under Art. XX does not have to be the “only means,” but can be part of a raft of complementary measures. Moreover, the concept of “reasonable availability” of alternatives within WTO jurisprudence allows a state’s *relative capacities* to be taken into account. At the same time, “necessary” measures under GATT Art. XX must also comply with Art. XX’s chapeau clause which serves to “distinguish..... between legitimate regulatory choices and

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exempt a state from liability where the underlying international obligation imposes such liability, it nonetheless serves many useful functions in the context of a BIT. If successfully invoked before an arbitral body established under Art. VII or VIII of the U.S.-Argentina BIT, it would, for example, preclude orders for specific performance and an order for immediate payment of compensation (as where the underlying peril that the state faces makes such payment impossible). Alvarez and Khamsi, *supra* note , at 458-60. To the extent the decision in *LG&E* suggested that its decision to excuse liability in that case would not have been different had the customary defense of necessity applied, this seems inconsistent with Art. 27 of the Articles of State Responsibility. Of course, *Continental Casualty*’s decision to permanently exempt Argentina from any liability to the extent Art. XI applied is directly contrary to Art. 27 of the Articles of State Responsibility and is one more indication that this tribunal viewed Art. XI as a wholly distinct defense.

<sup>64</sup> See CMS, Enron, *Sempra*

<sup>65</sup> Compare Art. 25 Articles of State Responsibility to Art. XX (a), (b), and (d). These are the only measures introduced by the word “necessary” in Art. XX. It is not clear from the decision in *Continental* whether that tribunal would examine the treatment of measures at (c), (e)-(j), which are introduced by different phrases such as “relating to” or “imposed for” or “essential to” as functionally equivalent to those that are “necessary.”

<sup>66</sup> Appellate Body Report, *Brazil – Measures Affecting Imports of Retreaded Tyres*, WT/DS332/Appellate Body/R, adopted 17 December 2007.

excuses for protectionism.”<sup>67</sup> If invoked successfully, Art. XX is a complete defense under the WTO dispute settlement system. If a respondent state succeeds in making out an Art. XX defense, there is no breach of the GATT. As WTO remedies are prospective, the temporal issues that arise in the CIL context – deciding whether, beyond the question of wrongfulness, compensation for prior injury remains due – are also not at play. Under the trade regime, unlike the investment regime, the sole question is whether a WTO obligation at the time a case is adjudicated is being breached (or nullified or impaired). In the trade regime, since there is no WTO remedy for harms incurred before the expiration of the reasonable period of time to implement an adverse ruling, there is no need to decide whether payment for injuries caused are merely postponed, as Alvarez and Khamsi suggest, or permanently excused, as *LG&E* and *Continental* found.<sup>68</sup>

Finally, the question of who bears the burden of proof is more complex in the trade context. While in principle, respondent states have the burden of satisfying Art. XX, as with any excuse eliciting a form of proportionality balancing, the actual burden of production of evidence in the trade regime may shift depending on the evidence advanced by either side. Thus, for example, where a respondent state advances a *prima facie* case that its measure seeks to advance a legitimate non-protectionist objective, it is expected that the claimant state would need to rebut that case. Further, the fact that the GATT, unlike investor-state arbitration, is an *interstate* dispute settlement system – where it is assumed that both governmental parties are generally familiar with legitimate policy objectives and can equally bear the burden of demonstrating these – is also likely to make decisions on ultimate burdens of proof more malleable.

The consequences of applying the WTO approach to necessity in the investment treaty context are greater than the consequences of borrowing other trade jurisprudence. Consider the meaning of non-discrimination or national treatment which has, to date, been the focus of most comparative work between the investment and trade regimes.<sup>69</sup> Whatever one’s position on

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<sup>67</sup> Benn McGrady, ‘Necessity Exceptions In WTO Law: Retreaded Tyres, Regulatory Purpose And Cumulative Regulatory Measures,’ (2008) *Journal of International Economic Law*’ 1 at 2. As discussed *infra*, *Continental* did not address this aspect of WTO law.

<sup>68</sup> Indeed, since GATT Art. XX does not address either political or economic crises at all, the issue of when such a crisis ends for purposes of determining liability does not arise.

<sup>69</sup> See, for example, Nicholas DiMascio and Joost Pauwelyn, ‘Non-discrimination In Trade And Investment Treaties: Worlds Apart Or Two Sides Of The Same Coin?’ (2008) *American Journal of International Law* 48; Jurgen Kurtz, ‘National Treatment, Foreign Investment and Regulatory Autonomy: The Search for Protectionism or something more?’ and Sylvie Tabet, ‘Application de l’obligation de traitement national et de traitement de la nation la plus favorisée dans la jurisprudence arbitrale en matière d’investissement: Nouveaux problèmes à la lumière de la

whether the national, most favored nation, and non-discrimination guarantees in BITs and in the GATT ought to bear comparable meanings, there are less grave consequences attached to making a mistake in this respect because few investment cases turn on the interpretation of these provisions alone.<sup>70</sup> Whether “like” product in the WTO context ought to bear a comparable interpretation to “in similar circumstances” for purposes of BITs goes merely to delineating the *scope* of the national treatment obligation; only in some contexts is that question likely to determine the result of a case. By contrast, the different interpretations of “necessity” at stake in *Continental* radically alter the standards as well as the scope of review in the context of a provision that, depending on whether trade or customary law is deemed the relevant comparator, is or is not exculpatory. For this reason alone, decisions to apply one standard over the other require careful consideration and justification.

#### B. Why Art. XI of the U.S.-Argentina BIT Should Be Read in Light of the CIL Defense of Necessity

In the context of *Continental*, the tribunal ended up using trade law to interpret Art. XI of the U.S.-Argentina only because it determined first, consistent with dicta contained in the *CMS* annulment committee’s decision, that Art. XI was not synonymous with the customary defense of necessity. One of us has argued extensively why this first finding was erroneous, and these arguments require but brief recitation here.

Alvarez and Khamsi have argued elsewhere that Art. XI of the U.S.-Argentina BIT, read in good faith and consistent with its plain meaning and object and purpose ought to be interpreted, consistently with the injunction to read treaties in light of all relevant rules of international law applicable in the relations between the parties, as consistent to and not a derogation from the customary defenses of force majeure, necessity, and distress.<sup>71</sup> They point out that Art. XI is, like several other provisions in the U.S. model BIT of the time, specifically intended to affirm

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jurisprudence de l’OMC’ in Thomas Walde and Philippe Kahn (eds.) *Les aspects nouveaux du droit des investissements internationaux* (Leiden; Boston: Martinus Nijhoff Publishers, 2007) 311 – 352 and 353-389; and Todd Weiler, “Prohibitions against Discrimination in NAFTA Chapter 11” in Weiler, (ed), *NAFTA Investment Law and Arbitration: Past Issues, Current Practice, Future Prospects* (NY: Transnational Publishers, Inc., 2004) 27-48.

<sup>70</sup> Instead, the absolute (that is non-relative) rights of compensation upon expropriation and the right to fair and equitable treatment have been the focus of the greatest number of investor-state claims to date, with the latter being the most successful route for claimants. This is hardly surprising given that the push towards stronger investment protections in the 1980s and 1990s were specifically directed at achieving protections beyond the “merely relative” national treatment standard. See, Andreas Lowenfield, *International Economic Law* (Oxford: Oxford University Press, 2002) 391-414.

<sup>71</sup> Alvarez and Khamsi, *supra* note , at 427-35.

existing customary rules – from the Hull rule to the international minimum standard to the requirement (in Art. X of the U.S.-Argentina BIT) that investors are entitled to the best treatment possible, including the better of national law and international law.<sup>72</sup> As was argued before the *CMS*, *Enron*, *Sempra* and *LG&E* tribunals, Art. XI was included in U.S. BITs not as a distinct carve-out but out of an “abundance of caution.”<sup>73</sup> The United States told prospective BIT parties that Art. XI was merely intended to affirm existing law and that its effects would produce results no different than under contemporaneous European BITs (which were silent on the point and therefore likely to be seen as including *sub silentio* all traditional customary defenses).<sup>74</sup>

Alvarez and Khamsi also show why the text of Art. XI, drafted in the early 1980s and long before the ILC had concluded its Articles of State Responsibility (released in 2001), was consistent with the contemporaneous understanding of the defenses of distress, force majeure and necessity. They contend that the tri-fold division in Art. XI permitting a state to take police action to maintain internal public order, defend itself from external security threats, and take multilateral action in defense of global interests corresponds to those traditional defenses as understood at that time.<sup>75</sup> They point out why it is anachronistic to expect the text of Art. XI to reflect the precise wording of Art. 25 of the Articles of State Responsibility (whose text was not finalized until later). They conclude, consistent with the rulings in the original *CMS* tribunal and *Enron* and *Sempra*, that everything that we know about Art. XI is inconsistent with an intention to make it *lex specialis* in the sense of displacing fundamental rules of international law such as the defense of necessity.<sup>76</sup>

For these reasons, we believe that the original *CMS* panel, along with *Enron* and *Sempra*, were correct in concluding that given the text, context, object and purpose of the U.S.-Argentina BIT, including its clauses granting investors all residual rights under international law, its Art. XI

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<sup>72</sup> *Id.*, at 409-12. Of course the inclusion of such customary norms in a BIT is not a superfluous act: it makes that law enforceable, along with BIT protections that exceed customary law, through investor-state arbitration.

<sup>73</sup> The United States’ cautionary stance appears to be borne out by cases such as *National Grid v. Argentina*, which seriously considered (but ultimately rejected) the contention that the United Kingdom was a persistent objector to the defense of necessity and that the failure to include that defense explicitly in the UK-Argentina BIT might have reflected the UK’s hesitation over that defense. See *National Grid*, para. 256.

<sup>74</sup>

<sup>75</sup> Alvarez and Khamsi, *supra* note , at 431-32.

<sup>76</sup> Alvarez and Khamsi, *supra* note , at 427-40. (noting, for example, that the drafters of Art. XI thought it unnecessary to spell out that “necessary” really means indispensable and assumed that a state could not expect to claim the benefit of Art. XI if it, consistent with general principles of equity or *ex injuria jus non oritur*, had contributed to the underlying crisis to which it is responding) .Cf. *Continental*, para. 234 (“Arguably, under Art. XI a Contracting Party may invoke necessity even if the need to protect its essential security interest has materialized as a consequence of a deliberate but still legitimate policy of that very State.”).

was essentially an attempt to preserve existing customary defenses and not to derogate from them.<sup>77</sup>

Alvarez and Khamsi also explain why, consistent with the understanding above, the wording of Art. XI (which addresses only whether parties can “take” measures) was intentionally drafted not to remove any financial liability even when successfully invoked – unlike other parts of the BIT which explicitly “terminate” its obligations or serve to “deny” claims.<sup>78</sup> They discuss the usefulness of such a provision (which like the underlying customary rule, only goes to wrongfulness and not financial liability) makes sense in a treaty that, depending on where it is invoked, could otherwise elicit demands for specific performance or injunctive relief.<sup>79</sup>

*Continental* addresses none of these arguments, many of which were left unaddressed by the *CMS* annulment decision, and even though most of them were suggested by the arbitrators in the original *CMS* tribunal as well as in *Enron* and *Sempra*. Instead, *Continental* explains that Art. XI is a “kind of *lex specialis*”<sup>80</sup> in essentially a single paragraph, where it concludes, in preemptory fashion, that Art. XI must mean something different from customary defenses because the BIT covers narrower obligations.<sup>81</sup> Insofar as the consequences of invoking Art. XI are concerned, *Continental* assumes, as did the *CMS* annulment committee and without any further explication, consideration of the wording of Art. XI in the context of the BIT as a whole, or dicta to the contrary by the original panel in *CMS*, and *Enron* and *Sempra*, that a party that successfully invokes Art. XI is permanently absolved of all liability. It assumes that payment for past injuries is not due even when a crisis has passed. Whether or not one is convinced by the arguments that Art. XI was intended to affirm and not to derogate from customary defenses such as necessity, it is surely the case that *Continental* fails to explain or to justify its conclusion to the contrary.

