

A Clash of Treaties: The Lawfulness of Countermeasures in International Trade Law and International Investment Law

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Abstract

Countermeasures are part of customary international law and have been incorporated into the WTO as a mechanism to facilitate compliance. In the NAFTA sugar disputes, Mexico claimed that the measure in dispute was a countermeasure against a breach of NAFTA by the United States. Three US investors also claimed against Mexico under the investment chapter of NAFTA. All three ICSID tribunals held, for different reasons, that trade countermeasures affecting investor rights would be unlawful. Some of the tribunals' reasoning that investors have direct rights could set up a clash between the trade and investment regimes. We argue that an authorized trade countermeasure should also be lawful in the investment law context. Coherence between the trade and investment regimes is essential in this age of global value chains in which investors are part of a complex trade network. We suggest ways to improve the jurisprudence and existing investment treaties.

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Keywords

countermeasures – lawfulness – trade and investment – independent investor rights

1 Introduction

The rise of investment arbitration as a means of resolving international disputes is a relatively recent phenomenon. The impact of this rise, which has resulted in many binding international awards on the policies of States, has increasingly become a major source for study by many scholars. However, few scholars have attempted to understand this rise in the context of the entire international economic law regime that governs economic activities between nations and within nations. In this article, we attempt to highlight one possible area in which the international trade law and international investment law regimes may need to receive some attention with regard to ensuring coherence: the area of trade countermeasures and the potential impacts of these measures on investors. Some recent cases in the international economic law field have highlighted the need to resolve the issue of countermeasures and the tensions when dealing with economic countermeasures.¹

The defence of countermeasures is well accepted in public international law as part of customary international law (CIL). Yet, the lawfulness of unilateral countermeasures as a response to a breach of an international obligation has always been a source for contention in international law.² Lawyers have attempted to limit unilateral actions of States by imposing requirements such as those found in the Articles on State Responsibility developed by the International Law Commission (ILC).³ Under Article 22 of the ILC Articles, although State B may breach its international obligation against State A, the wrongfulness of the breach can be precluded if State B can demonstrate that its act, subject to such limitations, constitutes a lawful countermeasure against State A's breach.

¹ *Archer Daniels Midland Company and Tate & Lyle Ingredients Americas, Inc v Mexico*, ICSID Case No ARB(AF)/04/5, Award (21 November 2007); *Corn Products International, Inc v Mexico*, ICSID Case No ARB(AF)/04/1, Decision on Responsibility (15 January 2008); *Cargill, Inc v Mexico*, ICSID Case No ARB(AF)/05/2, Award (18 September 2009).

² James Crawford, *State Responsibility: The General Part* (CUP 2013) 684.

³ 2001 Articles on Responsibility of States for Internationally Wrongful Acts, 53 UN GAOR Supp (No 10) 43, UN Doc A/56/83 (2001); see also International Law Commission, *Draft Articles on Responsibility of States for Internationally Wrongful Acts with Commentaries*, Yearbook of International Law Commission, 2001, vol II, Part Two.

A lawful countermeasure should only seek for cessation and/or to obtain reparation for the injury caused.⁴ Countermeasures under CIL are historically unilateral actions. It may be taken by a State at its own risk and may incur responsibility if it is later found that the measure is unlawful.⁵ The coverage of countermeasures is legally limited to preclude wrongfulness only against the wrongdoer.⁶ The measure must be temporary, and may not affect the following obligations: 1) the obligation to refrain from the threat or use of force, 2) obligations for the protection of fundamental human rights, 3) obligations of a humanitarian character prohibiting reprisals, 4) obligations under peremptory norms of general international law.⁷

According to the International Court of Justice (ICJ) in its *Gabčíkovo-Nagymaros* decision, a lawful countermeasure has to fulfil several additional prerequisites:⁸ such a countermeasure must be 1) taken in response to a previous international wrongful act of another State,⁹ 2) directed against that State,¹⁰ 3) taken after a prior call upon the responsible State and prior offer to negotiate,¹¹

⁴ ILC Articles and Commentary (n 3) 75.

⁵ David Harris, *Cases and Materials on International Law* (7th edn, Thomson Reuters 2010) 460–461; see James Crawford, ‘The ILC’s Articles on Responsibility of States for Internationally Wrongful Acts: A Retrospect’ (2002) 96 AJIL 874, 884; Mary Ellen O’Connell, *The Power and Purpose of International Law: Insights from the Theory and Practice of Enforcement* (OUP 2008) 3.

⁶ ILC Articles (n 3) article 49(1).

⁷ *ibid* article 50(1).

⁸ *Case Concerning the Gabčíkovo-Nagymaros Project (Hungary/Slovakia)*, Judgment (25 September 1997) ICJ Rep 7 paras 83–85. The Court also referred to past decisions including *Military and Paramilitary Activities in and against Nicaragua (Nicaragua/USA)*, Judgment (27 June 1986) ICJ Reports 1986, para 249.

⁹ *Portuguese Colonies case*, Award (31 July 1928) II UNRIIA 1027 (*Naulilaa*); ILC Articles and Commentary (n 3) 130 para 3. The breach of an international obligation does not have to be proven before an adjudicatory body prior to the taking of the countermeasure unless specified in a treaty.

¹⁰ *Portuguese Colonies case*, Award (30 June 1930) II UNRIIA 1056–1057 (*Cysne*); ILC Articles and Commentary (n 3) 75, 76, 130. The ILC Commentary provides that an indirect or consequential effects of countermeasures on third parties without an independent breach of any obligation to those third parties do not render the countermeasures unlawful. However, the State taking the countermeasure should endeavor to avoid or limit the indirect and unintentional consequence as far as possible.

¹¹ ILC Articles and Commentary (n 3) articles 52(1)(a) and (b), 136 paras 4–6; *Naulilaa* (n 9) 1027–1028. This requirement is fulfilled after the warning had been given continuously but remained unproductive or when negotiations have been conducted.

and 4) such a measure must be proportionate.¹² Additionally, the ILC Articles provide for two other conditions namely that a countermeasure be 1) temporary,¹³ and 2) not imposed when the dispute is pending before a court or tribunal.¹⁴ These prerequisites for a lawful countermeasure under CIL¹⁵ are important for our further analysis of this defence under the international trade law and international investment law regimes, respectively.

In the World Trade Organization (WTO), the rules on countermeasures are formally incorporated in the Understanding on Rules and Procedures Governing the Settlement of Disputes (DSU) of the WTO.¹⁶ Non-compliance with the ruling of the Dispute Settlement Body (DSB) may, subject to DSB approval, lead to a suspension of concessions or other WTO obligations (colloquially known as retaliation).¹⁷ For the purpose of this article and to avoid confusion, these types of countermeasure which are regulated under specific rules (*lex specialis*) and fulfil those rules will be referred to as 'authorized' as they have been approved and legitimized by the relevant regime, be it the WTO or in certain rare cases perhaps the relevant free trade agreement (FTA) regime. On the other hand, countermeasures which fulfil the prerequisites under CIL will be referred to as 'lawful'.

In contrast, to our knowledge, we know of no investment agreement that explicitly provides for countermeasures. Nevertheless, at least one arbitral tribunal has explicitly accepted countermeasures as a valid defence pursuant to the CIL as applied to an investment agreement.¹⁸ In doing so, it relied heavily on the ILC Articles and past cases¹⁹ to determine the lawfulness of the countermeasure.²⁰

¹² *Naulilaa* (n 9) 1028; ILC Articles and Commentary (n 3) articles 49(2) and 51; *Air Services Arbitration Case (France v United States)* (1978) 18 RIAA 416 (This arbitration started to use the term 'countermeasure' rather than 'reprisal'). Countermeasures must be commensurate with the injury suffered, taking into account the gravity of the internationally wrongful act and the rights in question. However, it is noted that the proportionality test could at best be accomplished by approximation.

¹³ ILC Articles (n 3) article 53; ILC Articles and Commentary (n 3) 131 para 7.

¹⁴ *ibid* article 52(3)(b), 136 para 8. A dispute is pending if a court/ tribunal has been constituted and is in position to deal with the case.

¹⁵ *ADM v Mexico* (n 1) para 125; *Corn Products v Mexico* (n 1) para 145.

¹⁶ Dispute Settlement Rules: Understanding on Rules and Procedures Governing the Settlement of Disputes, Annex 2, signed in 1994, 1869 UNTS 401, 33 ILM 1226.

¹⁷ *ibid* article 22(1)-(2).

¹⁸ *ADM v Mexico* (n 1) paras 111, 121.

¹⁹ *Gabčíkovo-Nagymaros* (n 8).

²⁰ *ADM v Mexico* (n 1) paras 121, 125.

There is a close relationship between countermeasures in international trade law and investment law. Authorized countermeasures may affect the interests of private individuals, including those of foreign investors. In such a situation, if there is an investment agreement between the two disputing WTO Members, an investor of one of the members impacted by a DSB-approved trade countermeasure may bring a claim of violation of the investment agreement against the other member.²¹ This opens the possibility for that other member to invoke the defence of countermeasure in the investment litigation despite the fact that the initial breach is against a WTO obligation.²²

The likelihood of such a situation is not remote, considering how closely trade and investment are interrelated through global value chains (GVCs). Goods are moved across borders often between subsidiaries of multinational companies (MNCs) or the MNCs may link up various unrelated producers into a chain for the production of its specific products; the most well-known examples of these GVCs include integrated production for cars or mobile phones. Another example occurred in the so-called Sugar War between Mexico and the United States, during which Mexico claimed that its measures affecting American investors were lawful countermeasures against a prior breach by the United States of its trade obligations under the North American Free Trade Agreement (NAFTA).²³ In this case, high fructose corn syrup was imported by various American MNCs into Mexico for use as a sweetener in Mexican soft drinks. While this concerned the NAFTA, an authorized countermeasure taken under the larger trade regime of the WTO may be similarly called into question. A negative response to this question may create a clash between the two regimes, namely by significantly restricting States' options to enforce their legitimate trade interests, as well as removing the value of countermeasures as an effective tool to ensure compliance in the WTO. This mechanism in the WTO will be explained further below.

²¹ ILC Articles and Commentary (n 3) 130. It is worth noting that countermeasures under CIL can be taken against another set of international obligations contained in a separate treaty and not confined to the initial treaty that the wrongdoer has breached. However, the test of proportionality will be applicable to determine the lawfulness of the measures.

²² Further discussion: N Jansen Calamita, 'Countermeasures and Jurisdiction: Between Effectiveness and Fragmentation' (2011) 42 *Geo J Intl L* 233, 243.

²³ North American Free Trade Agreement, signed on 17 December 1992 (1 January 1994) 32 *ILM* 289 and 605; see also Alvaro Antoni and Michael Ewing-Chow, 'Trade and Investment Convergence and Divergence: Revisiting the North American Sugar War' (2013) 11 *Latin American JITL* 321–325; Jürgen Kurtz, 'The Use and Abuse of WTO Law in Investor-State Arbitration: Competition and its Discontents' (2009) 20 *EJIL* 749–771.

The authors also note that the ongoing conflict over Crimea may raise a question of whether a trade countermeasure taken against a breach of a human rights treaty can be WTO-compliant. Such a question probes into the grey area of whether a unilateral countermeasure under CIL that may, on the face of it, breach WTO disciplines may still be in compliance with the DSU. This article will not address the question as one of the authors has already written on this issue to a certain extent in another article.²⁴ The analysis in this article will be limited to WTO-authorized countermeasures and their lawfulness in international investment law. Further, this article also refrains from addressing the lawfulness or legitimacy of countermeasures taken against a breach of an international investment agreement (IIA) as other authors have already explored those areas.²⁵

This article is a continuation of the analysis that was conducted by one of the authors in a previous article on convergence and divergence between trade and investment law.²⁶ This article seeks to explore the issue in a greater detail in the following sequence. Part 2 will analyze countermeasures in international trade law, specifically in WTO law. Part 3 will analyze the defence of countermeasures in international investment law by analyzing arbitral awards that have dealt with the matter. Part 4 will explore the interaction of countermeasures in international trade law and international investment law, and provide recommendations. Here, we particularly will suggest that the nature of investor rights and the procedural rights found in IIAs should not be conflated and should be separately analyzed, that the relationship between investor rights and countermeasures should be better understood, and that a legislative solution either by issuing a joint-interpretation or adding a provision to the relevant IIAs should be considered. Part 5 will conclude.

