Kaplan Lecture 2022

Investor-State Arbitration, a New Frontier? - Investor Protections, the State's Regulatory Space and the Margin of Appreciation

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A. Preliminary Remarks and Structure of Lecture

1. Ladies and gentlemen, I wish to begin by thanking Neil Kaplan and the organisers for inviting me to deliver the 2022 Kaplan Lecture. It is a great honour and a pleasure.

   The global order of investment and trade does not operate in a vacuum. We live in an age of uncertainty and upheaval. Governments are increasingly having to react to internal and external regulatory pressures triggered by conflict, resulting in an energy crisis, and natural phenomena like the Covid-19 pandemic and climate change. This has and will engender disputes about investor rights under multilateral and bilateral investment treaties and affect the legitimacy and integrity of investor-state arbitration. Investor-state arbitration is thus at the cusp of a new era, a new frontier has to be traversed in which arbitral tribunals will increasingly have to reconcile conflicting interests of the protected investor, on the one hand, and the public interest invoked by national authorities in the host state, on the other.

2. A salient issue in this reconciliation process, and the focus of this lecture, is the legal articulation of the space for manoeuvre (*the regulatory space*, often termed the State's *police powers* in investment treaty law), that dispute resolution mechanisms at international level are often asked to grant national authorities in fulfilling their obligations under international treaties. In determining the scope and contours of the State's regulatory space, international courts and arbitral tribunals have sometimes employed formulations such as a "margin of discretion", a "margin of deference" or utilised an umbrella concept, the doctrine of the "margin of appreciation".

3. The margin of appreciation primarily encompasses a framework of analysis for standards of review when States use their regulatory powers to restrict or limit rights of individuals or legal persons guaranteed under international treaties or as provided for by customary norms of public international law. In the last decade or so much

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academic ink has been spilled on whether the margin of appreciation applies in investor-state arbitration as well as arbitrators wielding their pens on this issue. Forceful arguments have been adduced for and against an affirmative answer where some camps have taken a rather absolutist approach to this issue.[23]

4. In this lecture I will reflect on this debate and in particular pose the question whether traversing this new frontier in international investment law can succeed if a black and white approach is adopted. Some have claimed that arguments can be adduced in favour of a middle ground which accepts as a methodological starting point that the conceptual core of the doctrine of the margin of appreciation can potentially inform the operation of review in investor-state cases. Without taking any firm position myself in this lecture, I would wish to explore this claim by drawing on the operation of the doctrine as it has been applied in cases brought under the European Convention on Human Rights, (the ECHR), and decided by the European Court of Human Rights where I had to the honour to serve as a Judge for nine years between 2013-2022, and as its President for the last two and half years of my term.

5. I will proceed in three parts. First, I will discuss whether the doctrine of the margin of appreciation, as developed by the Strasbourg Court, is at all fit for purpose in investor-state cases. As I will explain, the margin of appreciation seems not, as such, to be applicable in all of its essential elements without the doctrine or a similar standard of review being reasonably adduced from the text or overall structure of a bilateral or multilateral investment treaty. The four corners of the treaty in question indeed limit and constrain the interpretive process so as to conform to the object and purpose of such treaties. In the second part of the lecture, I will however explore those claims that have been made that it may be helpful to have regard to the core conceptual elements of the doctrine in certain cases. By this argument, it has been submitted that the doctrine may assist in developing a consistent and coherent conceptual framework in formulating standards of review in investor-state cases when tribunal review of host State action is indeed required by the text, object or purpose of the relevant treaty provision. Investor protections would, it is claimed, actually be strengthened at the level of foreseeability and substance whilst at the same time informing further the scope and content of the "regulatory space" left to

[2] See, Barnali Choudhury, "Recapturing Public Power: Is Investment Arbitration's Engagement of the Public Interest Contributing to the Democratic Deficit?", 41 *Vand. J. Transnatl'l* 775 (2008); William W. Burke-White & Andreas von Staden, "Private Litigation in a Public Sphere: The Standards of Review in Investor-State Arbitrations", 35 *Yale J. Int'l* 283 (2010); Andreas von Staden, "Deference or No Deference, That is the Question: Legitimacy and Standards of Review in Investor-State Arbitration", *Investment Treaty News*, 4, Vol. 2, 2012, 3-4; Julian Arato, "The Margin of Appreciation in International Investment Law", 54 *Va. Int'L.* 545-578 (2013-2014); Gary Born, Danielle Morris & Stephanie Forrest, "A Margin of Appreciation": Appreciating Its Irrelevance in International Law", Vol 61, No. 1, *Harvard International Law Journal* (2020), 65-134.

[3] In a recent article, authored along with two of his associates, Gary Born, attempts to demonstrate the „irrelevance" of the margin of appreciation in investor-state arbitration, indeed in international law in general. The article begins with a metaphor referring to the old adage: „if all you have is a hammer, then every problem looks like a nail". It then argues that this adage applies to „international investment arbitration where a few investment tribunals have recently referred a so-called „margin of appreciation" when determining whether particular governmental measures have violated a host state's international obligations".Gary Born et al, ibid, 66.

the States under the police powers doctrine. In this manner, the argument is made that the complete disregard of the margin of appreciation in investment treaty law may in fact weaken investor protections, not the inverse, as well as create uncertainty as to the commitments entered into by the host State. On this basis, and as elaborated in my third and final part, the correct question to ask in a particular investor-state case is then what, objectively, should be the level of intensity of review applied to the particular facts, taking account of the special characteristics and purposes of investment treaties, (and in particular the provision(s) implicated), and whether the doctrine of the margin of appreciation can assist in that assessment. I will in this final part draw some conclusions from existing arbitral practice in the investor-state field.