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<sup>77</sup> Pincites.

<sup>78</sup> Alvarez and Khamsi, *supra* note , at 456-57.ah

<sup>79</sup> *Id.*, at 459-60.

<sup>80</sup> *Continental*, para. 168. *Continental* does not explain what this half-way house between *lex specialis* and not means. Compare the ILC’s recent efforts in its fragmentation project to distinguish three approaches to interpreting whether a treaty provision is or is not *lex specialis* (fall-back, harmonized fall-back, and contract-out). See also *infra* at .

<sup>81</sup> *Continental*, para. 167. See also para. 192 where *Continental* tribunal mentions the contrary *Enron* holding but gives no other reasons for not following it. The argument in its para. 167 seems , on its face, absurd. The mere fact that BITs address only investors’ rights does not, in itself, explain why Art. XI is or is not *lex specialis*. As a number of international tribunals have found, fundamental rules of customary law are not displaced by a treaty – no matter what its subject matter is – unless the treaty explicitly says so. The fact that treaties usually address a narrower range of subjects than the universe covered by customary rules has nothing to do with whether fundamental rules of custom, from those addressing remedies to those covering permissible exceptions from wrongfulness, continue to apply to them. Cf. cases presuming no derogation from fundamental customary rules absent express treaty language to the contrary. See also ILC Fragmentation Project.

### C. On the Application of GATT Art. XX

*Continental's* decision to all but ignore the customary defense of necessity can be attributed to the CMS annulment decision. While we disagree with this aspect of *Continental*, we recognize that some scholars, as well as *LG&E*, have taken a different view and of the underlying ICJ decisions that support the contrary holdings on point by the original *CMS* panel, *Enron* and *Sempra*.<sup>82</sup> But the second critical decision made in *Continental* – to import GATT Art. XX jurisprudence to interpret Art. XI- was a mistake that this tribunal made all on its own. The rest of this section critiques this aspect of the decision on a number of distinct grounds.

#### 1. Failure to Explain Reasons

*Continental's* reach for trade law might have been justified by the application of Art. 31(3)(c) of the Vienna Convention on the Law of Treaties which provides that “any relevant rules of international law applicable in the relations between the parties shall also be taken into account.” But if so, it is striking that the *Continental* arbitrators spend no time in parsing the requisites of this rule. They scarcely address (except as discussed below) why trade jurisprudence on the GATT’s Art. XX, whose language is strikingly different from that in Art. XI, covers different subject matter, and has no claim to being a fundamental or customary rule (unlike the defense of necessity) is a “relevant” rule for purposes of the U.S.-Argentina BIT.

*Continental's* arbitrators had an increasingly rich jurisprudence to draw from concerning how Art. 31(3)(c) is supposed to work and may even constitute a principle of “systemic integration” capable of alleviating the risks of “fragmentation” among diverse international legal regimes.<sup>83</sup> They also had an increasingly sophisticated jurisprudence on how to determine whether a treaty provision is or is not *lex specialis*. As the ILC in its report on the fragmentation of international law recently suggested, determining whether to reach for other relevant rules of international law or whether to interpret a treaty provision as *sui generis* or *lex specialis* requires a nuanced examination of all the traditional rules of treaty interpretation.<sup>84</sup> It requires close attention to treaty text viewed in good faith and consistent with the treaty’s object and purpose and its other provisions (context). As the ILC suggests, at least three possibilities exist: (i) where

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<sup>82</sup> It has been suggested, for example, contrary to the view expressed by Alvarez and Khamsi, *supra* note at 439-40, that the ICJ interpreted the essential security exceptions in FCNs in light of the CIL defense of necessity in the *Nicaragua* and *Oil Platforms* cases only because those decisions involved use of force. Cite.

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<sup>84</sup> ILC, *Fragmentation of International Law: Difficulties arising from the Diversification and Expansion of International Law*, Report of the Study Group of the ILC, UN Doc. A/CN4/L.682 (Apr. 13, 2006);

a treaty is silent on a matter, fully applying the CIL rule (*fall-back*) is encouraged; (ii) where the treaty is not silent, but the terms used are unclear and yet have a recognized meaning in CIL, interpreting the treaty rule consistently with the CIL rule is encouraged (*harmonized fall-back*); and (iii) where the treaty is clear and leads to a different result to the CIL rule, applying the treaty rule to the exclusion of the CIL rule (*contract-out*).<sup>85</sup>

While none of the Argentina tribunals discussed here explicitly articulated the relationship of Art. XI to customary defenses using the ILC's terminology, the approach taken by the *Continental* tribunal is particularly ambiguous. On the one hand, it found that Art. XI and the CIL rule were separate defenses that dealt with different situations. This would suggest that none of the three potential sources of interaction outlined by the ILC are applicable.<sup>86</sup> On the other hand, *Continental* indicated that the outcome would be the same should Art. XI be regarded as *lex specialis*, that is, as a provision that pre-empts recourse to the CIL rule.<sup>87</sup> This invokes the third 'contract out' approach. At the same time, the tribunal suggested that the two defenses were "linked" or that the customary defense of necessity was "relevant,"<sup>88</sup> thereby suggesting that it was applying the second, 'harmonized fall-back' approach. To make matters worse, in the end, *Continental's* arbitrators did not fall-back on CIL to interpret Art. XI, but opted instead to apply a different international law defense altogether, notably, that under GATT Art. XX. They did not explain whether this decision ought to be considered as a form of harmonized fall-back or as the application of another 'rule of international law applicable in the relations between the parties to the treaty' under the VCT's Art. 31(3)(c).<sup>89</sup>

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<sup>85</sup> This approach is generally consistent with established law and relevant precedents. Cite inter alia Art. 55 and Commentaries, Articles of State Responsibility (rule on *lex specialis*).

<sup>86</sup> It is interesting to note that one factor that was very important to the tribunal's interpretation of Art. XI as a separate defense was the distinction between so-called 'primary' and 'secondary' rules. The tribunal argued that a non-precluded measures clause such as Art. XI. was fundamentally different from ILC Art. 25 because, unlike Art. 25, there was no question of a breach whose wrongfulness was precluded when its conditions were met. Unlike ILC Art. 25, Art. XI did not, in the tribunal's view, require to it to first consider whether a breach of one of the treaty's substantive guarantees had occurred (para. 168). It is curious to note, therefore, that the non-precluded measures clause in GATT Art. XX that forms the basis for the tribunal's interpretation of Art. XI, does *not* make the same distinction. In the WTO, a panel will never consider Art. XX before having found a breach of a substantive provision. The distinction between primary and second rules that seems so important to the tribunal's decision to distinguish Art. XI and Art. 25 is therefore not present in the WTO system on whose approach it relies.

<sup>87</sup> *Continental*, para. 168. Some of the same flaws appear in LG&E. See Alvarez and Khamsi, at

<sup>88</sup> *Continental*, para. 168.

<sup>89</sup> This can be contrasted with some NAFTA decisions where tribunals have, in referring to, if not actually applying WTO law, identified the relevance of WTO jurisprudence through the application of the VCT's interpretation rules. See, for example, *Marvin Feldman v. Mexico*, ICSID Case no. ARB(AF)/99/1, Award (Dec. 16, 2002), para. 165.

Even assuming, as some believe, that the customary defense of necessity was irrelevant to the interpretation of Art. XI, why, consistent with the traditional rules of treaty interpretation, would it be proper for an arbitrator to look beyond the ordinary meaning of the terms “necessary to,” “maintenance of public order” and “essential security” in Art. XI and go to the WTO jurisprudence without at least attempting to distill meaning for these terms in light of the context, object and purpose, and any supplementary means of interpretation, such as the *travaux préparatoires*, of the U.S.-Argentina BIT? Curiously, the tribunal did recognize the importance of negotiating history<sup>90</sup> but only in the context of determining whether Art XI was self-judging and whether “essential security” could incorporate economic interests.<sup>91</sup> It did not otherwise refer to the U.S.-Argentina BIT’s negotiating history as discussed by other Argentine investor-state decisions to help it determine the meaning of crucial terms, such as the meaning of “necessary.” But as the ILC has observed, the way in which ‘other law’ is ‘taken into account’ under Art. 31(3)(c) VCT is crucial to the parties and to the outcome of any single case—and, of course, to the subsequent legitimacy of any decision reached and possibly to efforts to enforce that decision.<sup>92</sup>

*Continental*’s interpretive leap, undertaken with decisive implications, was not explained, whether by reference to the text itself (for example, relevant similarities between Art. XI and GATT Art. XX) or, as is further explained below, the historical record (that is, the relationship between GATT Art. XX, FCNs, and the U.S. BIT), or the VCT’s Art. 31(3) (c ). The GATT clearly contains rules of international law that might be “applicable” between the United States and Argentina, but *Continental* does not tell us how the particular trade rule at issue is “relevant” to a dispute arising from an investment treaty that grants private investors directly enforceable rights. Here, as elsewhere, the interpretive steps set out in Arts. 31 and 32 of the VCT are entirely absent from the tribunal’s analysis.<sup>93</sup>

In *CMS*, the Annulment Committee set aside the tribunal’s decision on the umbrella clause in Art. II(2)(c) for failure to state reasons,<sup>94</sup> in part because there was “no discussion in the

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<sup>90</sup> *Continental*, para 176.

<sup>91</sup> *Id.*, at paras. 177-81.

<sup>92</sup> ILC Report on Fragmentation of International Law, above n 50 at para 480.

<sup>93</sup> The tribunal does ‘refer’ to the VCLT in finding the content of Art. XI “different” from the content of ILC Art. 25. See paras. 163-164. However, the VCLT is not applied to support its application of WTO law.

<sup>94</sup> *CMS Annulment*, para 97.



award of the *travaux* of the BIT on this point, or of the prior understandings of the proponents of the umbrella clause as to its function.”<sup>95</sup> A similar criticism seems applicable here. The failure to consider, through a faithful application of the VCT’s principles of treaty interpretation, why the WTO approach in GATT Art. XX should be applied to interpret Art. XI of the US-Argentina BIT is a major weakness of the tribunal’s methodology.

## 2. Bad History

This section looks behind the absence of reasons and critiques the principal justification given by *Continental* for applying GATT Art. XX, namely, that “Art. XI derives from the parallel model clause of the US FCN treaties and these treaties in turn reflect the formulation of Art. XX of GATT 1947.”<sup>96</sup> Not providing reasons or supporting evidence could perhaps be excused if this statement were accurate.<sup>97</sup> However, *Continental’s* view of history is terribly misleading. It is certainly true that a number of post-World War II U.S. Friendship, Commerce and Navigation (FCN) Treaties included an exceptions clause that combined *some* aspects of the current GATT Art. XX with *some* aspects of Art. XI of the U.S.-Argentina BIT. What *Continental* ignores however, are the fundamental, presumably intentional, differences between these provisions.

Annex B contains the three relevant exceptions clauses at issue: from a typical FCN, Art. XI of the U.S.-Argentina BIT, and the GATT’s Art. XX.<sup>98</sup> As comparison of the three clauses reveals, Art. XI is based on only one sub-provision within the FCN’s lengthier list of exceptions and Art. XI bears no resemblance to the GATT’s Art. XX. Further, not only is the GATT’s Art. XX’s chapeau clause (requiring consideration of whether any measures sought to be justified under the Article are arbitrary and discriminatory) missing from the BIT’s exceptions clause, but the substantive government measures embraced by these two provisions cover *entirely different subject matter*. The “essential security” exception in the GATT which more closely tracks the subject-matter of Art. XI (as well as Art. XX(d) of the typical modern FCN) is the GATT’s Art.

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<sup>95</sup>Id at para 95.

<sup>96</sup> *Continental*, para. 192.

