International

Legal Protection in International Tax Disputes – How Investment Protection Agreements Address Arbitration

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The authors, in this article, examine whether or not international tax disputes can fall within the scope of bilateral investment protection agreements and, if so, to what extent and under what circumstances.

1. Introduction: Inadequacies of Legal Protection under Tax Treaties

Tax treaties have long been considered the best way of avoiding double taxation in international relationships. The division of taxation between states envisaged by such treaties is generally based on the internationally accepted principles and methods laid down in the OECD Model (2010) and its Commentary. [1]

OECD Member countries are overwhelmingly affluent with a high per capita income. Large emerging economies, such as Brazil, India and China, have yet to be admitted to the OECD club. Their emergence has meant that multinational companies increasingly regard investment in these countries as important and recent decades have seen this importance grow. At the same time, these countries have increasingly become more economically self-aware.

In practice, examples of foreign investment in these emerging economies show that particular attention is being paid to the situs principle when exercising the right to taxation. This involves, in particular, the unusual practice of levying withholding taxes on capital gains that are indirectly related to assets located in the country in question. This tax is levied as a withholding tax in the hands of the buyer. There are numerous examples of situations where the interpretation of accepted international tax concepts, such as that relating to permanent establishments (PEs), deviates from prevailing international standards.

Confronted with such forms of taxation, a foreign business will, of course, first and foremost try to reverse its effects by taking advantage of the legal recourse available in the relevant country. However, domestic courts are not always completely independent, and even if this is the case, it is possible that the court will share the view of international standards and conventions held by the domestic tax authorities.

Multinational companies will, therefore, also consider remedies other than recourse to the domestic courts. In this respect, tax treaties offer an alternative, as they generally provide for mutual agreement procedures between the competent authorities of the contracting states. [2] Most tax treaties do not contain a requirement to achieve results in regard to the mutual consultation procedure, only to use best efforts. Such a mutual consultation procedure, therefore, does not automatically result in the states involved reaching agreement or an acceptable outcome for the taxpayer, who is not a party to the procedure.

For this reason, an arbitration clause [3] was drafted for inclusion in the OECD Model (2010). The arbitration clause makes arbitration compulsory if the competent authorities cannot successfully reach a comprehensive solution to the dispute. The aim is to include such a compulsory arbitration clause in new and previously concluded tax treaties. The Netherlands has included such a clause in the recently concluded tax treaties with the United Kingdom [4] and Japan. [5]

Nevertheless, it will be some time before a compulsory arbitration clause is included in most tax treaties. Notwithstanding this fact, the current issue is just how effective such a clause will be given that there has, to date, been little experience with such arbitration. Moreover, it is not completely clear how such a clause will be put into practice. For example, how will the arbitration tribunal be appointed and, if the number of arbitration cases were to increase, would it not be preferable to have the appointment of the tribunal fall under the auspices of an international body?

International tax disputes do not, however, appear to be solely governed by tax treaties and the procedures prescribed therein. States also conclude investment protection agreements in respect of cross-border investment, the aim of such agreements being to protect investments. In the event of a dispute, the World Bank's International Centre for Settlement of Investment Disputes (ICSID) can be requested to appoint an arbitration tribunal. The investor involved, rather than the contracting states, can make such a request.

This article examines whether international tax disputes can fall within the scope of bilateral investment protection agreements and, if so, to what extent and under what circumstances.

2. A Review of Investment Protection Agreements

2.1. Nature and content of investment protection agreements

The first bilateral investment protection agreement was concluded in 1959 between Germany and Pakistan. [6] The current investment protection agreement network includes more than 2600 [7] bilateral treaties, as well as a large number of multilateral investment treaties. The network of investment treaties, therefore, provides broad coverage. Often, a bilateral investment protection agreement is concluded with countries with which a tax treaty has yet to be concluded; this is, for example, the case for the Netherlands.

While tax treaties are mostly based on the OECD Model (2010), there is no such generally accepted model available for bilateral investment protection agreements. [8] Numerous countries, including the Netherlands, [9] do, however, have their own model agreement. [10] More comprehensive agreements also include provisions similar to those included in investment protection agreements. [11] As such, the legal form of investment protection agreements can differ. [12] Despite this difference, investment protection agreements often adopt a similar structure, pursuant to which investments are stimulated and protected by means of comparable guarantees. [13]

This can be explained by the fact that the letter and spirit of every investment protection agreement is ultimately the same: the creation of a favourable investment climate by protecting and stimulating investments. [14] [15] The provisions of nearly all investment protection agreements, therefore, provide for the *protection* of investments (against expropriation and unreasonable treatment), liberalization (the abolition of legal limitations, such as prohibitions on investment) and the creation of a level playing field (for example, non-discrimination, equal treatment). [16]