2 Countermeasures in International Trade Law

2.1 *WTO DSU as Lex Specialis*

For the purpose of this discussion, international trade law hereinafter refers specifically to the regime of the WTO—with a more established system requiring

²⁴ Michael Ewing-Chow, 'First Do No Harm: Myanmar Trade Sanctions and Human Rights' (2007) 5(2) *JHR* 154–180; see also *US – Procurement*, WTO DS88 (1997), but the panel was never constituted.

²⁵ Martins Paparinskis, 'Equivalent Primary Rules and Differential Secondary Rules: Countermeasures in WTO and Investment Protection Law' in Tomer Broude and Yuval Shany (eds), *Multi-Sourced Equivalent Norms in International Law* (Hart Publishing 2011) 280–287.

²⁶ Antoni and Ewing-Chow (n 23).

pre-authorization of countermeasures. We note that the defence of countermeasure may also exist in other FTAs and the principles explored in our analysis in Part 4 may also be applicable to some of those countermeasures which share the same characteristics as countermeasures in the WTO.

The DSU, one of the cornerstones of the Marrakesh Agreement Establishing the WTO²⁷ applies to disputes brought pursuant to the dispute settlement provisions of the agreements listed in Appendix 1 of the DSU:²⁸ 1) the Marrakesh Agreement, 2) multilateral agreements on trade in goods,²⁹ 3) the General Agreement on Trade in Services (GATS),³⁰ 4) the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS),³¹ and 5) plurilateral trade agreements. This makes the WTO DSU a largely self-contained regime within international law,³² at least with respect to the legal consequences stemming from a breach. The mandate of the WTO adjudicatory bodies are also limited³³ and panels or the Appellate Body (AB) cannot decide on disputes brought to it under non-WTO agreements, including FTAs to which the disputing members are parties.³⁴

The DSU contains a *lex specialis* system of retaliation.³⁵ It specifically regulates when WTO Members can take a countermeasure for an alleged breach of

²⁷ Marrakesh Agreement Establishing the World Trade Organization, signed on 15 April 1994, 1867 UNTS 154, 33 ILM 1144.

²⁸ WTO DSU (n 16) articles 1(1) and 3(2).

²⁹ This includes the General Agreement on Tariffs and Trade 1994, signed on 15 April 1994, Annex 1A, 1867 UNTS 187, 33 ILM 1153.

³⁰ General Agreement on Trade in Services, Annex 1B, signed on 15 April 1994, 1869 UNTS 183, 33 ILM 1167.

³¹ Agreement on Trade-Related Aspects of Intellectual Property Rights, Annex 1C, signed on 15 April 1994, 1869 UNTS 299, 33 ILM 1197.

³² Peter Jan Kuijper, 'The Law of GATT as a Special Field of International Law' (1994) Neth YBIL 227; Bruno Simma, 'Self-Contained Regimes' (1985) Neth YBIL 111.

³³ WTO DSU (n 16) article 3.2; Chang-Fa Lo, 'Dispute Settlement under Free Trade Agreements: Its Interaction and Relationship with WTO Dispute Settlement Procedures' in Yasuhei Taniguchi, Alan Yanovich and Jan Bohanes (eds), *The WTO in the Twenty-first Century: Dispute Settlement, Negotiations, and Regionalism in Asia* (CUP 2007) 467.

³⁴ WTO DSU (n 16) article 3(2); *Mexico – Tax Measures on Soft Drinks and Other Beverages*, WT/DS308/AB/R, Report of the Appellate Body (6 March 2006) para 78; see also Joost Pauwelyn, 'Enforcement and Countermeasures in the WTO: Rules are Rules – Toward a More Collective Approach' (2000) 94 AJIL 335, 341 where he suggests that DSU article 3.2 demonstrates that the WTO legal system is not to be seen as a self-contained regime because they have to be interpreted in accordance with customary rules of public international law.

³⁵ Gabrielle Marceau and Jennifer A Hamaoui, 'Implementation of Recommendations and Rulings in the WTO System' in Laurence Boisson de Chazournes, Marcelo G Kohen and Jorge E Vinuales (eds), *Diplomatic and Judicial Means of Dispute Settlement* (Brill 2013) 188–189.

a WTO commitment by other Members. Due to the *lex specialis* nature of the regulation of countermeasures, WTO Members cannot resort to rules of countermeasures under CIL, i.e., unilateral countermeasures.³⁶

2.2 Requirements for a WTO-Authorized Countermeasure

The DSU allows WTO Members to take countermeasures against a breach of WTO Law as authorized by the DSB. The DSU imposes several requirements for a countermeasure to be WTO-authorized.

2.2.1 Proper Subject

Article 22.3(a) of the DSU provides a general principle that the complaining WTO Member should first seek suspension of concessions or other obligations with respect to the same sector(s) as that in which the panel or the AB has found a violation or other nullification or impairment. Only when this is not practicable or effective, Articles 22.3(b) and (c) of the DSU allow the complaining Member to suspend concessions or other obligations in other sectors under the same agreement (cross-sector retaliation) or under a different agreement (cross-agreement retaliation).

TABLE 1 *Examples of countermeasures taken in the WTO*

Case	Initial violation	Approved countermeasures			Status of sanction
		Same sector	Same agreement	Other sector and agreements	
<i>US – Upland Cotton</i> ³⁷	Subsidies on cotton (GATT and SCM Agreement)	Imposition of additional custom duties under Annex 1A on medical products, food, and arms.		GATS Horizontal and/or sectoral concessions and obligations for all sectors in Brazil's schedule under the GATS, including: business services, communication services, etc.	Both parties concluded a mutual framework agreement to resolve the issue.

³⁶ *US-Section 301-310 of the Trade Act 1974*, WT/DS152/R, Report of the Panel (22 December 1999) paras 7.38-7.39.

³⁷ *United States – Subsidies on Upland Cotton*, WT/DS267/R and Corr.1, Add.1, Add.2 and Add.3, WT/DS267/AB/R, WT/DS267/ARB/2, Report of the Panel (8 September 2004), Recourse to Article 22.6 Arbitration Report (31 August 2009).

Case	Initial violation	Approved countermeasures			Status of sanction
		Same sector	Same agreement	Other sector and agreements	
<i>US – Gambling</i> ³⁸	Limitations on market access in gambling and betting services, not specified in its Schedule (GATS).	Not practicable.	Not practicable due to the risk of economic disruption.	TRIPS Copyright and related rights, trademarks, industrial designs, patents, etc. TRIPS Copyrights and related rights, trademarks, industrial designs, patents, etc.	The United States provided certain payments to Brazil. The DSB authorized Antigua to take countermeasures according to the Decision of Arbitrators, i.e., in respect of intellectual property rights.
<i>EC – Bananas III (Ecuador)</i> ³⁹	Tariff quota reallocation; export certificate requirement; import licensing procedures (GATT and GATS)	Suspension of tariff concessions under the GATT (not including investment goods or primary goods used as inputs in manufacturing and processing industries).	GATS Wholesale trade services in the principal distribution services. TRIPS Article 14 on protection of performers, producers of phonograms and broadcasting organizations.	The DSB authorized Ecuador to take countermeasures. Eventually the parties reached a mutually agreed solution in 2012.	

³⁸ *United States – Measures Affecting the Cross-Border Supply of Gambling and Betting Services*, WT/DS285/ARB, Decision of the Arbitrators (Art. 22.6 DSU) (21 December 2007).

³⁹ *European Communities — Regime for the Importation, Sale and Distribution of Bananas (EC – Bananas III (Ecuador))*, WT/DS27/ARB/ECU, Decision of the Arbitrators (Art. 22.6 DSU) (9 April 1999).

TABLE 1 *Examples of countermeasures taken in the WTO (cont.)*

Case	Initial violation	Approved countermeasures			Status of sanction
		Same sector	Same agreement	Other sector and agreements	
<i>EC-Hormones</i> ⁴⁰	Ban on imports of hormone treated beef (Article 5.1 of the Agreement on the Application of Sanitary and Phytosanitary Measures)	Suspension of concessions for import of goods, e.g., meat, pork	-	Or in general, Annex 1 Trade in Goods Agreement.	The United States imposed retaliatory duties (100% <i>ad valorem</i>) on imports of agricultural products, e.g., meat, poultry, cheese; and manufactured goods, e.g., Italian scarves, hair clippers.

As illustrated by the cases above, most of the countermeasures involved imposition of duties in addition to the duties existing in the schedule of the retaliating Member. Other approved countermeasures included suspension of obligations under TRIPS usually involving the suspension of the protection afforded to intellectual property rights owned by nationals of the non-complying State. In *EC-Bananas III (Ecuador)*, for example, Ecuador proposed to take countermeasures by suspending obligations under Article 14 of TRIPS regarding protection of rights of performers, producers of phonograms (sound recordings) and broadcasting organizations,⁴² by allowing phonograms copies to be made in Ecuador without the consent of the right holders in the country of production.⁴³ This demonstrates that the retaliations authorized by the

⁴⁰ *European Communities — Measures Concerning Meat and Meat Products (Hormones)*, WT/DS26/ARB, Decision of the Arbitrators (Art 22.6 DSU) (12 July 1999).

⁴¹ *ibid* para 80.

⁴² *EC-Bananas III (Ecuador)* (n 39) para 144.

⁴³ *ibid* para 155.

WTO actually cover fields that directly affect individuals,⁴⁴ and it is difficult to imagine a trade measure that does not affect any individual.

2.2.2 Level of Countermeasure

Article 22.4 of the DSU requires the level of countermeasures to be equivalent to the level of nullification or impairment—limited to the harm suffered by the complaining Member. The ‘equivalent’ requirement is fulfilled when the level is ‘equal to or below the level of nullification or impairment sustained.’⁴⁵ The arbitration in *Canada-Aircraft* found that ‘a countermeasure is “appropriate” *inter alia* if it *effectively* induces compliance.’⁴⁶ It may be more onerous than one calculated to be merely ‘equivalent’ to the wrong inflicted, as long as it is not ‘disproportionate’ to the objective of ending non-compliance.⁴⁷ This requirement is somewhat similar to the requirement of proportionality in CIL.

2.2.3 Non-Retrospective Remedies

Since the main objective of the WTO dispute settlement is ‘to secure the withdrawal of the measures’ found to be illegal,⁴⁸ the remedies granted under the system are limited to harm that occurs after a WTO Member fails to implement a panel or AB report within a reasonable period of time.⁴⁹ Pauwelyn suggests that the WTO legal system should consider including reparation for past damage to bring it closer to public international law, as well as to strengthen the predictability and stability of the multilateral trading system.⁵⁰

2.2.4 Prior Authorization from the DSB

Articles 3.7 and 22.2 of the DSU allows Members to take countermeasures subject to authorization by the DSB. According to Article 22.6 of the DSU, the DSB (which consists of all WTO Members) grants authorization for countermeasures within 30 days of the expiry of the reasonable period of time unless all members decided by consensus to reject the request.

⁴⁴ Pauwelyn (n 34) 341.

⁴⁵ *United States – 1916 Act (EC)*, WT/DS136/ARB, Decision of the Arbitrators (Art 22.6 DSU) (24 February 2004) para 5.21.