<sup>97</sup> The grounds for annulment in Art. 52 of the ICSID Convention are permissive – the ad-hoc Committee may, but is not obliged, to set aside a decision if one of the grounds is met. See, for example, the discussion in *Compañía De Aguas Del Aconquija S.A. an Vivendi Universal v. Argentine Republic*, Case No. ARB/97/3, Decision on Annulment (Jul. 3, 2002) paras. 65, 86 and 115.

<sup>98</sup> Article XX(d) of the typical post WWII FCN reproduced in Annex A is identical to the U.S.-Iran and U.S.-Nicaragua FCNs addressed by the International Court of Justice in the Oil Platforms and Nicaragua cases.

XXI,<sup>99</sup> not its Art. XX. Note, however, that even the GATT's Art. XXI differs from Art. XI of the BIT insofar as the GATT's definition of 'essential security' is restricted to the three types of measures in (b) (i)-(iii).

As is well known and has been the subject of some attention at the International Court of Justice, the key difference between the "essential security" clauses of the typical FCN and the GATT's Art. XXI is that the latter contains the phrase "which it considers." As the International Court of Justice has opined, this suggests that within the GATT, states have the power to self-judge or auto-interpret threats to their essential security and that the invocation of Art. XXI, if it can be examined by GATT dispute settlers at all, is examined on an extremely deferential "good faith" basis.<sup>100</sup> FCNs, as the ICJ has pointed out, leave the determination of "essential security" for objective evaluation. This distinction between the self-judging GATT essential security clause and the "objective" essential security clauses of BITs and post-WWII FCNs has been affirmed by every arbitral body that has considered the question in the context of Art. XI of the

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<sup>99</sup> GATT Art. XXI provides:

*Security Exceptions*

Nothing in this Agreement shall be construed

- (a) to require any contracting party to furnish any information the disclosure of which it considers contrary to its essential security interests; or
- (b) to prevent any contracting party from taking any action which it considers necessary for the protection of its essential security interests
  - (i) relating to fissionable materials or the materials from which they are derived;
  - (ii) relating to the traffic in arms, ammunition and implements of war and to such traffic in other goods and materials as is carried on directly or indirectly for the purpose of supplying a military establishment;
  - (iii) taken in time of war or other emergency in international relations; or
- (c) to prevent any contracting party from taking any action in pursuance of its obligations under the United Nations Charter for the maintenance of international peace and security.

<sup>100</sup> Argentina has repeatedly attempted, without any success to date, to import this self-judging aspect into the interpretation of Art. XI of the U.S.-Argentina BIT. Note that this effort ignores the fact that GATT Art. XXI incorporates a self-judging exception at the same time that it restricts the definition of essential security to the three examples given in (b)(i)-(iii). This suggests that in the GATT, the decision to make this exception self-judging was taken alongside with a decision to restrict the scope of what "essential security" means. The first decision was evidently a quid pro quo for the second. See also Alvarez and Khamsi (elaborating the many reasons why clauses like Art. XI of the BIT are not self-judging). It is striking that the arbitrators in *Continental* failed to address, even in passing, relevant jurisprudence concerning the meaning of Art. XI considered by prior arbitral tribunals. Nor does *Continental* really address or attempt to distinguish relevant ICJ jurisprudence on the essential security exception in FCNs addressed by the original *CMS*, *Enron* and *Sempra* tribunals. In both the *Oil Platforms case* and *Nicaragua*, the ICJ applied the CIL standard of necessity (not GATT jurisprudence) to the interpretation of that clause and on the key issue of whether non-precluded measures clauses were self-judging, these decisions distinguished the security exception in GATT Art. XXI from FCN clauses, finding that the latter, whose wording most approximates that in U.S. BITs, not self-judging. See Alvarez and Khamsi, supra note , at . If, as the *Continental* tribunal argued, FCN treaties developed from the GATT, this is clearly one example where arbitrators and international judges have found that they explicitly derogated from it.

U.S.-Argentina BIT.<sup>101</sup> As this critical distinction between the essential security clauses of the GATT and those in the U.S.-Argentina BIT and most FCNs suggest, although FCNs did influence the drafting of both the GATT and U.S. BITs, the three texts of exceptions in these treaties differ in terms of subject matter and scope, and especially with respect to the extent of deference to be accorded governments when invoking them.

For the reasons that we explain below, Art. XI of the U.S.-Argentina BIT builds on the “objective” (non-self-judging) language of the FCNs but at the same time severely restricts the universe of possible non-precluded measures contained in either the GATT’s Art. XX or the typical FCN. Art. XI of the U.S.-Argentina BIT adds the “maintenance of public order” to the language that it lifts from Art. XX (d) of the typical FCN. As discussed earlier, the U.S. drafters of the model BIT used at this time incorporated “maintenance of public order” to avoid any doubt that U.S. BITs would interfere with states’ normal police powers. This was consistent with their intent to have Art. XI reflect the three traditional CIL defenses of distress, force majeure and necessity, which also protect the right of states to defend itself from internal civil disorders. We therefore agree with Argentina’s apparent argument in *Continental*, that the maintenance of public order would include measures that are necessary to ensure internal security.<sup>102</sup> But we strongly disagree with *Continental*’s apparent finding that the phrase seeks to embrace “the French legal concept of “*ordre public*” in public and criminal life.”<sup>103</sup> Had the U.S. drafters wished to embrace the broad governmental measures included in GATT Art. XX or Art. XXI of the FCN, they clearly knew how to do so without resort to a foreign civil law concept such as *ordre public* which does not appear in either FCNs or the GATT.

Of course, the GATT jurisprudence on the meaning of the word “necessary” that is deployed by the *Continental* tribunal has not been concerned either with “essential security” measures or those taken pursuant to a state’s police power. The WTO cases have dealt with the actual topics addressed in GATT Art. XX (a), (b), (d) and (i), namely, the protection of

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<sup>102</sup> *Continental*, para. 172.

<sup>103</sup> *Continental*, para. 174. But it is not altogether clear, despite their reference to the French concept of *ordre public*, that the arbitrators in *Continental* really adopted that civil law concept. Their discussion of public order was couched in terms that suggest what the United States would call a state’s police power and not the general right to regulate in the public interest. Thus, *Continental* stressed that the covered measures were about maintaining the “public peace” and that they justified actions necessary for a “central government to preserve or to restore civil peace and the normal life of society,” including “to prevent and repress illegal actions and disturbances that may infringe such civil peace and potentially threaten the legal order . . . .” *Continental*, para. 174.

morals,<sup>104</sup> health and environment<sup>105</sup> and the enforcement of WTO-consistent laws and regulations,<sup>106</sup> subjects that are nowhere to be found in Art. XI of the BIT.

If there are similarities between other treaties and Art. XI of the U.S.-Argentina BIT, they are between Art. XI and a single sub-part within the broader FCN exceptions clause, and not between Art. XI and GATT Art. XX. Moreover, the GATT, which is subject to a presumably self-judging essential security clause in Art. XXI, is a singularly odd place to turn for guidance on how an exception relating to essential security should be interpreted.<sup>107</sup> There is no WTO case law on Art XXI. Since the WTO's inception in 1995, Art XXI has not been raised before a panel,<sup>108</sup> and during the GATT years, only one panel was convened to consider an Art XXI defense, but under specific and limited terms of reference.<sup>109</sup>

But why did drafters of U.S. BITs (and most BITs at least prior to 2004)<sup>110</sup> not include the broad list of exceptions contained in both FCNs and the GATT? The likely answer provides more reasons to bemoan *Continental's* erroneous reading of history.

As is well known, the move from FCNs to BITs was driven by the fact that those parts of FCNs that secured non-discriminatory treatment of trade in goods were increasingly deemed unnecessary given the rise of the GATT, while the failure to conclude the broader Havana Charter (as well as the failure of other multilateral efforts dealing with investment) suggested a continuing need to protect foreign investors. In developing a treaty focused exclusively on investment protection, however, the drafters of BITs went beyond the scant coverage of that subject in FCNs. *They turned a treaty that was primarily focused on protecting treaty traders from discrimination into an instrument that emphasized the protection of tangible property rights and that provided third parties whose property rights were harmed with a direct and enforceable*

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<sup>104</sup> *US-Gambling*, above n 29.

<sup>105</sup> *Brazil – Tyres*, above n 45.

<sup>106</sup> *Korea – Beef*, above n 26.

<sup>107</sup> This is so even if one ignores that the GATT's Art. XXI is not about all measures that a state might attempt to justify as within its essential security but only those identified in Art. XXI (b) (i-iii).

<sup>108</sup> The closest the WTO has come to adjudicating Art XXI was in respect of an EC complaint regarding the *US Helms/Burton Act*. Following inconclusive consultations, a panel was established to adjudicate the EC complaint. However, the EC subsequently requested the suspension of the panel's work, in order for it to reach a mutually acceptable solution with the US (WTO Doc WT/DS38/5 of 25 April 1997). The WTO was never notified of any mutually acceptable solution. The panel lapsed and the EC never resurrected its original complaint

<sup>109</sup> *United States - Trade Measures Affecting Nicaragua*, Report by the Panel, GATT Doc. L/6053, 13 October 1986 (unadopted).

<sup>110</sup> According to one survey of existing BITs, nine of ten of the treaties examined contained no exceptions or NPM clause at all, even for "essential security." Burke-White

*remedy, that is compensation for prior injury.* In doing so, they approached the question of exceptions to the treaty differently.

With respect to exceptions from national treatment and most-favored nation treatment, the drafters of the U.S. model on which the U.S.-Argentina BIT was based did not opt for an enumeration of a laundry list of permissible non-protectionist measures identified by their rationale. They permitted BIT parties to identify specific sectoral exceptions to national treatment and MFN.<sup>111</sup> They insisted that these sectors be identified by the time a BIT was concluded in order to be sure that these were mutually acceptable to both parties.<sup>112</sup> For BIT drafters, this was an alternative solution to the goal pursued by Art. XX of the GATT, namely reducing the scope for protectionist measures.

Other substantive investor protections contained in the BIT, however, were designed not to prevent state actions driven by bad (protectionist) motives but to insure the protection of property rights. These rights were not based on the relative treatment accorded to other investors, national or foreign. These “absolute” guarantees have no analogues in the GATT and include BIT provisions ensuring fair and equitable treatment, the residual protections of the international minimum standard, compensation upon expropriation, the rights to free transfer, and full protection and security. As a number of arbitrations have now found, these rights do not require discriminatory intent to be actionable and are not excused by the absence of such intent. Indeed, most of these, which replicate or have analogues in long-standing customary protection owed to aliens (and not just investors) under the doctrine of state responsibility, do not require evidence of governmental intent at all. These guarantees, which predictably have been the subject of most of the successful investor-claims filed to date, were not regarded as appropriate subjects for the public policy exceptions identified in the GATT’s Art. XX.

Why this made sense to U.S. BIT drafters is clearest with respect to these treaties’ guarantees on direct expropriations. As is well known, the United States was keenly interested in using its BIT to defend its oft-stated Hull Rule (providing for prompt, adequate and effective compensation) precisely to contend with the wave of direct nationalizations and expropriations arising in the 1960s and 1970s. These classic expropriations – full-scale government takeovers of foreign enterprises, frequently by outright decree, like those seen in Cuba and Libya, and not

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<sup>111</sup> See U.S.-Argentina BIT, arts. II(1), Protocol, paras. 2-5., Annex A.