In general, the letter and spirit of an investment protection agreement is realized through a number of substantive rights. [17] First and foremost, expropriation is prohibited unless the expropriation is non-discriminatory and in the general interest. In that event, the affected investor is entitled to adequate compensation. [18] Second, investors are entitled to have their investments treated in a fair and equitable manner and to complete protection and security. [19] Third, the investment protection agreement guarantees equal treatment and prohibits discrimination based on nationality. A most-favoured-nation (MFN) clause is often included. [20] Fourth, the investment protection agreement protects the repatriation of income earned from the relevant investments. [21] Fifth, a bilateral investment protection agreement can include a reference to prevailing international law; in this respect, elements of international law that are more favourable than the provisions included in the relevant investment protection agreement are given preference over the provisions in the investment protection agreement. [22] A final means of protection is offered by the umbrella clause, [23] which requires the contracting states to fulfill all the undertakings given in respect of an investment. [24] By means of these substantive rights, contracting states can guarantee investors that their investments will be free of certain risks. [25]

2.2. Legal protection: investor v. state proceedings before an independent tribunal

In addition to these substantive rights, investment treaties also contain procedural rights that make the realization of substantive rights possible. [26] The legal structure of the investment protection agreement allows the aggrieved party to directly, i.e. without government intervention, enforce its rights by means of an arbitration tribunal specifically appointed for that purpose. [27] This differs considerably from the situation under tax treaties, where disputes must generally be resolved through a mutual agreement procedure in respect of which the interested parties have little or no influence. However, a procedure under an investment protection agreement allows the interested party to maintain control over all facets of the procedure, from commencement of the action to the hearing itself. [28] This can be particularly advantageous if the country in which the investment was made cannot provide fair and balanced legal protection due to, for example, corruption and the absence of an independent judiciary. [29] In such a situation, an investment protection agreement guarantees permanent and adequate legal protection.

The investment protection agreement designates the body, or bodies, that are competent to decide investment disputes under the applicable agreement. In most cases, an arbitration tribunal appointed by the ICSID is opted for. [30] More than 140 countries recognize the ICSID. [31] Case law on the application and interpretation of investment treaties does not serve as a precedent in regard to each and every individual investment protection agreement due to the fact that investment protection agreements can differ and case law on the application and interpretation of these agreements comes from different bodies. Case law does, however, provide a guideline for the interpretation of these agreements. Investment protection agreements are similar in a lot of ways, the letter and spirit of the agreements being the same and, therefore, the competent tribunals will interpret them according to the Vienna Convention on the Law of Treaties. [32]

2.3. Accessibility of investment protection agreements

Three things are necessary to successfully invoke the protection offered by an investment protection agreement: (1) a qualifying investment in the territory of one of the contracting states, made by (2) a qualified investor from the other contracting state, in respect of whom (3) an obligation contained in the investment protection agreement has been violated. Almost all investment treaties contain a provision defining "investment". [33] The definition is generally broad, such as, "every kind of asset invested in accordance with the national laws and regulations of the Contracting Party in the territory of which the investment is made" [34] or "every kind of asset", [35] followed by a non-exhaustive list of examples of qualifying investments. [36] [37] It is not surprising that the broad definition of "investment" has led to it being broadly interpreted in the case law. [38] Arbitration tribunals have shown that they are prepared to give as broad an interpretation as possible to ensure the scope of protection provided in regard to investments is extensive. [39] In particular, the investor activities must be assessed on an aggregate basis: if the activities consist of separate elements that are only considered an investment when viewed jointly, then protection under an investment protection agreement is possible, even if only one of those elements has been breached. [40] A territorial factor must also be present for an investment to qualify. The investment must be attributable to one of the contracting states, i.e. there must be a sufficient nexus with the host country. This requirement is also interpreted broadly in the case law. [41] This is evidenced by the fact that a large number of treaties include a provision that makes the agreement applicable to investments that are indirectly held by way of a business resident in a third state. [42] [43]

The next issue that arises after a particular investment has been found to be covered by the agreement is whether or not the holder of the investment has access to the investment protection agreement. Traditionally, the definition of "investor" included in most investment treaties applies to natural persons, legal entities and partnerships. [44] Natural persons qualify as an investor if they hold the nationality of one of the contracting states. This must be determined according to the domestic law of the relevant state. [45] Different combinations of different criteria are used to determine if a legal entity or partnership qualifies as an investor. This includes the place of incorporation [46] and where control [47] is exercised.

A more detailed discussion of investment protection agreements is beyond the scope of this article. Previously published literature on the topic should, therefore, be referred to. [48]

3. Taxation under Investment Protection Agreements

3.1. In general

Having outlined the general contours of a bilateral investment protection agreement, section 3. discusses whether or not such an agreement can provide protection in regard to tax measures. As previously described, in certain cases, the legal protection provided by a tax treaty is inadequate. The additional legal protection provided under an investment protection agreement can, in these circumstances, be of great significance.