⁴⁶ *Brazil-Export Financing*, WT/DS46/ARB, Decision of the Arbitrators (28 August 2000) para 3.58.

⁴⁷ *ibid* para 3.51 note 51; for further discussion, Thomas M Franck, ‘On Proportionality of Countermeasures in International Law’ (2008) 102 (4) *AJIL* 715, 743–752.

⁴⁸ WTO DSU (n 16) articles 3.7 and 19.1.

⁴⁹ *United States — Import Measures on Certain Products from the European Communities*, WT/DS165/R, Report of the Panel (17 July 2000) para 6.106.

⁵⁰ Pauwelyn (n 34) 346.

Within the WTO, the potential issue of DSB-authorized countermeasures interfering with private rights of investor has actually been identified, particularly in the discussion of the *EC-Bananas III (Ecuador)* arbitrators during the Art. 22.6 DSU proceeding. The discussion recognized that countermeasures of the GATS would affect service suppliers who are commercially present in the territory of the Member taking countermeasures and could lead to conflicts with rights to, e.g., equal treatment embodied in national legislation or international treaties.⁵¹ Similarly, countermeasures under TRIPS may interfere with private rights owned by natural or legal persons.⁵² While there is an awareness of the problem, the arbitrators left the resolution of the problem entirely to the prerogative of the Member implementing the countermeasures.⁵³ This in itself does not resolve the problems that may arise from authorized trade countermeasures, as we will see further below.

3 Countermeasures in International Investment Law

In international investment law, the defence of countermeasures is never mentioned explicitly in investment treaties. Not many cases have dealt with this issue, perhaps because it has rarely been argued as a defence. Nevertheless, there are several NAFTA Chapter 11 cases that may provide some guidance on how arbitral tribunals view this defence.

The most prominent cases are those arising from the Sugar War between Mexico and the United States, dealing with the imposition of tax on beverages containing high-fructose corn syrup (HFCS) by Mexico.⁵⁴ Despite the similar set of facts, the tribunals had different views regarding the lawfulness of Mexico's claimed countermeasure.

3.1 *The Facts of the United States – Mexico Sugar War*

The Sugar War involved three dispute settlement forums, the WTO DSB (two different cases),⁵⁵ a NAFTA Chapter 19 tribunal⁵⁶ and three NAFTA Chapter 11 investor-State arbitration tribunals. The underlying reason for the dispute was

⁵¹ *EC-Bananas III (Ecuador)* (n 39) paras 113, 157.

⁵² *ibid* para 157.

⁵³ *ibid* para 158.

⁵⁴ *ADM v Mexico* (n 1); *Corn Products v Mexico* (n 1); *Cargill v Mexico* (n 1).

⁵⁵ *Mexico – Anti-Dumping Investigation of High Fructose Corn Syrup from the United States*, WT/DS132/R, Report of the Panel (28 January 2000); *Mexico - Taxes on Soft Drinks* (n 34) Report of the Appellate Body and WT/DS308/R, Report of the Panel (7 October 2005).

⁵⁶ *Review of the Final Determination of the Antidumping Investigation on Imports of High Fructose Corn Syrup, Originating from the United States of America* [2001] MEX-USA-98-1904-01.

the disagreement between Mexico and the United States on the American sugar import quotas allocated to Mexico under the NAFTA.⁵⁷

Mexico sought to clarify the uncertainties created by the Exchange of Letters between the United States and Mexico regarding the quota for its sugar export by resorting to the dispute settlement mechanism established under NAFTA Chapter 20. However, the United States had not formally established its roster of panel and refused to cooperate in the composition of the panel.⁵⁸ As there was no automaticity in panel formation, there was little Mexico could do about this and no NAFTA Chapter 20 panel could be formed.

Left without a NAFTA dispute settlement option, Mexico initiated an anti-dumping investigation of American exports of HFCS to Mexico and decided to impose provisional duties in 1997 and definitive duties in 1998. The United States successfully challenged these duties before a NAFTA panel⁵⁹ and the WTO, as a result of which Mexico was obliged to withdraw the duties.⁶⁰

In 2002, the Mexican Congress, stating that it was 'committed to protecting the domestic sugar industry',⁶¹ introduced a series of measures to 'stop the displacement of domestic cane sugar by imported HFCS and soft drinks and syrup sweetened with HFCS':⁶² (1) a 20 per cent tax on the transfer and importation of soft drinks using any sweetener other than cane sugar (soft drinks tax); (2) a 20 per cent tax on the commissioning, mediation, agency, representation, brokerage, consignment and distribution of soft drinks using any sweetener other than cane sugar (distribution tax); and (3) a number of bookkeeping requirements on taxpayers subject to the soft drink tax and the distribution tax.

These measures were challenged before the WTO.⁶³ The dispute was eventually resolved in 2006 when both sides agreed to achieve free trade in HFCS by 2008, as well as repealing Mexican measures as of 2007.⁶⁴ However, a number of American investors in Mexico also filed investment disputes against Mexico under the investor-State dispute settlement mechanism established under NAFTA Chapter 11, seeking damages for their losses during the period when the measures were in place. In the arbitration proceedings, Mexico attempted to justify its measures by claiming that they constituted lawful countermeasures

⁵⁷ For a more comprehensive elaboration of the facts: see Antoni and Ewing-Chow (n 23) 325–328.

⁵⁸ *ibid* 327.

⁵⁹ *Antidumping Determination on HFCS* (n 56).

⁶⁰ *Mexico – Corn Syrup* (n 55).

⁶¹ *ADM v Mexico* (n 1) para 80.

⁶² *Mexico – Taxes on Soft Drinks* (n 55) Report of the Panel, para 8.3.

⁶³ *ibid*.

⁶⁴ *ADM v Mexico* (n 1) para 97; *Cargill v Mexico* (n 1) para 124.

against the United States for violating its obligations under NAFTA Chapter 7 and Chapter 20.⁶⁵

3.2 *Contextualizing the NAFTA Dispute Settlement Bodies*

Under NAFTA, Members can request the establishment of a tribunal or a panel under different chapters. For purposes of our analysis, NAFTA Chapter 11 and Chapter 20 are particularly relevant.

A panel's competence under Chapter 11 is limited to a claim of breach of an obligation under Section A of Chapter 11 and NAFTA Article 1503(2) and Article 1502(3)(a). On the other hand, a panel's competence under Chapter 20 is broader and encompasses disputes between the State Parties regarding the interpretation or application of NAFTA,⁶⁶ but not disputes arising from Chapter 11.

The issue of countermeasures is regulated in NAFTA Article 2019 concerning the suspension of benefits for failing to implement a NAFTA ruling. To a certain extent, countermeasures under this provision are similar to that of the WTO DSU. However, there is no requirement to obtain an authorization. Only if one of the disputing parties disagrees to the level of a proposed countermeasure, the Free Trade Commission (FTC) may establish a panel to determine whether the level of the countermeasure is manifestly excessive—providing a mechanism to prevent abusive countermeasures.

In the Sugar War cases before the arbitral tribunals, Mexico may have a stronger case if its countermeasures were taken in accordance with NAFTA Article 2019 and legitimized by the FTC. However, Mexico could not raise this issue because a NAFTA Chapter 20 panel could not be formed thus there was no initial finding of the United States' breach of its NAFTA obligations.

3.3 *Countermeasures Analysis by Investor-State Arbitration Tribunals*

The tribunals in the three cases concerning Mexico's tax measures on soft drinks dealt in different ways with Mexico's claims that the measures were countermeasures taken in response to the alleged breach of the United States' obligations under NAFTA. The awards were issued in the following order, *ADM v Mexico* (2007), *Corn Products v Mexico* (2008), and *Cargill v Mexico* (2009). Only the tribunal in *Cargill v Mexico* actually considered the previous award of *ADM v Mexico* (the award in *Corn Products* was not publicly released in time).

⁶⁵ *ADM v Mexico* (n 1) para 110; *Cargill v Mexico* (n 1) para 379; *Corn Products v Mexico* (n 1) para 144.

⁶⁶ NAFTA (n 23) article 2004.

We will assess the following aspects of the tribunals' awards: 1) the availability of the defence of countermeasures under NAFTA Chapter 11 and 2) the jurisdiction of arbitral tribunals to assess the defence.

3.3.1 Availability of the Defence of Countermeasures under NAFTA Chapter 11

As mentioned earlier, NAFTA Chapter 11 does not explicitly provide for the defence of countermeasures. In all three cases Mexico argued that the defence arises from CIL.⁶⁷ These countermeasures could have been also invoked under NAFTA Chapter 20, but for reasons we elaborate below, Mexico could not avail itself of that dispute settlement mechanism. We will analyse both countermeasures under CIL and countermeasures under NAFTA Chapter 20 below.

3.3.1.1 *Countermeasures under CIL*

The Tribunal in *ADM v Mexico* found that although not provided for in Chapter 11, countermeasures are not explicitly prohibited and thus are available by the incorporation of CIL pursuant to the reference to 'applicable rules of international law' in NAFTA Article 1131.⁶⁸ The authors agree with this view because this defence is a part of the 'secondary rules'⁶⁹ of responsibility of States under international law in addition to the substantive rules in the treaty.⁷⁰ Although they did not state explicitly their positions regarding the availability of this defence under Chapter 11, the tribunals in *Corn Products v Mexico* and *Cargill v Mexico* strongly believed that countermeasures could not be applied under Chapter 11 to preclude wrongfulness against foreign investors.⁷¹ In *Corn Products v Mexico*, the Tribunal opined that 'there is no room for a defence based upon the alleged wrongdoing not of the claimant but of its State of nationality, which is not a party to the proceedings.'⁷² It supported this argument with lengthy discussion regarding the nature of rights and obligations arising under Chapter 11.

⁶⁷ *ADM v Mexico* (n 1) para 110; *Cargill v Mexico* (n 1) para 379; *Corn Products v Mexico* (n 1) para 158.

⁶⁸ *ADM v Mexico* (n 1) para 120.

⁶⁹ Crawford (n 2) 64–65.

⁷⁰ *ibid* 91–92. In this regard, the rules of countermeasures under CIL can be found in the Articles on State Responsibility, a non-binding text but has been applied by various tribunals as part of the fabric of general international law; Crawford (n 5) 876.

⁷¹ *Corn Products v Mexico* (n 1) para 191; *Cargill v Mexico* (n 1) para 430.

⁷² *Corn Products v Mexico* (n 1) para 161; *Cargill v Mexico* (n 1) paras 422–429; for a discussion about this jurisdictional bar to the tribunal's analysis of the defence, see Martins Paporinskis, 'Investment Arbitration and the Law of Countermeasures' (2009) 79(1) BYIL 264–352, 337–340.

The *Corn Products* and *Cargill* tribunals' analyses lead us to the assessment of the rights under NAFTA Chapter 11. This is particularly important because under the ILC Articles, countermeasures may not preclude wrongfulness against third parties, especially if they have individual rights,⁷³ though the term 'individual rights' was not defined further.

In *ADM v Mexico*, this issue was addressed in one of the requirements for lawful countermeasures, namely non-impairment of individual substantive rights of claimants. Although claimed to be derived from CIL,⁷⁴ the requirement is neither present in *Gabčíkovo-Nagymaros* nor the ILC Articles.⁷⁵ The Tribunal examined whether NAFTA Chapter 11 provides a self-contained mechanism endorsing substantive and procedural rights for qualified investors, and whether such rights are independent from the rights of the Member States.⁷⁶

The *ADM* tribunal considered three theories: 1) the traditional derivative theory—'when investors trigger arbitration proceedings against a State, they are in reality stepping into the shoes and asserting the rights of their home State,'⁷⁷ 2) an intermediate theory—'investors are vested only with an exceptional procedural right to claim State responsibility under Section B before an international arbitral tribunal,'⁷⁸ and 3) a direct theory – 'investors ... are vested with direct independent rights and that they are immune from the legal relationship between the Member States.'⁷⁹

The Tribunal adopted the intermediate theory,⁸⁰ a position which Mexico had supported by citing NAFTA jurisprudence, scholarly writings and the position of the Member States in their intervention in other NAFTA Chapter 11 proceedings.⁸¹ Specifically, the Tribunal in *Loewen v US*⁸² opined that under Chapter 11, 'claimants are permitted for convenience to enforce what are in origin the rights of Party states.'⁸³

⁷³ ILC Articles (n 3) article 49.