<sup>112</sup>

more subtle regulatory takings – was the principal target of the expropriation guarantee in the U.S.-Argentina BIT. Reflecting contemporaneous U.S. takings jurisprudence, that provision imposes a right to compensation for direct takings of property irrespective of the government’s purpose. That clause explicitly anticipates that compensation will be due *even when expropriation occurs for a public purpose and is not discriminatory*.<sup>113</sup> It anticipates, in other words, that governments expropriate for public purposes and may continue to do so but that when they do, compensation still needs to be paid. An exception from compensation for a direct taking of property because the expropriating government was pursuing one of the public purposes enumerated in the GATT’s Art. XX would not only be inconsistent with the BIT’s expropriation guarantee itself but also with the pre-existing customary Hull Rule which the United States sought to incorporate in these treaties.<sup>114</sup> Those who drafted BITs also found it hard to imagine the need for a list of exceptions for non-protectionist measures when it came to most violations of the international minimum standard, including denials of justice by local courts, or for most refusals to accord full protection and security, as for failure to provide investors with police protection during a riot. Moreover, to the extent U.S. BITs included, as does the U.S.-Argentina BIT, an umbrella clause seeking to ensure that government contracts between investors and their host states would not be breached,<sup>115</sup> the assumption was that, consistent with existing U.S. law, compensation for violating such contracts could only be avoided in accordance with contractual terms – and not because a state comes up with a legitimate non-protectionist reason consistent with the public welfare to avoid its express commitments.

Given the nature of most of the substantive rights contained in BITs, it is hardly surprising then that the United States incorporated only those exceptions deemed applicable with respect to all or most treaties, namely the customary defenses of distress, force majeure, and

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<sup>113</sup> U.S.-Argentina BIT, art. IV (1), Annex A. As is addressed in a number of arbitral decisions and by scholars, when expropriation occurs without a public purpose or in a discriminatory fashion, the resulting illegal taking arguably triggers a greater amount of damages, including, for example, lost profits. Cites.

<sup>114</sup> Thus, in the well-known exchange between Secretary of State Hull and the Mexican foreign minister the latter argued that its actions “were inspired by legitimate causes and the aspirations of social justice.” Note that Art. X of the U.S.-Argentina BIT, preserves to investors the better of any rights accorded under national law, the BIT, or other international law. While there have been long-standing disputes over whether customary law requires compensation equivalent to fair market value when the government engages in certain types of widespread expropriations and not discrete takings, as with respect to nationalizations for purposes of land reform, this is a far narrower potential exception to the expropriation provision in BITs or the Hull Rule than any suggested by Art. XX.

<sup>115</sup> U.S.-Argentina BIT, Art. 11(2) (c), Annex A.

necessity which, as suggested above, Art. XI reflects. It was also no accident that even these exceptions only sought to preserve governments' existing sovereign right to *take* action but not their duties under existing law to accord compensation when such actions were taken. This too was consistent with pre-BIT U.S. law, which generally provides that the United States can always take property (or breach its contracts) but that this right does not typically exclude compensation otherwise due.<sup>116</sup>

This helps to explain why, even today, when the United States (now as frequent NAFTA defendant) is recoiling from some of the investor-protective provisions of its old BITs and has released a model BIT that dramatically decreases the scope of investment protections as compared to the U.S.-Argentina BIT, the United States continues to resist inclusion of a broad exceptions list as in the GATT's Art. XX.<sup>117</sup> It has instead, adhered to a more limited approach whereby comparable exceptions are now included with respect to particular BIT guarantees but not as general exceptions for the entire treaty. Thus, the U.S. model of 2004 and subsequent U.S. BITs clarify the meaning of "indirect" expropriations such that, consistent with U.S. takings law on regulatory takings, "non-discriminatory regulatory actions by a Party that are designed and applied to protect legitimate public welfare objectives, such as public health, safety, and the environment, do not constitute indirect expropriations."<sup>118</sup> While some might see this as a cut-back on the original U.S. BIT, in all likelihood this reflects an attempt by the United States to clarify the meaning of a provision that, as it always explained to prospective BIT parties, meant to reflect existing property protections accorded under U.S. constitutional jurisprudence for indirect takings.<sup>119</sup> Interestingly, *Continental's* arbitrators acknowledge the differences between direct and regulatory takings of property and that, depending on the "material impact on property," public policy purposes may be irrelevant to a requirement under BITs to compensate

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<sup>116</sup> Thus, even in the context of *Dames & Moore*, in which the U.S. Supreme Court affirmed the ability of the U.S. executive branch's establishment of the U.S.-Iran Claims Tribunal as a mechanism to resolve disputes arising from a foreign policy crisis, the Court was cautious in noting that it was not resolving the question of whether those who suffered a clear taking of their property as a result of U.S. actions were owed compensation under the takings clause of the U.S. Constitution. Cite. This is not to suggest, however, that the U.S. BIT provisions on expropriation are otherwise identical to those under U.S. takings jurisprudence. Cf. Vicki Been (suggesting possible ways that BIT expropriation provisions might grant broader protections to foreign investors).

<sup>117</sup> For debates on this see State Department Advisory Committee Report.

<sup>118</sup> U.S. Model BIT 2004, Annex B, para. 4(b), available at <http://www.state.gov/documents/organization/117601.pdf>.

<sup>119</sup> See, e.g., *Penn-Central v. City of New York*, 438 U.S. 104, at 123-26 (1978).

for some expropriations.<sup>120</sup> They do not appear to realize, however, how this undermines their conclusion that the exceptions of Art. XI need to be interpreted consistently with the public policy exceptions of GATT Art. XX and operate as a primary rule to the exclusion of the substantive guarantees of the BIT.

Another example from the 2004 U.S. model BIT deals with certain performance requirements. Under the increasingly detailed provision on point, the 2004 U.S. model (at Art. 8(3)(c)), mirrors the subject matter contained in GATT Art. XX (b), (d) and (g) – measures taken in defense of health, the environment, and to secure compliance with treaty-consistent laws and regulations. Art. 8(3)(c) is not, however, a ‘general exception’ to all obligations under the treaty (cf. GATT Art. XX), but rather applies so as not to preclude only certain *performance requirements*. Notably, even this provision is not identical to the GATT’s Art. XX and the underlying GATT jurisprudence needs to be considered with caution when interpreting this clause. The preambular language in the BIT that borrows from the GATT Art. XX chapeau does not prevent discrimination “between countries where the same conditions prevail.” This phrase is omitted in the 2004 U.S. BIT. While this is in part a function of the provision applying to investors and investments, it could presumably allow distinctions to be drawn between such investors and investments so long as that distinction was not *otherwise* unjustifiable. What this means is that WTO case law may be able to provide useful guidance on how the substantive subject matter of the exceptions, such as “exhaustible natural resources” should be defined (a matter on which consistency across international agreements is important), as well on the *standard* of review with respect to necessity in the context of a provision that contains a similar, albeit not identical, controlling ‘chapeau.’ However, the application of this exception in a specific case cannot be divorced from the obligations to which it is an exception and in this respect, WTO case law may be of limited assistance.

For example, Article 8(3)(c) of the U.S. Model BIT provides that the obligation not to “impose or enforce any requirement...to transfer a particular technology, a production process, or other proprietary knowledge” shall not be construed to prevent a Party from adopting measures necessary to protect, for example, human health. This obligation with respect to “technology transfer” has no analogue in the GATT and whether, for example, a measure is necessary to protect public health in this context, is a fact-specific inquiry that existing WTO

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<sup>120</sup> Continental, para. 276.



case law would not be well placed to answer. Of course neither the clarifications for indirect expropriations nor the language on performance requirements discussed above appears in the U.S.-Argentina BIT.

Note that we are *not* suggesting that it would be inappropriate to include an exceptions clause like the GATT's Art. XX in a BIT. If BIT parties want to delimit investor protections, including those under customary law, in this fashion they can surely do so. The Canadian government, for example, has included an exceptions clause in its latest model BIT that bears a greater resemblance to GATT Art. XX than does Art. XI of the U.S.-Argentina BIT.<sup>121</sup> That clause, article 10, permits governments to take measures to protect human, animal or plant life or health, to ensure compliance with laws that are not inconsistent with the BIT, and to conserve living or non-living exhaustible natural resources, provided that these are not taken in an arbitrary or discriminatory manner or as a disguised restriction on international trade or investment. Article 10's chapeau clause is obviously similar to that of GATT Art. XX but note that it covers a smaller category of type of government action and the rest of Art. 10 contains general exceptions that do not replicate those in GATT Art. 10, including strikingly broad exceptions for "reasonable measures for prudential reasons" to protect the state's financial system that are not conditioned on that article's chapeau clause. The new Canadian BIT also includes an essential security clause, Art. 10(4), that replicates the GATT's "self-judging" essential security clause in Art. XXI.

Given the latest financial crisis and government actions in their wake, Canada's new exceptions, including its carve out for measures to protect its financial system, may well be a prudent cut-back on traditional investor guarantees. At the same time, the new Canadian BIT explicitly requires that some of these general exceptions need to satisfy a hurdle that is comparable to that in the chapeau clause of GATT Art. XX. What this tells us is that even the new Canadian model would not go as far as *Continental* did in removing any consideration of whether governmental measures are not only "necessary" to promote a legitimate government purpose but also not discriminatory.<sup>122</sup> Of course, it remains unclear whether WTO jurisprudence relating to Art. XX is fully importable into the new Canadian model BIT given the textual differences between Art. 10 of the Canadian BIT and GATT Art. XX as well as the

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<sup>121</sup> For the text, see Annex C.

<sup>122</sup> For further discussion of the significance of the chapeaux clause in GATT Art. XX, see part III(C)(3) *infra*.

differences in structures between the BIT and WTO regimes that we discuss in Part III (C)(5) *infra*.

Nor are we suggesting that the U.S. BIT's conscious omission of an exceptions à la GATT Art. XX derogates from governments' rights to regulate in the public interest. As discussed in Part IV, the drafters of the U.S. BIT sought only to limit government actions to the extent provided in the substantive guarantees provided to investors and it is within those substantive guarantees that the residual "right to regulate" properly resides.

### 3. Failure to Consider the Text of Art. XX

For a decision that purports to apply GATT Art. XX jurisprudence, *Continental* is oddly reticent about considering the provisions of Art. XX itself. *Continental* goes directly to cases interpreting the word "necessity" in Art. XX without considering the rest of the text of Art. XX and how that affects what "necessity" means in Art. XX (a), (b) and (d). Specifically the tribunal ignores Art. XX's chapeau clause, what that chapeau does with respect to what is deemed "necessary" for purposes of (a), (b), and (d), and what the absence of an equivalent chapeau in Art. XI of the BIT might mean.

Compliance with GATT Art. XX is a two-tier process. The party invoking the exception must first establish the substantive consistency of its measure with one of the sub-paragraphs. In this regard, the measure must fall within the scope of policies mentioned in the sub-paragraph and it must be shown necessary to achieve the specific policy objective. Second, the measure must be applied consistently with the chapeau, that is, it must not be arbitrary or constitute unjustifiable discrimination. More specifically, the measure cannot constitute "arbitrary or unjustifiable discrimination between countries where the same conditions prevail" or represent a "disguised restriction on trade." The purpose of the chapeau is to prevent the abuse of the exceptions that would undermine the trade-liberalizing objectives of the GATT. This has clear implications for how arbitrators interpret the legitimate government measures identified in (a) through (j) of GATT Art. XX.

It seems apparent that the chapeau of Art. XX has dramatically affected the degree of deference WTO dispute settlement accord to GATT Contracting Parties under that clause and

what those dispute settlers consider to be “necessary.”<sup>123</sup> Article XX of the GATT is grounded in a balancing test, built into its chapeau, that is absent from the text of U.S.-Argentina BIT’s Article XI.<sup>124</sup> There is more leeway within the necessity analysis in the GATT because states’ measures under XX (a)-(j) are, in any case, assessed against the chapeau of Art. XX which prevents regulatory interventions which are protectionist (and thus contrary to the object and purpose of the treaty). Art. XI, by contrast, as interpreted by *Continental* as a primary rule that excludes any consideration of the rest of the substantive guarantees of the BIT, provides no opportunity for applying that treaty’s guarantees barring, for example, arbitrary or discriminatory measures.<sup>125</sup> Applying the deferential necessity analysis of GATT Art. XX without considering the other filters for impermissible government action contained in Art. XX suggests that what *Continental* applied as “WTO law” does not even accurately reflect trade law much less investment law.