In most countries, autonomous tax policy, in particular the right to taxation is a sensitive subject. This also finds expression in investment protection agreements. In general, states will be wary of possible, undesired limitations being placed on taxation as a result of an investment protection agreement. [49] This concern manifests itself in a number of investment protection agreements through the inclusion of a carve-out provision [50] that excludes the applicability of the agreement in its entirety in cases of taxation. However, numerous other agreements only include a partial exclusion. [51] The protocol to the Germany–Mexico investment protection agreement [52] states that tax measures that violate provisions of an investment protection agreement, other than those provisions relating to national or MFN treatment, can be subject to arbitration. [53]

3.2. Taxation as a form of indirect expropriation under investment treaties

The definition of expropriation in investment protection agreements usually follows the definition found under international law. [54] Expropriation [55] can occur both directly and indirectly. [56] Direct expropriation occurs if the investment is nationalized or otherwise directly confiscated by means of a legal transfer of ownership or a direct physical takeover. [57] Indirect expropriation occurs when a state interferes in the use of an investment or in the benefits received from that investment, even if the investment has not been physically seized and the legal ownership of the good has not been affected. The effect of such government action is equal to that of expropriation. A governmental measure can also qualify as indirect expropriation if the investment's market value decreased as a result thereof, [58] or if the economic benefit that could reasonably be expected was denied. [59] Direct expropriations are, however, rare; indirect expropriations are more common. [60]

Taxation [61] represents, in principle, a partial breach of property rights. As such, most forms of taxation could be contested by invoking an investment protection agreement, although this could not reasonably be expected to be the intention of such an agreement. [62] As a general rule, taxation does not qualify as expropriation under international law. [63] Under international law, a state cannot, in principle, be held liable for loss of ownership as a result of a bona fide tax that is generally accepted as a legal expression of the executive power of a government. [64]

3.2.1. In exceptional circumstances a tax measure does qualify as expropriation

This does not mean that taxation cannot fall under the scope of the definition of expropriation. In certain circumstances, taxation can constitute expropriation under international law, [65] [66] [67] as a result of which a tax dispute between a tax authority and an investor can be resolved by arbitration. [68] In *Link Trading v. Moldova* (2002), the arbitration tribunal ruled that taxation can be considered an expropriation if the nature of the tax involves "abusive taking". According to the tribunal, a tax is considered "abusive taking" if it is unreasonable, arbitrary, discriminatory or contrary to existing agreements. [69] In *Encana v. Ecuador* (2006), where a refusal to refund Ecuadorian VAT was in dispute, the tribunal concluded that taxation falls under the scope of the definition of expropriation if it can be qualified as "extraordinary, punitive in amount or arbitrary in its incidence". [70]

As a result of the current paucity of case law in regard to tax disputes, it can be concluded that two types of taxation can be identified under an investment protection agreement. Taxation that results in an indirect expropriation must be distinguished from taxation that, while having a substantial negative impact on the market value of the investment, nevertheless must be regarded as legitimate and, therefore, does not qualify as an indirect expropriation under an investment protection agreement. [71]

3.2.2. Assessment framework

Certain elements can be extracted from case law and the literature that, taken together, can create an assessment framework for distinguishing between bona fide tax measures and taxation that qualifies as expropriation. These are as follows: (1) the government measures must lead to a substantial decrease in value, (2) that interferes with the reasonable expectations underlying the investment and (3) deviates from internationally accepted norms (characteristics test). [72] [73] This assessment framework was confirmed in *Archer Daniels Midland v. Mexico* (2008), where the tribunal ruled that, as well as a substantial decrease in value or paralyzing government interference, other factors needed to be looked at:

> [...] including whether the measure was proportionate or necessary for a legitimate purpose; whether it discriminated in law or in practice; whether it was not adopted in accordance with due process of law; or whether it interfered with the investor's legitimate expectations when the investment was made. [74]

In the *Revere Brass and Copper* (1978) case, [75] the arbitration tribunal ruled that mining tax and royalties, imposed in violation of a concluded advance tax ruling, qualified as expropriation. The ruling formed part of a concession given to a subsidiary for the extraction of bauxite in Jamaica. The newly elected government, however, ignored the ruling and increased the tax burden by introducing a new mining tax. Revere considered the negative impact on profitability excessive and ended its subsidiary's activities. The arbitration tribunal recognized that Revere's subsidiary still had full ownership and could have continued with its activities but regarded the matter as an expropriation under international law because Revere could no longer make an economically effective use of the business, i.e. the profitability of the investment was severely impaired.

3.2.3. Substantial financial damages

While it is difficult to determine what damage must result from a tax measure for it to qualify as expropriation, general agreement does exist on the fact that the bar is set very high. [76] The United

Nations Conference on Trade and Development (UNCTAD) considered that this must include "a significant depreciation". [77] In addition, it is argued that a partial proportional relationship must exist between the assessment framework's criteria, so that if a measure is extremely discriminatory or absurd, the extent of financial damage will need to be less than for a more common measure. [78] In *Occidental v. Ecuador* (2004) [79] the tribunal again dealt with a refusal by the Ecuadorian tax authorities, contrary to earlier agreements, to refund VAT. The taxpayer, i.e. the investor, invoked the expropriation clause of the investment protection agreement. According to the tribunal, the refusal did not qualify as expropriation since it did not deprive the taxpayer of the economic benefits that were reasonably to be expected or inflict substantial damages on the investment. The tribunal came to this conclusion because the right to a VAT refund was not a substantial part of the investment. [80] The previously cited *ADM v. Mexico* case is one of the few rulings that attempt to define the criterion for damages. The tribunal concluded that the damage criterion, i.e. the criterion that, according to the tribunal, is decisive, is met if the taxpayer is deprived of all or the majority of the benefits generated by the investment. Not only is the scope relevant but also the duration of the measure. A permanent loss of value will carry more weight than a temporary loss of value. [81]