⁷⁴ *ADM v Mexico* (n 1) para 133.

⁷⁵ *ibid* para 126.

⁷⁶ *ibid* para 161.

⁷⁷ *ibid* para 163.

⁷⁸ *ibid*.

⁷⁹ *ibid* para 166.

⁸⁰ *ibid* para 171.

⁸¹ *ibid* para 167.

⁸² *Loewen Group, Inc & Raymond L. Loewen v United States of America*, ICSID Case No ARB (AF)/98/3, Award (26 June 2003).

⁸³ *ibid* para 233.

The intermediate theory was viewed as one that respected the traditional structure of international law and the object and purpose of Chapter 11.⁸⁴ The Tribunal viewed Section A of Chapter 11 as substantive obligations which were inter-State instead of accruing individual rights.⁸⁵ It opined that the proper interpretation of NAFTA would not lead to an approach where investors are granted individual rights. In doing so, it distinguished the structure of NAFTA Chapter 11 and human right treaties.⁸⁶ The former only granted a procedural right of action under Section B of Chapter 11—that would not otherwise exist under international law—and simply complemented the promotion and protection of aliens under CIL.⁸⁷ With this theory, since individuals do not have rights under NAFTA, the defence of countermeasures may preclude wrongfulness of violations under Chapter 11.

In contrast, the Tribunal in *Corn Products v Mexico* found that under Chapter 11, an investor has rights of its own, distinct from those of the State of its nationality⁸⁸ as demonstrated by the conferral of procedural rights on investors, thereby implying the parties' intention to also confer substantive rights. Otherwise, a procedural right to institute proceedings to enforce rights which were not theirs would be counterintuitive.⁸⁹

The Tribunal further opined that since the State of nationality did not control the conduct of the case, nor received any payment of compensation, investors have independent rights.⁹⁰ It cited *Republic of Ecuador v Occidental Exploration* whereby the Court of Appeal for England and Wales found that investors under both NAFTA and bilateral investment treaties were asserting rights of their own rather than exercising a mere procedural power to enforce the rights of their State.⁹¹

⁸⁴ *ADM v Mexico* (n 1) para 168.

⁸⁵ *ibid.*

⁸⁶ See also Anastasios Gourgourinis, "Investors" Rights *qua* Human Rights? Revisiting the "Direct"/ "Derivative" Rights Debate' in Malgosia Fitzmaurice and Panos Merkouris (eds), *The Interpretation and Application of the European Convention of Human Rights: Legal and Practical Implications* (Martinus Nijhoff 2013) 147–182.

⁸⁷ *ibid* 171, 173–174.

⁸⁸ *Corn Products v Mexico* (n 1) para 165.

⁸⁹ *ibid* para 169.

⁹⁰ *ibid* para 173.

⁹¹ *ibid* note 72, citing *Republic of Ecuador v Occidental Exploration and Production Co*, Judgment (9 September 2005) [2006] EWCA Civ 1116, [2006] QB 432, para 14.22; see also Martins Paparinskis, 'Investment Treaty Arbitration and the (New) Law of State Responsibility' (2013) 24(2) EJIL 617–647; Tillmann R Braun, 'Globalization-Driven Innovation: The Investor as a Partial Subject in Public International Law' (2014) 15 JWIT 73, 87–88.

Gourgourinis opines that the statement reflects the Tribunal's view that 'non-state actors enjoy rights under IIAs which are inalienable, even insofar as their home State is concerned,'⁹² He further states that this is another indication of the alleged normative similarities between investor rights and human rights under the European Convention of Human Rights.

The Tribunal in *Cargill v Mexico* also believed that it would be a fiction to say that investors' rights under NAFTA Chapter 11 are the rights of the State.⁹³ The Claimant also cited the *Ecuador v Occidental* decision that it was artificial and wrong in principle to suggest that the investor pursued a claim vested in his or its home State.⁹⁴

The Tribunal agreed that the rights of investors under Chapter 11 was derived from the agreement of the State parties, and may be dependent on the continuation of that agreement. However, it argued that rights of individuals conferred by municipal legal systems did not negate the existence of such rights. The Tribunal emphasized that the investor institutes the claim, calls a tribunal into existence, and is the named party in the proceedings and award.⁹⁵

Thus, unlike the *ADM* tribunal, the other two tribunals strongly believe that Chapter 11 provides independent individual rights to investors.

3.3.1.2 *Countermeasures under NAFTA Chapter 20*

Article 31(1) of the Vienna Convention on the Law of Treaties (VCLT)⁹⁶ obliges tribunals to look at the ordinary meaning to the terms of the treaty in their *context* and in the light of its object and purpose when interpreting the treaty. While Chapter 11 does not explicitly provide for the defence of countermeasures, it is part of the comprehensive framework of NAFTA that provides for the right to countermeasures under NAFTA Article 2019. The claimants and Mexico in both *ADM v Mexico* and *Cargill v Mexico* argued about this. The claimants argued that the CIL right to countermeasures for violations of NAFTA provisions had been waived by the NAFTA Parties because NAFTA was *lex specialis*.⁹⁷ They argued that NAFTA specifies what constitutes an internationally wrongful act under the FTA and its legal consequences, as well as its own dispute settlement mechanism under NAFTA Chapters 11, 19 and 20.⁹⁸

⁹² Gourgourinis (n 86) 173.

⁹³ *Cargill v Mexico* (n 1) paras 386–387, 426.

⁹⁴ *Ecuador v Occidental* (n 91) para 17.

⁹⁵ *Cargill v Mexico* (n 1) paras 425–6.

⁹⁶ Vienna Convention on the Law of Treaties, signed on 23 May 1969, UN Doc. A/Conf.39/27, 1155 UNTS 331, 8 ILM 679.

⁹⁷ ILC Articles (n 3) article 51.

⁹⁸ *ADM v Mexico* (n 1) paras 113–114; see also *Cargill v Mexico* (n 1) paras 395–396.

It is true that under NAFTA Chapter 20, countermeasures can only be taken when there is non-compliance with a decision rendered in a Chapter 20 State-to-State arbitration,⁹⁹ and in this case, such a decision did not exist.¹⁰⁰ However, Mexico responded to the claimants' arguments stating that a party 'cannot be bound by a *lex specialis* that has proved impossible to invoke,¹⁰¹ referring to the refusal of the United States to cooperate in the composition of a panel. Mexico could have supported its position with Article 52(4) of the ILC Articles which provides that the *lex specialis* rule (pending dispute before a tribunal) does not apply if the breaching State failed to implement the dispute settlement procedures in good faith—namely the United States' refusal to provide a roster of panelists to establish a NAFTA Chapter 20 panel.¹⁰²

The Tribunal in *ADM v Mexico* dismissed the claimant's *lex specialis* argument and ruled that CIL should continue to govern all matters not covered by Chapter 11, including countermeasures.¹⁰³ The Tribunal did not address the relationship between countermeasures under Chapter 20 and obligations under Chapter 11.

In *Cargill v Mexico*, Mexico raised this concern when the tribunal assessed the nature of the rights of investors under Chapter 11. Mexico submitted that if investors had inviolable rights, this would undermine NAFTA Article 2019 on countermeasures, would constrain States' basic rights under international law, negate a 'fundamental right' of Parties under Chapter 20, and endow investors with greater rights than States.¹⁰⁴ The Tribunal noted Mexico's argument but found that there is always a range of possible countermeasures to be adopted that may not affect investors,¹⁰⁵ without considering that in a world where GVCs have become the norm, it is hard to imagine how any trade countermeasure could avoid affecting investors.

NAFTA Article 1115 provides that, '[w]ithout prejudice to the rights and obligations of the Parties under Chapter Twenty (Institutional Arrangements and Dispute Settlement Procedures), this Section establishes a mechanism for the settlement of investment disputes.' (emphasis added). NAFTA Article 1112 also provides that in the case of inconsistency between Chapter 11 with another NAFTA Chapter, the other Chapter shall prevail. If these were taken into

⁹⁹ See also *ADM v Mexico* (n 1) para 122, but it considered that the default regime under CIL applied to the situation in the case (presumably the Tribunal referred to Chapter 11).

¹⁰⁰ *ibid* para 115.

¹⁰¹ *ibid*; *Cargill v Mexico* (n 1) paras 397, 400–401.

¹⁰² ILC Articles and Commentary (n 3) 137.

¹⁰³ *ADM v Mexico* (n 1) para 119.

¹⁰⁴ *ibid* paras 391–392.

¹⁰⁵ *ibid* para 428.

account, it will be clear that States' rights to take countermeasures under Chapter 20 will prevail over its obligations under Chapter 11. Otherwise, there would be ongoing tension in the agreement itself. If lawful countermeasures under NAFTA Chapter 20 could preclude wrongfulness under Chapter 11, by extension, other trade—in particular WTO-authorized—countermeasures incorporated by CIL should also be similarly exempted.

3.3.2 Jurisdiction over the Defence of Countermeasures

In *ADM v Mexico*, the Tribunal immediately found it had jurisdiction as the defence of countermeasures arose from CIL¹⁰⁶ against the alleged violation of obligations under Chapter 11.¹⁰⁷ Interestingly, the Tribunal eventually decided that it lacked jurisdiction over one of the conditions of lawful countermeasures under the ILC Articles, namely whether the United States breached its international obligation.¹⁰⁸ Nonetheless, it proceeded to analyze the compliance of the countermeasures with other requirements, and suggested that if Mexico fulfilled these other requirements, it would consider Mexico's request for a stay of the proceedings until a Chapter 20 procedure was completed.¹⁰⁹ Paparinskis suggests that this jurisdictional hurdle—referred to as the *Monetary Gold* doctrine—actually makes the direct rights approach preferable.¹¹⁰ In order to assess the lawfulness of countermeasures, an investor-State tribunal needs to determine the existence of a prior wrongful act by the home State. This may create a strategic obstacle to admissibility of investment claims as it opens the possibility for host States to frame its breach of IIA as countermeasures.¹¹¹ He believes that if the derivative rights approach is adopted, then it would leave 'investors substantively and procedurally helpless before host state's countermeasures.'¹¹²

Indeed, jurisdiction to assess whether an initial breach had occurred can be an issue in determining the lawfulness of a countermeasure, especially when the countermeasure is imposed before there is a finding of the initial breach.¹¹³ However, we believe that the issue does not and should not affect the nature of investor rights in IIAs, particularly as regards authorized countermeasures by the WTO DSB which have gone through the rigorous process of the WTO's

¹⁰⁶ NAFTA (n 23) article 1131(1).

¹⁰⁷ *ADM v Mexico* (n 1) paras 111–120.

¹⁰⁸ *ibid* para 131.

¹⁰⁹ *ibid* para 133.

¹¹⁰ Paparinskis (n 72) 337.

¹¹¹ *ibid* 341.

¹¹² *ibid* 342.

¹¹³ For further reading on this issue, see Calamita (n 22).

dispute settlement mechanism, including a finding of the initial breach. Although this hurdle may appear for countermeasures involving initial breach of obligations under FTAs, we remain doubtful that it has any effect on the nature of investor rights.