Consider the implications of what we have noted thus far. Had *Continental* considered carefully the texts of the treaties that it was comparing – of the exceptions contained in FCNs, the GATT covered agreements, and the U.S.-Argentina BIT – it would have noted considerable differences between them, including with respect to the deference each anticipates would be accorded to governmental actions. GATT Art. XXI, dealing with *certain* (but not all) essential security measures, accords the greatest measure of deference; indeed, its presumptively self-judging (“which it considers”) language scarcely anticipates any room for independent assessment by a third party adjudicator, let alone “balancing.” GATT Art. XX appears to anticipate differential levels of scrutiny, dependent on which provision a government cites in justification (compare “relating to” in XX (e) to “necessary to” in XX (a), (b) and (d)). But, all measures identified in Art. XX, even those subject to a “least reasonable alternative” test, are, in addition, subject to a separate evaluation to consider whether the measure in question is arbitrary, discriminatory, or otherwise protectionist.

The FCNs’ Art. XXI encompasses all the exceptions listed in GATT Art. XX (see FCN, Art. XXI(3)) and those in GATT Art. XX (see FCN, Art. XXI(1)(a-c)). But FCNs impose a

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<sup>123</sup> Or for that matter “relating to” for purposes of Art. XX (g). And while we have yet to have WTO decisions, we surmise that the same would hold true for the meaning of “imposed for” for purposes of Art XX (f); “undertaken in pursuance of” for purposes of Art. XX (h); or “essential to” for purposes of Art. XX (j).

<sup>124</sup> Id at 55.

<sup>125</sup> See U.S.-Argentina BIT, art. II(2)(b), Annex A.

necessity test only with respect to obligations for international peace and security and essential security (FCN, Art. XXI (d)). The FCN's Art. XXI otherwise says nothing about the level of deference owed to governments with respect to its listed measures. As we will address next, the considerable overlap between the GATT's and the FCNs' exceptions clauses make sense since the two treaty regimes principally address the same subject: trade in goods.

Art. XI of the U.S.-Argentina adopts none of these texts, although its language most approximates Art. XXI(d) of the FCN and *not* either of the GATT clauses. In our view, that provision has little if anything to do with a state's general right to regulate in the public interest and everything to do with preserving states' narrow customary law defenses.

#### 4. Failure to Consider the Differing Purposes of BITs and the GATT

The chapeau of Art. XX suggests a larger problem with importing Art. XX jurisprudence into investor-state disputes. The purpose of the GATT, as reflected in its preamble and in the chapeau of Art. XX, is “the substantial reduction of tariffs and other barriers to trade and the elimination of discriminatory treatment in international commerce.”<sup>126</sup> It has the twin objectives of trade liberalization (positive) and the prevention of protectionism (negative). But the purpose of the trade regime is not to provide a remedy to individuals whose property rights have been harmed, to calculate the monetary recompense due for such past harms, or to discipline the behavior of states during periods of alleged economic crisis – to cite but three of the purposes that arbitrators and scholars have attributed to the U.S.-Argentina BIT and other U.S. BITs of this period.<sup>127</sup> *Continental* fails to consider that the word “necessary” in Art. XI needs to be read in light of a particular treaty whose object and purpose may have been precisely to provide assurances to investors that their investments will be safe, *particularly* in the case of a volatile or unstable economy when investor rights are most vulnerable; that is, in situations comparable to those that faced Mexico when the United States asserted the Hull Rule.<sup>128</sup> *Continental* never asks whether Art. XI was intended to be an all-encompassing excuse from compensation, no matter what the nature of the governmental action is, so long as it is undertaken during a period of an economic crisis. It never considers whether such a blanket excuse was intended in the context of a country that had repeatedly resorted to such crises to escape its obligations to foreign

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<sup>128</sup> As was suggested by the panels in *CMS*, *Enron* and *Sempra*.

investors and had indicated that it was entering into the BIT with the United States (and others) precisely to provide a credible commitment that it would no longer do so in the future.<sup>129</sup> It also failed to consider how such a blanket excuse from liability in cases of crisis are compatible with a treaty that explicitly anticipates continuing obligations by a state to an investor not to discriminate even in the wake of crisis, namely “armed conflict, revolution, state of national emergency, insurrection, civil disturbance or other similar events.”<sup>130</sup>

In *Continental*, the tribunal cited the WTO Appellate Body’s decision in *US – Gambling* to explain its reliance on the notion of “reasonable availability.” That case defined “a ‘reasonably available’ alternative measure” as one “that would preserve for the responding Member its right to achieve *its desired level of protection with respect to the objective pursued* under the paragraph...” This makes sense in the WTO context because the GATT is a negative integration agreement. In the areas covered by GATT Art. XX (or its equivalent in GATS Art. XIV), it does not seek to harmonize Members’ laws and does not put into question regulatory diversity. Instead, the GATT disciplines trade instruments (tariffs, quotas), but, as a general rule, limits its behind-the-border interventions to domestic policies that are protectionist.<sup>131</sup> BITs, at least those following the U.S. model used for the U.S.-Argentina BIT, reach much deeper into the state parties’ regulatory pockets, to prevent, for example, not only direct takings but direct breaches of government contracts (or at least those prompted by sovereign, non-commercial actions) and, as noted above, even certain discriminatory actions taken in the course of armed conflict.<sup>132</sup> Rather than focusing on protectionist intent and discrimination to the exclusion of all else, these treaties speak to protecting investors’ sunk costs and their individual property rights.

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<sup>129</sup> Cf. *CMS*, at ; *Enron*, at ; and *Sempra*, at . See also Alvarez and Khamsi, supra note , at 414-15 (arguing that the U.S.-Argentina BIT, given Argentina’s century-long penchant for proclaiming emergencies, was intended to forestall exactly the broad brush defense of necessity raised by Argentina in these cases).

<sup>130</sup> Art. IV (1), Annex A. Under *Continental*’s interpretation of Art. XI as “primary” rule this obligation, along with all others in the BIT, would be inapplicable precisely due to events anticipated by the very obligation itself.

<sup>131</sup> The WTO’s new generation agreements, in particular, the TBT and SPS Agreement do venture behind the border in requiring that any such measures not only be non-discriminatory, and in the case of SPS, based on science, but also be ‘necessary.’ The discipline is closely tied up with the issue of international standards (these should be followed and where they are, measures based on them are presumed to be necessary) but to date, there is little jurisprudence on the “necessity” of measures in the absence of such international standards that may provide a broader body of ‘necessity’ case law in the WTO from which to draw in considering any relevance to investment treaty arbitration.

<sup>132</sup> See U.S.-Argentina BIT, articles II(2)(c), IV(1-2), and IV (3). For purposes of this paper, we need not address controversies over the scope of these treaties’ umbrella clauses, such as Art. II(2)(c) in the U.S.-Argentina BIT. At the very least most agree that these clauses protect the rights of investors to be compensated for breaches of contracts that they enter into directly with governments where the breach occurs through the exercise of the government’s sovereign actions. Cites.

## 5. Failure to Consider the Structural Differences between Investor-State and WTO Dispute Settlement

Anyone seeking to import WTO jurisprudence should also consider other structural differences between that regime's dispute settlement scheme and investor-state arbitration. The U.S.-Argentina BIT, like most U.S. BITs of the same period, focus on the rights of third parties who invest in host states in reliance on these treaties. Accordingly, the chief remedies they authorize are the prospect of damages to third parties for past harms incurred because of government action. BITs also authorize those third parties to bring such claims for damages themselves, thereby displacing the usual espousal practice dependent on intervention by the home investor's home country. As is often noted, BITs turn their third party beneficiaries, namely foreign investors, into a species of "private attorneys general" charged with treaty enforcement.<sup>133</sup> This has normative consequences. Since investors activate the BIT claims process, choose what claims to bring and what arguments to present, they can effectively control the arbitral agenda and effectively develop international investment law.

The trade regime, by contrast, is far more state-centric and it is structured to secure prospective relief of a particular kind. It tries to get a state to remove an offending measure and, on rare occasions, authorizes trade retaliation, a form of counter-measure, to secure that end. It is also, of course, an *interstate* dispute settlement system comparable to old-fashioned diplomatic espousal in one critical sense: it anticipates that states will weigh the costs and benefits of bringing WTO claims against each other and anticipates that some states may decide not to do so because of fears of reciprocal claims or of establishing troubling legal precedents. (Indeed, this may help to explain the absence of WTO claims based on assertions of "essential security.") It is also striking that although *Continental* relied on the *CMS* annulment decision's distinction between primary and secondary rules, no such distinction appears in GATT jurisprudence and indeed, the concept seems alien to its remedial scheme.<sup>134</sup>

Given these structural differences and others besides – such as the absence of an appellate body in the investor-state regime, probable differences in the expertise of the adjudicators

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<sup>133</sup> Indeed, some have suggested that BITs thereby "privatize" what, in the age of espousal, was a governmental function.

<sup>134</sup> See note *supra*.

involved,<sup>135</sup> the lack of a legal secretariat to provide continuity in caselaw in the investor-state context -- it is not clear why treaty exceptions to very different types of obligations, undertaken for very different reasons, and subject to very different remedies should be viewed as comparable. One could imagine many reasons why, given the WTO's interstate structure and limited remedies, WTO dispute settlers might opt for a deferential view of what constitutes a legitimate government measure.<sup>136</sup> One could also imagine many reasons why, by contrast, investor-state arbitrators, charged with interpreting treaties that are often more intent on protecting the rights of their third party beneficiaries, might not be quite as deferential. There are also clear reasons why the latter regime would be more insistent that the government entity (which is better able to articulate the alternatives that it considered (and rejected) in responding to a crisis) and not a private party, should bear the burden of proof.<sup>137</sup>

The differing possibilities for exit and voice between the two remedial schemes ought also to be weighed. As is well known, the multilateral nature and institutionalization of the WTO, not to mention its tradition of consensus decision-making, makes exit (including waivers from or amendments to the underlying arrangements) difficult. In addition, while WTO Members in effect choose to submit to trade retaliation by refusing to remove their offending measure, those trade measures are imposed by another state and their imposition are therefore outside the losing state's control. Further, within the WTO there are other pressures to ensure the losing state's ultimate compliance. In the context of a single institution consisting of the same repeat

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<sup>135</sup> Although the President of the *Continental* tribunal, Giorgio Sacerdoti, was a member of the WTO Appellate Body from 2001-2009, it is rare for such trade experts to be appointed to investor-state tribunals. Investor-state arbitrators are more frequently drawn from those with experience in commercial arbitration or public international law but not necessarily trade law.

<sup>136</sup> The same might be said with respect to *Continental's* references to the European Court of Human Rights's "margin of appreciation" doctrine. See *Continental*, para. 181 and notes 266 and 270. Consideration of the "margin of appreciation" doctrine lies outside the scope of this paper. But see Alvarez and Khamsi, *supra* note , at 441-448 (suggesting the many attributes of that doctrine that appear inapplicable in the investor-state context). It is worth noting that *Continental's* suggestion, at para. 181, note 266, that Art. XI's reference to a party's "own" security interests licenses resort to a deferential margin of appreciation on behalf of the state suggests a misreading of that provision. That phrase was intended to distinguish two of the situations covered by Art. XI, namely a party's ability to respond to external threats that it faces as well as its ability to respond to the needs of others, including the international community of states. In so doing, the United States was presumably responding to the fact that inclusion of both within the traditional defense of necessity was still a point of contention during this period as the ILC's sought to finalize what became Art. 25 of its rules of state responsibility. See Alvarez and Khamsi, *supra* note , at 430-31.

<sup>137</sup> Investor-state arbitrators might also be concerned about the equitable impact of imposing the burden of proof with respect to such issues on any party other than a state, particularly given the impact of such a decision on small investors.

(state) players, GATT contracting parties ignore a binding GATT panel or WTO Appellate Body decision at their (reputational) peril.

