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THE BATTLE AGAINST TOBACCO REGULATION THROUGH INTERNATIONAL TRIBUNALS: PHILLIP MORRIS V AUSTRALIA AND URUGUAY[*]

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ABSTRACT: This work analyses the controversial disputes that Philip Morris brought against Australia and Uruguay in international investor-state arbitral tribunals. Although these disputes took place in different tribunals, they are about similar measures regulating the control and packaging of tobacco designed to reduce its consumption. Philip Morris claimed that these measures violate norms contained in international agreements for the protection of foreign investors, such as the provisions regulating fair and equitable treatment and indirect expropriation. This work examines these disputes in the light of the practice and case-law of previous investor-state arbitrations, in the context of the growing criticism of the current international rules protecting foreign investors and the most recent transpacific and transatlantic negotiations on this subject.

KEY WORDS: Foreign investment, cigarette plain packaging, indirect expropriation, fair and equitable treatment

RESUMEN*:* Este estudio analiza los polémicos litigios que la multinacional tabacalera Philip Morris ha planteado contra Australia y Uruguay ante tribunales internacionales arbitrales para la protección de inversores extranjeros. Aunque tales litigios tienen lugar en tribunales arbitrales distintos, se refieren a medidas parecidas, sobre el control y etiquetado del tabaco para desalentar su consumo. Philip Morris ha alegado que tales medidas violan normas previstas en acuerdos internacionales para la protección de inversores extranjeros, como las disposiciones sobre trato justo y equitativo o sobre expropiaciones indirectas. Este estudio examina tales litigios a la luz de la práctica y la jurisprudencia de previos arbitrajes inversor-Estado, en el contexto de las crecientes críticas a las vigentes regulaciones internacionales para la protección de los inversores extranjeros y de las más recientes negociaciones transpacíficas y transatlánticas sobre la materia.

PALABRAS CLAVE: Inversión extranjera, empaquetado neutro de cigarrillos, expropiación indirecta, trato justo y equitativo.

RESUM: Aquest estudi analitza els polèmics litigis que la multinacional tabaquera Philip Morris ha plantejat contra Austràlia i Uruguai davant de tribunals internacionals arbitrals per a la protecció d'inversors estrangers. Encara que aquests litigis tenen lloc a tribunals arbitrals diferents, es refereixen a mesures semblants, sobre el control i etiquetatge del tabac per tal de disminuir el seu consum. Philip Morris ha al·legat que aquestes mesures violen normes previstes a acords internacionals per a la protecció d'inversors estrangers, com les disposicions sobre tracte just i equitatiu o sobre expropiacions indirectes. Aquest estudi examina aquests litigis a la llum de la pràctica i la jurisprudència de previs arbitratges inversor-Estat, en el context de les creixents crítiques a les vigents regulacions internacionals per a la protecció dels inversors estrangers i de les més recents negociacions transpacífiques i transatlàntiques sobre la matèria.

PARAULES CLAU: Inversió estrangera, empaquetat neutre de cigarretes, expropiació indirecta, tracte just i equitatiu.

ABBREVIATIONS

BIT – Bilateral Investment Treaty

CETA – Comprehensive Economic and Trade Agreement

CJEU – Court of Justice of the European Union CIL – Customary International Law

EEA – European Economic Area

EFTA – European Free Trade Area

FET – Fair and Equitable Treatment

ICSID – International Centre for the Settlement of Investment Disputes

LCIA – London Court of International Arbitration

MFN – Most Favoured Nation

NAFTA – North American Free Trade Agreement

PCA – Permanent Court of Arbitration

PCIJ – Permanent Court of International Justice

PPD – Police Powers Doctrine

SED – Sole Effect Doctrine

TTIP – Transatlantic Trade and Investment Partnership

UNCITRAL – United Nations Commission on International Trade Law Arbitration Rules

UNCTAD – United Nations Conference on Trade and Development

You must have a cigarette. A cigarette is the perfect type of perfect pleasure. It is exquisite, and it leaves one unsatisfied. What more can one want?

- Chapter IV, *The Picture of Dorian Grey,* OSCAR WILDE

1. INTRODUCTION

1.1. General Introduction

In March 2010, one of the leading cigarette manufacturers in the world[2], Philip Morris International instituted international proceedings against Uruguay to vindicate the rights it contended that it was owed through a bilateral trade agreement ('BIT') signed between that country and Switzerland ('the Uruguay BIT'). It claimed its intellectual property had been expropriated by Uruguay and demanded compensation. In June 2011, the same company instituted proceedings against Australia under a BIT signed with Hong Kong ('the Australia BIT'). In a similar way to the Uruguayan case, Philip Morris contended the intellectual property of its brands had been expropriated and was entitled to compensation.

To the critics of investor-state arbitrations the cases brought by Philip Morris against Uruguay and Australia are merely the most egregious examples of how the law of investor-state arbitrations has been subverted to serve only the interests of multinational companies. Even amongst those that favour the current system, few think that Philip Morris could or should win its cases. However, for them the Philip Morris litigations are only isolated examples of vexatious litigation that will be adequately dealt with by the current law.

In October 2015 hundreds of thousands of people took to the streets of Berlin to protest against the proposed Transatlantic Trade and Investment Partnership ('TTIP') between the

[2] *Key Facts and Financial Data* (2016) [online]. Philip Morris International. 2016. [visited: 24 June 2016]. Available at:<http://www.pmi.com/eng/about_us/company_overview/pages/key_facts_and_financial_data.aspx>

United States and the European Union[3]. The most urgent and fundamental objections voiced by the protestors concerned the investment chapter of the TTIP (‘draft TTIP’[4]). It has been described as a undermining democracy and threatening the ability of states to regulate in the interests of their citizens[5].

The litigations started by Philip Morris and the protests of civil society in the streets are connected. One cannot understand one without the other. I will explore how the Philip Morris cases have highlighted criticisms of the law of investor-state disputes. Three key areas of concern are the jurisdiction of tribunals, the fair and equitable ('FET') standard of treatment, and the law of expropriation. Although I will address all of the areas outlined, I will pay particular attention to the law of expropriation as this is the area on which the disputes turn. In addition, I will submit that the current case law does not support Philip Morris’ contention that there is an expropriation. However, I will explore the hypothetical situation that a country wished to ban tobacco products in their entirety. Although it is debatable whether a measure of this type would ultimately amount to an expropriation, I will put forward the argument that it could be. Finally, I will examine the reforms of the law of expropriation proposed in the draft TTIP. Rather than reducing the uncertainty in this area of the law, I will argue that the current drafting of the TTIP tends to codify these uncertainties.

1.2. Introduction to the Disputes

While both cases are taking place in different forums and concern different measures taken by states they share a common theme in that they concern the regulation of tobacco by states. More than this, they bring into relief the way which multinationals use the international investor state arbitration legal framework to challenge measures that states take to restrict the sale of tobacco products.

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[3] The Guardian, *Berlin anti-TTIP trade deal rally attracts hundreds of thousand* [online]. 10 October 2015,[visited: 13 June 2016]. Available at:<http://www.theguardian.com/world/2015/oct/10/berlin-anti-ttip-trade-deal-rally-hundreds-thousands-protesters>

[4] *Commission draft text TTIP – investment* [online]. European Commission. September 2015. [visited: 22 June 2016]. Transatlantic Trade and Investment Partnership, Trade in Services, Investment and E-commerce, Chapter II – Investment. Available at: <http://trade.ec.europa.eu/doclib/docs/2015/september/tradoc_153807.pdf>

[5] Friends of the Earth. *Briefing: The Transatlantic Trade and Investment Partnership (TTIP)* [online]. November 2015, [visited: 29 December 2016]. Available at: <https://www.foe.co.uk/sites/default/files/downloads/briefing-transatlantic-trade-investment-partnership-91913.pdf>

The case between Philip Morris and Australia[6] ('Australia Case') took place in the Permanent Court of Arbitration following the UNCITRAL rules. The dispute has its origin in the enactment of the Tobacco Plain Packaging Act ('the Act') which received Royal Assent on the 1 December 2011. The Act envisages the introduction of a standardised form of packaging for cigarettes in Pantone 448C (according to market research the ugliest colour identified)[7] and with all aspects of the font on the box and the shape of the cigarettes established by law. In addition, 75% of the front and 90% of the back of the box is covered by graphic warnings of the effects of smoking.

Philip Morris Australia ('PM Australia') was incorporated in Victoria, Australia on the 17 March 1954[8]. Prior to February 2011 100% of the shares of PM Australia were owned by Philip Morris Brands Sàrl, a company that has its seat in Neuchâtel, Switzerland. However, on the 23 February 2011 Philip Morris' Hong Kong based company, Philip Morris Asia ("PM Asia") bought the shares in PM Australia from Philip Morris Brands Sàrl[9].

By a notice dated the 15 July 2011 and an expanded notice dated the 21 November 2011, Philip Morris informed the Australian government that it intended to sue the Australia under the 1993 bilateral investment treaty signed between Australia and Hong Kong. As well as invoking some of the duties that Australia owes under the TRIPS agreement, Philip Morris alleged that introduction of the Act had indirectly expropriated their intellectual property[10]. This is because the intellectual property of Philip Morris is one of their most valuable assets and enables the company to distinguish its products from that of competitors[11]. As well as this, Philip Morris alleged that the introduction of the Measure violated the FET that Australia owes under the Treaty. On the 17 December 2015, the tribunal ruled that it did not have jurisdiction to hear the case.

[6] PCA (UNCITRAL). *Phillip Morris Asia Limited (Hong Kong) v. The Commonwealth of Australia.* Case 2012-12, Award on Jurisidiction and Admissibility, 17 December 2015.

[7] El Huffington Post, *¿Cuál es el color más feo del mundo? Los expertos dicen este, el Pantone 448C* [online]. 8 June 2016. [visited: 16 June 2016].
Available at: <http://www.huffingtonpost.es/2016/06/08/story_n_10351454.html>

[8] Philip Morris Asia Limited. *Notice of Arbitration.* 21 November 2011. At 4.1.

[9] *Philip Morris Asia v Australia. Ibid.* P. 163.