3.3. Other provisions in international investment protection agreements providing legal protection against tax measures

3.3.1. Equal, national treatment under non-discriminatory provisions of an investment protection agreement

In section 2., the *ADM v. Mexico* case was referred to. This case involved a 20% tax imposed by Mexico on soft drinks containing a corn syrup sweetener. The tax did not apply to soft drinks sweetened with sugar cane. The reason for this measure appeared to have been the protection of the Mexican sugar cane market. As a result of this measure, ADM, a US manufacturer of corn syrup, saw a sharp decline in the value of its Mexican investments. ADM challenged the tax under the North American Free Trade Agreement (NAFTA – a multilateral investment protection agreement), one of the grounds being that the tax qualified as expropriation.

The arbitration tribunal applied the assessment framework described above and concluded that the impact of the tax on Archer Daniels' investments was not sufficient to constitute expropriation. However, the arbitration tribunal considered the tax a violation of the investment protection agreement, in particular, the non-discrimination provision that guarantees the domestic and equal treatment of foreign investments. The arbitration tribunal ruled that the effect of the tax was such that US manufacturers and distributors of corn syrup in Mexico received a less favourable treatment than Mexican manufacturers of sugar cane, as a result of which the tax violated the investment protection agreement. The ADM had invoked article 1102 of the NAFTA.

3.3.2. Fair and equitable treatment under an investment protection agreement

The *Occidental v. Ecuador* case, [82] in respect of which a decision was given under the US–Ecuador investment protection agreement (1993) is similar to the *ADM v. Mexico* case. Initially, the arbitration tribunal rejected a claim based on the expropriation provision, because revoking a right to a VAT refund did not qualify as expropriation. However, after further consideration, the revocation of the refund was considered to be an unauthorized violation of the investment protection agreement. The arbitration tribunal considered that the right to fair and equitable treatment [83] had been violated. This right to a VAT refund had been laid down in an agreement with the Ecuadorian tax authorities, which interpreted national legislation (the ruling). The arbitration tribunal emphasized that a consequence of the right to fair and equitable treatment is that the contracting states must provide investors with a stable and predictable legal infrastructure. The tribunal propounded this general principle even though it did not directly relate to the underlying issue, i.e. whether or not any legal right could be derived from the ruling. The tribunal also emphasized that this right gives rise to an objective obligation – whether or not the contracting state had acted in bad faith was irrelevant. Based on the underlying facts, the tribunal concluded that the legal structure in Ecuador, more specifically the domestic VAT legislation and its subsequent interpretation in a ruling, which had contributed to Occidental's decision to invest in Ecuador, had changed substantially. The tribunal concluded that, "[t]he tax law was changed without providing any clarity about its meaning and extent, and the practice and regulations were also inconsistent with such changes." [84] As such, the tribunal ruled that Ecuador had failed in its obligation to provide a stable and predictable legal system. The revoked refund, therefore, resulted in a violation of the existing investment protection agreement. [85]

4. Conclusions

In this article, the authors have shown that an investment protection agreement can provide protection

against certain forms of taxation. While the exact scope of the substantive rights included in an investment protection agreement are difficult to define in a tax context, partly due to the scarcity of case law on the subject, it is a fact that taxation can constitute a violation of the provisions of an investment protection agreement. In particular, the provisions on expropriation, non-discrimination and the right to a fair and equitable treatment set limits on the contracting states' right to taxation.

A qualifying expropriation is considered to have taken place if the tax results in a substantial decrease in the investment's value and if it also detrimentally affects the reasonable expectations of the investor, which formed the basis for its investment.

Moreover, a situation that deviates from internationally accepted legal standards must be present. The most obvious example of this is the principle of non-discrimination. The tendency in case law appears to be that the more flagrant the violation of such generally accepted legal principles, the less substantial the relative impact of the disputed government action on the investment needs to be in order to uphold the claim of the affected investor.

Future case law will have to determine whether or not, under certain circumstances, a violation of specific international tax principles can also be considered a deviation from internationally accepted legal standards, for example, taxation that is contrary to internationally accepted principles of taxation, in particular in respect of distinguishing between the right to taxation of the state of residence and source state. In such a situation, it is expected that the tribunal will apply a high standard. By this, the authors mean that the taxation will not only have to have a significant impact on the investment's value, but will also have to be at odds with the reasonable expectations of the investor at the time the investment was made. If both these conditions are met, it is conceivable that a tribunal will conclude that such taxation qualifies as indirect expropriation. What is interesting about legal protection under an investment protection agreement is that the affected business is, procedurally, a direct party to the arbitration and can instigate arbitration proceedings itself. This means that the business can exercise control over the proceedings. The generous legal protection offered by an investment protection agreement stands in stark contrast to arbitration under a tax treaty, which is still in the formative stages.