The investment regime provides greater potential for exit and voice. This is suggested by the recent actions of Bolivia, Ecuador, and Venezuela, all of which have attempted to terminate some of their BITs, to exit from ICSID, or to modify their agreements to arbitration.<sup>138</sup> Other states, such as the parties to the NAFTA, and parties to post-2004 U.S. BITs, now have an option within their agreements enabling them to issue joint interstate interpretations of what their investment agreements mean from time to time; these interpretations are binding on investor-state arbitrators. Indeed, at least in the NAFTA, such interpretations appear to be valid even in the midst (or in response to) pending investor-state claims.<sup>139</sup> As is already clear in the NAFTA, through such interpretations the state parties can react to adverse arbitral rulings and “correct” those with which they disagree.<sup>140</sup> It is worth noting that all or most BITs, including the U.S.-Argentina BIT, include another option for mutually agreed interstate “clarifications” of their terms, namely an interstate dispute clause like that in Art. VIII of the U.S.-Argentina BIT. This is another way that the contracting state parties to a BIT can initiate and generate binding interpretations of their agreement, thereby removing some interpretative questions from the domain of investor-state arbitration.<sup>141</sup>

Exit and voice in the investment regime also exists given the weaknesses of its scheme for enforcing any subsequent investor-state arbitral awards. As is becoming starkly apparent from Argentina’s successful resistance to date with respect to the execution of the various awards rendered against it, the investment regime has not managed to overcome the powerful impediment of sovereign immunity from the execution of judgments. By contrast with the WTO regime where the prospect of trade retaliation cannot be blocked by any assertion of state immunity, states such as Argentina have it within their power to assert their “civil disobedience” vis-à-vis the investment regime. Of course, Argentina could also choose to modify its existing BITs and, subject to its leverage vis-à-vis distinct BIT parties, may well be able secure new

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<sup>138</sup> But see (citations to potential limitations on all of these efforts).

<sup>139</sup> See, e.g., *Pope and Talbot v. Canada*

<sup>140</sup> Although in theory these are meant to be restricted to mere “interpretations” of a treaty and are not to be used in lieu of the far more arduous process involved in amending such treaties, it is not likely that arbitrators would defy such an interpretation on that basis. Compare, *Pope and Talbot*; Brower, et al.

<sup>141</sup> But note that arbitrators considering interstate interpretative BIT disputes might find it difficult to justify interpretations that disturb previously acquired rights owed to existing investors. Cf. Art. XIV of the U.S.-Argentina Bit (anticipating a 10 year period of protection for existing investors even if the BIT is terminated).



treaties on better terms. Even BITs that prohibit termination for a set period of years can be modified if both parties agree and indeed, the U.S-Argentina BIT itself can be terminated, even without the United States' agreement, in 2011.<sup>142</sup> The greater possibilities for exit from particular BITs or even the investment regime as a whole needs to be considered when deciding how flexibly these treaties ought to be interpreted – and may suggest caution about drawing facile conclusions from regimes where the possibility of exit/voice is far more constrained.

The legitimacy of cross-regime borrowing may turn on whether arbitrators factor these structural concerns into their articulated reasons to borrow. Investor-state arbitrators who are, as in *Continental*, drawn to doctrines or principles deployed by other international tribunals, from trade law jurisprudence to the “margin of appreciation” used by the European Court of Human Rights, need to consider the ways the structures of such institutions have influenced the principles that they adopt as well as their application. They should also consider how permanency itself may affect what adjudicators do. It is risky to draw interpretative approaches from permanent adjudicators – whether the WTO Appellate Body or the European Court of Justice – without considering the institutional factors that may make it more appropriate or politically legitimate for such bodies to engage in expansive, “constitutional,” or teleological treaty interpretations than would be less wise for arbitrators who serve, perhaps only once in their lifetime, in a single ad hoc investor-state arbitration.<sup>143</sup>

Analogies to the use of foreign law by national courts seem appropriate here. National judges who seek inspiration from foreign law expose themselves to charges of lack of principle or incompetence should they fail to consider, for example, the structural differences between civil and common law trials when extrapolating applicable rules of evidence from one system to the other. Why should it be any more acceptable to ignore the very real (and sharper) distinctions among our international dispute settlers?

We will address in the next part whether our conclusions on *Continental* render BITs unfair vis-à-vis states or instruments whose application in strict accordance with their terms and intents is “suicidal” as Stone Sweet suggests. For now, our point is simply that while all or most

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<sup>142</sup> See Art. XIV, Annex A (but also indicating that existing investors may secure continued protection for an additional ten year period). These clauses further confirm the significance of sunk costs and detrimental reliance to BIT drafters.

<sup>143</sup> Indeed those who propose establishing an international investment court, such as Gus Van Harten, operate on the assumption that such a permanent body, because of its permanency, is likely to make more cohesive, harmonious and sometimes expansive, international investment law. See, e.g., Gus Van Harten, *Investment Treaty Arbitration and Public Law* (pincite) (2007).

treaties result in the delegation of some state power, the powers that they delegate, particularly to dispute settlers, are not necessarily the same.

#### IV. WAS ANY OF THIS NECESSARY?

Questioning the appropriateness of applying the WTO's approach to necessity under GATT Art. XX is *not* to suggest there is no place for the weighing and balancing of private rights and public interests under BITs. The issue is where as well as how this balancing should occur.

The arguments presented by the parties in *Continental* suggests an alternative way that proportionality balancing may come into play. As the tribunal points out, Argentina contended that Article II(2)(a) of that treaty, including the protection from fair and equitable treatment, needs to be applied in light of the “dramatic economic situation” that Argentina was facing.<sup>144</sup> Argentina argued that its emergency measures were consistent with the “legitimate expectations” that investors might be deemed to have had,<sup>145</sup> while the claimant argued that it had a legitimate expectation that the convertibility regime would not be changed, free transfers would be maintained, and that the terms of existing dollar-denominated securities and deposits would be respected.<sup>146</sup> The tribunal suggested some sympathy with Argentina's position. It noted, for example, that the obligation to treat an investor fairly, “even when applicable “at all times” . . . varies in part depending on the circumstances in which the standard is invoked: the concept of fairness being inherently related to keeping justice in variable factual contexts.”<sup>147</sup> It also suggested that investors' legitimate expectations turn in part on the specificity of the government assurances on which they were relying and that in this instance, unlike many other cases against Argentina, the type of assurances on which the claimant was relying were mostly general legislative pronouncements of a “legislative” type and not the kind of specific contractual assurances that had led to breaches of both the fair and equitable treatment and umbrella clauses in prior Argentina cases.<sup>148</sup> These considerations appear to ground *Continental's* finding that the claimant could not invoke legitimate expectations as to the change of the convertibility regime in 1991 and its conclusion that the claimant should have “maintained a reduced trust in the

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<sup>144</sup> *Continental*, para. 248.

<sup>145</sup> *Continental*, para. 248.

<sup>146</sup> *Continental*, para. 251.

<sup>147</sup> *Continental*, para. 255.

<sup>148</sup> *Continental*, paras. 257-261.

Intangibility Law of September 2001, since this was enacted when the worsening of the crisis was evident . . . .”<sup>149</sup>

But the *Continental* tribunal short-circuits its analysis of how the BIT’s fair and equitable treatment guarantee comports with the more specific contractual obligations allegedly offered to the claimants. It relies on Argentina’s necessity defense to avoid considering the investors’ claims arising from the specific modalities of de-dollarization, the restructuring of the GGLs, or the pesification of the LETEs.<sup>150</sup> Thanks to the necessity defense, the arbitrators also avoid considering claimants’ allegations that some of Argentina’s measures constitute an expropriation under Art. IV of the BIT<sup>151</sup> or breaches of the BIT’s umbrella clause.<sup>152</sup>

It is outside the scope of this paper to consider the substantive merits of all of these claims.<sup>153</sup> Nonetheless, it is instructive to consider another tribunal’s effort to consider the effects of Argentina’s crisis in a context where the BIT at issue, the UK-Argentina BIT, did not contain a clause comparable to Art. XI and the customary defense of necessity was therefore applicable. In that case, *National Grid v. Argentina*, the tribunal rejected Argentina’s defense of necessity but nonetheless deemed the economic crisis relevant to its interpretation of fair and equitable guarantee in that treaty.<sup>154</sup> That tribunal stressed that the legitimate expectations protected by the FET clause “must have been reasonable and legitimate in the context in which the investment was made.”<sup>155</sup> It cited a prior investor-state decision, *Saluka*, for the proposition that: “No investor may reasonably expect that the circumstances prevailing at the time the investment is made remain totally unchanged. In order to determine whether frustration of the foreign investor’s expectations was justified and reasonable, the host State’s legitimate right subsequently to regulate domestic matters in the public interest must be taken into consideration as well.”<sup>156</sup> While *National Grid* determined that Argentina had indeed breached the FET standard, it qualified its determination of when breach occurred because it found that “[w]hat would be unfair and inequitable in normal circumstances may not be so in a situation of an

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<sup>149</sup> *Continental*, para. 262.

<sup>150</sup> *Continental*, para. 262-63; para. 265,

<sup>151</sup> *Continental*, para. 275 and para. 283.

<sup>152</sup> *Continental*, para. 302.

<sup>153</sup> Indeed this effort is made more difficult precisely because the tribunal short-circuited the elaboration of these claims.

<sup>154</sup> *National Grid P.L.C. v. Argentine Republic*, UNCITRAL Award, Nov. 3, 2008. The FET provision in the UK-Argentina BIT was comparable to the one in the U.S.-Argentina BIT.

<sup>155</sup> *National Grid*, supra note , para. 175.

<sup>156</sup> *Continental*, para. 175 (citing *Saluka v. Czech Republic*, para. 305).

economic and social crisis. The investor may not be totally insulated from situations such as the ones the Argentina Republic underwent in December 2001 and the months that followed. For these reasons, the Tribunal concludes that the breach of the fair and equitable treatment standard did not occur at the time the measures were taken on January 6, 2002 but on June 25, 2002 when the Respondent required that companies such as Claimant renounce to [sic] the legal remedies they may have recourse as a condition to re-negotiate the Concession.”<sup>157</sup>

While the rationale in *National Grid* is not a model of clarity, that tribunal appeared to have determined that Argentina’s actions on Jan. 6, 2002, namely its termination of the right to calculate public utility tariffs in dollars and the right to adjust those tariffs on the basis of international prices, was not, given the circumstances, unfair and inequitable, but that its later decision to renounce the specific legal remedies that it had offered the claimant was unlawful. While *National Grid* did not explicitly adopt what Stone Sweet calls “proportionality balancing,” it seems to have balanced implicitly the investors’ expectations against Argentina’s need to take actions in the public interest at a time of crisis. They determined that Argentina’s actions breached the FET standard only when its most extreme actions, blatantly in violation of specific assurances that it had made to the investor, were so disproportionate that they could not be said to have been within the investor’s reasonable contemplation. Hints of comparable balancing of investor/state interests, outside the context of applying the defense of necessity, have also appeared in the other Argentina cases discussed here.<sup>158</sup>

Stone Sweet cites the same quotation from *Saluka* mentioned in the *National Grid* decision in support of the use of proportionality balancing in interpreting BITs’ FET provisions. He argues that the adoption of proportionality makes particular sense in this context, where its use could produce greater uniformity of jurisprudence with respect to a guarantee whose very elasticity and imprecision would otherwise provoke anxiety about the unlimited scope of arbitral discretion.<sup>159</sup> We heartily agree and would suggest that much greater consideration needs to be given to how measures taken in the midst of an Argentina-type crisis might affect the interpretation of a BIT’s substantive guarantees, including FET, full protection and security, its

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<sup>157</sup> *National Grid*, para. 180.

<sup>158</sup> Such balancing was in fact exercised by other Argentina tribunals in their discussion of FET. These tribunals were prepared to accept that certain measures taken by the Argentine government might not have been, on balance, unfair or inequitable, but drew the line, for example, when Argentina unilaterally abrogated its prior commitments to engage in *mutual negotiations* over gas tariff rates. See, e.g., Alvarez and Khamsi, *supra* note , at 471-72.