The Tribunal in *Cargill* also found it had jurisdiction over the defence,¹¹⁴ despite it being not available to preclude wrongfulness under Chapter 11 as the obligations therein are owed to the nationals of the offending State.¹¹⁵ Even so, in its earlier statement, the Tribunal recognized that ‘countermeasures directed at an offending State will *in many, if not most*, circumstances have its intended effect on the offending State through its impact on nationals of that offending State.’¹¹⁶ This finding was peculiar because while recognizing how countermeasures work, the Tribunal still decided it would not apply in the context of the investment agreement.

In contrast to the claimants in the two previous arbitrations, the Claimant in *Corn Products International* argued that Mexico could not rely on the defence of countermeasures because the measures had been brought before a WTO Panel and the AB, and they held that the measures could not be justified under Article XX(d) of the GATT 1994 which provides for an exception for measures ‘necessary to secure compliance with laws or regulations.’¹¹⁷ The Tribunal rejected CPI’s argument because although the AB found that the measures were in violation of the GATT 1994 and could not be justified by Article XX(d),¹¹⁸ the AB did not make any findings of whether they were countermeasures, or whether they could preclude wrongfulness under NAFTA.¹¹⁹ Thus, the question of whether the measures were countermeasures under NAFTA, or under CIL remained open.¹²⁰

4 Resolving the Tension between Countermeasures in International Trade and Investment Law

Of all issues addressed by the tribunals above, the biggest systemic issue is whether WTO-compliant and WTO-authorized countermeasures can be

¹¹⁴ *Cargill v Mexico* (n 1) para 430.

¹¹⁵ *ibid* para 422.

¹¹⁶ *ibid* para 421 (emphasis added).

¹¹⁷ *Corn Products v Mexico* (n 1) para 152.

¹¹⁸ *Mexico-Tax Measures on Soft Drink* (n 34) para 75.

¹¹⁹ *Corn Products v Mexico* (n 1) para 156.

¹²⁰ *ibid* para 159.

lawful under NAFTA Chapter 11 or other similar investment agreements. Absent the defence, WTO Members may not be able to take WTO-authorized countermeasures which impact investors. This section seeks to propose several options to resolve the tension between the two regimes.

4.1 *Separating the Nature of Investor Rights and the Component Rights Found in IIAs: A Theory of Dependent Rights*

Future tribunals should refine the analyses in *Corn Products v Mexico* and *Cargill v Mexico* which equate procedural rights with independent rights. Individuals may have a right separate from States, arising from contracts with States (including concession contracts), inalienable human rights, and constitutional rights. However, what is less clear is whether the rights granted by IIAs (BITs or investment chapters in FTAs) are separate independent rights. We suggest that rights from IIAs are dependent on the State parties and not severable independent rights.¹²¹ In analysing the nature of investor rights under an IIA, the most critical factor is the intention of the State parties to the treaty.¹²²

The Tribunal in *Cargill v Mexico* emphasized that the ability of the investor to institute a claim demonstrated that investors enjoy independent rights under the treaty.¹²³ The Tribunal in *Corn Products v Mexico* also shared such a view that 'NAFTA confers upon investors substantive rights *separate and distinct* from those of the State...'.¹²⁴ Nevertheless, looking at the enforcement mechanism as an indicator does not provide us with guidance as to whether rights contained in a treaty are independent. Douglas argues that investment treaties encapsulate a direct model because of an investor's functional control of the claim instead of the State of the investor's nationality.¹²⁵ He adds that Article 33(2) of the ILC Articles mentions that investment treaties give rise to a situation where a 'primary obligation is owed to a non-state entity', and the entity can invoke State responsibility on its own.¹²⁶ However, this argument only focuses on the procedural right of investors.

¹²¹ See also Robert Volterra, 'International Law Commission Articles on State Responsibility and Investor-State Arbitration: Do Investors Have Rights?' (2010) 25(1) ICSID Review-FILJ 218, 219.

¹²² VCLT (n 96) article 31; *Avena and other Mexican Nationals (Mexico v United States)*, Judgment (31 March 2004) ICJ Rep 12; *LaGrand (Germany v United States)*, Judgment (27 June 2001) ICJ Rep 466.

¹²³ *Cargill v Mexico* (n 1) para 426.

¹²⁴ *Corn Products* (n 1) para 167 (emphasis added), see also paras 169–174.

¹²⁵ Zachary Douglas, *The International Law of Investment Claims* (CUP 2009) 17–32; Braun (n 91) 91–92.

¹²⁶ Douglas (n 125) 96–97.

Arguably, the direct rights approach has been endorsed *in passim* by several arbitral tribunals.¹²⁷ In formulating this approach, we believe that the arbitral tribunals have conflated the rights and their implications.

Such a conflated analysis needs to be unpacked to understand the true nature of investor rights in IIAs—whether it is independent from the treaty parties. The protection of individuals could be done through rules which benefit or protect individuals by the imposition of obligations on States, or rules those confer rights directly on individuals.¹²⁸ According to Parlett, '[t]here is no discernible pattern distinction between the application of one or other of these normative frameworks, and in particular there seems to have been no consideration given to the question of which normative framework was better suited to the type of benefit or protection.'¹²⁹ It is true that some treaties demonstrate the intention of the parties to grant individual rights,¹³⁰ as seen mostly in international human right treaties.¹³¹ Despite the fact that most investment treaties do not use 'rights-creating language,'¹³² we do not argue against the existence such rights for investors. However, it is less clear whether the methods of enforcing rights directly—as argued by some scholars and tribunals as direct rights—actually determine the independent nature of the rights.

The traditional method of enforcing the protection of individuals in international law has been through the exercise of diplomatic protection. An injury to an individual by a foreign State is actionable by the individual's State of nationality which espouses the claim since individuals normally do not have direct access to an international adjudicatory body such as the ICJ.¹³³ This option is not always available because the State of nationality may refuse to espouse the claim or because the ICJ does not have jurisdiction if the respondent State has

¹²⁷ *RosInvest Co UK Ltd v Russian Federation*, SCC Case No Vo79/2005, Jurisdiction Award (5 October 2007) para 153; *El Paso v Argentina Energy International Company v Argentina*, ICSID Case No ARB/03/15, Award (27 October 2011) para 551.

¹²⁸ Kate Parlett, *The Individual in the International Legal System* (CUP 2011) 348.

¹²⁹ *ibid.*

¹³⁰ See *La Grand and Avena* (n 122).

¹³¹ Universal Declaration of Human Rights, signed on 10 December 1948, UNGA Res 217 A (III); International Covenant on Civil and Political Rights, signed on 16 December 1966, 999 UNTS 171; International Covenant on Economic, Social & Cultural Rights, signed on 16 December 1966, 993 UNTS 3.

¹³² Anthea Roberts, 'State-to-State Investment Treaty Arbitration: A Hybrid Theory of Interdependent Rights and Shared Interpretative Theory' (2014) 55 Harv ILJ 20.

¹³³ See also Curtis A Bradley and Mitu Gulati, 'Customary International Law and Withdrawal Rights in an Age of Treaties' (2010) 21(1) Duke JICL 1, 4.

not accepted the court's compulsory jurisdiction and does not voluntarily submit to ICJ jurisdiction.

The application of diplomatic protection began in the late 18th century. Vattel opined that the rights and obligations of the protection of citizens were State rights, not individual rights.¹³⁴ In the 19th and early 20th centuries, various arbitrations had taken place relating to disputes over claims relating to the treatment of nationals (arrest or imprisonment),¹³⁵ expropriation of property,¹³⁶ and breach of contract by a State.¹³⁷ The procedures used in these arbitrations suggested that the claims were inter-State claims.¹³⁸ The exception at that time was the Central American Court of Justice which gave individuals exclusive control of claims,¹³⁹ but treated them as having merely procedural rights.¹⁴⁰

The Permanent Court of International Justice (PCIJ) affirmed the doctrine of diplomatic protection in *Mavrommatis* as a right of a State to ensure respect for the rules of international law.¹⁴¹ The ICJ in *Interhandel* affirmed this, but also mentioned in its *obiter dictum* that the State had 'adopted the cause of its national' whose rights had been violated.¹⁴² This demonstrates the recognition of individual rights in international law. This was made clearer in *La Grand*, when the ICJ proclaimed that individuals can have rights created by international treaties if the State parties intended to confer it, as indicated in the text of the treaty.¹⁴³ This is confirmed in *Avena v Mexico*, where the court found that Article 36(1) of the VCCR confers rights to individuals.¹⁴⁴ In *Avena*, the ICJ recognized

¹³⁴ Emer de Vattel, *The Law of Nations or, Principles of the Law of Nature Applied to the Conduct and Affairs of Nations and Sovereigns* (first published in 1758, Béla Kapossy and Richard Whatmore (eds), Liberty Fund 2008), bk II, ch VI, 298, 71.

¹³⁵ *Great Britain – Peru* (1864) in John Bassett Moore, *History and Digest of the International Arbitrations to Which the United States Has Been a Party* (vol V, Government Printing Office 1898) 4967; *Spain – US* (1870) in *ibid* (vol II) 1007; *Great Britain – Colombia* (1872) in *ibid* (vol II) 2050.

¹³⁶ *Great Britain – Russia* (1902) IX UNRIIA 51.

¹³⁷ *US – Paraguay* (1859) in Moore (n 135) (vol II) 1485; *Great Britain – US* (1863) in Moore (n 135) (vol I) 237.

¹³⁸ Parlett (n 128) 53.

¹³⁹ Convention for the Establishment of a Central American Court of Justice, signed on 20 December 1907, 2 AJIL 231, article 2.

¹⁴⁰ Parlett (n 128) 65.

¹⁴¹ *Mavrommatis Palestine Concessions (Greece v United Kingdom)*, Judgment No 2 (30 August 1924) PCIJ Rep Ser A No 2, 12.

¹⁴² *Interhandel (Switzerland v United States)*, Judgment (21 March 1959) ICJ Rep 1959, 26–27.

¹⁴³ *La Grand* (n 122) para 77.

¹⁴⁴ *ibid*; *Avena* (n 122) para 40.

the 'special circumstances of interdependence of the rights of the State and of individual rights' within the context of the ability of both parties to submit a claim.¹⁴⁵ Nevertheless, in neither of these cases, the PCIJ or the ICJ opine about the nature of the individual rights, specifically whether they were independent or dependent on the State parties.

Quoting the ICJ's characterization of rights in *Avena*, Roberts suggests a conceptualization of interdependent rights where 'substantive investment treaty rights are held jointly by investors and their home states' in the context that either the investor or the home State, but not both, could bring a claim, as one would preclude the other.¹⁴⁶

She also contends that given that both home States and investors have been granted a procedural mechanism in vindicating investment treaty obligation, one should presume that both have been granted substantive rights under investment treaties absent clear wording to the contrary.¹⁴⁷ While we agree that the substantive rights may exist, we question the nature of the rights. In fact, we suggest that the rights of investors remain dependent on the State— it can be overridden by the rights of the State parties.

On the other end of the spectrum, Reisman argues that investment treaties create rights for third-party beneficiaries.¹⁴⁸ However, he puts a lot of weight on the rights and expectations of the third-party beneficiaries and argues that State parties' interpretation obtained through a State-to-State dispute settlement mechanism should not undermine them.¹⁴⁹ This view is problematic because such a formulation cannot be found in IIAs. Moreover, an additional argument that may be brought to bear is that Article 37(2) of the VCLT provides as follows:

When a right has arisen for a third State in conformity with article 36, the right may not be revoked or modified by the parties if it is established that the right was intended not to be revocable or subject to modification without the consent of the third State.

While this strictly applies to rights between States, it suggests that international law recognizes that rights can be revoked if the parties intended for

¹⁴⁵ *ibid.*

¹⁴⁶ Roberts (n 132) 18, 22.