[10] Philip Morris Asia Limited. *Notice of Arbitration. Ibid.* At 6.6

[11] Philip Morris Asia Limited. *Notice of Arbitration. Ibid.* At 7.3

The second case is between Philip Morris and Uruguay[12](‘the *Uruguay case*’). This is taking place in the ICSID in Washington D.C. and concerns a BIT concluded between Uruguay and Switzerland. This case was brought by three entities, FTR Holding S.A., Philip Morris Products S.A., and Abal Hermanos S.A., (hereinafter ‘FTR’, ‘PMP’, and ‘Abal’). They commenced proceedings against Uruguay in February 2010. FTR and PMP are *sociétés anonymes* incorporated under the laws of Switzerland[13]. FTR owned 100% of the shares of Abal until they were sold to Philip Morris Brands Sàrl which is a *Société à responsabilité limitée* and also incorporated in Switzerland. It owns 100% of the shares in Abal and has continued the litigation[14].

The dispute stems from the introduction of a number of measures taken by the Uruguayan government. These are the enactment of a series of ordinances of the Uruguayan Ministry of Public Health and the enactment of a presidential decree. These measures had the effect of limiting the differing packaging of cigarette brands and mandating the display of the negative effects of smoking over 80% of the surface area of the box of cigarettes[15]. Unlike the Australia Case, the tribunal decided it did have jurisdiction and, at the time of writing (June 2016), the case continues.

2. PROCEDURAL OBJECTIONS

2.1. The Importance of Procedural Objections in International Investor -State Disputes

Procedural objections often play a much more important role in investor -state arbitrations than in national litigations. The ICJ identifies three sources of international law: customary international law (‘CIL’), general principles of law as recognised by ‘civilised nations’, and conventional law[16]. As there is no binding custom or general principle of law that provides that disputes between states and investors will be submitted to international arbitration

[12] *Philip Morris Brands SÀRL, Philip Morris Products S.A. and Abal Hermanos S.A. v Oriental Republic of Uruguay.* International Centre for Settlement of Investment Disputes. ICSID Case No. ARB/10/7

[13] *Philip Morris v Uruguay.* Decision on Jurisdiction. 2 July 2013. Para. 1

[14] *Philip Morris v Uruguay. Ibid.* Para. 2

[15] *Philip Morris v Uruguay. Ibid.* Para. 4.

[16] Article 38. United Nations, *Charter of the United Nations.* 24 October 1945. 1 UNTS XVI. Judicial decisions and writings of the ‘most highly qualified publicists’ constitute auxiliary means of interpretation

tribunals, it falls that states must consent that a dispute is brought to such a tribunal. Most of the time this consent is given in advance, in the BIT that was signed.

The BIT also informs us exactly which investors the state has consented to having the right to take their case to an international tribunal. In addition, the BIT will also define which investments benefits from the obligations contained in the treaty. As the wording of every BIT differs, the exact meaning of investor and investment varies between agreements and can be difficult to define. In order to be able to take a dispute to an international arbitral tribunal, the investor must show that they fulfil the requirements as set out under the BIT.

BITs typically specify the method through which the nationality of an investor will be recognised and the conditions for the admission of the investment into the territory. This often requires that the investor has complied with all local laws when making their investment. Some BITs have domestic litigation limitations which require that an investor takes their dispute to a domestic court before initiating international proceedings.

From the founding of ICSID in 1966 until the year 2009, it has been calculated that 15% of all disputes brought under the convention were struck out at the jurisdiction phase[17]. The Australia Case demonstrates this point, with the case being struck out at the jurisdiction phase. While the *Uruguay case* has continued beyond the jurisdiction stage, there are grounds on which to criticise this result.

2.2. Procedural Objections in the Australia Case

Article 1(b) (i) of the Australia – Hong Kong Treaty defines investors as:

> "corporations, partnerships, associations, trusts or other legally recognised entities incorporated or constituted or otherwise duly organised under the law in force in its area or under the law of a non-Contracting Party and owned or controlled by entities described in this sub-paragraph or by physical persons who have the right of abode in its area, regardless of whether or not the entities referred to in this sub -paragraph are organised for pecuniary gain, privately or otherwise owned, or organised with limited or unlimited liability".[18]

[17] MCARTHUR, K.S. & ORMACHEA. P.A. International Investor-State Arbitration: An Empirical Analysis of ICSID Decisions on Jurisdiction. *The Review of Litigation*. 2009, vol. 2, p. 568.

[18] Agreement between the Government of Australia and the Government of Hong Kong for the Promotion and Protection of Investments. 15 October 1993. Article 1(b)(i). [ATS 30].

As the reader can see from the above, the definition of an investor is extremely wide ranging. It does not just include any legal or physical person who is legally incorporated or resident in the territory of Hong Kong but practically any sort of body. A definition of an investor in such terms is typical of many BITs.

This approach to determine the nationality of a company is not universal. Some countries specify that the head office of the company must reside in one of the signatories. For example, the BIT between Italy and Nicaragua specifies that a company must have its *'sede principal de negocios'*[19] in the signatory country. These provisions are designed to exclude companies that are not headquartered in a signatory jurisdiction. This limitation on jurisdiction is supported by proponents of reform because it limits the number of investors who can sue under a BIT. However, it would not have prevented Philip Morris from bringing the case against Australia.

This line of reasoning presents interesting questions in the present case. The investor in the Australia Case is PM Asia, a company that undoubtedly has its headquarters in Hong Kong. However, PM Asia is controlled by PM International, a company that is headquartered in the state of Virginia, and has its executive offices in New York in the United States[20]. Therefore, while it can be said that Philip Morris Asia has its '*sede principal*' or headquarters in Hong Kong, this does not reflect the fact that it is only a part of a multinational enterprise headquartered elsewhere. The issue of to what extent an investment must be controlled by a national of one of the contracting parties is further brought into relief when considering what investments are protected.

Article 1(e) Australia – Hong Kong Treaty defines the investments protected by the BIT as:

> "“investment” means every kind of asset, owned or *controlled* by investors of one Contracting Party subject to its law and investment policies as applicable from time to time.For the purposes of this Agreement, a physical person or company shall be regarded as controlling a company or an investment if the person or company has a substantial interest in the company or the investment”.[21]

[19] Acuerdo entre el Gobierno de la República de Nicaragua y el Gobierno de la República Italiana sobre la Promoción y Protección de Inversores. 20 April 2004. Article 2.

[20] Philip Morris International. *Annual Report 2014.* Part I, p 1.

[21] (emphasis added). Australia BIT. *Ibid.*

Australia objected that the tribunal had jurisdiction to hear the case because PM Asia became an investor only after the announcement to introduce plain packaging for cigarettes had been made and a dispute was therefore foreseeable .[22] PM Asia attempted to rebut this assertion in a number of ways. Firstly, it highlighted the fact that under the wording of the BIT, investments 'controlled' by a Hong Kong investor are protected. PM Asia attempted to show that although it did not own any equity stake in PM Australia until after the announcement of the introduction of cigarette plain packaging, it had exercised control of the business to the extent on having a 'substantial interest'.[23] The tribunal rejected this argument in the absence of clear evidence of PM Asia's prior control of PM Australia.[24]

The tribunal stated that the meaning of 'substantial interest', as stated in the BIT, 'may be' best understood as 'an economic contribution of a certain duration which involves some element of risk.'[25]Ultimately, the tribunal left open the question whether mere management control would amount to a 'substantial interest' and allow an investor to enjoy the protections of the BIT.[26] This can be considered a problematic result. One of the central arguments for the existence of BITs is that they encourage the flow of FDI to states and through this spur economic growth and development. If an investor can gain a 'substantial interest' without actually making this economic contribution, it would seem to undermine this central aim of investment treaties.

Restrictions on the nationality of investors who can invoke BITs is an important limitation for states of their liability. The fact that mere management control could be sufficient to allow investors to benefit from the protections in BITs builds on a line of cases with problematic results where panels have often been slow to 'pierce the corporate veil'[27] of corporate structuring. In the case of *Tokio Tokelès v Ukraine*[28] the fact that 99% of the shareholders in a company incorporated in Lithuania were nationals of Ukraine was held not to prevent that company suing under the BIT signed between Ukraine and Lithuania. Additionally, in the

[22] *Philip Morris Asia v Australia. Ibid.* Para. 354.

[23] *Philip Morris Asia v Australia. Ibid.* Para. 496.

[24] *Philip Morris v Australia. Ibid.* Para. 509.

[25] *Ibid.* Para. 502.

[26] *Ibid,* Para. 505.

[27] DOLZER, R. & SCHREUER, C.,*Principles of International Investment Law.* 2nd ed. Oxford: University Press. 2008. P. 48. ISBN: 9780199651801.

[28] ICSID. *Tokio Tolkelès v Ukraine – Decision on Jurisdiction*. 29 April 004. ICSID Case No. ARB/02/18.

case of *Saluka v Czech Republic*[29] the panel reasoned that it could not look at whether a company has invested into the country in the sense that it had made a real economic contribution to the country's economy because the BIT did not give them jurisdiction to do so.[30]

Another method to consider the nationality of an investor is presented to us by the control theory of investor nationality. This says that the real nationality of a company is the nationality of the shareholders which own it and this should be the manner to determine whether a company can sue under an investment treaty or not.[31] The classic case of the *Barcelona Traction Company*[32], a case heard in the International Court of Justice, illustrates this theory in practice. A Canadian company, the Barcelona Traction Company ('BTC'), was declared bankrupt by a court of the host state, Spain. The circumstances of this declaration of bankruptcy were such that it amounted to a type of indirect expropriation. The Canadian government made no complaint about the actions of the Spanish government. The majority shareholder in BTC was a Belgian company called SIDO and the Belgian government attempted to pursue Spain on behalf of the shareholders who were its nationals.[33]

The ICJ refused their demand on the basis that the nationality of a company is determined by its nationality of incorporation, not the nationality of its owners.[34] There were good practical reasons for this result. The shareholding of a publicly listed company changes continuously and through this the nationality of the owners of the capital in a company change in tandem. Another problem is to determine the nationality of the ultimate holder of the capital.

In our present case the shares of PM Asia are owned by PM International, a Swiss company. Following the control theory of investor nationality, PM Asia should be considered as a Swiss company with no standing to sue under the Australia BIT. However, PM International is itself owned by shareholders. As a publicly listed company its shares are subject to sale on the open market and the nationality of its shareholders change accordingly. Taken to its extreme, this

[29] PCA (UNCITRAL). *Saluka v Czech Republic.* Partial Award. 17 March 2006.

[30] *Saluka v Czech Republic. Ibid*. Para. 211.