<sup>159</sup> Stone Sweet, *supra* note , at 12-14.

umbrella and free transfers clauses, and possibly even its non-discrimination provisions.<sup>160</sup> In addition, as Alvarez and Khamsi suggest, balancing of investor versus state interests could also come into play when tribunals allocate and calculate financial liability after finding a breach of a BIT, including in situations where the breach occurred in the course of serious economic crisis.<sup>161</sup>

In our view, *Continental* would have produced a more legitimate result had it not short-circuited its consideration of these questions and the merits of many of the claims before it by (mis)applying that treaty's Art. XI. We express no views on whether, had it done so, the results for the claimant would have been different.

But we believe that how proportionality balancing is applied and to which part of an investment treaty matters. We believe that the decision to apply it as does *National Grid* is likely to be seen as far more legitimate and principled than the approach taken in *Continental*, however "sophisticated" the latter's approach to balancing may appear to be. This is so because while international lawyers differ considerably on whether the substantive rules produced by their disparate legal regimes are suitable for cross-fertilization, they scarcely differ on the point that whenever treaty interpretation occurs, the traditional rules of treaty interpretation ought to be applied. Those rules are the least controversial tool for the "defragmentation" of international law that international lawyers have.<sup>162</sup> *National Grid* adhered far more plausibly to those traditional rules of treaty interpretation – plain meaning in light of context and object and

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<sup>160</sup> This is not to suggest, however, that every investor protection contained in a BIT or every investor claim made under them might be subject to "balancing." Balancing seems inherent to many, but not all, allegations of a violation of FET. One can more readily see an effort to "balance" investor and state rights with respect to deciding whether a particular government action was or was not within the contemplation of either for purposes of deciding whether a violation of their legitimate expectations occurred but it may be harder to justify such balancing when the allegation is that the state denied justice to an investor by denying access to its courts. Balancing seems inherent to claims based on indirect takings but it is harder to see its role when the investor is asserting clear violations of specific contractual undertakings made by a state. In addition, we find it hard to imagine circumstances where a state's handling of an economic crisis justifies discriminating against or between foreign investors. Compare Joseph Weiler's efforts, in the course of the first presentation at the NYU Investment Forum, to broaden the concept of "in like circumstances" to embrace states' legitimate public welfare objectives to Anne van Aaken and Jürgen Kurtz, "Prudence or Discrimination? Emergency Measures, The Global Financial Crisis and International Economic Law," 12 J. Int'l Econ. L. 859 (2009)(indicating ways that governments' responses to the current economic crisis might violate investor protections in BITs and FCNs, including the guarantee of national treatment).

<sup>161</sup> This is especially a possibility in the course of treaties, such as the U.S.-Argentina BIT, which lack explicit provisions on the type of compensation owed for breach of their substantive provisions other than expropriation (where prompt, adequate and effective compensation is anticipated). See Alvarez and Khamsi, *supra* note , at 406 (noting that the original *CMS*, *Enron* and *Sempra* tribunals all suggested that they considered the impact of Argentina's crisis on the calculation of damages despite these tribunals' rejection of Argentina's defense of necessity).

<sup>162</sup> See, e.g., ILC's Fragmentation project.

purpose – than did *Continental's* arbitrators, who, in our view, appeared to ignore text, context, object and purpose *and* relevant negotiating history. We do not believe it is necessary to jettison those rules in order to avoid politically “suicidal” results.

Stone Sweet and others who would praise *Continental's* approach should also consider why applying proportionality balancing to consider the impact of an economic crisis *both* for purposes of applying the treaty's substantive rights (such as FET) and as a blanket Art. XI defense to any and all liability under a BIT makes sense. Of course, it is important to realize that “proportionality balancing” comes in various shapes and sizes – embracing forms as distinct as rational basis/strict scrutiny in U.S. constitutional jurisprudence involving the protection of “discrete and insular” minorities and women, balancing the respective rights of states of the United States versus those of the federal government,<sup>163</sup> applications of subsidiarity as used by the European Court of Justice, and the “margin of appreciation” deployed by the European Court of Human Rights. This paper does not seek to resolve which form of “balancing” might be appropriate to apply to BITs' substantive provisions or indeed whether any single model is suitable for all investment treaties or even all parts of a single BIT. We believe that investor-state arbitrators are only now beginning to confront these questions, as the claims they consider become more complex. Unlike Stone Sweet, we do not believe that *Continental's* approach was particularly “sophisticated.” That tribunal simply reached for an off-the-shelf model of balancing presumably because it was familiar -- at least to the president of that tribunal.

We also need to consider what precisely we are seeking to achieve when we “balance.” If the point of proportionality balancing is not simply to increase a state's regulatory options vis-à-vis foreign investors but to lessen the gap between the way foreign investors are treated under the BIT and how all investors fare under national law, applying proportionality where it is not usually applicable under national law is perverse.<sup>164</sup> Consider once more the effects of

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<sup>163</sup> See, e.g., *American Insurance Ass. v. Garamendi*, 539 U.S. 396 (2003).

<sup>164</sup> This is not to suggest a return to the Calvo Clause. What we have in mind is that in some cases, as suggested by the original CMS award, consideration of the existing national law and regulations in place when an investor originally made his investment may be relevant to determining whether a BIT has been violated, as where investors are attempting to prove the basis for their “legitimate expectations.” It may also be relevant because, as is anticipated by Art. X of the U.S.-Argentina BIT, an investor has the right to the better of any treatment accorded under the BIT, international law, or national law. In neither case are we suggesting that BITs have the same effect as old fashioned stabilization clauses in investment contracts. To the extent arbitrators are asked to determine what are the “legitimate expectations” of the parties, we believe that they need to examine, among other things, the types of regulatory changes that investors might have reasonably contemplated given, for example, the regulatory “density” in a particular sector.

*Continental's* decision to apply Art. XI as an on/off primary rule eliminating all state responsibility. This inflexible interpretation makes it impossible to decide that a state's action, though wrongful, might still require compensation, even if national law, absent the state's "emergency" measures, would have led to that result.<sup>165</sup> *Continental's* interpretation means that if an Art. XI plea is accepted, all governmental measures – including direct takings and denials of justice – are left unexamined and are presumptively valid – again, even if national law is to the contrary.<sup>166</sup> Moreover, if *Continental* means to adopt the list of permissible measures in GATT Art. XX and not merely its necessity test,<sup>167</sup> this importation of trade law restricts the universe of legitimate government actions to the categories identified in Art. XX, irrespective of existing national law. Those desiring to preserve states' general right to regulate in the public interest need to realize that the GATT's Art. XX recognizes no such *general* right; it merely identifies what some legitimate government actions might be.

Considering the possible impact of Argentina's crisis measures for purposes of each part of the BIT's substantive guarantees, by contrast, permits a nuanced consideration of whether, under preexisting national law, including the residual right to regulate in the public interest, what Argentina did was proportionate. Such an approach could readily distinguish the relevance of an economic crisis (or any other legitimate regulatory concern, whether or not identified in GATT Art. XX) depending on the type of government action that is asserted to be a violation of FET or of other BIT provisions– from denial of due process in court to lack of transparency in government regulation.<sup>168</sup> With respect to only some of these claims would Argentina's crisis (and its measures in response) be a relevant consideration, and in at least some of these cases the impact could be more appropriately addressed by a diminution, but not the total evisceration, of damages.

There is yet one other important reason to prefer *National Grid's* application of proportionality balancing to *Continental's*. According to at least one survey of the world of BITs, as many as nine out of ten BITs do not have an essential security or NPM clause at all and

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<sup>165</sup> Compare Alvarez and Khamsi, *supra* note , at 456-60 (discussing the rationales for Art. XI, apart from a rule precluding financial liability).

<sup>166</sup> Of course, such a result would contradict BIT provisions such as Art. X of the U.S.-Argentina BIT which anticipate that investors get the better of any rights assured under national law, international law, or the BIT.

<sup>167</sup> As might be implied by that tribunal's turn to the French concept of *ordre public* to interpret Art. XI. See *supra* note .

<sup>168</sup> Whether a state's general right to regulate or the existence of an economic crisis is relevant to a particular BIT claim requires a contextual inquiry and is not a necessary element of every FET claim.

are otherwise silent with respect to public policy exceptions. In these cases, as *National Grid* and other arbitral tribunals have properly decided, under standard canons of treaty interpretation, fundamental rules of international law, such as the rules governing state attribution or traditional defenses such as necessity, continue to apply.<sup>169</sup> As even Stone Sweet acknowledges, the customary defense of necessity poses much larger hurdles for advocates of proportionality balancing.<sup>170</sup> Accordingly, if the opportunity to apply proportionality balancing turns on the presence of a NPM clause, the likelihood that balancing will play the role in investor-state arbitration that its advocates desire is greatly diminished. Further, if arbitrators come to see the presence of an explicit Article XI exception in a BIT as *Continental* seems to have done, *namely as the basis for a state's more general right to regulate in the public interest*,<sup>171</sup> there is a possibility that some tribunals, less sensitive to state concerns than *National Grid*, could fail to consider the alternative possibility that the state's right to regulate in the public interest ought to be considered *whenever the BIT's substantive rights are applied and irrespective of whether a NPM clause exists*. It would appear to be better, for the sake of producing more harmonious international investment law responsive to the needs to balance the interests of all the regime's stakeholders, if the residual right to regulate is regularly considered in the context of the many substantive guarantees that BITs have in common, such as FET, and not emerge only in those rare instances where the presence of an essential security or NPM clause prompts its consideration. Preserving governments' mutual and continued ability to regulate in the public interest – which is arguably either a CIL rule or a general principle of law -- was surely contemplated by BIT parties. For that reason alone, it should be part and parcel of the interpretation of all of a BIT's substantive rights – and not a *deus ex machina* defense that comes from on high to the rescue by elbowing the rest of the treaty aside.<sup>172</sup>

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<sup>170</sup> As he notes, “textually, Art XI of the BIT is relatively hospitable to proportionality, although Art 25’s used of the word ‘only’ is less hospitable.”

<sup>171</sup> This is, of course, suggested by *Continental*’s turn to GATT Art. XX to interpret that clause. But it is all the more likely should others accept, along with Stone Sweet (see Stone Sweet, *supra* note , at 22-23), and possibly the arbitrators in *Continental* (see *supra* note ), that the phrase “the maintenance of public order” in NPM clauses is an all-purpose reference to regulating in the public interest. Those who would rely on such a clause may rue the day when its absence suggests that no such general right to regulate is preserved.

<sup>172</sup> Indeed, the draconian effects of *Continental*’s interpretation, which would dismiss all claims, no matter how meritorious, counsels against its use.



## V. CONCLUSIONS

The debate concerning the interpretative stance taken in *Continental* is, of course, part of a broader inquiry about the role that GATT/WTO jurisprudence ought to play with respect to the interpretation of investment treaties. Nothing that we say here is intended to prejudge issues such as whether the trade jurisprudence concerning national treatment ought to influence BIT arbitrators. We do believe, however, that some of the same concerns, such as faithfulness to the traditional rules of treaty interpretation and sensitivity to the differing structures, objectives and remedies of the trade and investment regimes, need to be kept in mind with respect to such questions.