¹⁴⁷ *ibid* 20–21; see further Anthea Roberts, 'Triangular Treaties: Rethinking the Extent and Limits of Investment Treaty Rights' (2015) Harv Intl LJ (forthcoming).

¹⁴⁸ *Republic of Ecuador v United States of America*, Expert Opinion with Respect to Jurisdiction in the Interstate Arbitration initiated by Ecuador against the United States (Professor W Michael Reisman) (Permanent Ct Arb Case No 2012–5, 24 April 2012) paras 15, 26, 29–32.

¹⁴⁹ *ibid* para 4.

those rights to be revocable. We know of no IIA that specifically or impliedly provides that the rights granted to investors were not intended to be revocable or modifiable.

Some international agreements may provide that certain individuals may have an access to international tribunals to bring a direct claim against a State.¹⁵⁰ This is evident in some international human rights treaties¹⁵¹ as well as some IIAs with investor-State dispute settlement (ISDS) clauses. However, we suggest that this access does not mean that the rights are independent. We suggest that individuals may enjoy rights under CIL and treaties but the rights granted may still be dependent or independent of the State parties, depending on the intention of the States.

The reasoning of the tribunal in *Corn Products* and *Cargill* that direct enforcement mechanism in ISDS provisions indicates the desire of the States to grant independent individual rights to investors, separate from the States¹⁵² appears to make a logical leap.

First, this reasoning is not supported by customary rules of interpretation. According to Article 31 of the VCLT, in interpreting a treaty, one should look into the ordinary meaning of the text in their context and in the light of its object and purpose. The ICJ in *Avena* and *La Grand* also ruled that the text of the treaty demonstrates the intention of the parties.¹⁵³

No IIA states that rights of the investors are independent of the State parties. Most IIAs provide for the ability of States—the masters of the treaty—to amend¹⁵⁴ or terminate¹⁵⁵ IIAs and this may suggest that the rights therein are not intended to be independent.

This seems to be supported by the premise behind the recent United Nations Convention on Transparency in Treaty-based Investor-State Arbitration adopted on 10 December 2014.¹⁵⁶ The Convention allows two state parties to agree to

¹⁵⁰ Parlett (n 128) 47; David Harris, *Cases and Materials on International Law* (7th edn, Thomson Reuters 2010) 628.

¹⁵¹ Convention for the Protection of Human Rights and Fundamental Freedoms, signed on 4 November 1950 and its protocols ETS 5; 213 UNTS 221, article 34.

¹⁵² *Corn Products v Mexico* (n 1) para 173; *Cargill v Mexico* (n 1) para 426; *Ecuador v Occidental* (n 91) para 14.22. Douglas (n 125) 167–184; Braun (n 91) 91, 97; Andrea K Bjorklund, 'Private Rights and Public International Law: Why Competition Among International Economic Law Tribunals is Not Working' (2007–2008) 59(2) *Hastings Law Journal* 241–307, 265.

¹⁵³ *La Grand* (n 122) para 77; *Avena* (n 122) para 40.

¹⁵⁴ VCLT (n 96) articles 39–41.

¹⁵⁵ *ibid* articles 54–64.

¹⁵⁶ United Nations Information Service, 'General Assembly's adoption of the United Nations Convention on Transparency in Treaty-based Investor-State Arbitration', UNIS/L/210 (2014).

apply the UNCITRAL Transparency Rules to any investor-state arbitration proceedings, without necessarily obtaining the prior consent from existing investors. Unless the rights only accrue to investors upon the filing of a claim,¹⁵⁷ this suggests that the drafters of the Convention assumed that the rights were dependent on the state parties.

The so-called procedural rights—direct access to international arbitration through an ISDS clause— can be modified. For example, unilateral denunciations of the Convention on the Settlement of Investment Disputes between States and Nationals of Other States (ICSID Convention) by several countries may affect the procedural rights of investors.¹⁵⁸ Treaties can also be amended with the consent of all the parties without the consent of the investor.

Second, the reasoning that essentially promotes investor rights as an independent right, similar to human rights seems flawed.¹⁵⁹ It is true that there are overlaps between the two regimes.¹⁶⁰ However, human rights obligations are universal and protect individuals from the actions of all States including and sometimes especially those of their home State. Further, the formulation of the language in an IIA is weaker than in human right treaties. Compared to human right treaties which recognize the inherent rights of humans, IIAs do not recognize the ‘inherent’ right of investors.¹⁶¹ On the other hand, IIAs concern protection of individuals from actions of a host State on a reciprocal basis and based on equal obligations undertaken by the State parties.¹⁶² Gourgourinis draws a

¹⁵⁷ United Nations General Assembly, ‘Settlement of commercial disputes: Draft convention on transparency in treaty-based investor-State arbitration’, A/CN.9/812 (4 March 2014). Article 5 provides that the rules do not apply to any proceedings commenced before the Convention takes effect between the state parties.

¹⁵⁸ See also Christoph Schreuer, ‘Consent to Arbitration’ (2005) 2(5) TDM 7; Christoph Schreuer, ‘Denunciation of the ICSID Convention and Consent to Arbitration’ in Michael Waibel and others (eds), *The Backlash Against Investment Arbitration: Perceptions and Reality* (Kluwer Law International 2010) 353, 358; compare with Michael Nolan and Frederic Caivano, ‘Limits of Consent – Arbitration without Privity and Beyond’ in MA Fernandez-Ballesteros and David Arias (eds), *Liber Amicorum Bernardo Cremades* (La Ley 2010) 873, 875–886 and 880–890; Andrés Mezgravis and Carolina González, ‘Denunciation of the ICSID Convention: Two Problems: One Seen and One Overlooked’ (2012) 7 TDM 1, 5–10; VCLT (n 96) article 70(1)(b).

¹⁵⁹ Gourgourinis (n 86) 173–174.

¹⁶⁰ Paporinskis (n 91) 623; Ioana Knoll-Tudor, ‘The Fair and Equitable Treatment Standard and Human Rights Norms’ in Pierre-Marie Dupuy, Ernst-Ulrich Petersmann and Francesco Francioni (eds), *Human Rights in International Investment Law and Arbitration* (OUP 2009) 335.

¹⁶¹ Roberts (n 132) 20.

¹⁶² Tania Voon, Andrew Mitchell and James Munro, ‘Parting Ways: The Impact of Mutual Termination of Investment Treaties on Investor Rights’ (2014) 29 ICSID Review–FILJ 451, 457–458.

distinction between human rights and investor rights by stating that the normative consequence of human right treaties, aside from its wording, ‘disentangles protection from nationality, but also of integral or interdependent nature of human rights obligations by the violation of which cannot be excused by virtue of an unilateral decision by the State of nationality of the victim and its force of obligation is self-existent, absolute, and inherent for each party, lacking reciprocity.’¹⁶³ Paparinskis also opines that, ‘it is hard to arrive at a conclusion that investment protection treaties can be excluded from countermeasures because of their substantive similarities to human rights.’¹⁶⁴

Conversely, some human rights norms are recognized as inalienable despite the fact that their enforcement may have to be done by virtue of diplomatic protection. This further reinforces our argument that the direct enforcement mechanism is not determinative of the independence of investor rights under IIAs. We believe that this disentangling of the methods of enforcement of rights and the nature of those rights militates against any analysis that conflates them.

Volterra suggests that there is some room to argue that investors have rights directly vested on them because they can waive those substantive rights. However, he argues that if investors only enjoy derivative procedural rights to bring the claim, they cannot waive any substantive rights.¹⁶⁵ Some awards have recognized that, in theory, an investor can waive his rights under an investment treaty.¹⁶⁶ We agree that investors may enjoy substantive rights under an IIA and may waive the invocation of these rights. Nonetheless, it is not entirely clear to us why these rights must be directly vested on the investor and must be independent in order to be waived. It remains possible that these substantive rights continue to be dependent on the State parties’ consent to the agreement and are not separate rights. In fact, they could be third-party rights dependent on the States’ continued agreement but capable of being waived by investors. Some domestic jurisdictions recognize such third party rights, for example in the case of famous English *Himalaya* clause.¹⁶⁷ We are not suggesting that investor rights are definitely third-party rights, but we contest the notion that

¹⁶³ Gourgourinis (n 86) 169, 174; see for inalienable nature of human rights: General Assembly Resolution 32/130, 32 UN GAOR Supp (No 45) at 151, UN Doc A/32/45 (1977); Louis B Sohn, ‘The New International Law: Protection of the Rights of Individuals Rather than State’ (1982) 32(1) Am U L Rev 18.

¹⁶⁴ Paparinskis (n 72) 264–352, 330.

¹⁶⁵ Volterra (n 121) 222.

¹⁶⁶ *Duke Energy Electroquil v Republic of Ecuador*, ICSID Case No ARB/04/19, Award (18 August 2008) para 159; compare with *TSA Spectrum de Argentina v Argentine Republic*, ICSID Case No ARB/05/5, Award (19 December 2008) paras 54–55.

¹⁶⁷ See more William Tetley, ‘The Himalaya Clause-Revisited’ (2003) 9 JIML 40, 41.

they must be separate rights merely because they can be waived. We suggest instead that the nature of investor rights could more easily fit into a model of third-party rights since the termination of IIAs without the consent of the investors potentially terminates their rights, subject to any survival clause.¹⁶⁸

4.2 *Redefining 'Individual Rights' and Countermeasures*

Future tribunals can also reconsider the inviolability of individual rights in IIAs particularly in the context of countermeasures under CIL. As argued above, although individual rights may exist in IIAs, they are not necessarily independent. If these individual rights are dependent on the rights of their home State, it could mean that countermeasures affecting such individual rights may preclude wrongfulness under Article 49 of the ILC Articles.

Paragraph 5 of the Commentary to Article 49 provides:

This does not mean that countermeasures may not incidentally affect the position of *third States* or indeed *other third parties*. For example, if the injured State suspends transit rights with the responsible State in accordance with this chapter, other parties, including third States, may be affected thereby. If they have no individual rights in the matter they cannot complain.¹⁶⁹

Third States clearly have their own independent rights which are separate from the rights of other States. We argue that this is the type of individual rights referred to by the Commentary. Crawford opines that, 'the ILC Articles make no attempt to regulate questions of breach between a state and a private party such as a foreign investor.'¹⁷⁰ Indeed, the ILC did not take any view as regards whether investors' rights under investment treaties are the rights owed to their home States or rights accrued directly from international treaties.¹⁷¹ Thus, if third parties like investors have no independent individual rights—*sans* attachment to the rights of States, such as inalienable human rights—countermeasures against their home State which may incidentally affect them may be defensible. This interpretation is further supported by the fact that the ILC Articles clearly accept the possibility that companies may lose business or even go bankrupt

¹⁶⁸ Voon, Mitchell and Munro (n 160).

¹⁶⁹ ILC Articles and Commentary (n 3) 130 para 5 (emphasis added).

¹⁷⁰ James Crawford, 'Investment Arbitration and the ILC Articles on State Responsibility' (2010) 25 ICSID Review-FILJ 127, 130.

¹⁷¹ Crawford (n 5) 888; Volterra (n 121) 222.

because of certain countermeasures, as '[s]uch indirect or collateral effects cannot be entirely avoided.'¹⁷²

We submit that the individual rights of investors that are obtained through IIAs remain revocable by the master of treaties, namely States. The rights are not independent, but instead fully dependent on the State parties and rely on the existence of the treaty.¹⁷³

In connection with a WTO-authorized countermeasure, the breach of the right of the home State under the relevant IIA—right to have its citizens protected in the host State—is lawful because of the home State's initial breach of its WTO obligations. Since the right of the investor is dependent on the forfeited right of the home State, the breach of the right of the investor is also justified by the lawful countermeasure.