[31] SCHOKKAERT J. & HECKSCHER, Y., *International Investments Protection.* Antwerp: Bruylant. 2009. P. 257. ISBN-13: 9782802726289.

[32] *Barcelona Traction, Light and Power Company, Limited, Judgment.* 5 February 1970. I.C.J Reports 1970. P. 3.

[33] *Ibid.* Para. 2.

[34] *Ibid.* Para. 71.

theory would mean that an investor of any nationality that could demonstrate that it had a 'substantial interest' in the firm would be able to sue. The nationality requirements in the BIT would become practically non - existent.

However, as the law currently stands, the requirements of nationality *are* practically non-existent. PM International is headquartered in Switzerland. Following the tribunal's conclusions in the Australia Case, it could sue on any BIT signed between that nation and another. This could be true even if it only exercised management control and had made no financial investment. If there was a BIT between Switzerland and Australia, Philip Morris could have sued under that treaty. However, developed countries do not tend to sign BITs between themselves. The practical result is that developing countries are disproportionately impacted by BITs.

The fact that developing countries are respondents in investor-state arbitrations to a disproportionate degree is frequently cited by critics of the current system as a problematic result of the current law of investor-state arbitration.[35] Supporters respond that developing countries are those in most need of FDI which BITs tend to increase[36]. However, as I observed before, the attraction of this capital is the main reason why countries sign BITs. If companies can sue without making this capital investment, this aim is undermined. In addition, a multinational headquartered in the developed world will be better placed to sue developing countries. This is because it is far more likely that there will be BIT signed between the developed and the developing country. It cannot even be said that the developing country was the recipient of development -promoting capital because management control suffices.

If PM Asia could have shown that in fact it exercised management control of PM Australia before the dispute arose, then the claim would have gone ahead. This is in fact what occurred in the Uruguay case where the tribunal ruled that it did have jurisdiction to hear the case.[37]The

[35] CORRERA, C.; SYAM, N. & VELÁSQUEZ, G., Los tratados comerciales y de inversión: obstáculos para las medidas nacionales de salud pública y de control del tobacco . *South Centre Informe Sobre Políticas* [online]. 12 November 2012, No. 12 [visited: 7 January 2017]. P. 5. Available at:<https://www.southcentre.int/wp-content/uploads/2013/06/PB-12_National-Public-Health-and-Tabacco-Control_ES.pdf>.

[36] European Federation for Investment Law and Arbitration. A Response to the Criticism against ISDS by EFILA. *Journal of International Arbitration* [online]. 17 May 2015, vol 33, núm 1 [visited: 7 January 2017]. P. 32. Available at: <http://efila.org/wp-content/uploads/2015/05/EFILA_in_response_to_the criticism_of_ISDS_final_draft.pdf>

[37] *Philip Morris v Uruguay. Ibid.*

only difference in the Uruguay case is that Philip Morris was not acting through its Hong Kong office but as though it was a Swiss company. This leaves us in the situation where an essentially American company, Philip Morris, can at one moment be Swiss and another time from Hong Kong, depending on its business priorities.

2.3. Procedural Objections in the Uruguay Case

The challenges that Uruguay raised to pursue their case bring important questions of procedure to the fore. As I have shown above, procedural requirements to arbitration often serve a purpose to restrict the number of cases which can be brought to international tribunals. I will argue that the ruling in the Uruguay case means that these requirements are significantly undermined.

The Uruguay BIT contains a number of procedural steps through which a potential claimant must go before it can institute proceedings in an international tribunal. Before having recourse to an international tribunal, the claimant has to attempt to settle the disputes amicably for at least six months. [38] After this period, there is an 18 months domestic litigation requirement. [39] Uruguay claimed that Philip Morris had failed to discharge both of these requirements.[40]

The tribunal quickly rejected the objection to the six month requirement because the claimants had attempted to engage with the Uruguayan authorities during a six month period. Not having received a reply to their objections, they instituted proceedings in the domestic courts.[41] This is an uncontroversial finding and indeed, when asked by the arbiters whether the six month requirement had been met, counsel for the respondent answered 'the answer is yes, they satisfied the six-month requirement'.[42]

Uruguay objected that the claimant had not satisfied the domestic litigation requirement because the domestic legal claim was made under different heads of claim. This was rejected by the tribunal who found that the reference to disputes in the BIT meant the domestic and

[38] Agreement between the Swiss Confederation and the Oriental Republic of Uruguay Concerning the Reciprocal Promotion and Protection of Investments. 22 April 1991. [UNTC 33771], Article 10(1).

[39] *Ibid.* Article 10(2).

[40] *Philip Morris v Uruguay. Ibid.* Para. 39.

[41] *Philip Morris v Uruguay. Ibid,* Para. 95.

[42] *Philip Morris v Uruguay. Ibid.* Para. 96.

international claims must have the broadly the same factual basis do not need to be brought on the same legal basis.[43]

Litigation in the domestic courts was instituted on the 9 June 2009 and the international arbitration case in the ICSID was brought against Uruguay on the 26 March 2010 .[44] As can be seen from these dates, the eighteen-month domestic litigation requirement had not been discharged when the international case was brought. The tribunal held that this was no bar to the case being heard at an international level.[45] I would submit that this ruling significantly weakens the domestic legal requirement protection for states.

In practice this means that an investor can start international proceedings at the same time or very shortly after the commencement of domestic proceedings. The international litigation can run concurrently with the domestic litigation. It would not be at all unusual for eighteen months to elapse from the commencement of litigation in an international forum to the hearing. In addition, the tribunal does not carry out a rigorous test of whether the investor has litigated the matter in the national courts with any earnestness. Simply filing a claim that is related to the relevant investment, alleging broadly the same facts would seem to be sufficient. A minimal effort on the half of the investor to keep the case alive until the eighteen months expires or they receive a judgment will dispose of their domestic litigation duty. While the tribunal highlighted that the domestic litigation requirement should not be considered 'futile'[46] I would submit that it is exactly what the requirement becomes under this formulation.

This result goes against the wording of the BIT which the tribunal pointed out as mandating that domestic litigation is started before 'appeal' may be had to an international tribunal[47]. It also seems to run counter to the spirit of the Uruguay – Switzerland BIT when this provision is read in conjunction with the requirement that the claimant try to resolve the case amicably before initiating domestic legal proceedings. To reach this conclusion, the tribunal relies on ICJ case-law from ninety years ago which discusses principles of public international law[48]. It

[43] *Philip Morris v Uruguay. Ibid.* Para. 110.

[44] *Philip Morris v Uruguay. Ibid.* Para. 131.

[45] *Philip Morris v Uruguay. Ibid.* Para. 144.

[46] *Philip Morris v Uruguay. Ibid.* Para. 136.

[47] *Philip Morris v Uruguay. Ibid.* Para. 111.

[48] *Philip Morris v Uruguay. Ibid.* Para 145. Citing *Mavrommatis Plaestina Concession* case. Judgment No.2. 30 August 1924. PCIJ. Series A, No. 2, p. 34.

is not clear on what basis this case should determine a question of jurisdiction in a modern investment law case.

One of the leading cases regarding the expiration of domestic litigation requires is the *Maffezini case.*[49] When discussing whether the reading of the BIT should be so that no domestic litigation requirement is necessary, the court highlighted that:

> "Claimant's interpretation ... would deprive this provision of any meaning, a result that would not be compatible with generally accepted principles of treaty interpretation, particularly those of the Vienna Convention on the Law of Treaties".[50]

I would submit that the tribunal's interpretation of the Uruguay – Switzerland BIT leaves the domestic litigation provision deprived of any meaning. It becomes a mere formality that an investor must do before pursuing a claim in the international courts.

3. FAIR AND EQUITABLE TREATMENT

3.1. Introduction to Fair and Equitable Treatment

This obligation to afford foreign investors of fair and equitable treatment is frequently included in BITs. There is also a rule of international customary law that requires that states act in a way that is FET compliant. Whether the standards of FET as stated in BITs is an autonomous conventionally agreed standard or merely a restatement of the CIL standard has long been a point of debate. FET is an internationally accepted minimum standard which may surpass the protection granted to domestic investors.[51]

While some authors maintain that the meaning of FET is obvious from the plain reading of the words 'fair and equitable'[52], in practice, this is often an extremely difficult concept to adequately define. The concept is vague and all-encompassing and the International Institute for Sustainable Development highlights that:

> "The fundamental uncertainty regarding the meaning of the obligation has prompted states to explore options to prevent the steadily growing expansive reading of the

[49] ICSID. *Maffezini v Kingdom of Spain – Decision of the Tribunal on Objections to Jurisdiction.* 25 January 2000. Case No. ARB97/7.

[50] *Maffezini v Spain. Ibid.* Para. 36.

[51] SCHOKKAERT, J. & HECKSCHER, Y., *Ibid.* P. 330.

[52] SCHOKKAERT, J. & HECKSCHER, Y., *Ibid. Ibid.* P. 332.

> standard, which it is feared can be used as a tool to force states to pay for the development of law in the public interest where changes in the law or its implementation leads to costs or reduced profits for the investor".[53]

A key complication to defining the content of the FET is the debate about its exact nature. If a BIT contains the commitment to FET is this simply a restatement of the standard owed under international customary law or a guarantee of more stringent protection? Some contend that it is a separate, more stringent standard of behaviour. If the contracting parties had wished to make references to customary international law standard, they could have done so.[54] However, others support the notion of FET as merely a restatement of the duties states owe investors under customary international law. For example, in a resolution adopted on the 6 April 2011 the European Parliament stated that FET should be defined by reference to customary international law in the investment treaties signed with the EU.[55]

In the NAFTA, article 1105 contains a provision that the contracting states will afford FET to investors. In a note written by the Free Trade Commission, a body that represents the contracting states and can adopt binding interpretations of the agreement stated that FET reflects international customary law.[56] The wider relevance of this measure has been doubted because of the specificity of the language used in the NAFTA. It explicitly references international law and article 1105 is entitled 'Minimum Standard of Treatment'. Alternatively, in BITs not reflecting the wording of the NAFTA, many tribunals have argued that an autonomous, higher standard of protection is most appropriate[57].