6. In sum, today, I will attempt, to the best of my abilities, explore the arguments for and against a reliance on the doctrine of the margin of appreciation in investor-state arbitration, in particular whether a possible middle ground is realistic between those that fully embrace the doctrine of the margin of appreciation, as a viable method of analysis in investor-state cases, and those that fully reject its application as irrelevant or illegitimate. Having just stepped down from my role as President of the European Court of Human Rights and now entering private practice at Gibson, Dunn and Crutcher within the investor-state field, I hope that I can in this manner contribute to a modest extent to this very interesting and important debate on standards of review in investor-state arbitration.

B. Review under the ECHR and investment treaties: functional similarities and normative differences

7. Now to my first part, a sketch of the manner in which review of government action under the ECHR operates and the functional similarities and normative differences with review under bilateral or multilateral investment treaties.

8. When it comes to adjudication in the Strasbourg Court, on the one hand, and before investor-state tribunals, on the other, one should not overlook the similarities and complementarities, viewed functionally, between the two regimes, as others have correctly identified.[4] Both regimes empower individuals to bring suit against states directly before an international dispute resolution mechanism over alleged violations of treaty rights. Moreover, both under the European Convention and its property rights provision of Article 1 of Protocol 1, and under investment treaties, property rights protection is central. The juridical relationship forming the basis of

[4] Charline Daelman, "The European Court of Human Rights and International Investment Arbitration: Existence of a Judicial Dialogue?", *Human Rights with a Human Touch, Liber Amicorum, Paul Lemmens* (Koen Lemmens, Stephan Parmentier and Louise Reyntjens (eds.), Intersentia (2020), 633-651, 635: "... In comparison to the classic concept of public international law, non-state actors are provided with direct rights and claims against a sovereign state in both international investment law and human rights law. Both fields are thus characterised by an asymmetrical relationship, in which the individual is protected against the unlawful interference of the state". See, also, Julian Arato, ibid, 550.

the adjudication is the same in cases under the ECHR as under investment treaties: in both situations a private actor files a claim against a sovereign state before an international dispute resolution mechanism having the power to issue legally binding decisions on whether the State has contravened an international norm regulating the boundaries of legitimate public action or omission. The nature of the adjudicative review process is also similar when it comes to the gravamen of the legal issues to be resolved.

9. But that is as far as the similarities go for the following four reasons:

Firstly, the margin of appreciation is constructed on the basis of certain fundamental structural features of the Convention system. In accordance with Article 1 of the Convention, States Parties are under a legal obligation to "secure within their jurisdiction the rights and freedoms defined" therein. Moreover, Article 35 of the Convention reflects the customary international law principle of the exhaustion of domestic remedies,[5] making it an unequivocable condition for lodging an application before the Strasbourg Court that effective remedies at national level have been utilised, most often judicial remedies. Together, along with other structural features of the system, these provisions encapsulate the overarching principle of subsidiarity which forms the normative cornerstone of the doctrine of the margin of appreciation. The principle of subsidiarity refers to the Convention's functional premise which is that the member States are themselves under a duty to secure and protect human rights at national level, including all branches of Government. This is a normatively different starting-point than the one flowing from the overall structure, object and purposes of investment treaties.[6]

Secondly, the margin of appreciation is primarily applicable when it comes to rights and freedoms under the Convention which are textually couched in qualitative terms, thus providing for exceptions which refer to governmental measures which are "necessary in a democratic society" (cf. Articles 8-11) or, when it comes to property rights, "necessary to control the use of property", as it is worded in paragraph 2 of Article 1 of Protocol 1.[7] It is then the role of the Strasbourg Court, within the context of what it has termed "European supervision", to review the initial "necessity" assessment of the national authorities after domestic remedies have been exhausted.

Thirdly, whilst the margin of appreciation developed for decades in Strasbourg case-law without any explicit textual basis in the Convention, as of 1 August 2021,

[5] Martin Dietrich Brauch, "Exhaustion of Local Remedies in International Investment Law", *IISD Best Practices Series* (2017), 1-28, 2-6, available at: iisd.org.

[6] However, it should be noted that under Article 26 of the *ICSID Convention* (Convention on the Settlement of Investment Disputes between States and Nationals of Other States) "[consent] of the parties to arbitration under [the] Convention shall, unless otherwise stated, be deemed consent to such arbitration to the exclusion of any other remedy. A Contracting State may [however] require the exhaustion of local administrative or judicial remedies as a condition of its consent to arbitration under [the] Convention."

[7] To be clear, the point being made here is not that a "necessity" exception is, as such, alien to the field of international investment law. Indeed, such clauses do quite often figure in BITs, for example in Article XI of the Argentina-United States of Ameria BIT of 1991. Moreover, a variant of such a norm is also explicitly stated in Article 25 of the Draft Articles on Responsibility of States for Internationally Wrongful Acts.

the doctrine has now been inserted into the Preamble, along with the principle of subsidiarity, with the coming into force of Protocol 15. Therefore, the doctrine has now explicitly been confirmed by the States Parties. This, certainly, has normative implications for the overall legitimacy of the doctrine for the purposes of review in Strasbourg.

Fourthly, it is also important to be cognisant of the fact that the formulation of the right to property under Article 1 of Protocol 1 to the Convention is not, when it comes to its conceptual force and strength, necessarily similar to the more significant weight ascribed to investor rights under bilateral or multilateral investment treaties. It has been argued by some commentators that the text of Article 1 of Protocol 1 itself shows that there is greater scope for state interference with property rights than other Convention rights.[8] This argument needs to be qualified in my view. As I will revert to in more detail in a moment, it is not necessarily the case that the intensity of review in a particular case under Article 1 of Protocol No. 1 will ultimately be considered less strict on the facts. Several important elements may in fact lead to the opposite conclusion.

10. In sum, for these reasons, the ECHR doctrine of the margin of appreciation cannot, as such, be transposed wholesale to the investor-state field. However, the question then arises, have those arbitral tribunals that have indeed applied, or at least referred to, the margin of appreciation in the last couple of decades or so been wrong as a starting point of principle? I will first reflect on the current state of public international law and then revert to some relevant policy arguments.