Arbitration under a tax treaty or an investment protection agreement does not necessarily have to be mutually exclusive. The competent authority in the state of residence can be requested to start mutual agreement proceedings – if necessary resulting in binding arbitration – under the relevant tax treaty, while, in principle, at the same time commencing proceedings under the existing investment protection agreement, although this may require that all avenues for domestic legal recourse have been exhausted first. In this respect, arbitration under an investment protection agreement can, at the very least, keep pressure on the mutual consultation procedure under the tax treaty.

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1. *OECD Model Tax Convention on Income and on Capital* (22 July 2010), Models IBFD.
2. Art. 25(5) *OECD Model* (2010).
3. Art. 25(5) *OECD Model* (2010), which provides that:

Where:

a)	under paragraph 1, a person has presented a case to the competent authority of a Contracting State on the basis that the actions of one or both of the Contracting States have resulted for that person in taxation not in accordance with the provisions of this Convention, and
b)	the competent authorities are unable to reach an agreement to resolve that case pursuant to paragraph 2 within two years from the presentation of the case to the competent authority of the other Contracting State,

any unresolved issues arising from the case shall be submitted to arbitration if the person so requests. These unresolved issues shall not, however, be submitted to arbitration if a decision on these issues has already been rendered by a court or

> administrative tribunal of either State. Unless a person directly affected by the case does not accept the mutual agreement that implements the arbitration decision, that decision shall be binding on both Contracting States and shall be implemented notwithstanding any time limits in the domestic laws of these States. The competent authorities of the Contracting States shall by mutual agreement settle the mode of application of this paragraph.

4. *Convention between the Government of the United Kingdom and Northern Ireland and the Government of the Kingdom of the Netherlands for the avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income and on capital gains, including a Protocol and Explanatory Memorandum* art. 25 (26 September 2008), Treaties IBFD (in force).

5. *Convention and protocol between the Kingdom of the Netherlands and Japan for the avoidance of of double taxation and the prevention of fiscal evasion with respect to taxes on income* art. 24 (25 Aug. 2010), Treaties IBFD. On 27 May 2011, the government sent Bill 32776, regarding approval of the tax treaty, to parliament.

6. J.W. Salacuse, *BIT by BIT: The Growth of Bilateral Investment Treaties and Their Impact on Foreign Investment in Developing Countries*, 24 Int'l L. pp. 655-675 (1990).

7. United Nations Conference On Trade And Development, *Recent Developments in International Investment Agreements* (2008-June 2009), IIA Monitor No. 3 (2009).

8. In the following, the term "investment protection agreement" refers to bilateral and multilateral investment agreements offering similar investment protection.

9. Available at: http://www.rijksoverheid.nl/onderwerpen/internationaal-ondernemen/documenten-en-publicaties/convenanten/2004/08/27/ibo-modelovereenkomst.html.

10. Such as the United States.

11. For example, *North American Free Trade Agreement* (17 Dec. 1992) (in effect since 1 January 1994); Chapter 6 of the *India–Singapore Comprehensive Economic Co-operation Agreement* (29 June 2005); and Chapter 11 of the *China–New Zealand Free Trade Agreement* (7 Apr. 2008).

12. For example: A. Newcombe & L. Paradell, *Law and Practice of Investment Treaties* (Kluwer Law International 2009).

13. Newcome & Paradell, *supra* n. 12.

14. For example, the preamble to the Agreement between the Republic of India and the Kingdom of the Netherlands for the Promotion and Protection of Investments (6 Nov. 1995) [hereinafter: *Neths.–India investment protection agreement*] provides as follows:

> Desiring to strengthen the traditional ties of friendship between their countries, to extend and intensify the economic relations between them particularly with respect to investments by the investors of one Contracting Party in the territory of the other Contracting Party,
>
> Recognising that reciprocal protection of such investments under an agreement will subserve the aforesaid objective and will be conducive to the stimulation of Individual business initiative and will increase prosperity in both States.

15. See S. Franck, *Foreign Direct Investment, Investment Treaty Arbitration, and the Rule of Law*, McGeorge Global Bus. and Dev. L. Journal 19, p. 337 (2007).

16. K.J. Vandevelde, *Bilateral Investment Treaties: History, Policy, and Interpretation* (Oxford University Press 2010).

17. See S. Franck, *The Legitimacy Crisis in Investment Treaty Arbitration: Privatizing Public International Law through Inconsistent Decisions*, 73 Fordham L. Rev. 4, pp. 152-165 (Mar. 2005).

18. For example, art. 5 of the *Neths.–India investment protection agreement* provides that: "Investments of investors of either Contracting Party shall not be nationalised, expropriated or subjected to measures having effect equivalent to nationalisation or expropriation, hereinafter referred to as 'expropriation', in the territory of the other Contracting Party except in the public interest in accordance with law, on a non-discriminatory basis and against compensation."

19. Art. 4(1) of the *Neths.–India investment protection agreement* states that:

> Investments 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 territory of the other Contracting Party.

20. Art. 4(2) of the *Neths.–India investment protection agreement* states that:

> Each Contracting Party shall accord to such Investments, including their operation, management, maintenance, use, enjoyment or disposal by such investors, treatment which shall not be less favourable than that accorded either to investments of Its own investors or to investments of investors of any third State, whichever is more favourable to the investor concerned.