An example of this is the case of *Azurix v Argentina* [58]where the tribunal held that FET was an autonomous concept that provides for a higher level of protection to investments. It further held that the reference to international law in the article guaranteeing FET set a minimum below which FET could not fall. The FET guaranteed by the treaty could supersede this

[53] International Institute for Sustainable Development. A Response to the European Commission's December 2013 Document "Investment Provision in the EU – Canada Free Trade Agreement (CETA) [online]. *IISD Report*, February 2014 [viewed: 7 January 2017]. Available at <http://www.iisd.org/pdf/2014/reponse_eu_ceta.pdf>

[54] DOLZER, R. & SCHREUER, C., *Ibid*. P. 135.

[55] European Parliament. EP Resolution of 11 April 2011. OJ 2011 C296 E.

[56] Free Trade Commission. *Interpretations of Chapter Eleven.* 31 July 2001. Para B(1).

[57] DUMBERRY, P. *The Fair and Equitable Treatment Standard: A Guide to NAFTA Case Law on Article 1105.* Kluwer Law International. 2013. P. 307, para. 4. ISBN: 9789041132888.

[58] ICSID. *Azurix v Argentina- Award*. 14 July 2006. ICSID Case No. ARB/01/12.

minimum found in customary international law. In a similar way, in the case of *Vivendi v Argentina*[59] the tribunal found that the provision that FET is interpreted 'in conformity' with international law meant that considerations beyond the minimum standard of international law should be taken into account.[60]

3.2. Legitimate Expectations

The exact nature and content of the FET standard is brought into sharp relief when the discussion about the legitimate expectations of the investor is considered. The theme of legitimate expectations and the need to have a stable and transparent legal system has been highlighted by tribunals in other situations.[61] Under the NAFTA, it has been held that the legitimate expectations created for the investor must take the host state's legal system when it made its investment as the first point.[62] The state will violate the FET standard when it changes the regulatory regime in a way which disappoints the legitimate expectations of an investor when they made their investment.

This rule that the legitimate expectations created in the mind of the investor have to be considered at the moment of making the investment has been followed by a number of tribunals in other cases.[63] An example is given by the case of *Occidental v Ecuador* [64]. In this case the investor was complaining of the inconsistent way in which VAT was reimbursed by the state. The tribunal found that the standard of FET had been violated because the framework in which the investor had been operating was subject to constant and opaque change since they invested.[65]

Another case following this line of reasoning is that of *CMS v Argentina*[66]. The guarantees enshrined in legislation, regulations, and the licence granted to the investor meant that it was a

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[59] ICSID. *Compañiá de Aguas del Aconquija S.A. and Vivendi Universal S.A. v Argentine Republic –Award*. 20 August 2007. ICSID Case No. ARB/97/3.

[60] DOLZER, R. & SCHREUER, C., *Ibid*. P. 137.

[61] ICSID. *Técnicas Medioambimentales v The United Mexican States – Award*. 29 May 2003. ICSID Case No. ARB (AF)/00/2. Para. 154.

[62] NAFTA (UNCITRAL). *GAMI v Mexico.* Award. 15 November 2004. Para. 93.

[63] DOLZER, R. & SCHREUER, C., *Ibid*. *Ibid*. P. 146.

[64] LCIA (UNCITRAL). *Occidental Exploration and Production Company v Ecuador – Final Award.* 1 July 2004. Case No. UN3467.

[65] *Occidental v Ecuador. Ibid.* Para 183.

[66] ICSID. *CMS Gas Transmission Company v The Argentine Republic – Award*, 12 May 2005. ICSID Case No. ARB/01/8.

violation of the FET standard of treatment for this legal framework to be repudiated. The tribunal went on to state that 'a stable legal and business environment is an essential of fair and equitable treatment.'[67]

The line of reasoning present in the above cases supports Philip Morris in its assertion that the measures violate the FET standard. It brings the concept of legitimate expectations into a much wider sphere. It is understandable that tribunals will find a failure to discharge the obligation to provide FET to investors where specific inducements have been given to investors to tempt them to invest. On the contrary, the above cases concerned general regulatory changes. This area of law is not settled and it can be argued that to impose a duty to provide a stable regulatory regime is an impermissible expansion of the FET standard.

One argument against this reading of the FET standard is provided by the existence of stabilisation clauses in some BITs. These clauses have their purposes to prevent the host state from legislating in a way that is unfavourable towards foreign investors. For example, article 4 of the France – Montenegro BIT[68] provides that:

> *"Les ressortissants français, personnes physiques ou morales, bénéficieront pour les investissements visés à l'article 1re de la présente Convention ainsi que pour 1'exercice des activités professionnelles et économiques liées à ces investissements, du traitement le plus favorable accordé en la matière a des ressortissants de tout autre pays tiers par la législation yougoslave. Au cas où celle-ci serait modifiée dans un sens moins favorable, lesdits investissements resteront régis par les dispositions en vigueur à la date où ils ont été agrées".*

The paragraph of the above article guarantees most favoured nation ('MFN') treatment for French investors. In the case of a change in the law that is unfavourable to their investments, the investments will still benefit from the legislation that was in force at the time of the investment. A clause of this nature mean that the host state is precluded from legislating in a manner that is less favourable to investors from the capital exporting state. In addition, the above example is an example of a unilateral obligation of this type. Only French investors

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[67] *CMS v Argentina. Ibid.* Para. 274.

[68] France Diplomatie. *Convention entre le Gouvernement de la République Française et le Gouvernement de la République Socialiste Fédérative de Yougoslave sur la Protection des Investissements* [online]. 3 March 1975. Treaty Number : 19740088 [viewed : 17 June 2016]. Available at: <http://basedoc.diplomatie.gouv.fr/exlphp/cadcgp.php?CMD=CHERCHE&QUERY=1&MODELE=vues/mae_internet___traites/home.html&VUE=mae_internet___traites&NOM=cadic__anonyme&FROM_LOGIN=1>

benefit from the stabilisation clause. If Argentina had wished to provide an obligation to provide a stable regulatory environment towards foreign investors in the *CMS* case, it could have done so explicitly through a clause similar to the above.

A case which reflects this view is *EDF v Romania.*[69]The tribunal highlighted the dangers of *CMS* formulation being stated too broadly as it would preclude virtual any change to the domestic legal system. In the absence of any specific representations to the investor it is unlikely that a tribunal will find that their legitimate expectations have been disappointed.[70]On this basis the *CMS* case may have been correctly decided because the state granted a specific licence for the transportation of gas. The state would still be able to change the regulatory framework of gas transportation by waiting until licences expired or by paying compensation.

Paragraph 4 of article 3 of the TTIP also reflects a recognition of the dangers of a too wide duty of FET:

> "When applying the above fair and equitable treatment obligation, a tribunal may take into account whether a Party made a specific representation to an investor to induce a covered investment, that created a legitimate expectation, and upon which the investor relied in deciding to make or maintain the covered investment, but that the Party subsequently frustrated."

By specifying that the representation was 'specific' the CETA formulation excludes that general regulatory measures could form the basis of a claim for a violation of FET. This is not to say that some measures of a general nature, if focussed on a particular part of the economy could not create legitimate expectations under this formulation[71]. The above wording also specifies that the representations would have had to induce the investment. This further limits the potential investors who could rely on the legitimate expectations created by government actions.

An example of a case which reaffirms the right of states to legislate is *Methanex v Mexic* [72] where it was held that the possibility of increased environmental regulation should have been

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[69] ICSID. *Total S.A. v The Argentine Republic – Decision on Liability*. 27 December 2010. ICSID Case No. ARB/04/01. Para 164.

[70] KRIEBAUM, U., FET and Expropriation in the Comprehensive Economic Trade Agreement between the European Union and Canada. *Transnational Disputes Management*. 1 March 2016, vol. 13, núm 1, p. 15.

[71] KRIEBAUM, U., *Ibid.* P. 21

[72] NAFTA (UNCTRAL). *Methanex Corporation v United States of America – Partial Award.* 7 August 2002.

foreseeable by a prudent investor when they made their investment. On the other hand, in the *Metalclad case*[73] the investment had only gone ahead on the reasonable belief that all the necessary permits had been obtained to build and operate the facility. Taken in context with the other case-law showing that only specific undertakings of a government can constitute the basis of the legitimate expectations of an investor, this point has important implications for the Philip Morris cases.

3.3. Fair and Equitable Treatment in the Present Disputes

Article 2 of the Australia Treaty stipulates that:

> "Investments and returns of investors of each Contracting Party shall at all times be accorded fair and equitable treatment and shall enjoy full protection and security in the area of the other Contracting Party. Neither Contracting Party shall, without prejudice to its laws, in any way impair by unreasonable or discriminatory measures the management, maintenance, use, enjoyment or disposal of investments in its area of investors of the other Contracting Party. Each Contracting Party shall observe any obligation it may have entered into with regard to investments of investors of the other Contracting Party. This Agreement shall not prevent an investor of one Contracting Party from taking advantage of the provisions of any law or policy of the other Contracting Party which are more favourable than the provisions of this Agreement".[74]

In the Australian government's response to the notice of the claim of arbitration it is underlined that the purchase of shares by PM Asia in PM Australia occurred only after the announcement of the introduction of cigarette plain packaging[75]. The Australian government also highlighted that this measure was introduced in the context of progressively stricter regulation of smoking in Australia since the 1970s[76]. In this context, it cannot be said that the legitimate expectations of the investor were disappointed when it made the investment to buy shares in the Australian business.

Neither the Australia nor the Uruguay Treaties contain stabilisation clauses. If the states who signed theses BITs had wanted to give a general guarantee of regulatory stability they could

[73] ICSID. *Metalclad Corporation v The United* Mexican States – Award. 30 August 2000. ICSID Case No. ARB(AF)/97/1.

[74] Australia BIT. *Ibid.* Article 2.

[75] Commonwealth of Australia. *Response to Notice of Arbitration.* 21 December 2011. Para. 30.

[76] Commonwealth of Australia. *Ibid.* Para. 14.

have done so. In addition, there were no specific representations made either generally or to individual domestic or foreign investors that the regulatory regime around tobacco would not change.

Article 3 of the Uruguay Treaty couches the FET obligation in similar terms:

> "(1) Each Contracting Party shall protect within its territory investments made in accordance with its legislation by investors of the other Contracting Party and shall not impair by unreasonable or discriminatory measures the management, maintenance, use, enjoyment, extension, sale and, should it so happen, liquidation of such investments. In particular, each Contracting Party shall issue the necessary authorizations mentioned in Article 2, paragraph (2) of this Agreement.
> (2) Each Contracting Party shall ensure fair and equitable treatment within its territory of the investments of the investors of the other Contracting Party. This treatment shall not be less favourable than that granted by each Contracting Party to investments made within its territory by its own investors, or than that granted by each Contracting Party to the investments made within its territory by investors of the most favoured nation, if this latter treatment is more favourable."