11. As to *public international law*, it has been argued that the margin of appreciation has no basis in customary international law. Therefore, it has been claimed, reliance on the doctrine, whether by drawing inspiration from the ECHR doctrine or other sources of international law, is inapposite.[9] It is also true that there is an example in investor-state arbitral practice, in the 2007 award in *Siemens v Argentina*, of a tribunal opining, and I quote, that "the European Convention on Human Rights permits a margin of appreciation not found in customary international law".[10]

12. I leave aside the question whether it is correct, as a matter of the current state of public international law, that the margin of appreciation cannot be considered an existing norm. For the time being, the salient question is whether the margin of appreciation, as a standard of review of States' regulatory actions (or omissions), must be considered a fixed, binding rule or legal principle, thus requiring a clear normative basis in public international law so as to permit arbitral tribunals to make

[8] Andrew Legg, ibid, 215.
[9] Gary Born et al, ibid, 77: "As these and other decisions demonstrate, the clear weight of contemporary international authority not only does not support, but instead affirmatively rejects, the margin of appreciation as a general rule of international law" (citations omitted).
[10] *Siemens A.G. v the Argentine Republic*, ICSID Case No. ARB/02/8, Award, (6 February 2007), § 354.

use of it in their awards without a clear textual mandate in the investment treaty in question.

13. At the outset, I note that there are several examples in recent awards of tribunals referring to a margin of appreciation (or a margin of discretion or deference) in their findings. From these awards, which I will refer to in a moment, it seems to transpire that some arbitral tribunals have considered that sometimes the threshold question to answer in a particular investor-state case is whether the *text, object and purpose of the respective investment treaty* in play inherently requires the arbitral tribunal seized of the matter to apply a standard of review when examining states' regulatory policy decisions impacting investor protections, for example fair and equitable treatment, most favoured nation provisions, obligations of national treatment or essential security provisions. Within this context, tribunals seem to have considered that it is open to them to seek inspiration from other relevant fields of international law. I read these awards as suggesting that the issue in question is then one of applying a methodological framework of analysis related to standards of review by an international dispute resolution mechanism with competence to review State action.

14. At the more doctrinal level, allow me moreover to note the following.

15. In this context the *principle of systemic integration*[11] has been referred to by some arbitral tribunals in investor-state practice to support this approach.[12] In particular in the award in *Urbaser v Argentina* of 2016[13] the Tribunal stated as follows:

"The Tribunal further retains that the Convention has to be interpreted in the light of the rules set out in the Vienna Convention on the Law of Treaties of May 23, 1969, and that Article 31 § 3 (c) of that Treaty indicates that account is to be taken of "any relevant rules of international law applicable in the relations between the parties." The BIT cannot be interpreted and applied in a vacuum. The Tribunal must certainly be mindful of the BIT's special purpose as a Treaty promoting foreign investments, but it cannot do so without taking the relevant rules of international law into account. The BIT has to be construed in harmony with other rules of international law of which it forms part, including those relating to human rights.

16. Furthermore, in the award in *Tulip Real Estate Development*,[14] reference is made in this regard to the International Law Commission (ILC) Study Group which rejected in its much discussed *Fragmentation Report* of 2006 any suggestion that

[11] See, in general, Campbell McLachlan, "The Principle of Systemic Integration and Article 31(3)(c) of the Vienna Convention", *ICLQ*, Vol. 54 (2005), 279-320.
[12] See, in particular, *Tulip Real Estate Development Netherlands B.V. v the Republic of Turkey*, ICSID/ARB/11/28, Decision on Annullment, (30 December 2015), §§ 86-92.
[13] See, for example, *Urbaser S.A. and Consorcio de Aguas Bilbao Bizkaia, Bilbao Bizkaia Ur Partzuergoa v the Argentine Republic*, ICSID Case No. ARB/07/26, 8 December 2016, § 1200.
[14] *Tulip Real Estate Development Netherlands B.V. v the Republic of Turkey*, ibid, §§ 89-90.

international tribunals should completely restrict themselves to the treaty upon which their jurisdiction is based and which constitutes the treaty under dispute.[15]

17. Inversely, as many commentators have also forcefully argued, there are of course arguments against adopting a methodological approach in the interpretation of investment treaties that infuse, externally, standards of review not reasonably drawn from the text, object or purpose of the treaty, even seeking inspiration from the normative framework laid down by the Vienna Convention on the Law of Treaties. Indeed, as I opined myself in a separate opinion in an important Grand Chamber judgment delivered by the Strasbourg Court:[16] "Words matter when interpreting a legal text, including an international treaty. That proposition is the cornerstone of the fundamental interpretive principle provided for in Article 31 of the VCLT which provides, [...], that the starting point is the good-faith interpretation of the terms of the treaty in question in accordance with the *ordinary meaning* to be given to the terms *in their context*."

18. As to relevant policy grounds, it is difficult to reasonably argue with the cogency of the claim that the interpretive assessment by arbitral tribunals in investor-state cases should be "strictly objective"[17] and based on the "text, object and purpose" of a treaty or a particular treaty provision viewed in their context in accordance with Article 31 (1) of the VCLT. These are also the interpretive benchmarks under the ECHR.[18]

19. If one attempts to draw conclusions from the arbitral awards I mentioned above, such as Urbaser and Tulip Real Estate Development, it seems however that some arbitrators have considered that resolving cases lodged by private actors, including investors, seeking protection against unlawful regulatory measures imposed by a sovereign State, will, inevitably require an approach in determining the standards of review to be applied. Just as with investment treaties, the substantive provisions of the European Convention were silent for decades as to the nature and scope of

[15] ILC, Report of a study group on Fragmentation of International Law: Difficulties Arising from the Diversification and Expansion of International Law, UN Doc A/CN.4/L.682, paras. 410-480 (April 13, 2006), § 423 (citations omitted, italics original).