This is different from rights arising from concessions contracts entered into between a State and a private individual. In such a contract, both parties have their own respective rights and obligations. Private individuals have rights in the contract and can enforce the contract before tribunals, including arbitration if the terms of the contract provides as such. In contradistinction, in the last 50 years in order to create a better investment climate, States have decided to render benefits to investors, regardless the fact that they are not direct parties to the treaties by way of BITs and Investment Chapters in FTAs. Only in the former case of a direct contract with States like a concessions contract, do investors enjoy independent individual rights and in such a case, it may be that a countermeasure which affects those rights may result in State responsibility.

Thus, we suggest that absent any such independent rights, investor rights based on IIAs between States may be affected by countermeasures without incurring State responsibility provided that those countermeasures are WTO-authorized and proportional.

4.3 *Countermeasures and Innocent Bystanders*

One potential critique of our theory is the argument of 'innocent bystanders'¹⁷⁴—innocent investors have to suffer from the breach conducted by its home State.

¹⁷² ILC Articles and Commentary (n 3) 130 para 5.

¹⁷³ Andrew Newcombe and Lluís Paradell, *Law and Practice of Investment Treaties: Standards of Treatment* (Kluwer Law International 2009) 511 para 10.19; see also Francisco Gonzales de Cossio, 'Investment Protection Rights: Substantive or Procedural' <<http://208.56.169.136/PDF/arbitraje/Investor%20Rights%20Procedural%20or%20Substantive.pdf>> accessed 8 October 2014, at 10; Roberts (n 132) 21.

¹⁷⁴ This issue has also been raised exclusively within the trade regime as identified in Marco Bronckers and Naboth van der Broek, 'Financial Compensation in the WTO—Improving the Remedies of the WTO Dispute Settlement' (2005) 8(1) JIEL 101–126, 103.

Among the questions raised could be why innocent investors should be paying for the wrongs of its home State, and who should compensate these investors for the losses incurred.

Dani mentions that countermeasures in the WTO have been criticized as contradicting the WTO constitutive purpose and may amplify the relative economic importance of the parties.¹⁷⁵ Bronckers and Van der Broek add that trade countermeasures can negatively affect economic freedom in both exporting and importing countries.¹⁷⁶ This is true, countermeasures are not preferred options; compliance is the preferred WTO option. However, if State compliance is not forthcoming, a second-best remedy in the form of countermeasures is better than none.

Indeed, the Tribunal in *Cargill v Mexico* recognized that ‘countermeasures directed at an offending State will in many, if not most, circumstances have its intended effect on the offending State through its impact on nationals of that offending State.’¹⁷⁷ We argue that unfortunately, negative effects of innocent bystanders are unavoidable and part of the systemic order.¹⁷⁸

In *FIAMM & Fedon*, Italian nationals brought such a claim as innocent bystanders against the European Union (EU) before the European Court of Justice demanding compensation for the losses they suffered due to a countermeasure against the EU, rather than against the State imposing such countermeasure (United States).¹⁷⁹ In that case, the Court refused the claims mainly because Community Law did not provide for a regime that enabled the claimants to argue that the Community was liable for its legislative conduct that violated the WTO agreements.¹⁸⁰

The Claimants also argued that, in the alternative, the Community was liable for its lawful act that adversely affected individual interests. However, the Court also rejected this argument.¹⁸¹ The Court noted that the right to property and the freedom to pursue a trade or profession were general principles of

¹⁷⁵ Marco Dani, ‘Remedying European Legal Pluralism: The *FIAMM and Fedon* Litigation and the Judicial Protection of International Trade Bystanders’ (2010) 21(2) EJIL 303, 320.

¹⁷⁶ Steve Charnovitz, ‘Rethinking WTO Trade Sanctions’ (2001) 95 AJIL 810–811; Bronckers and van der Broek (n 174) 103–104.

¹⁷⁷ *Cargill v Mexico* (n 1) 421.

¹⁷⁸ ILC Articles and Commentary (n 3) 167.

¹⁷⁹ Joined cases C-120/06 P and C-121/06 P, *Fabbrica italiana accumulatori motocarri Montecchio SpA (FIAMM) and others v Council and Commission* and *Giorgio Fedon & Figli SpA and others v Council and Commission*, Judgment of the Court (Grand Chamber) (9 September 2008) ECR 2008 I-6513.

¹⁸⁰ *ibid* paras 176, 188.

¹⁸¹ *ibid* para 175.

Community Law. Yet these right and freedom were not absolute and subject to objectives of general interest pursued by the Community.¹⁸² Any restrictions to the right may give rise to non-contractual liability of the Community if it ‘impair[s] the very substance of those rights in a *disproportionate* and *intolerable* manner ...’.¹⁸³ The Court also pointed that the lack of provision to deal with compensation calculated to avoid or remedy that impairment could render the Community’s legislation disproportionate and intolerable.¹⁸⁴

In *FIAMM & Fedon*, the Court opined that the right to property and the freedom to pursue a trade or profession ‘cannot be extended to protect *mere commercial interests or opportunities*, the uncertainties of which are part of the very essence of economic activity.’¹⁸⁵ The Court opined further that international traders must be aware that their businesses and commercial position may be affected and altered by various circumstances, including countermeasures.¹⁸⁶

Applying the Court’s reasoning to this context, we argue similarly that foreign investors must also be aware of this possibility of countermeasures. It is part of the risks of their commercial activities. The host State should not be responsible compensating these foreign investors. Nevertheless, we are sympathetic to the case of innocent bystanders. Therefore, in the following Section, we suggest that the proportionality test for an authorized countermeasure should be applied.

4.4 *Proportionality Test for Countermeasures in International Investment Law*

The Tribunal in *ADM v Mexico* provided us with a hint of the proportionality test in international investment law. This test was applied as part of the requirements for a lawful countermeasure under CIL, as reflected in Article 51 of the ILC Articles—countermeasures must be ‘commensurate with the injury suffered, taking into account the gravity of the internationally wrongful act and the rights in question’. The Tribunal assessed proportionality based on the appropriateness of the aim compared to the structure and content of the breached rule (an ‘aims and effects’ approach),¹⁸⁷ and based on a qualitative comparison between the breach and the rights in question.¹⁸⁸

¹⁸² *ibid* para 183.

¹⁸³ *ibid* para 184 (emphasis added).

¹⁸⁴ *ibid*.

¹⁸⁵ *ibid* para 185 (emphasis added).

¹⁸⁶ *ibid* para 186.

¹⁸⁷ *ibid* para 154.

¹⁸⁸ *ADM v Mexico* (n 1) para 155.

The Tribunal cited the *Tehran Hostages Case* to illustrate that the aim of the countermeasure has to be connected to the alleged breach. In that case, Iran claimed in letters by its Minister of Foreign Affairs that the United States' breach of international obligations justified the seizure of the US diplomatic offices and personnel in Tehran.¹⁸⁹

It is surprising that the Tribunal cited the *Tehran Hostages* case because Iran did not specifically raise the defence as countermeasures under CIL nor furnished any further information regarding the alleged criminal activities of the United States.¹⁹⁰ In fact, the ICJ did not specifically make a finding about proportionality in rejecting the defence. Rather the ICJ only found that the defence was unacceptable 'because diplomatic law provides necessary means of defence against, and sanction for, illicit activities by members of diplomatic or consular missions.'¹⁹¹ The case really turned on the *lex specialis* nature of diplomatic or consular issues as regulated under the Vienna Convention on Consular Relations (VCCR)¹⁹² as reflected in Article 50(2)(b) of the ILC Articles on the inviolability of diplomatic or consular agents, premises, archives and documents. However, the Tribunal still relied on the case and found that the failure to resort to other available measures which did not impair the legal obligations to end an alleged wrongful act reflected a different aim, thus was not proportional.¹⁹³

It remains questionable whether this approach can be adopted in the context of countermeasures in trade and investment law because by nature, countermeasures are breaches of international law whose wrongfulness is by definition precluded. Requiring non-violation of the law in a more general context seems to be excessively demanding and will make the countermeasures always disproportionate.

The Tribunal then assessed the proportionality of the countermeasures based on a qualitative-comparison approach. It considered the alleged breaches of NAFTA Chapter 7 and Chapter 20 on trade-related obligations with regard to agricultural goods and to sanitary and phytosanitary measures, as well as obligations for State-State dispute settlement, and compared them with NAFTA Chapter 11 obligations which make private individuals (investors)

¹⁸⁹ *Case Concerning the United States Diplomatic and Consular Staff in Tehran (United States v Iran)*, Judgment (24 May 1980) ICJ Rep 3 para 81.

¹⁹⁰ *ibid* para 82; Calamita (n 22) 283.

¹⁹¹ *Tehran Hostages Case* (n 187) para 83.

¹⁹² Vienna Convention on Consular Relations, signed on 18 April 1961, 596 UNTS 261; 21 UST 77; TIAS 6820.

¹⁹³ *ADM v Mexico* (n 1) para 156.

as the direct object and beneficiaries, notwithstanding the fact that they do not hold individual substantive rights.¹⁹⁴

The Tribunal found that since the obligations allegedly breached by the United States were inter-State obligations, but as the countermeasures breached obligations towards private individuals, the countermeasure was not proportionate nor necessary nor reasonably connected to the aim of Mexico of inducing compliance by the United States.¹⁹⁵ The Tribunal stated that 'Mexico's aim to secure compliance by the United States of its obligations under Chapter VII and XX could have been attained by other measures not impairing the investment protection standards under Section A [Chapter XI of NAFTA],¹⁹⁶ without specifying the alternative measure, and simply concluded that Mexico's countermeasures disproportionate.¹⁹⁷

This is startling because if followed to its logical conclusion, WTO-compliant countermeasures, which in nature would always arise out of inter-State obligations, will almost never be lawful countermeasures in international investment law and could lead to a responsibility to compensate all affected investors. Today, no longer are goods manufactured only in one country and then shipped across to another. As highlighted earlier, complex integrated production networks, commonly known as GVCs have resulted in MNCs setting up subsidiaries all over the world in order to achieve production efficiency. This means that goods are often traded between subsidiaries which are by definition investors present in most parts of the world. These investors can be affected by trade measures of WTO Members, for example: suspension of concessions in the agreements on trade in goods – e.g., duties, taxes, suspension of concession in GATS, or suspension of protection of IP rights.

The *ADM v Mexico* tribunal's proportionality test should also be refined. The proportionality of the measure should be weighed against the alleged breach and the reasonableness of the measures to reach its intended goal. In the assessment of the reasonableness of the measures, the effect on investors may be taken into consideration. However, one should avoid a reductive conclusion that merely affecting investors renders the countermeasure disproportionate.

Perhaps the proportionality principle found in many other international law regimes might serve as a starting point to develop a better test. As this

¹⁹⁴ *ibid* para 157.

¹⁹⁵ *ibid* para 158.

¹⁹⁶ *ibid* para 159.

¹⁹⁷ *ibid* para 160.

matter of proportionality for countermeasures has not yet been the subject of investor-State jurisprudence, it is difficult to fully conceptualize a test for such a proportionality doctrine, much less justify it clearly on jurisprudential grounds. However we note that with respect to the necessity doctrine and the application of proportionality to that doctrine, there have been at least one investment case¹⁹⁸ and many scholarly commentaries.¹⁹⁹ Some scholars suggest bringing in the proportionality test through the methodology of ‘general principles of law’,²⁰⁰ or through an interpretation of the word ‘necessary’ found in many IIAs’ exception clauses.²⁰¹ It is not within the scope of this article to fully grapple with this and we hope to do so in a future article. It remains only for us to suggest that a proportionality test be used to safeguard against abuses of completely unregulated countermeasures and that such a proportionality test might be one that is perhaps similar to the less restrictive measure approach²⁰² in the WTO which requires the complaining Member to identify the possible alternatives to the measure that the other Member could have taken.²⁰³ Although the availability of a less-restrictive measure may be

¹⁹⁸ *Continental Casualty Company v Argentine*, ICSID Case No ARB/03/9, Decision on the Application for Partial Annulment of Continental Casualty Company and the Application for Partial Annulment of the Argentine Republic (16 September 2011) para 133.