21. For example, art. 7 of the *Neths.–India investment protection agreement* provides that:

> Each Contracting Party shall assure to investors of the other Contracting Party, without delay and on a non-discriminatory basis, the unrestricted transfer inter alia of: (a) Capital [...]; (b) Net operating profits [...]; (c) repayments of any loan, including interest thereon, [...]; (d) Payment of royalties [...]; (e) Proceeds of sale or liquidation [...]; (f) The earnings of nationals of one Contracting Party or of any third State who work in connection with Investments In the territory of the other Contracting Party.

22. Art. 3(5) of the *Agreement on encouragement and reciprocal protection of investments between the Kingdom of the Netherlands and the Czech and Slovak Federal Republic* (21 Apr. 1991) states that: "If the provisions of law of either Contracting Party or obligations under international law existing at present or established hereafter between the Contracting Parties in addition to the present Agreement contain rules, whether general or specific, entitling investments by investors of the other Contracting Party to a treatment more favourable than is provided for by the present Agreement, such rules shall to the extent that they are more favourable prevail over the present Agreement."

23. R. Dolzer & M. Stevens, *Bilateral Investment Treaties*, pp. 81-82 (Kluwer Law International 1995).

24. Art. 4(5) of the *Neth.–India investment protection agreement*:

> Each Contracting Party shall observe any obligation it may have entered into with regard to investments of investors of the other Contracting Party.

25. See also Franck, *supra* n. 17.

26. Franck, *supra* n. 17.

27. Certain limitations can be placed on the instigation of arbitration proceedings, such as an obligation to first exhaust all domestic legal proceedings available, although this is dependent on the procedural provisions included in the relevant investment treaty. A "fork in the road provision" may also be included, as a result of which a binding choice must be made between a procedure under domestic law or arbitration. Case law shows that an MFN clause can, under certain conditions, be used to invoke the more favourable procedural provisions of another investment protection agreement. See, for example, ES: ICSID, 25 Jan. 2000, Case No. ARB/97/7, paras. 38-64, *Maffezini v. Spain*, which dealt with objections to jurisdiction and AR: ICSID, 3 Aug. 2004, Case No. ARB/02/8, *Siemens v. Argentina*.

28. H.L. Buxbaum, *The Private Attorney General in a Global Age: Public Interests in Private International Antitrust Litigation*, 26 Yale Intl. L. J. pp. 219-263 (2001).

29. See also Vandevelde, *supra* n. 16.

30. The ICSID is part of the World Bank.

31. Franck, *supra* n. 15.

32. *Vienna Convention on the Law of Treaties* (23 May 1969), Treaties IBFD. *See* Franck, *supra* n. 17. See also L.J. de Heer, *Leerstuk verdragsinterpretatie, NDFR encyclopedie internationaal belastingrecht* (SDU, looseleaf).

33. Dolzer & Stevens, *supra* n. 23, p. 26.

34. Art. 1(a) of the *Neth.-India investment protection agreement.*

35. For example, Art. 1(1)(a) of the *Germany–Afghanistan investment protection agreement* (19 and 20 April 2005).

36. For example, Art. 1(a) of the *Neths.–India investment protection agreement* :

(i) movable and immovable property as well as other property rights such as mortgages, leases, liens, or pledges;
(ii) rights derived from shares, bonds and other kinds of interest in companies;
(iii) rights to money or to any performance having value;
(iv) intellectual property rights, technical processes, goodwill and know how in accordance with the relevant laws of the respective contracting parties;
(v) rights granted under law or under contract such as business concessions to search for and extract oil, natural gas and other minerals.

37. Dolzer & Stevens, *supra* n. 23, p. 27.

38. AR: ICSID, 14 Jan. 2004, Case No. ARB/01/3, *Enron v. Argentina*, para. 44 and Vandevelde, *supra* n. 16, p. 137.

39. M. Sornarajah, *The International Law on Foreign Investment* p. 9 (Cambridge University Press 2004).

40. EC: ICSID, 18 Aug. 2008, Case No. ARB/04/19, *Duke Energy v. Ecuador.*

41. For example, in AL: ICSID, 26 Apr. 1999, Case No ARB/94/2, *Tradex Hellas v. Albania* and CZ: UNCITRAL, 14 Mar. 2003, IIC 62 (2003), *CME v. Czech Republic*, the court stated that,"[it is not required that] the assets or funds be imported from abroad or specifically from [territoriality of the other contracting state] or have been contributed by the investor itself." See also Vandevelde, *supra* n. 16, p. 148.

42. For example, art. 2 of the *Neth.-India investment protection agreement*: "This Agreement shall apply to any investment made by investors of either Contracting Party in the territory of the other Contracting party *including an indirect investment made through another company, wherever located, which is fully owned by such investors*". [emphasis added]

43. This means that for indirect investments more than one investment protection agreement can be applicable.

44. UNCTAD, Bilateral investment treaties 1995-2006: Trends in investment rule making p. 12 (United Nations 2007).

45. Id., p. 13.

46. For example, art. 1(c) of the *Neth.–India investment protection agreement* defines "companies" as:

(i) in respect of India: corporations, firms and associations incorporated or constituted under the law in force in any part of India;
(ii) In respect of the Netherlands: legal persons constituted under the law of the Netherlands.