[16] *Magyar Helsinki Bizottság v Hungary* [GC], no. 18030/11, 8 November 2016, dissenting opinion of Judge Spano, joined by Judge Kjølbro, § 4.

[17] See, Gary Born et al, ibid, ___.

[18] Article 31 of the VCLT is also the interpretive starting point in the interpretation of European Convention on Human Rights, see for example the Grand Chamber judgment in *Magyar Helsinki Bizottság v Hungary* [GC], no. 18030/11, 8 November 2016, §§ 118-119, where the Court stated as follows: "118**.** The Court has emphasised that, as an international treaty, the Convention must be interpreted in the light of the rules of interpretation provided for in Articles 31 to 33 of the Vienna Convention of 23 May 1969 on the Law of Treaties (see *Golder*, cited above, § 29; *Lithgow and Others v. the United Kingdom*, 8 July 1986, §§ 114 and 117, Series A no. 102; *Johnston and Others v. Ireland*, 18 December 1986, §§ 51 et seq., Series A no. 112; and *Witold Litwa v. Poland*, no. 26629/95, §§ 57-59, ECHR 2000-III). ... 119. Thus, in accordance with the Vienna Convention, the Court is required to ascertain the ordinary meaning to be given to the words in their context and in the light of the object and purpose of the provision from which they are drawn (see *Johnston and Others*, cited above, § 51, and Article 31 § 1 of the Vienna Convention quoted above in paragraph 35)." See, for a critical analysis, Vassilis P. Tzeveloks, "The Use of Article 31(3)(c) of the VLCT in the Case-Law of the ECtHR: an Effective Anti-Fragmentation Tool or A Selective Loophole for the Reinforcement of Human Rights Teleology", *Michigan Journal of International Law*, Vol 31, Issue 3, (2010), 621-690.

such standards, albeit the margin of appreciation having been inserted in the Preamble as of 1 August 2021. Therefore, it seems to be argued, a strictly textualist and teleological approach[19] within the four corners of an international treaty, which is silent on standards of review, will ultimately not suffice in constructing a principled framework of methodological analysis when it comes to reviewing State action, whether under investment treaties or the European Convention. More conceptual work is needed to preempt legitimate criticism couched in terms of lack of legal certainty and foreseeability within the respective dispute resolution mechanism, all values which lie at the core of the rule of law.[20]

20. To sum up, I am comfortable in concluding that the wholesale transposition of the ECHR doctrine of the margin of appreciation to the investment treaty field is neither justified as a matter of legal principle flowing from public international law nor on policy grounds, as others have also argued convincingly.[21] However, and here I am not in a position to take a firm view at present as it requires more intellectual thinking on my part, if one analyses the development of arbitral practice, and arguments drawn from the current state of public international law and policy, it does seem that a lively debate is ongoing on whether a potential middle ground approach is legally justified. Such an approach would it seems entail extrapolating, when appropriate, the core conceptual elements of the doctrine of the margin of appreciation in determining whether they can justifiably operate in a manner which promotes the underlying purposes and values of investment treaty law. Again, it is prudent it seems to me not to opine on the feasibility of such an approach in the abstract. Hence, I will limit myself to hopefully contributing to informing this debate by explaining, from my vantage point as a former Strasbourg Judge and President of that Court, how the margin of appreciation actually operates under the ECHR. It will then be for arbitrators and practitioners to make their considered assessment as to whether this framework of analysis is relevant for investor-state arbitration.

C. The core conceptual elements of the margin of appreciation

21. So, what are the core conceptual elements of the margin of appreciation? Here, it is important to be precise when seeking guidance from Strasbourg case-law. It is

[19] See for an interesting analysis, Sanja Djajić, "Searching for purpose: Critical assessment of teleological interpretation of treaties in investment arbitration", *International Review of Law* 2016:iit.4, 1-28.
[20] Rolf Knieper, "Rethinking Investment Arbitration", *German Arbitration Journal* (SchiedsVZ) (2015), 25: "Fundamental problems of procedure and substance, the evolution of international public law are at stake, as well as seemingly technical questions of the application of procedural rules and routine and a burgeoning jurisprudence, which is far from being coherent and constant". See also, Julian Arato, ibid, 556: "... Different arbitral panels have identified and relied on a dizzying set of standards of review in different cases, drawn from international and national orders, and both civil and common law jurisdictions. ... The effect is a state of general uncertainty as to what the standard of review might be from one case to the next – whether the state will be entitled to significant deference in comporting with its treaty obligations, or whether it will be subject to more exacting review. ..."
[21] Julian Arato, ibid, 577: "While adopting the margin of appreciation doctrine wholesale is the wrong way to go, there is still much to be gained from looking at how the ECtHR applies the margin in specific cases."

insufficient to analyse the doctrine as applied under provisions that do not implicate, explicitly or implicitly, the type of rights claimed by investors in arbitral proceedings when relying on provisions of investment treaties. To ascertain the core elements the proper starting point is the Strasbourg Court‘s case-law under Article 1 of Protocol 1 which protects a persons enjoyment of his or her possessions.

22. Before analysing these core elements, it is firstly important to explain briefly the overall structure of Article 1 of Protocol 1.[22] The provision includes three rules. The first rule, set out in the first paragraph, is of a general nature and enunciates the principle of the peaceful enjoyment of property. The second rule, contained in the second sentence of the first paragraph, covers deprivations of property and subjects it to conditions. The third rule, stated in the second paragraph, recognises that the States are entitled, among other things, to control the use of property in accordance with the general interest. As the Strasbourg Court has explained, the second and third rules, which are concerned with particular instances of interference with the right to property, must be read in the light of the general principle laid down in the first rule.[23]

23. When analysing the case-law of the Court under Article 1 of Protocol No. 1, it is secondly important to bear in mind that the way in which the doctrine of the margin of appreciation operates is not captured in its full extent by isolated references to the Court granting States a “wide”, “narrow” or “certain” margin of appreciation or the like in particular case. The Strasbourg Court’s overall standard of review, whilst described in general under the heading of the margin of appreciation, is more complex and requires more careful analysis. To a certain extent, the Court is itself to blame for this lack of clarity. However, on close analysis of Article 1 of Protocol No. 1 case-law one can discern a conceptual framework with certain core elements.