The FET obligation is expressed in a similar way in the two BITs albeit with slightly different wording. There is an addition in the Uruguay Treaty that provides further evidence that the FET obligation should not extend to general legislative acts. The BIT specifies that "each Contracting Party shall issue the necessary authorizations mentioned in Article 2, paragraph (2) of this Agreement". These authorisations are described as the 'necessary permits'[77] that are needed for an investment to carry out its activities once it has been admitted to the country. This narrows the scope of the FET obligation to a duty when granting such permits to specific investors.

Even without this particularity of the Uruguay Treaty, to propose that there has been a violation of the FET in either case, is a difficult argument to sustain. As the draft TTIP shows, the FET is being increasingly understood as protecting individual investors in their dealings with the host state. It also gives a list of instances of a breach of the FET to situations where a state denies justice, breaches due process, acts in an arbitrary manner, or discriminates against investors based on their gender, race, or religious beliefs .[78] There have been no

[77] Uruguay BIT. Article 2(2).

[78] TTIP. Article 3(2).

representations made by either of the states to any tobacco company which would give rise to a legitimate expectation on which a claim for a breach of FET could be founded. The measures are general in nature and take place in the context of the increasing regulation of tobacco products over the last forty years.

4. EXPROPRIATIONS AND NATIONALISATIONS

4.1. Introduction to Expropriation

The protection of the right to own property is one of the great constitutional rights of the Western legal tradition[79]. For example, the European Convention of Human Rights (ECHR) states, 'Every natural or legal person is entitled to the peaceful enjoyment of his possessions.'[80]However it goes on to qualify this right:

> "The preceding provisions shall not, however, in any way impair the right of a State to enforce such laws as it deems necessary to control the use of property in accordance with the general interest or to secure the payment of taxes or other contributions or penalties".[81]

The example of the ECHR demonstrates that while the right to own property is guaranteed by international law, it is not absolute. The state retains the right to take property for public purposes.

The two main ways that property can be taken from a proprietor by a state are through expropriation and nationalisation. Nationalisation is the bringing of economic sectors into public ownership, typically by the creation of a state monopoly. In contrast, expropriation is the taking of a private property for a public purpose[82].

It should be first noted that states retain the right to expropriate private property for public purposes. To expropriate property in a valid way, a state must (i) expropriate it for a public purpose, (ii) in a non-discriminatory manner, (iii) by the due process of law, and (iv) on the payment of just compensation. As can be seen above, the public purpose of the expropriation

[79] SCHOKKAERT, J. & HECKSCHER, Y., *Ibid.* P. 366.

[80] Article 1 of Protocol 1 ECHR

[81] Article 1(2) of Protocol 1 ECHR

[82] SCHOKKAERT, J. & HECKSCHER, Y., *Ibid.* P. 370.

does not negate the duty to compensate. In customary international law, the determination of the compensation for a valid and an invalid expropriation can differ.

When a state commits an illegal act such as an invalid expropriation, the state must compensate the investor to 'wipe out the consequences of the illegal act'.[83] The compensation for a valid expropriation is fixed at the fair market value of the property immediately before the expropriation. However, the compensation for an invalid expropriation can be fixed at a different point in time to fully reflect the loss of value of the property due to the expropriation.[84] An expropriation without compensation will be by definition an invalid expropriation. While the ability of tribunals to follow this rule of customary international law where there is a BIT that specifies how compensation should be calculated is controversial, commentators support that the principle of full compensation should be maintained.[85]

4.2. Introduction to Indirect Expropriation

Increasingly, the focus of international investment protection litigation has moved away from direct expropriation to indirect expropriations. Indirect expropriations are state actions which leave the investor's title to the property intact but deny their enjoyment of their property. Certain actions that have the practical effect of denying an investor enjoyment of their property have long been recognised as giving rise to an obligation to compensate. However, it is more difficult to draw the line between state regulations and the measures which are taken that are compensable indirect expropriations of property.[86] Most BITs have provisions which explicitly make actions which have an effect equivalent or tantamount to an expropriation property compensable.[87]

The case-law of indirect expropriation displays a lack of consistency in which takings of property are indirect expropriations and therefore compensable and those that are not.

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[83] *Case Concerning the Factory at Chorzów (Claim for Indemnity) (Germany v. Poland)* (1928) PCIJ Ser. A. No. 17. Para. 47.

[84] NEWCOMBE, A. & PARADELL, L., Law and Practice of Investment Treaties: Standards of Treatment. Alphen aan den Rijn: Kluwer Law International. 2009. 7.38. ISBN 978-90-411-2351-0

[85] NEWCOMBE, A. & PARADELL, L.,*Ibid.*

[86] NEWCOMBE, A. The Boundaries of Regulatory Expropriation in International Law In KAHN, P. & WÄLDE, T., *Les aspects nouveaux du droit des investissements internationaux.* 2007. Leiden: Brill. P. 394. ISBN13: 978-90-0415-3721.

[87] DOLZER, R. & SCHREUER, C. *Ibid.* P. 103.

4.2.1. Substantial Deprivation of Property

The starting point of an analysis of whether there has been an interference with the property rights of the investor equivalent to an expropriation. This reflects the classic phrasing of a BIT which specifies that acts equivalent or 'tantamount' to expropriations compensable. The *Metalclad case* gives us some useful indications on the level of interference with property that will amount to an expropriation. In this case, the US investor had been granted a federal permit to develop and operate a hazardous waste disposal plant in Mexico. Despite having the federal permit, the state authorities refused to allow the plant to operate[88]. The tribunal found that the actions of the state authorities amounted to an indirect expropriation of the investor's property. The key to their reasoning was that the actions of the state authorities was such that they had the effect of 'depriving the owner, in whole or in significant part, of the use or the reasonably-to-be expected benefit of property.'[89]

The case of *CMS v Argentina*[90] further illustrates this point. The Argentine government unilaterally suspended an agreed tariff adjustment scheme for the transportation of gas. CMS, an investor in the Argentina gas transportation sector, claimed that its business had been expropriated by this measure. This claim was rejected even though the tribunal accepted that it had a profound impact on CMS's business[91]. The tribunal started that the test for expropriation is whether the 'enjoyment of the property has been effectively neutralized.'[92] The deprivation of property which will amount to an expropriation has also been described as when an investor is 'radically deprived'[93] of their property. In addition, some tribunals have described that the level of deprivation must be a 'substantial deprivation'.[94]

[88] ICSID. *Metalclad Corporation v The United Mexican States – Award.* 30 August 2000. ICSID Case No. ARB(AF)/97/1. Para. 59.

[89] ICSID. *Metalclad v Mexico. Ibid.* Para. 103.

[90] ICSID. *CMS Gas Transmission Company v The Argentine Republic – Award.* 12 May 2005. ICSID Case No. ARB/01/8.

[91] ICSID. *CMS Gas Transmission Company v The Argentine Republic – Award. Ibid.* Para. 263.

[92] ICSID. *CMS Gas Transmission Company v The Argentine Republic – Award. Ibid.* Para. 262.

[93] ICSID. *Técnicas Medioambimentales v The United Mexican States – Award.* 29 May 2003. ICSID Case No. ARB (AF)/00/2. Para. 115.

[94] NAFTA (UNCTRAL). *Pope & Talbot v Canada.* Interim Award. 26 June 2000. Para. 102.

There is some disagreement to whether there must be an interference with the rights of ownership or whether a diminution in value will suffice to amount to an expropriation. However, on either of these tests it is clear that the interference or the diminution of value must be high. The investor must be left with practically no control of the investment and its value must be reduced to practically nothing.

However, once a 'substantial deprivation' of property has been identified there is a divergence in the case-law of what further analysis the tribunal should carry out.

4.2.2. *Sole Effect Doctrine*

The first method to consider indirect expropriation is known as the sole-effect doctrine ('SED'). This is where the tribunal looks at effect the measure has on the investment and does not 'decide or consider the motivation or intent of the adoption of the [Measure].'[95]The analysis of the tribunal stops at whether there has been a 'substantial' deprivation of the property. There have been several formulations of to what extent property must be taken in order to amount to an expropriation. Tribunals have shied away from making a numerical assessment of the extent of deprivation of the property, but they have held that it must be complete or nearly complete.[96]Once it has been established that there has been a substantial deprivation of property, an indirect expropriation will be found.

Several arguments are advanced to support the SED approach. The first is that there is nothing in the formulation of an expropriation that says that the purpose of a government excuses the duty to compensate. Indeed, the public purpose is only one condition of a legitimate expropriation along with compensation. Secondly, the supporters of this approach highlight that the risks to the state's ability to regulate are overstated. Only those takings of property that amount to an expropriation will be liable to be compensated for.

Critics of the SED approach to determining indirect expropriation point that it would make compensable several takings of property which are widely considered to be non-compensable. If a taking falls within the customarily accepted police powers of that state, then it is not compensable.[97] The exact measures which states can take which fall into their non-compensable police powers doctrine are not yet fully identified. Despite this, the adherents to

[95] ICSID. *Metalclad Corporation v The United Mexican* States – Award. 30 August 2000. ICSID Case No. ARB(AF)/97/1. Para. 111.

[96] NEWCOMBE, A. & PARADELL, L. *Ibid,* Para. 7.16

[97] PCA (UNCITRAL). *Saluka v Czech Republic.* Partial Award. 17 March 2006. Para. 263.

the PPD would support there is evidence from state practice and an *opinio juris* that takings falling into the state's general regulatory powers are not compensable. To ignore this rule of customary international law and impose the SED is to misunderstand the law as it stands.

4.2.3. Police Powers Doctrine

The alternative manner to determine whether there has been an indirect expropriation is given by the police powers doctrine ('PPD'). The doctrine starts at the same point as the SED; that there must be a substantial deprivation of the property. However, unlike the SED, in order to determine whether there has been an indirect expropriation of property, the tribunal 'must look at the real interests involved and the *purpose* and effect of the government measure.'[98] If there has been a use of the state's police powers then there will be no indirect expropriation and therefore no duty to compensate the investor.