¹⁹⁹ See Markus Wagner, ‘Regulatory Space in International Investment Law and International Trade Law’, 36 U Penn JIL 1 (2015), available at <http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2403959> accessed 8 October 2014.

²⁰⁰ Alec Stone Sweet and Giacinto della Cananea, ‘Proportionality, General Principles of Law, and Investor-State Arbitration: A Response to Jose Alvarez’ (2014) Yale University, <http://works.bepress.com/cgi/viewcontent.cgi?article=1059&context=alec_stone_sweet> accessed 8 October 2014; Benedict Kingsbury and Stephan W Schill, ‘Public Law Concepts to Balance Investors’ Rights with State Regulatory Actions in the Public Interest - The Concept of Proportionality’ in Stephan W Schill (ed), *International Investment Law and Comparative Public Law* (OUP 2010) 75; for a contrasting view see Jose E Alvarez and Tegan Brink, ‘Revisiting the Necessity Defense’ (2012) *Yearbook on International Investment Law and Policy 2010–2011*, 319.

²⁰¹ Andrew D Mitchell and Caroline Henckels, ‘Variations on a Theme: Comparing the Concept of “Necessity” in International Investment Law and WTO Law’ (2013) 14 CJIL 93.

²⁰² *United States — Standards for Reformulated and Conventional Gasoline*, WT/DS2/R, Report of the Panel (29 January 1996) paras 6.26, 6.28; *US — Gasoline*, WT/DS2/AB/R, Report of the Appellate Body (29 April 1996) paras 23–24; *European Communities — Measures Affecting Asbestos and Products Containing Asbestos*, WT/DS135/AB/R, Report of the Appellate Body (12 March 2001) para 171; a similar test can be found in the case of *R. Buet v Ministère public*, Case C-382/87, 1982 ECR 1235, 1251, para 11.

²⁰³ *Brazil — Measures Affecting Imports of Retreaded Tyres*, WT/DS332/AB/R, Report of the Appellate Body (3 December 2007) para 156.

taken into account for this proportionality test, the simple fact that another measure is available should not by itself render countermeasures disproportionate. This should require further analysis of the measures by looking at the degree of its reasonableness to reach its intended goal²⁰⁴ - namely to induce compliance. The best example of this 'weighing and balancing' test in the trade jurisprudence can be found in WTO cases such as in *Brazil-Retreaded Tyres*²⁰⁵ and *China-Publications & Audiovisual*.²⁰⁶ We do not make any concrete recommendation in this regard and suggest only that this requires further study.

As mentioned above international law recognizes that incidental damage caused by a countermeasure is sometimes unavoidable. However, States should not take a measure that is expected to cause incidental damage to investors, which would be excessive (disproportionate) in relation to the concrete advantage anticipated.²⁰⁷ In the EU, the test applied is weighing the adverse effect on the applicant's legally protected interest against the importance of the lawful aim served by the regulation.²⁰⁸ In addition, the tribunal should also consider whether the measure is applied discriminatorily, e.g., only to foreign investors and not on domestic investors whose investments are in like circumstances.

4.5 *Joint-Interpretation or an Additional Provision into an IIA*

If our arguments for the unpacking the nature of investor rights and the need to reconsider the effect of countermeasures still does not convince tribunals and they continue to take the position that investment treaties confer independent individual rights on investors, a legislative solution may be needed.²⁰⁹ It is alarming that WTO-compliant countermeasures duly authorized by the DSB could conceivably be considered unlawful before an arbitral tribunal either established under the NAFTA or other IIAs. This will potentially undermine the compliance mechanism of the WTO DSM. We do not believe that it is

²⁰⁴ *ibid*; *US-Gambling* (n 38) WT/DS285/AB/R, Report of the Appellate Body (7 April 2005) para 308.

²⁰⁵ *Brazil-Retreaded Tyres* (n 203) paras 210–211.

²⁰⁶ *China-Publications and Audiovisual*, WT/DS363/AB/R, Report of the Appellate Body (21 December 2009) para 242 n 455.

²⁰⁷ This test can also be seen in Protocol I of 1977 to the Geneva Conventions; see Thomas M Franck, 'On Proportionality of Countermeasures in International Law' (2008) 102 (4) AJIL 715, 725.

²⁰⁸ *ibid* 753; *The Queen v Minister for Agriculture, Fisheries and Food, ex parte Fedesa*, Case C-331/88, 1990 ECR I-4023.

²⁰⁹ See also Michael Ewing-Chow and Junianto James Losari, 'Which Is to Be the Master?: Extra-Arbitral Interpretative Procedures for IIAs' (2014) 11(1) TDM.

in the interest of any State to do so—especially not in the interest of WTO Members.

In the case of NAFTA, this tension between trade and investment law could be resolved by the NAFTA FTC²¹⁰ through issuance of a binding interpretation under NAFTA Article 1131. In its interpretation, the FTC could state the following:

Nothing in Chapter 11 of the NAFTA may prohibit a Party to take measures in accordance with NAFTA Article 2019 or WTO DSU Article 22.

This type of clause may address the issue better because the tribunal is not required to analyze what constitutes ‘individual rights’ under Article 49 of the ILC Articles.

While some other FTAs like the United States-Singapore FTA²¹¹ and the ACIA,²¹² among others, provide for a joint-interpretation mechanism, most older BITs do not have such a joint-interpretation mechanism. In such a case, Article 31(3)(a) of the VCLT makes possible for treaty parties to issue a joint-interpretation which can be highly persuasive to tribunals.²¹³ Since no BIT contains a provision on countermeasures, we suggest for a joint-interpretation on provisions regarding instituting a claim before investor-State arbitration. The joint-interpretation may include a clause such as, ‘[a]n investor may bring a claim against the breach of this agreement subject to authorized countermeasures under any FTAs of the contracting parties or WTO DSU Article 22.’

This may seem to be an oversimplification of joint-interpretation, and we recognize that if the joint-interpretation in effect actually amends the treaty, it should properly go through the procedures prescribed by the BIT and the relevant domestic laws. However, we argue that in this case, it does not amend the BIT because as recognized by the tribunals, the notion of countermeasures under CIL does exist for treaty parties of IIAs.²¹⁴ Additionally, it merely restates the CIL position on State responsibility.

²¹⁰ NAFTA (n 23) article 2001.

²¹¹ Singapore – United States FTA, signed on 6 May 2003, 19 USC 3805, article 15.21.

²¹² ASEAN Comprehensive Investment Agreement, signed on 26 February 2009, article 40(2); see also Canada – European Union Free Trade Agreement (CETA) Draft, published on 26 September 2014, article X.27.

²¹³ See also Anthea Roberts, ‘Power and Persuasion in Investment Treaty Interpretation: The Dual Role of States’ (2010) 104 AJIL 179.

²¹⁴ This is especially true in the case of ICSID Arbitration where the parties to the BIT do not agree on the applicable law, article 42(1) of the ICSID Convention shall apply namely international law, including CIL.

We also note that an issue may arise as regards the willingness of the treaty parties to issue this type of joint-interpretation. However, the past investment disputes on this issue actually raise an important concern for the trade interests of these States.

Alternatively, for agreements without any joint-interpretation mechanism, it may provide more certainty for the parties to add a clause into their existing IIAs (including by way of a protocol) that recognizes the right of parties to take countermeasures. This is especially useful for the parties who are members of the WTO or members of certain FTAs. The clause can be formulated as follows:

Nothing in this agreement shall prevent a Contracting Party from taking a trade countermeasure that has been authorized by the Dispute Settlement Body of the World Trade Organization or the authorized body of another relevant trade agreement against the other Contracting Party, despite the fact that the countermeasure may have effects on investments of nationals or companies of the other Contracting Party under this agreement.

In fact, there are several BITs which provide implicitly the possibility of raising WTO-compliant countermeasures in IIAs. For example, Article 3(5) of the 2002 Thailand – Russia BIT provides:

Nothing in this Agreement shall oblige the Contracting Parties to grant to investor and investment of each other the treatment under this Article which is more favourable, than the treatment that they will grant to each other pursuant to the obligations under the Agreement Establishing the World Trade Organization (WTO) of April 15, 1994, including obligations under General Agreement on Trade in Services (GATS) and also under any other multilateral arrangement concerning the treatment of investments which both Contracting Parties are parties to.

We acknowledge that amending an IIA is not simple. Where an IIA does not specify the procedure to amend, Article 39 of the VCLT provides it can be done by an agreement between the parties. This may not be necessarily difficult to achieve especially when both treaty parties are members of the WTO because there is greater interest for their potential future WTO-compliant countermeasures to be recognized in the investment regime.

An amendment may need to happen long before any countermeasures are to be imposed. Otherwise, the party subject to the countermeasures may be

reluctant to agree to such an amendment, especially when its affected investor has lobbied the government regarding the negative impacts that he/she may suffer. The other difficulty is the requirement to obtain ratification which will involve the legislative branch of the parties. Where political interest is at play, this is not an easy task.

Alternatively, where the parties cannot agree to amend an existing treaty arrangement, State parties may simply terminate or let an existing treaty lapse, and renegotiate a new treaty. However, the former will be subject to the termination clause of each treaty whereby consent by both members is needed in the process, and the ratification process may pose an extreme political challenge to both parties, similar to an actual amendment procedure.

5 Conclusion

The article has highlighted the increasing tension between the regimes of trade and investment law. This will be an area of more future conflict of laws as the way trade and investment by MNCs today converge in the form of GVCs. More attention will need to be given to the interaction of the regimes.

In this particular instance, it is hard to discern that a WTO-compliant countermeasure—that has gone through assessment of a dispute settlement body (panel, potentially the AB and potentially arbitration tribunals) and authorized by the DSB—can lead to an investment claim against the State. The central issue in this specific case is the nature of individual rights under IIAs. It is critical to determine whether countermeasures can preclude wrongfulness under the IIAs.

Article 31(1) of the VCLT provides that all treaties including IIAs must be interpreted in good faith based on their ordinary meaning in their context and in the light of its object and purpose. The context of an IIA requires us to look at its general framework, the international law regime which acts as its foundation, and its relationship with other international treaties especially those dealing with international economic law. Even though textual reading of the procedures found in some IIAs may impressionistically suggest that they confer rights to investors, in reality the rights are not independent from the State parties. No IIA explicitly provides that investor rights therein are independent. This is clearly shown from the fact that State parties may jointly revoke the treaty without the consent of the investors. This is different from individual rights in human right treaties, or even

in concession contracts entered by an investor and a State, where the individuals do enjoy independent rights and in some cases inalienable rights on a non-reciprocal basis.

We have recommended several ways to resolve the tension. First, by separating the nature of investor rights and the component rights found in IIAs. Second, by reviewing the understanding of third party rights or 'individual rights' in the ILC Articles in the context of countermeasures. Third, by introducing a legislative solution either by issuing a joint-interpretation or adding a provision to the relevant IIAs. The first and second suggestions may depend on an appropriate investment tribunal being given a relevant case. In addition, we have also addressed some concerns about the theory and interpretation method. Yet, there is no guarantee that the relevant tribunals will adopt them. Meanwhile the third suggestion will require further actions by State parties of IIAs, each requiring different political actions and may have their own difficulties.

Regardless, there is a great need to develop ways in which the international investment law and international trade law regimes will not just co-exist but also operate coherently so as to facilitate economic development around the world through legalization and the rule of law.