24. The margin of appreciation under Article 1 of Protocol No. 1 is determined by three factors, the (i) nature and scope of the *public interest* or governmental aim which forms the basis of the interference or restriction of a property right, interest or a legitimate expectation, (ii) the nature and scope of the governmental *measure* that is the source of the alleged interference or restriction and (iii) the extent or scope of the *consequences* that the measure has had on the property right, interest or legitimate expection claimed. The operation of the margin of appreciation in a property rights case under the ECHR thus requires a *three step analysis* which will determine the standard of review in the case at hand. Therefore, the ECHR doctrine of the margin of appreciation is not a fixed, one-size-fits-all standard of review,

[22] Article 1 of Protocol No. 1 to the ECHR reads as follows: 1. Every natural or legal person is entitled to the peaceful enjoyment of his possessions. No one shall be deprived of his possessions except in the public interest and subject to the conditions provided for by law and by the general principles of international law. 2. The preceding provisions shall not, however, in any way impair the right of the State to enforce such laws as it deems necessary to control the use of property in accordance with the general interest or to secure payment of taxes or other contributions or penalties.

[23] See, for example, *Lekić v Slovenia* [GC], no. 36480/07, 11 December 2018, § 92.

determined once and for all at the outset, but rather an ensemble of core conceptual elements that operate as gradations in the intensity of review throughout the process of adjudication ultimately guiding the process through a step-by-step analysis to the ultimate substantive outcome.

25. Under the *first step of the analysis*, the actual words („the margin of appreciation“) are usually employed by the Court to describe the overarching framework of deference in which the second and third steps take place. Here, the Court is analysing the nature and scope of the public interest or governmental aim pursued by the regulatory measure in question. It is clear that if the measure is considered to fall within the scope of economic and social policy, the Court will consider the margin of appreciation to be "wide".[24] However, this statement is limited to the question whether the aim pursued can be accepted as legitimate (or more accurately, in the *public interest*) within the meaning of the Convention. Thus, under the Court‘s case-law, the Court will not find a violation of the Convention on this basis unless the assessment by the Government is "manifestly without reasonable foundation".[25] This constitutes simple rational basis review where the Court will be examining clear evidence of arbitrariness on behalf of the Government, a high hurdle for the property rights holder to meet. However the salient point is that this high level of deference is limited to the first step of the margin of appreciation analysis.

26. If the Court accepts under the first step that the aim pursued is legitimate, as being in the public interest, the *second step of the analysis* requires the determination of the level of deference taking account of the nature and scope of the governmental measure that is the source of the alleged interference or restriction. Here, the Court‘s case-law makes a crucial distinction between deprivations of possessions (in other words expropriation) under the second sentence of the first paragraph, on the one hand, and the control of use of property under the second paragraph, on the other.[26] Whilst the Court may, in the field of economic and social policy, find that the margin of appreciation is wide under the first step, as being limited to the determination of the aim pursued, if the regulatory measure in question constitutes expropriation then the margin of appreciation invariably becomes substantially more narrow under the second step of the analysis triggering a form of strict

[24] *Vistiņš and Perepjolkins v Latvia* [GC], no. 71243/01, 25 October 2012, § 106: " ... The Court, finding it natural that the margin of appreciation available to the legislature in implementing social and economic policies should be a wide one ..."
[25] *Jahn and Others v Germany* [GC], nos. 4672099 and 2 others, ECHR 2005-VI, § 91 and *Lekić v Slovenia* ibid, § 105.
[26] See, in comparison, *Vistiņš and Perepjolkins v Latvia*, ibid, § 94, and *Capital Bank AD v. Bulgaria*, no. 49429/99, 24 November 2005, § 131: " ... the Court observes that the BNB‘s decision to revoke the [banking] licence was clearly taken as a measure to control the banking sector in the country. It is true that it involved a deprivation of property, insofar as the licence itself could be considered a possession, but in the circumstances the deprivation formed a constituent element of a scheme for controlling the banking industry. The Court therefore considers that it is the second paragraph of Article 1 of Protocol No. 1 which is applicable ..."

scrutiny. In this respect, a particularly important case is the landmark Grand Chamber judgment of 2012 in the case of *Vistiņš and Perepjolkins v Latvia.*[27]

27. The applicants owned five plots of land on the island of Kundziņsala, situated close to the mouth of the Daugava River, which is part of the city of Riga. The island mainly consists of port facilities. In 1995-1996, all the privately owned land within the port's boundaries became subject to a servitude for the benefit of the public corporation responsible for the port‘s management. In return, the corporation was to the pay the owners annual compensation of not more than 5% of the cadastral value of the plots of land in question. Before the Strasbourg Court, the applicants claimed that they had been subject to unlawful expropriation in violation of Article 1 of Protocol No. 1. A majority of the Grand Chamber agreed.