47. For example, art. 1 of the *Peru–Venezuela investment protection agreement* (*Convenio Entre El Gobiemo De La República Del Perú Y El Gobiemo De La República De Venezuela Sobre Promoción Y Protección De Inversions*) (12 Jan. 1996) provides that: "3) 'Company' applies to all judicial persons, including civil and commercial corporations and other associations which exercise an economic activity comprised within the ambit of this Agreement and that are effectively controlled, directly or indirectly, by nationals of one of the Contracting Parties." [unofficial translation of the UNCTAD].

48. Dolzer & Stevens, *supra* n. 33, Sornarajah, *supra* n. 39 and T. Weiler (redraft), *International Investment Law and Interpretation: Leading Cases from the ICSID, NAFTA, Bilateral Treaties and Customary International Law* (Cameron May Ltd 2005).

49. UNCTAD, *supra* n. 44, p. 81.

50. For example, art. 5 of the *Agreement between the Government of the Argentine Republic and the Government of New Zealand for the Promotion and Reciprocal Protection of Investments* (27 Aug. 1999) states that: "The provisions of this Agreement shall not apply to matters of taxation in the territory of either Contracting Party. Such matters shall be governed by the domestic laws of each Contracting Party and the terms of any agreement relating to taxation concluded between the Contracting Parties."

51. UNCTAD, *supra* n. 44, p. 82.

52. The *Agreement between the United Mexican States and the Federal Republic of Germany on the*

Promotion and Reciprocal Protection of Investments (25 Aug. 1998) provides that: "The provisions in Article 3 [domestic treatment and MFN clause] are not binding for a Contracting State to extend to the natural persons and companies resident in the other Contracting State's territory: the tax benefits, exemptions and reductions which according to tax laws are applicable only to natural persons and residents in the Contracting State's territory."

53. UNCTAD, *supra* n. 44, p. 83.

54. A.F. Rodriguez, *International Arbitration Claims against Domestic Tax Measures Deemed Expropriatory or Unfair and Inequitable, Inter-American Development Bank*, Occasional Paper-SITI-11, p. 7 (Jan. 2006).

55. Weston considers "expropriation" to be ambiguous and unsuitable. He proposes using "wealth deprivation". See B. Weston, "*Constructive taking" under International Law: A Modest Foray into the Problem of "Creeping Expropriation*", Virginia Journal of Intl. L. 16, pp.103-175 (1975).

56. For example, UNCTAD, *supra* n. 44, p. 44 and OECD, *Working Papers On International Investment*, No. 2004/4, *Indirect Expropriation* and *The Right to Regulate,* in *International Investment Law* p. 3 (OECD 2004).

57. OECD, *supra* n. 56, p. 3.

58. MX: ICSID, 21 Nov. 2007, Case No. ARB(AF)/04/05, *Archer Daniels Midland Company v. Mexico*.

59. MX: ICSID, 30 Aug. 2000, Case No. ARB(AF)/97/1, *Metalclad Corporation v. Mexico.*

60. C.H. Schreuer, *Part 1 – Report: The concept of expropriation under the ECT and under investment protection treaties, Investment Arbitration and the Energy Charter Treaty* pp. 108-159 (C. Ribeiro ed., 2006); 2 Transnat'l Dispute Mgmt. 3, p. 108 (June 2005).

61. For practical reasons, the definition of "tax", as applied in investment treaties, is not discussed. In general, it is accepted that a tax measure will include legal provisions, procedures and their legal implementation.

62. For example, T. Walde & A. Kolo, *Investor-State Disputes: The Interface Between Treaty-Based International Investment Protection and Fiscal Sovereignty*, 35 Intertax 8/9, pp. 440-447 (2007).

63. For example, in MX: UNCITRAL, 3 Feb. 2006, LCIA Case No. UN3481, *EnCana v. Ecuador*, the court stated that, "a tax law is not a taking of property; if it were, a universal state prerogative would be denied by a guarantee against expropriation, which cannot be the case." In MX: ICSID, 16 Dec. 2002, Case No. ARB(AF)/99/1), *Feldman v. Mexico*, 7 ICSID Reports 318 (2003) 42 ILM 625, the tribunal argued that, "governments must be free to act in the broader public interest through protection of the environment, new or modified tax regime, the granting or withdrawal of government subsidies, reductions or increases in tariff levels, imposition of zoning restrictions and the like."

64. Sec. 712, *Restatement of the Law Third, the Foreign Relations of the U.S.A.* (American Law Institute 1987); *Feldman*, para. 105. See also A. Kolo, *Tax "Veto" as a Special Jurisdictional and Substantive Issue in Investor-State Arbitration: Need for Reassessment?, Symposium, 2009.*

65. "A signatory party may be responsible for an indirect expropriation of property when it subjects investor's property to taxation, regulation, or other action that is confiscatory, or that prevents, unreasonably interferes with, or unduly delays, effective enjoyment of investor's property, or when the actions makes it impossible for the firm to operate at a profit". Rodriguez, *supra* n. 54, p. 8. See also UK: London Court of International Court of Arbitration, 1 July 2004, Administered Case No. UN 3467, *Occidental v. Ecuador.*

66. See also L. B. Sohn & R.R. Baxter, *Draft Convention on the International Responsibility of States for Injuries to Aliens*, 55 A.J.I.L. 545, art. 10(5) (1961) (the "Harvard Draft"): "An uncompensated taking of property of an alien or a deprivation of the use or enjoyment of property of an alien which results [...] from the action of the competent authorities of the State in the maintenance of public order, health, or morality [...] shall not be considered wrongful, provided [...] it is not a clear and discriminatory violation of the law of the State concerned, [...] [and] it is not an unreasonable departure from the principles of justice recognized by the principal legal systems of the world."