The *Methanex case* shows how the PPD can be applied in practice. The tribunal held that because the measure was non-discriminatory, passed for a public purpose, and by the due process of law, it was not compensable. While this result may be applauded, it would seem to go against a reading of the provisions for expropriation that are included in most BITs. The plain meaning of the conditions of expropriation in the NAFTA certainly does require that a governmental measure fulfils these three conditions. However as it is stated in the NAFTA, it requires that these three conditions are met *and* compensation is paid. The test to determine if there was been an expropriation seems to have been conflated with the test of whether it was a validly executed expropriation. Before the tribunal can consider the four conditions of a validly executed expropriation, it must consider whether there has been an expropriation in the first place. The fact that the measure was non - discriminatory, for a valid public purpose, and implemented by due process do not negate the fourth condition of a valid expropriation of property, namely the payment of compensation.

4.3. The Present Disputes

Paragraph one of article five of the Uruguay Treaty deals with expropriation and nationalisations of property:

> "Neither of the Contracting Parties shall take, either directly or indirectly, measures of expropriation, nationalization or any **other measure having the same nature or the**

[98] (emphasis added *). Saluka v Czech Republic. Ibid.* Para. 285.

> **same effect against investments** belonging to investors of the other Contracting Party, unless the measures taken for the public benefit as established by law, are on a non-discriminatory basis, and under due process of law, and provided that provisions be made for effective and adequate compensation. The amount of compensation, interest included, shall be settled in the currency of the country of origin of the investment and paid without delay to the person entitled thereto."[99]

Article 6 of the Australia Treaty follows the classic formulation of the conditions of an expropriation as below:

> "Investors of either Contracting Party shall not be deprived of their investments nor subjected to measures **having effect equivalent to such deprivation** in the area of the other Contracting Party except under due process of law, for a public purpose related to the internal needs of that Party, on a non-discriminatory basis, and against compensation".[100]

There are differences between the two provisions. The Uruguay BIT classifies as an indirect expropriation any measure having the same 'nature' or 'effect' as an expropriation. Conversely, the Australia Treaty classifies indirect expropriations simply as those measures having 'effect equivalent'. It could be contended that the Uruguay BIT allows a tribunal to adopt a PPD reading of the provision. In a way that is not usual to BITs, it explicitly empowers the tribunal to look at the purpose behind the measure.

Another difference is that the Australia Treaty only allows expropriations for a public purpose which is related to the internal needs of the party. It could be hypothesised that at the time of drafting the BIT this was included because the negotiators feared that property in Hong Kong could be expropriated for a public purpose related to other territories of the People's Republic of China, of which Hong Kong is now a part. In any event, the protection of human health is undoubtedly a public purposes related to the internal needs of Australia.

In their notice of arbitration, Philip Morris contended that 'Plain packaging legislation destroys the commercial value of the intellectual property and goodwill'.[101] While it is undeniable that the measures taken by the Australian government deprive Philip Morris of the near totality of its intellectual property, that is not the same as expropriating its business.

[99] (emphasis added)

[100] (emphasis added)

[101] Philip Morris Asia Limited. *Notice of Arbitration, Australia/ Hong Kong Agreement for the Promotion and Protection of Investments.* 21 November 2011. Para. 7.4.

If we look at the tests employed in the cases above, it appears that the test is whether the business as a whole is left with any commercial value. Philip Morris is not being prohibited from selling cigarettes and indeed continues to make a considerable profit in Australia. On this basis, to establish that the actions of the Australian state amounted to an indirect expropriation is a difficult argument for Philip Morris to make.

This is not to say it would be an impossible argument. In some circumstances tribunals have considered that the rights of investors can be partially expropriated, regardless of their control over the totality of the property. For example in the case of *Middle East Cement v Egypt*[102] the investor had obtained a licence to import cement and built infrastructure to distribute cement. Egypt subsequently revoked the licence, leaving the infrastructure worthless and seized and sold a ship owned by the claimant.[103] The tribunal decided that the licence to operate was a separate investment to the infrastructure[104], the revocation of which was compensable.

Another example is given by the case of *Eureko v Poland*[105] .In this case an investor acquired a minority interest in a privatised insurance business and was granted the right to obtain the majority in the business. The Polish government repudiated this right meaning the investor could not obtain the majority share in the business.[106] The original investment was not affected by the repudiation of the right to acquire a majority share in the business. The tribunal considered that the repudiation of this subsequent right could be considered as an expropriation.[107]

It can be argued that the measures taken by Australia and Uruguay can be distinguished from the above cases. In the *Middle East Cement* case the revocation of the licence was held to be compensable because it subsequently left the rest of the business without value and was therefore a taking.[108] As I have shown above, the measures do not substantially deprive Philip Morris of its business in Australia or Uruguay.

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[102] ICSID. *Middle East Cement Shipping and Handling Co. S.A. v Arab Republic of Egypt – Award*. 12 April 2002. ICSID Case No. ARB/99/6.

[103] *Middle East Cement v Egypt*. *Ibid.* Para. 82.

[104] *Middle East Cement v Egypt, Ibid.* Para. 101.

[105] *Eureko B.V. v Republic of Poland.* Partial Award. 19 August 2005

[106] *Eureko v Poland. Ibid*. Para. 62.

[107] *Eureko v Poland. Ibid.* Para. 241.

[108] *Middle East Cement v Egypt. Ibid.* Para. 107.

In addition, a key distinction should be made between the above cases and the present disputes. In both of these cases the state had made a specific promise to the investor through a licence or a contract. It is debatable whether indirect expropriation was the most appropriate way to plead these cases. There is a great deal of potential overlap of the law governing umbrella clauses. In addition, it can be argued that these case is best understood under the law of FET. A specific representation was made to the cement importer through the granting of the licence that they would be able to import and distribute cement for a ten year period. The importer relied on this representation to invest in Egypt. They could not subsequently complain that their business was expropriated if at the end of the ten year period the licence was not renewed. No such specific representations were made in either the Australia or the Uruguay cases.

The *Eureko* case is also best understood following the law of FET. The bulk of the tribunal's judgment deals with the violations of FET and the umbrella clause. A mere six paragraphs of the judgment are devoted to the law of indirect expropriation. I would submit that the case is best understood in the terms of the legitimate expectations of the investor. The reason why it was held that there was unfair and inequitable treatment of the investor was because the Polish government had promised to sell the shares to give Eureko a controlling interest. This raised a legitimate expectation upon which the investor relied. If the Polish government had granted a promise to sell the shares but reserved the right to cancel this promise, then it could not be said that the legitimate expectations of the investor would be disappointed. Equally, it could not be said that a right to buy which was revocable at any time would be an investment that could be expropriated.

The Uruguay measures differ from the Australian ones in a way which is relevant to determine whether there has been a 'substantial deprivation' of Philip Morris' property for the purposes of indirect expropriation. In Uruguay cigarettes manufacturers will only be able to sell one variety of cigarettes under each brand to prevent the rebranding of cigarettes as lighter and therefore healthier.[109]Once again, it is impossible to show that the value of Philip Morris' business in Uruguay has been reduced to nothing. The Uruguayan measure also does not prohibit all branding on cigarettes but merely increases the size of the warnings against the dangers of smoking. Even if the intellectual property of the cigarette brands could be

[109] *Philip Morris v Uruguay. Ibid.* Para. 6.

separated from the ownership of the other parts of the investment, the value of the intellectual property has not been effectively neutralised.

Alternatively, the wording of the Uruguayan BIT could empower the tribunal to consider the measure following the police powers approach. While there are no cases where the protection of public health has justified an expropriation without compensation, there is evidence that tribunals would afford a wide latitude to states to act.[110]Furthermore, it can be contended that the Uruguayan measures are of a general, non-discriminatory nature and therefore fall into the police powers of the Uruguayan state.

A key question of the case-law is: when the tribunals referred to the word 'property' are they referring to the property in its entirely or to specific aspects of it? The word 'property' has been used by the tribunals to refer to the totality of the investment and by Philip Morris to refer to the intellectual property contained within the packaging of cigarettes. From the point of view of an investor-state tribunal, the intellectual property of an investor is just another part of their wider property which is protected under international customary law and international investment treaties. The substantial interference in one aspect of the investor's property will not constitute an indirect expropriation while the value of the investment has not been reduced to near worthlessness.

It therefore seems that whether we consider the measure following the SED or the PPD approach, it seems likely that Philip Morris would lose its cases on their merits. While the Australian litigation has been resolved by the tribunal declining jurisdiction due to abuse of process, at the time of writing[111] the Uruguay litigation goes on. If we can say with some certainty that Philip Morris would lose its cases, can we say that the current law of expropriation is adequate? I will present a problem which suggests it is not.

4.4. A Case for Reform of the Law of Indirect Expropriation

It would appear from the current case-law that the measures introduced by Australia and Uruguay would not give rise to an expropriation. However, if a state wish to ban tobacco products in their entirety, the current case-law leaves it open to argue that such a measure would be an indirect expropriation. While at the time of writing, only one state (Bhutan) has

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[110] NEWCOMBE, A. & PARADELL, L., *Ibid.* Para. 7.24(ii)

[111] June 2016.

outlawed tobacco completely[112], it is not inconceivable that within a number of decades, states like Australia may wish to prohibit the sale of cigarettes. It is possible that a measure outlawing the sale of tobacco products could constitute an indirect expropriation. While the investor would remain in control of their investment in name, the whole infrastructure of cigarette manufacture and distribution would become worthless. It is possible to envisage a measure with this effect amounting to a substantial deprivation of the investment and therefore an indirect expropriation.

Whether the prohibition of the sale of cigarettes would amount to an indirect expropriation is controversial. States prohibit and restrict the sale of products all the time and there has been no case so far that has held that such general regulatory measures would amount to an indirect expropriation. A WTO case that may provide some insight into how a tribunal could consider the question of indirect expropriation in this case is the *Asbestos case*[113]. The Appellate Body reaffirmed the right of states to protect their citizens from the health effects of asbestos as they see fit without discussion of compensation for the asbestos manufacturers.[114]

However, the TTP treaty states may request the non-applicability of the investment chapter to tobacco regulation.[115] This is true even if a dispute is on-going with a tobacco manufacturer. The fact that tobacco was excluded from the investor-state chapter could suggest that states do not think they could win a challenge to further tobacco regulation, at least without more costly and time-consuming litigation. Clearly while this approach solves the problem for states for tobacco, it leaves the problem unresolved for the rest of the economy. A more comprehensive approach would be to clearly delimit the types of regulation that will not give rise to a finding of indirect expropriation.