28. The Court affirmed that in "matters of general social and economic policy, on which opinions within a democratic society may reasonably differ widely, the domestic policy-maker should be afforded a particularly broad margin of appreciation", including in "respect of urban and regional planning policies". Therefore, the Court would respect the legislature's judgment as to what was "in the public interest" unless that judgment was manifestly without reasonable foundation.[28] However, due to the fact that the measure in question constitued expropriation of land, the Court made clear that it could not "abdicate its power of review" requiring it to "determine whether the requisite balance" between the applicant's property rights and the public interest had been respected.[29]

29. This stricter standard of review was therefore triggered under the second step of the analysis, the Court operationalising its review by relying on its classical test comprising four objective requirements in its assessment of the proportionality of the expropriation measure in question, namely (1) amount of compensation, (2) due process rights, (3) expeditiousness, stability and coherence of the governmental measure, (4) and an assessment whether less restrictive measures where envisaged or possible.

30. Firstly, the Court made clear that the "taking of property without payment of an amount reasonably related to its value would normally constitute a disproportionate interference". Compensation, the Court continued, "must normally be calculated on the basis of the value of the property at the date on which ownership thereof was lost. Any other approach could open the door to a degree of uncertainty or even arbitrariness". Secondly, where an "individual‘s property had been expropriated, there should be a procedure ensuring an overall assessment of the consequences of the expropriation". Thirdly, the public authorities must act in good time and in an appropriate and consistent manner. Fourthly, the Government would have to show

[27] *Vistiņš and Perepjolkins v Latvia* [GC], no. 71243/01, 25 October 2012.
[28] *Vistiņš and Perepjolkins v Latvia*, ibid, § 98 and 106.
[29] *Vistiņš and Perepjolkins v Latvia*, ibid, § 109.

that "less drastic measures than expropriation compensated for by purely symbolic means" was envisaged.[30]

31. Applying a strict standard of review under the second step of the Article 1 Protocol No. 1 analysis, the Court concluded that the expropriation in question failed to conform to all four of the objective requirements of the proportionality test. The State had therefore "overstepped its margin of appreciation" thus violating the applicants‘ property rights.[31]

32. Again, whilst the margin of appreciation afforded to the State in this case, at the first step of the analysis under Article 1 of Protocol No. 1, was wide, as the measure in question fell within the realm of economic and social policy (urban planning), the standard of review applied at the second step of the analysis nevertheless narrowed considerably the margin of appreciation due to the nature and scope of the expropriation measure in question. This distinction between the first and second step of the margin of appreciation analysis is one which a number of commentators, critical of the use of the doctrine, have failed to grasp fully. Indeed, as in this case, the standard of review in applying the margin of appreciation became ultimately quite reinforced as to the Court‘s level of scrutiny in the assessment of each of the four objective elements of the proportionality test.

33. Let me now turn to another feature of the ECHR's property rights jurisprudence of potential relevance for present purposes. If a regulatory measure is rather assessed as involving the control of use of property, within the meaning of the second paragraph of Article 1 of Protocol No. 1, and not expropriation, the margin of appreciation may also remain wide at the second step of the analysis. However, even in such circumstances, and this is also an important element to fully appreciate, the margin of appreciation afforded to the State under the first and second step of the analysis may still be narrowed under *the third step*, when assessing the extent or scope of the consequences that the measure has had on the property right, interest or legitimate expection claimed. An example of this type of case is the judgment of the Strasbourg Court in *Vékony v Hungary* of 2015, case which could also have been a classic matter to be resolved by way of arbitration.[32] I should disclose that I sat in this case in the Chamber panel of 7 Judges.

34. The applicant primarily alleged that the loss of his tobacco retail licence, by way of a statutory cancellation of all such licences and their non-renewal, had amounted to an unjustified deprivation of possession within the meaning of Article 1 of Protocol No. 1. The Court did not accept that the statute in question, cancelling the applicant’s licence, had amounted to expropriation, but rather that it “constituted a

[30] *Vistiņš and Perepjolkins v Latvia*, ibid, §§ 110-114 and 129.
[31] *Vistiņš and Perepjolkins v Latvia*, ibid, § 131.
[32] *Vékony v Hungary*, no. 65681/13, 13 January 2015.

measure of control of the use of property" under the second paragraph of the provision.[33]

35. The Court accepted that the Government had enjoyed a wide margin of appreciation due to the general interest underlying the measure which had been based on public health considerations and the nature and scope of the measure as constituting the control of use of property and not expropriation.[34] However, proceeding to the third step of its analysis, the Court observed that the "loss of the licence reduced [the applicant's] business by one-third of its turnover, leading eventually to winding-up. Given the serious economic consequences flowing from the criticised measure" the Court concluded that this was a "severe measure in the circumstances".

36. Therefore, applying the four objective requirements of its proportionality test, against the background of the severe consequences for the applicant's business due to the statutory measure in question thus triggering strict scrutiny, the Court concluded that the regulatory measure had failed to fulfil all of the four requirements of the test. First, the licence had been extinguished without compensation. Secondly, the measure was not subject to "any public scrutiny or legal remedy". Thirdly, the measure had been introduced "by way of constant changes of the law and with remarkable hastiness" and fourthly, had "not [been] alleviated by any positive measures on behalf of the State".[35]

37. To sum up, the core conceptual elements of the ECHR doctrine of the margin of appreciation, as applied in property cases under Article 1 of Protocol No. 1, comprise a *three-step analysis* in the formulation of the standard of review applied in a particular case to governmental measures interfering with property. Each step requires a fact-sensitive assessment in determining the intensity of review of such measures. The margin of appreciation thus constitutes a *multi-layered or polygonal framework of analysis* with fact-sensitive gradations of the intensity of review within which the *quadridimensional proportionality test*, with its four objective requirements, is operationalised on the facts of a particular case.

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[33] *Vékony v Hungary*, ibid, § 30.

[34] *Vékony v Hungary*, ibid, § 35.