67. The authors have deliberately chosen the definition of expropriation that can be extracted from European Court of Human Rights (ECHR) case law. The ECHR's doctrine cannot be unreservedly applied to investment treaties due to the textual differences between the European Convention on Human Rights and investment treaties. For example, R. Moloo & J. Jacinto, *Environmental and*

Health Regulation: Assessing Liability Under Investment Treaties, 29 Berkeley J. of Intl. L. 2, pp. 1-66 (2011).

68. Rodriguez, *supra* n. 54, p. 13; see also CA: NAFTA/UNCITRAL, 26 June 2000, *Pope & Talbot Inc. v. the Government of Canada*, Interim Award in which the tribunal concluded that, "a blanket exception for regulatory measures would create a gaping loophole in international protections against expropriation."

69. MD: UNCITRAL, 18 Apr. 2002, *Link v. Moldova*, available at http://italaw.com/documents/Link-Trading-Moldova.pdf.

70. MX: UNCITRAL, 3 Feb. 2006, LCIA Case No. UN3481, *EnCana v. Ecuador.*

71. Wälde & Kolo, *supra* n. 62; R.E. Walck, *Tax and currency issues in international arbitration*, 3 World Arb. & Med. Rev. 2, p. 176 (2009).

72. For example, *Archer Daniels*; Wälde & Kolo, *supra* n. 62, Harvard Draft Convention, *supra* n. 66 OECD, *supra* n. 56; Restatement, *supra*, n. 64, § 712, cmt. (g); Iran-US Claims tribunal, 29 Dec. 1989, Award No. 460-880-2, *Too v. Greater Modesto Insurance Assocs., et al.*; and Moloo & Jacinto, *supra* n. 67.

73. This framework has also been implemented in recent investment protection agreements concluded by the United States. For example, Annex B, 4(a) of the Treaty Between the United States of America and the Oriental Republic Of Uruguay Concerning the Encouragement and Reciprocal Protection of Investment (4 Nov. 2005).

74. *Archer Daniels,* para. 250.

75. 24 Aug. 1970, *Revere Copper and Brass Inc and Overseas Private Investment Corporation (1978)*, 56 ILR 258, discussed by M. Hunter & A.C. Sinclair, *Ammoil Revisited Reflections on a Story of Changing Circumstances*, in *Investment Law And Arbitration: Leading Cases From The ICSID, NAFTA, Bilateral Treaties and Customary International Law* p. 360 (T. Weiler ed., Cameron May 2005).

76. For example, Kolo, *supra* n. 64; *Archer Daniels*; Rodriguez, *supra* n. 54; and *Feldman,* para 103.

77. UNCTAD, *Series on Issues in International Investment Agreements: Taking of Property* 4 (2000). See also R. Higgins, *The Taking of Property by the State: Recent Developments in International Law*, 176 Recueil des Cours, pp. 259-324 (1982).

78. Wälde & Kolo, *supra* n. 62.

79. *Occidental v. Ecuador.*

80. *Occidental v. Ecuador.* See also ICSID, 13 Sept. 2006, Case No. ARB/04/15, *Pope & Talbot and Telenor v. Hungary.*

81. *Archer Daniels*, para. 240: "The test on which other Tribunals and doctrine have agreed – and on which the 'Claimants' rely – is the 'effects test'. Judicial practice indicates that the severity of the economic impact is the decisive criterion in deciding whether an indirect expropriation or a measure tantamount to expropriation has taken place. An expropriation occurs if the interference is substantial and deprives the investor of all or most of the benefits of the investment. There is a broad consensus in academic writings that the intensity and duration of the economic deprivation is the crucial factor in identifying an indirect expropriation or equivalent measure."

82. *Occidental v. Ecuador.*

83. Art. II(3)(a) of the Treaty between the United States of America and the Republic of Ecuador Concerning the Encouragement and Reciprocal Protection of Investment, with Protocol and a Related Exchange of Letters (27 Aug. 1993): "Investment shall at all times be accorded fair and equitable treatment, shall enjoy full protection and security and shall in no case be accorded treatment less than that required by international law."

84. *Occidental v. Ecuador*, para 184.

85. It should be noted that the tribunal in *EnCana v. Ecuador*, para. 173 considered that a contractual obligation was indeed more important than an obligation derived from general legislation and, therefore, applied to the underlying issue a more limited interpretation of the right to fair and equitable treatment: "[i]in the absence of a special commitment from the host state, the foreign investor has neither the right nor any legitimate expectation that the tax regime will not change,