Having said this, there has been no case brought against a state for a prohibition of this nature brought in an international tribunal. As I have endeavoured to show, the law of indirect expropriation is very unclear and it is possible to make arguments in favour of compensation. The distinction between legitimate government regulation which does not give rise to a duty

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112 Bhutan. Tobacco Control Act 2010, 16 June 2010

113 *European Communities — Measures Affecting Asbestos and Products Containing Asbestos.* Appellate Body Report DS135. 12 March 2001

114 *EC – Asbestos. Ibid,* Para. 168.

115 Australian Government. Trans-Pacific Partnership Treaty [online]. 2016. Chpater 9. Article 29.5. [viewed: 22 June 2016]. Available at: <http://dfat.gov.au/trade/agreements/tpp/official-documents/Pages/official-documents.aspx>

to compensate investors and indirect expropriation which does ha s been criticised as artificial:

> "Is this distinction intellectually viable? Is not the State in both cases (that is, either by taking for a public purpose [indirect expropriation], or by regulating) purporting to act in the common good? And in each case has the owner of the property not suffered a loss?"[116].

Where is the line drawn between those takings that are compensable and those that are not? Until that line can be drawn with clarity, states cannot be sure that they would win a challenge to a prohibition of cigarette sales. This is especially true considering t hat cigarette manufacturers are extremely well-financed and can afford to challenge attempts to regulate at multiple levels of national and international law. This result seems wrong, after all; is the protection of human health not one of the prime responsibilities of states? It would seem that states face the unappealing choice of either allowing investment activities which are damaging to society or compensating investors to remedy these problems.

Another reason that reform is desirable is because under the current law of indirect expropriation, cases have been very long and very expensive. The Australian litigation started in early 2011 and the redacted judgment was not delivered until May 2016. In addition, the Australian government estimates that it has spent A$50 million (€32 million) defending the Philip Morris case[117]. This sum would have been even higher had the case proceeded beyond the jurisdiction phase. The Uruguay case started even earlier, in March 2010, and a judgment still has not been delivered as of June 2016.

4.5. Appropriation in Indirect Expropriation

One suggestion to resolve the issue of government regulation is to consider whether there has been any appropriation of property by the host government.[118] In a series of cases, it has been

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[116] HIGGINS, Rosalyn. The Taking of Property by the State. *Recueil des Cours.* 1982 III, vol 176, p. 331. 117 The Sydney Morning Herald. *Australia faces $50m legal bill in cigarette plain packaging fight with Philip Morris* [online]. 28 July 2015 [visited: 14 June 2016]. Available at: <http://www.smh.com.au/federal-politics/political-news/australia-faces-50m-legal-bill-in-cigarette-plain-packaging-fight-with-philip-morris-20150728-gim4xo.html>

[117] The Sydney Morning Herald. Australia faces $50m legal bill in cigarette plain packaging fight with Philip Morris [online]. 28 July 2015 [visited: 14 June 2016]. Available at:<http://www.smh.com.au/federal-politics/political-news/australia-faces-50m-legal-bill-in-cigarette-plainpackaging-fight-with-philip-morris-20150728-gim4xo.html>

[118] NEWCOMBE, A., The Boundaries of Regulatory Expropriation in International Law In KAHN, P. & WÄLDE, T., *Les aspects nouveaux du droit des investissements internationaux.* 2007. Leiden: Brill. P. 391. ISBN13: 978-90-

long established that the fact that the host country was not directly enriched by the expropriation, does not affect its classification as an expropriation[119]. However, A. Newcombe highlights a series of early cases which challenges this orthodoxy.[120] For example, he points out that the cases of the *Norwegian Shipowners Claims*[121] and the *Certain German Interests in Polish Upper Silesia*[122], are traditionally cited as founding the rule that the state does not need to be enriched by its expropriation. However, in bot h of these cases there was a corresponding appropriation of the property by the state[123]. This test, when applied to the introduction of plain packaging for cigarettes, precludes the measure being characterised as an expropriation. The Australian or Uruguayan governments have not appropriated Philip Morris' intellectual property for their own use.

At paragraph 2(d) of article 8 of the draft TTIP text, tribunals are asked to consider the following when determining whether an indirect expropriation has taken place: "The character of the measure or series of measure, notably their object, content and intent".

We can see from the above, 2(d) requires that a tribunal considers the purpose of the legislation which has been passed. Presumably if the intent of the measure is not expropriatory, then the tribunal should find that it does not violate the TTIP. This has been described as problematic because the expression of intent of a state to expropriate property is in the case of indirect expropriation, excluded by definition[124]. It is also difficult to factually prove that a state had the intent to expropriate the investor's property.[125]

4.6. The Draft TTIP Proposals for Indirect Expropriation

The TTIP being negotiated between the US and the EU is an example of a new generation of agreement which aims to resolve the problems identified with traditional BITs. In doing so, they have abandoned reliance on the SED and expressly purport to introduce a variation of

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0415-3721.

[119] NEWCOMBE, A., *Ibid.* P. 401.

[120] NEWCOMBE, A., *Ibid.* P. 403.

[121] *Norwegian Shipowners' Claims (Norway v US)* (1922) 1 UNRIAA 307. 332.

[122] *Certain German Interests in Polish Upper Silesia (Germany v Poland)* (1926) PCIJ. Series A., No. 7.

[123] NEWCOMBE, A. *Ibid.* P. 403.

[124] KRIEBAUM, U., FET and Expropriation in the Comprehensive Economic Trade Agreement between the European Union and Canada. *Transnational Disputes Management*. March 2016, vol. 13, núm 1, p. 10.

[125] KRIEBAUM, U., *Ibid.*

PPD which considers the proportionality of the government measure taken. The aim of the draft TTIP is clear; to restrict the situations when a tribunal can find an indirect expropriation. However, the manner in which it tries to do this tends more to increase uncertainty.

At article 5 of section 2 of chapter 2 of the TTIP text replicates the classic formulation of expropriation:

> "1. Neither Party shall nationalize or expropriate a covered investment either directly or indirectly through measures having an effect equivalent to nationalisation or expropriation (hereinafter referred to as 'expropriation') except:
>
> (a) for a public purpose;
>
> (b) under due process of law;
>
> (c) in a non-discriminatory manner; and
>
> (d) against payment of prompt, adequate and effective compensation".[126]

A replication of the formulation of expropriation as it appears in traditional BITs already presents a problem. By repeating the wording of previous bilateral agreements, the provisions invites the tribunal to call upon the existing case-law of expropriation. This is a case-law which is very unclear and inconsistent. Faced with this problem the provision continues: "2. For greater certainty, this paragraph shall be interpreted in accordance with Annex I" [on expropriation].

The use of the phrase 'For greater certainty' is once again problematic. It suggests that the law of expropriation is already certain and the annex is merely a guide on how to inter pret some of the finer points of this area of law. As I have endeavoured to show, the classic formulation is anything but certain. Therefore the annex will become a vital tool in order to give some clarity to this area of law.

The annex[127] states:

> "ANNEX I: Expropriation
>
> The Parties confirm their shared understanding that:
>
> 1. Expropriation may be either direct or indirect:

[126] European Commission. *Commission draft text TTIP – investment* [online]. 12 November 2015 [visited:18 June 2016]. Available at: <http://trade.ec.europa.eu/doclib/press/index.cfm?id=1396>

[127] European Commission. *Commission draft text TTIP – investment* [online]. 12 November 2015 [visited:18 June 2016]. Annex I: Expropriation. Available at: <http://trade.ec.europa.eu/doclib/press/index.cfm?id=1396>

(a) direct expropriation occurs when an investment is nationalised or otherwise directly expropriated through formal transfer of title or outright seizure.

(b) direct expropriation occurs where a measure or series of measures by a Party has an effect equivalent to direct expropriation, in that it substantially deprives the investor of the fundamental attributes of property in its investment, including the right to use, enjoy and dispose of its investment, without formal transfer of title or outright seizure.

2. The determination of whether a measure or series of measures by a Party, in a specific fact situation, constitutes an indirect expropriation requires a case-by-case, fact-based inquiry that considers, among other factors:

(a) the economic impact of the measure or series of measures, although the sole fact that a measure or series of measures of a Party has an adverse effect on the economic value of an investment does not establish that an indirect expropriation has occurred;

(b) the duration of the measure or series of measures by a Party;

(c) the character of the measure or series of measures, notably their object and content.

3. For greater certainty, except in the rare circumstance when the impact of a measure or series of measures is so severe in light of its purpose that it appears manifestly excessive, non-discriminatory measures of a Party that are designed and applied to p rotect legitimate public welfare objectives, such as the protection of public health, safety, environment or public morals, social or consumer protection or promotion and protection of cultural diversity do not constitute indirect expropriations".

The first paragraph appears to codify the approach tribunals have taken when considering the SED. It echoes the traditional BIT wording by specifying measures having 'effect equivalent' to an expropriation. It also codifies the substantial deprivation test by recalling the formulation of this test by some tribunals as one where an investor is denied the 'fundamental attributes' of property. If this article was the only provision of the annex, tribunals could feel empowered to follow the line of cases encapsulating the SED. In this way, at least the uncertainty around this law would be reduced. Tribunals would also know within which conceptual framework they should be debating interpretations of the law.

However, this is not the case. Paragraph two states that expropriation should be considered through a 'case-by-case, fact-based enquiry'. The provision then goes on to say that the tribunal should consider the economic impact, duration and character of the measure. It also contains what seems to be an explicit rejection of the SED by specifying that the mere fact that a measure substantially deprives an investor of their investment is not enough to establish an indirect expropriation. By asking a tribunal to consider each case as different could undermine a key aim of the TTIP; to provide greater consistency to the law.

It could also create unnecessary litigation. When the law is unclear parties tend to litigate on every point. This is what happens in investor-state arbitrations contributing to their slowness and expense.[128] By reiterating that the considerations of the cases must be done individually and through a fact-based inquiry, these tendencies are exacerbated. It is of course possible that this paragraph is superfluous. Like any court, international tribunals already carry out case-by-case, fact-based inquiries.