[35] *Vékony v Hungary*, ibid, § 35-36. Article 1 of Protocol No. 1 makes a clear textual distinction between "deprivations" of possessions, which is, in principle, equivalent to the public international law concept of expropriation (both direct and indirect), on the one hand, and the "control of use" of property, on the other. Latter can on the facts of a particular case operate through the "consequences" limb of the quadri-dimensional proportionality test similarly to an indirect expropriation, as understood under the test usually recognised in public international law for both direct and indirect expropriation with its variable levels of intensity ('substantial deprivation' of property, see, for example, *Electrabel S.A. v the Republic of Hungary*, ICSID Case No. ARB/07/19, Decision on Jurisdiction, Applicable Law and Liability (30 November 2012), § 6.62), which must based on an analysis of the "nature and magnitude of the interference to the investor's property interests in its investment caused by the measure attributable to the Host State to determine whether those amounts acts amount to taking", see J. Paulsson & Z. Douglas, "Indirect Expropriation in Investment Treaty Arbitration", in N. Horn & S. Kröll (eds.), *Arbitrating Foreign Investment Disputes* 145, 148 (2004). In my view, the ECHR judgment in *Vékony v Hungary*, ibid., note ___, is an example of a similar factual and legal matrix.

38. Against this background, it is now finally instructive to proceed with analysing how arbitral tribunals have made use of the margin of appreciation in existing practice.

D. The doctrine of the margin of appreciation in investor-state arbitration - towards a middle ground?

39. Over the last two decades a number of arbitral tribunals in investor-state cases have relied upon various formulations of a "margin of appreciation" or a "margin of discretion" in their assessment of claims. Allow me here to highlight the following elements.

40. Firstly, arbitral tribunals have resorted to the *margin of appreciation* (or to a *margin of deference* or *discretion*) at the preliminary interpretive stage of assessing whether a governmental measure constitutes "deprivation of investment" under a BIT, as in *Saluka Investments BV*, or whether an "expropriation" has occurred, as in *Continental Casualty Company* and *Invesmart B.V.* I should note that applying the margin of appreciation in this manner is conceptually different from the way it is used in the case-law of the Strasbourg Court under Article 1 of Protocol No. 1. Under the latter case-law, the question whether a governmental measure constitutes "deprivation of possessions", or whether it should be classified as a "control of use" of property, is based on an objective analysis of the scope and content of the measure in question. The margin of appreciation does not, in principle, come into play at this stage of the analysis. In other words, a State is not afforded any discretion as to the initial classification of the measure in question. Interestingly, in this regard one may argue that the case-law of the Strasbourg Court is stricter in application towards the Government than transpires from existing investor-state arbitral practice, although the end result on the facts of a particular case may prove to be the same. This difference may at times simply be the result of the way certain BITs are textually formulated which is often quite different from the overall textual construction of Article 1 of Protocol No. 1 of the ECHR.[36]

41. For example, the Tribunal opined in *Saluka Investments BV* that Article 5 of the Netherlands/Czech BIT was "drafted very broadly and [did] not contain any exceptions for the exercise of its regulatory power". The Tribunal therefore interpreted the provision in the light of the general principle under customary international law that a State does not commit an expropriation when it adopts general regulations within its "police powers". Hence, on this view, the core question in *Saluka Investments BV* was a threshold question of the scope and content of the concept of "deprivation of investment" under Article 5 of the BIT which required a holistic examination, already at that early stage of the analysis, of whether the existence of "lawful and permissible regulatory action ... aimed at the

[36] See, n ___ above.

general welfare of the State" precluded a finding that the measure constituted a deprivation at all.

42. I leave aside the question whether the Strasbourg Court would have arrived at the same conclusion. In any event, the Court would probably have proceeded somewhat differently in its reasoning. It would have applied its three-step analysis and then examined the measure on the basis of its quadridimensional proportionality framework, as I elaborated a moment ago.

43. Secondly, it can be inferred from existing arbitral practice that Tribunals have resorted, in a similar manner to the way a case would be analysed under the ECHR, to the margin of appreciation in situations where they have been confronted with difficult questions of having to balance investor rights with the scope and content of the State's regulate space due to strong countervailing public interests, sometimes alleged as even being of an "essential" nature. The three awards of significance here are *Electrabel S.A.*, *Philip Morris Brands Sàrl and ors* and *Deutsche Telekom AG*.

44. In *Electrabel S.A.*, the interesting question for present purposes was the conformity of the governmental measure of regulated or "administrative" pricing with Article 10(1) of the Energy Charter Treaty, an issue which in the current landscape in Europe, due to the ongoing energy crisis, is certain to become ever more salient. Recall that the Tribunal found that Hungary "would enjoy a reasonable margin of appreciation in taking such measures before being held to account under the ECT's standards of protection". As to this starting-point, there is no reason to think that the methodological analysis would have been any different under Article 1 of Protocol No. 1 to the ECHR.

45. *Philip Morris Brands Sàrl and ors* is probably the award in current investment-treaty practice containing the most explicit elaboration of the applicability of the ECHR doctrine of the margin of appreciation in the resolution of disputes under bilateral investment treaties. It is also of interest because of the clear divide on this issue between the Tribunal members with one arbitrator filing a comprehensive separate opinion on this issue. The award merits the following two remarks.

46. Firstly, it seems clear that the majority's approach is similar to the Strasbourg Court's overall framework of analysis in affording the State a wide margin of appreciation when it comes to matters of public health,[37] at least under the first step of the latter's traditional methodological approach. Applying a high threshold, in the form of an arbitrariness standard under this first step is not surprising. It is to be recalled that the test under ECHR case-law under Article 1 of Protocol No. 1 is also whether the aim pursued by the State is "manifestly without reasonable foundation",

[37] See, *Vékony v Hungary*, ibid, § 35.

which is similar language to the one adopted by the majority in *Philip Morris Brands Sàrl and ors.*[38]