Consider the key debate in the national treatment context, namely the extent to which “like products” (GATT) and “like circumstances” (BITs) are coextensive, or whether the later is more about the regulatory context and less about competitive opportunities. DiMascio and Pauwelyn for example, support the latter,<sup>173</sup> whereas Kurtz sees it as more of an open question turning on whether national treatment in BITs is “aimed at protectionism or some broader guarantee of non-discrimination.”<sup>174</sup> This division is reflected in the investor-state case law to date. While the *Occidental*<sup>175</sup> and *Methanex*<sup>176</sup> tribunals rejected the relevance of the WTO approach, the tribunals in *Pope & Talbot*<sup>177</sup> and *S.D. Meyers*<sup>178</sup> took a more nuanced approach that Kurtz at least sees grounded in preventing protectionism. This was taken even further in the detailed separate opinion in *S.D. Myers* which argued that:

in determining whether a foreign investor had been discriminated against, contrary to Article 1102 (National Treatment) of NAFTA, a tribunal may in many cases have to pursue the same kind approach as would be taken in an Article XX case under the GATT. In particular, if a government has a legitimate environmental objective and something

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<sup>173</sup> DiMascio and Pauwelyn, above n 3 at 81: “What matters is not the positioning of those investments in relation to each other within the market (“competition test”), but rather the factual support for the government’s distinction between the two when taking regulatory action (“regulatory context test”). Within investment law there are conceivably circumstances that would warrant discrepant regulation of two companies even if they are competitors, just as there are circumstances that would warrant equal regulation of two companies that do not even compete.”

<sup>174</sup> Kurtz, above n 47 at 322.

<sup>175</sup> *Occidental Exploration and Production Company v. The Republic of Ecuador*, London Court of International Arbitration (UNCITRAL arbitration rules), Final Award (Jul. 1, 2004).

<sup>176</sup> *Methanex v. United States*, Award, Part IV, Chapter B (Aug. 3, 2005), 44 I.L.M. 1345.

<sup>177</sup> *Pope & Talbot v. Canada*, Award on the Merits, Phase 2 (Apr. 10, 2001) 7 ICSID Reports 102.

<sup>178</sup> *S.D. Myers, Inc. v. Government of Canada*, NAFTA Arbitration, Partial Award (Nov. 13, 2000).

about the situation of foreign investors unavoidably requires them to be treated differently from local investors in order to achieve that environmental objective then the appropriate conclusion will generally be that that the foreign investors is not being subjected to the kind of discrimination that is prohibited by Article 1102 (National Treatment) of NAFTA.<sup>179</sup>

The separate opinion in *Myers* suggests that preventing protectionism should be read as the controlling purpose of both the national treatment provisions of BITs and in the GATT. Given the existence of a myriad of other substantive guarantees in BITs, in particular, the minimum standard of treatment, including FET, which are “protectionism-plus” in terms of the rights they provide, this approach has merit. It ascribes a particular purpose to the national treatment provision of BITs consistent with the principle of effectiveness and renders that clause distinct from the rights accorded under FET, for example. But it is important not to confuse the purposes of the national treatment provisions of a BIT for the object and purposes of that treaty as a whole and it would be improper, in our view, to suggest that the object and purpose of BITs is the same as the GATT’s, that is to avoid government action motivated by protectionist intent. Note, however, that importing national treatment trade jurisprudence may not solve other interpretative questions concerning the most-favored-nation clauses of BITs, such as whether these apply to give investors the benefit of more advantageous dispute settlement provisions in other BITs.<sup>180</sup> Nor does trade jurisprudence necessarily resolve interpretative questions arising from the application of BITs’ distinct guarantees barring “arbitrary” or “discriminatory” treatment (as under the U.S.-Argentina BIT).<sup>181</sup> These self-standing provisions may not be limited to differential treatment undertaken on the basis of nationality.

Debates over cross-fertilization also need to consider that investment treaties, unlike the WTO, are subject to continuous change. The international investment “regime” (if a single “regime” can be said to exist at all)<sup>182</sup> is a moving target. The contours of the relationship

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<sup>181</sup> Compare U.S.-Argentina BIT, Arts. II(1) and II(2)(b), Annex A.

<sup>182</sup> Given changes to recent model BITs announced by, or actual investment treaties concluded by, countries such as Canada, China, the United States, and Norway, it is no longer plausible to suggest that all investment treaties share a common purpose. See, e.g., José E. Alvarez, “The Evolving BIT,” TDM (June 2009), available at <http://www.transnational-dispute-management.com/members/recentlypublished/content.asp#280>. Compare Robert Keohane and David Victor, *The Regime Complex for Climate Change* (defining a “regime complex” as embracing a number of discrete treaty and other efforts). To the extent the nearly 3000 investment treaties now in force,

between the trade and investment regime, structurally and textually, varies with the investment treaty that is being applied and may be changing more generally in more recent investment treaties. Our analysis here applies to the 1991 U.S.-Argentina BIT and to other BITs with comparable terms, such as those negotiated off the U.S. model BITs of 1984 and 1987. It is important to remember that the non-precluded measures clause in the U.S.-Argentina BIT no longer exists in post-2004 U.S. investment treaties, which have now dropped the reference to “public order” contained in Art. XI and have made the state’s invocation of “essential security” self-judging.<sup>183</sup> As this suggests, the United States’ new non-precluded measures clause is both narrower and broader than Art. XI. At the same time, the post-2004 U.S. model has sharply curtailed nearly all of the substantive investor protections in that treaty, reflecting a new more general attempt to re-balance the rights of investors and states.<sup>184</sup> Although the post-2004 U.S. model has not adopted an exceptions clause à la GATT Art. XX, it may provide new opportunities for cross-fertilization of trade and investment law in other respects. Other countries are also changing their BITs, and sometimes even the overall articulated objects and purposes of their treaties, and these changes may either enhance or derail efforts to import trade law into their interpretation.<sup>185</sup>

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reflecting different models characteristic of different generations of BITs, are more like a “regime complex,” this is yet one more reason to be skeptical of efforts to import jurisprudence from the far more unified WTO regime. This is an entirely different question from whether, given those commonalities that actually exist among investment treaties, new and old, these treaties have come to affect (as well as reflect) *certain* rules of customary international law. For an argument that investment treaties affect custom, see José E. Alvarez, “A Bit on Custom” (forthcoming N.Y. Univ. J. Int’l L. and Pol. 2010).

<sup>183</sup> According to the text of some recent U.S. BITs, the intent is to make state invocations of essential security non-reviewable in the course of investor-state dispute settlement. See, e.g., U.S.-Peru BIT (stating that invocation by a state of essential security makes the underlying claim inadmissible). This constitutes, we submit, a substantial change from Art. XI of the U.S.-Argentina BIT which, as noted, has been uniformly interpreted to incorporate an objective, not self-judging standard, that is fully subject to arbitral assessment. The change appears to reflect a post-9/11 environment in the United States (and elsewhere) where “essential security” concerns trump traditional investor (and property) protections. The change in the BIT presumably seeks to preserve the United States’ abilities, pursuant to new post-9/11 U.S. laws and regulations, to protect its essential security. See, e.g., (changes to U.S. CFIUS review authority over foreign mergers and acquisitions that pose a threat to “essential security”); (post 9/11 changes to International Emergency Economic Powers Act (IEEPA) permitting the President to confiscate property of a foreign entity or state that has attacked or engaged in armed hostilities against the United States).

<sup>184</sup> For a summary of changes, including a table comparing the respective texts of the U.S. Model BITs of 1984 and 2004, see Alvarez, “The Evolving BIT,” *supra* note . As Alvarez indicates, the United States has also been careful to preclude the invocation of the MFN clauses in its post-2004 BITs to secure greater investor protections in its earlier BITs.

<sup>185</sup> As one of us has noted, the meaning of an FET provision located within a pro-investor instrument such as the U.S.-Argentina BIT is surely likely to be different from a comparable clause in a treaty such as the new Norwegian Model BIT. Compare the preamble of the U.S.-Argentina BIT to the preamble of the Norway Model, the latter at Annex D. Arbitrators faithfully applying the traditional rules of treaty interpretation are not likely to take the same approach to “balancing” these treaties’ respective FET clauses.

The prospects for greater overlap between the trade and investment jurisprudence may also be enhanced by the rise of investment chapters within broader free trade agreements, such as the NAFTA. Such mixed agreements in lieu of BITs present more complex questions of object and purpose, and depending on the dispute settlement procedures adopted, more opportunities for cross-pollination between adjudicators charged with adjudicating either trade or investment questions. On the other hand, free trade agreements may discourage cross-references on occasion. Consider, for example, the NAFTA tribunal's decision in *Methanex*, where the tribunal agreed with the United States' contention that had the drafters intended to incorporate WTO concepts (in this case the concept of "likeness") into the NAFTA's investment chapter, they would have done so explicitly, as they had in other parts of NAFTA, such as the goods, SPS and TBT chapters.<sup>186</sup> Of course, the political dynamics of free trade agreements, in which investment protection is part of a broader package deal consisting of a number of trade-offs, is likely to sharpen the differences among investment treaties as a whole. Since a greater number of these FTAs are likely to include parties that are both capital exporters and capital importers (like Canada and the United States in the NAFTA), the balances struck between the needs of investors and states is likely to be different than those in earlier BITs that were often negotiated by capital exporters on take-it-or-leave-it terms.<sup>187</sup> These differences among investment agreements will make it more difficult, at least in the short term, for arbitrators to elucidate common principles of investment law.

*Continental's* interpretative approach raises questions concerning the role of investor-state arbitrators. For some, the role of these arbitrators is not different from those who settle commercial disputes between private parties -- often in private and without published opinions. On this view, investor-state arbitrators do their job when they settle the dispute before them on whatever terms manage to satisfy the opposing parties such that enforcement is assured and it is of no great consequence what reasons arbitrators articulate since their decisions, even if published, have no bearing on the next set of arbitrators formed to hear the next ad hoc dispute.<sup>188</sup> Others, perhaps the majority of scholars and observers, see an increasing divide between investor-state arbitrations, particularly those emerging from the advance consent accorded in BITs and FTAs, and commercial arbitration involving only rarely high profile issues

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<sup>186</sup> *Methanex v. United States*, *supra* note , at paras. 29-35.

<sup>187</sup> Kenneth Vandeveld, *United States Investment Treaties: Policy and Practice*, 82 (1992).

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of public policy. For most of us, it matters greatly that investor-state decisions adhere to the rising expectations we have for other forms of global governance, whether or not we characterize the investment regime as a form of global administrative law.<sup>189</sup> On this view, it is important that investor-state proceedings, the underlying documents and, of course, arbitral decisions be transparent and publicly available, responsive to prior relevant “precedent,” fully reasoned, and attentive to distinct stakeholders’ expectations.<sup>190</sup>

As is obvious from the preceding, we associate ourselves with the latter view. Although we believe that investor-state arbitrators need to apply, first and foremost, the specific treaty before them, even if this sometimes comes at the expense of advancing harmonious international investment law, we do not believe that they operate as independent contractors charged merely with resolving one dispute at a time. Our disagreement with *Continental* rests precisely on its inadequate and flawed reasoning. We are concerned lest it inspire comparable decisions, equally unsupported leaps to trade or other international law, that may undermine the legitimacy of investor-state arbitration. Apart from our legalistic concerns, we are also worried that *Continental*’s approach may encourage resort to an all-purpose necessity defense at the expense of a thorough airing of the substantive merits of claims. If others follow *Continental*’s lead, arbitrators would address the most critical questions at the heart of state sovereignty – including the merits of a state’s invocation of an essential security threat – at the outset, even when such decisions are not necessary. We are mindful of Ted Stein’s insight, inspired by the work of the Iran-U.S. Claims Tribunal, that international jurists would be prudent to limit their jurisprudence to avoid such politically loaded issues whenever possible.<sup>191</sup> *Continental* might have been decided on much narrower grounds, namely the merits of the claims, rather than through a blunderbuss approach that excuses more than is strictly necessary and confuses both trade and investment law.

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<sup>189</sup> See, e.g., Benedict Kingsbury and Stephan Schill, “Investor-State Arbitration as Governance: Fair and Equitable Treatment, Proportionality, and the Emerging Global Administrative Law,” in *El nuevo derecho administrativo Global en América Latina* 221 (2009).

<sup>190</sup> *Id.*

<sup>191</sup> Ted L. Stein, “Jurisprudence and Jurists’ Prudence: The Iranian-Forum Clause Decisions of the Iran-U.S. Claims Tribunal,” 78 AJIL 1 (1984).1