Paragraph three seems to codify the approach that tribunals have adopted when following the PPD approach to indirect expropriation. As well as this, it appears to invite a tribunal to consider the proportionality of the measure. If the measure is ‘manifestly excessive’ to its aim then there will have been an expropriation. This adds another element of uncertainty into the article. When will a measure be ‘manifestly disproportionate’? While there are many examples of tribunals considering the proportionality of a measure with its aims in international law, the phrase ‘manifestly’ is not used to describe a measure disproportionate to its aims.[129]

Each of the paragraphs of the TTIP formulation could be a method to determine whether there has been an indirect expropriation of property on their own. How each paragraph relates to the other, and which should be given precedence by a tribunal in the case of conflict between them is extremely unclear. Each one seems to codify approaches taken by tribunals under the different doctrines of SED and PPD. Rather than clarifying by choosing one approach, the TTIP codifies the confusion and inconsistency of the current case-law.

Having said that, it should be said that there is EU case-law which does touch upon the proportionality of measures to their aims. In particular, an annex to the Treaty on the Functioning of the European Union (‘TFEU’)[130] mandates that the economic impact of a measure must be taken into account when European legislation is passed.

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[128] UNCTAD. Reform of Investor-State Dispute Settlement: In Search of a Roadmap. *IIA Issues Note*, No. 2. June 2013. P. 4.

[129] DOLZER, R. & SCHREUER, C., *Ibid.* P. 115.

[130] European Union. TFEU 2010/C 83/01. Protocol (No 2) on the application of the principles of subsidiarity and proportionality. Article 5.

An example of the importance of this provisions is shown by the challenge to Commission Directive 2014/40[131] in the Court of Justice of the European Union ('CJEU') brought by Poland.[132] The Directive more tightly regulates various aspects of tobacco sales including banning mentholated cigarettes. One of the assertions of Poland was that this ban was disproportionate to the aim of protecting human health.[133] The court noted that the EU legislature had noted the possible negative economic social effects of the measure and had enacted ways by which these negative effects would be limited.[134] The fact that the legislature considered the economic impact on tobacco producers and sought to limit them was considered by the court as strong evidence that the measure was proportionate.[135] This example shows us how current EU law does not consider that investors should be compensated for measures which negatively affect them. It also leaves the political decision to balance the competing interests of general and society and investors to elected politicians.

Faced with the confusion of the TTIP in its current draft, it is impossible to predict how the hypothetical example of the complete prohibition of tobacco products would be considered. I have considered the approach as should be considered under the SED, an approach which is arguably the correct one under the current formulation of indirect expropriation. I will now consider the element of proportionality, as it is contained in the TTIP.

4.7. Proportionality in Indirect Expropriation

An interesting case which demonstrates how the TTIP proportionality could consider a prohibition of tobacco is provided by *Philip Morris v Norway*[136] case held under the European Economic Area (EEA) Agreement. This agreement provides for free trade between the European Union and Liechtenstein, Norway, and Iceland. It applies the European Union treaties and applies the same rules as the CJEU and is thus an illustrative example of European jurisprudence in this area.

[131] OJ L 127/1

[132] Case C-358/14. *Poland v Commission.* [2016]. ECLI:EU:C:2016:323

[133] Case C-358/14. I*bid*. Para. 73.

[134] Case C-358/14. *Ibid*. Para. 99.

[135] Case C-358/14. *Ibid*. Para. 102.

[136] *Philip Morris Norway SA v Staten v/Helsen.* EFTC. Judgment of the Court. 12 September 2011. E-16/10

The case concerned a measure taken by Norway to ban all point of sale advertisements of cigarettes and tobacco products in its territory. While this measure falls short of a total ban of tobacco in a jurisdiction, it does illustrate the legal tests that could be used to determine whether there is an indirect expropriation.

In the Norway case the European Free Trade Association Court found that such a ban was indirectly discriminatory against products coming from within the EEA and could only be justified under article 13 of the Agreement of the EEA. This article allows measures having discriminatory effect if they were both for a legitimate public good and proportionate to achieve this good. On this point the court said:

> "In the area of human health EEA States should enjoy a wide margin of discretion. Accordingly, in the present case, it is not enough for the Plaintiff to allege that no evidence can be produced to support the argument that a visual display ban influences tobacco consumption. Instead, it suffices to show, as the Defendant has done, that there are reasonable grounds to assume that the display ban will have an effect on consumption".[137]

As we can see from the above formulation, this is a test which does not demand that a state actually shows that the measure will reduce consumption but that there are reasonable grounds to assume it does. When considering the issue of proportionality in the EEA the measure must be the least restrictive measure to the circulation of goods available to meet the public welfare objective. This is a higher test than that which is contained in the TTIP where the disproportionality of the impact of the measure must be 'manifestly excessive'.

However, even considering a higher test contained in the TTIP, the EFTA Court can give useful guidance to tribunals. When considering the jurisprudence of proportionality in the EEA, the court stated:

> "[…] that an assessment of whether the principle of proportionality has been observed in the field of public health must take account of the fact that an EEA State has the power to determine the degree of protection that it wishes to afford to public health and the way in which that protection is to be achieved".[138]

[137] *Philip Morris Norway SA v Norway*. European Free Trade Association Court. E-16/10. Judgment of the Court. 12 September 2011. Para. 72.

[138] *Philip Morris Norway SA v Norway*. *Ibid.* Para 80

I would submit that here the EEA formula is a step in the right direction to balance the competing demands of states and investors. States are left to carry out the sovereign functions of determining which public welfare objectives should be prioritised and the manner in which they will be achieved. In the case of there being no relation between the measure taken and the public good or of its being manifestly excessive in its impact on an investor, that investor will receive compensation to the degree that their property has been indirectly expropriated.

When applied to the example the complete prohibition of tobacco, this reaffirmation of the state's power to set the priorities for legislation is welcome. While one state may prioritise human health and ban smoking completely, another state may prioritise tax revenue growth and be involved in the sale and distribution of cigarettes. The key would be for the state to correctly phrase the public welfare they are trying to achieve. For example, if a state says that it is merely trying to reduce tobacco consumption, it may be open to a tribunal to say that a complete prohibition of the sale of cigarettes is manifestly disproportionate.

On the other hand, if a state says that it wishes to reduce the number of smoking-related deaths to zero, a complete ban on all tobacco products would seem a necessary step to achieving this. The European jurisprudence on proportionality shows us that it is not open to tribunals to question the legislative priorities of the state. The TTIP formulation of proportionality can restrict tribunals' role to testing that there has been no protectionist behaviour in the guise of protecting human health by seeing if there is a logical connection between the aim and the measure and the measure is not manifestly excessive. Providing there is a logical connection between the aim and the public welfare attempting to be achieved, a measure to ban cigarettes would seem to be permitted under a proportionality test of this type.

At this point it is convenient to highlight the limits to help which European jurisprudence can help tribunals considering the TTIP. European law uses different principles than international investment law. In particular it applies a much stricter rule of proportionality than the wording of the TTIP would allow. For example, in the *Scottish alcohol case*[139] the tribunal struck down legislation establishing a minimum price of alcohol. The tribunal established that the measure disproportionality affected alcohol imported from other EU states and was therefore a restriction on trade.[140]It then fell to the tribunal to decide whether this restriction on trade was proportionate to the Scottish government's public health objective (reducing hazardous

[139] C333-14. *Scotch Whisky Association v Scotland.* [2015]. (not yet published)

[140] *Scottish alcohol case. Ibid.* Para. 24.

alcohol consumption). The CJE decided it was not because there are other less restrictive means of achieving a reduction in the number of people drinking alcohol to hazardous levels such as general taxation on alcoholic drinks.[141] This test is well-established in EU case-law and fits within the constitutional structure of the democratic institutions of the EU. International tribunals will only be empowered to order compensation for that legislation which is manifestly excessive. 'Manifestly excessive' is a much higher level than in EU law and tribunals would be unwise to follow too closely EU case-law in this respect.

5. CONCLUSIONS

In conclusion, the cases brought against Uruguay and Australia by Philip Morris illustrate many important questions for the law of investor-state disputes. Current case law significantly weakens the jurisdictional protections contained for states. It also weakens the domestic litigations requirements which require an investor to seriously engage with the domestic legal system of the host nation. Additionally, the cases show how the law of FET must not be allowed to impose an impermissible restraint on the ability of states to legislate.

While the law of expropriation remains unclear and contradictory, a number of common elements can be drawn out. Firstly, the taking of the property must be substantial, meaning nearly complete. Secondly, tribunals have usually considered the effect on the property as a whole, not as individual parts of property. Thirdly, in certain circumstances customary international law allows states to take property for public purposes without the payment of compensation.

As I have previously stated, the weight of authority seems to suggest that Philip Morris will not win its cases for expropriation. However, as I have also highlighted, this result comes after years of litigation which has cost the Australian and Uruguayan taxpayers millions of dollars. The fact that Philip Morris was even able to advance its case is evidence enough of the need for reform.

The TTIP investment chapter goes some way to advancing this reform. It clearly tries to exclude general regulatory measures from being considered expropriations in all those except the most exceptional cases. This is a more comprehensive approach to reform than that followed in the TTP where tobacco regulation can simply be excluded from the investment

[141] *Scottish alcohol case. Ibid.* Para 46.

chapter. However, the manner in which it does this serves only to reinforce the conflicts and confusion which is at the heart of the current law of expropriation. It calls upon the case-law of tribunals which have adhered to both the SED and the PPD. In goes on to reiterate that every case should be considered individually, a formulation tending towards unnecessary litigation.

Fundamentally a political decision needs to be made to what extent states wish to protect property at the expense of their ability to regulate. The SED embedded in the traditional formulation of BITs is not accidental. They were designed in a period when countries were newly independent and asserting their sovereignty over their natural resources. [142]During this period many countries denied that there was even a rule of customary international law to compensate investors for expropriations.[143] The formulation of BITs was in direct opposition to these trends and codifies a very strong defence of investor's property rights.

The world has changed since then. These agreements have been signed by every country in the world yet the wording of the BITs remains unchanged from the original treaties, drafted in the 1960s in a particular political context. Furthermore, traditionally capital-exporting countries in the developed world are now importers of capital as well. The obligations that for a long time have only been felt by developing countries are now felt everywhere. It has become clear that for many people, the privileging of the protection of property over the state's right to regulate which is contained in these BITs is neither necessary nor desirable.

[142] NEWCOMBE, A. & PARADELL, L., *Ibid.* 1.14

[143] Institute for Sustainable Development. NIKIÈMA, Suzy. *Compensation for Expropriation* [online]. March 2013 [viewed: 7 January 2017]. P. 1. Available at: <http://www.iisd.org/pdf/2013/best_practice_compensation_expropriation_en.pdf>

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