47. Secondly, when analysing the reasoning in more detail it is justifiable to conclude from the Tribunal‘s analysis under the FET standard in Article 3(2) of the BIT that the challenged measures had not required the application of a stricter standard of scrutiny, akin to the second and third steps adopted by the Strasbourg Court, due to their nature, content and consequences. However, it is likely that had the case been litigated in Strasbourg, the challenged measures would have undergone a more systematic analysis within the context of the quadridimensional proportionality test and had thus been subjected to an assessment under the four objective requirements I have already explained. Having said that when it came to the claimants‘ argument based on the lack of *stability of the legal framework*, the Tribunal‘s analysis seems line with the approach taken in similar cases by the Strasbourg Court.[39]

48. In *Deutsche Telekom AG,* the Tribunal was faced with having to examine an argument by the respondent Government relying on its right to protect "essential security interests" within the meaning of Article of the 1995 Germany/India BIT. First, its finding that this provision of the BIT, as with similar provisions of other BITs, cannot be equated with the customary international law defence of "state of necessity" is noteworthy in the light of the current status of public international law. I take myself no view on the substance of this finding as it would require a separate lecture, but it is indeed of potential relevance for the wider array of current societal problems, including in the climate change field, which will undoubtedly permeate the field of international arbitration in the years to come.

49. Secondly, the Tribunal accepted India’s initial assessment, that its measure (the annulment of an Agreement for the lease of S-band electromagnetic spectrum on two satellites) should be afforded a "degree of deference" and a "margin of deference" given the State's "proximity to the situation, expertise and competence". This finding is in line with the first step of the ECHR approach when applying the doctrine of the margin of appreciation. Moreover, the Tribunal’s limitation of the scope of the margin of deference, the Tribunal opining that it "[could] not be unlimited" due to the high threshold nature of the "essential security provision" under the BIT, is also broadly commensurate to the second step under the Strasbourg Court’s methodological approach in Article 1 of Protocol No. 1 cases of a similar kind.

[38] *Philip Morris Brands Sàrl and ors,* ibid, § 399: “... [t]he sole inquiry for the Tribunal ... is whether or not there was a manifest lack of reasons for the legislation”.

[39] See, *mutatis mutandis*, *Vékony v Hungary*, ibid, § 35-36. It is noteworthy here to refer to Article 8.9 of *CETA* (the Comprehensive Economic and Trade Agreement between Canada and the European Union, signed in 2016, but not yet in force) which states: “For the purpose of this Chapter, the Parties reaffirm their right to regulate within their territories to achieve legitimate policy objectives, such as the protection of public health, safety, the environment or public morals, social or consumer protection or the promotion and protection of cultural diversity.”

50. Turning to the Tribunal's proportionality analysis in *Deutsche Telekom AG*, it focused on (1) whether the measure in question was "principally targeted" to protect essential security interests at stake, (2) whether it was "objectively required in order to achieve that protection" and (3) whether the State had "reasonable alternatives, less in conflict or more compliant with its international obligations". Finally, it analysed (4) the "import and intended effect" of the annulment decision as well as from subsequent events.

51. It is clear that the Tribunal did not transpose, wholesale, the doctrine of the margin of appreciation under the ECHR into its analysis, but proceeded cautiously, albeit rigorously, based on the particular elements flowing from Article 12 of the BIT. It should in this regard be noted that it transpires from an overall assessment of the award that the Tribunal contextualised its assessment within the interpretive framework as laid down in Article 31 of the VCLT.

52. Ladies and gentlemen, allow me now to sum up before I conclude.

53. It is firstly not the case that existing arbitral practice demonstrates that the ECHR doctrine of the margin of appreciation has, as such, been transposed wholesale into the investment-treaty field, far from it. As argued above, such a conclusion would not, in any event, be conceptually sound as a matter of legal principle or policy. It may secondly be argued that the trajectory of investor-state awards from *Saluka* to *Deutsche Telekom* shows that arbitral tribunals have not, it seems, applied an internally coherent or unified doctrine of the margin of appreciation in practice to date. However, arbitral tribunals have sometimes been sensitive to the fact that in certain circumstances a standard of review, applying some of the core elements of the doctrine of the margin of appreciation (sometimes referred to as a margin of deference), may be relevant taking account of the particular circumstances of the case and the provisions of investment treaties implicated.

E. Conclusion

54. Allow me no conclude this lecture.

55. Criticism levelled in recent years against the system of investor-state arbitration[40] has, at times, been based on factual assumptions which have been proven to be incorrect, for example the claim that investors win most investor-state cases, as the

[40] See, for example, Rolf Knieper, ibid, 25-26: "Observers portray the recent evolution of investment arbitration in contradictory terms. They confirm an unbroken dynamic, ever growing numbers of cases and amounts, confidence and voluntary compliance with awards on the one hand and alarming signs of fading legitimacy and credibility to increasing challenges, on the other"; Alessandra Arcuri & Federica Violi, "Human Rights and Investor-State Dispute Settlement: Changing (Almost) Everything, so that Everything Stays the Same?" *Diritti Umani e Diritto Internazionale* (2019), available at: ssrn.com/abstract=3459961, 1: "As is well known, the Investor-State Dispute Settlement system (ISDS) is facing a major legitimacy crisis."

current Secretary-General of ICSID, Meg Kinnear, has made clear is erroneous.[41] But stakeholders' perceptions remain and perceptions, even empirically incorrect ones, are often difficult to countenance. They must be taken seriously, in particular for a legitimate and authoritative system of international dispute resolution, whether in international arbitration or within the permanent international judiciary like the European Court of Human Rights and the International Court of Justice, where trust and confidence in the impartial and independent delivery of justice are fundamental components of legitimacy.

56. For any international dispute resolution system to be sustainable in the long-term, it is imperative that the starting-point be one of impartial appearance and methodological coherence.[42] In investor-state cases neither Party must seem to have an edge, an upper-hand or a trump card in the arbitral process. Again referring to the words of the Secretary-General of ICSID, "from the beginning, there has been a clear commitment in the ICSID system to balancing the interests of investors and host States".[43]

57. Whilst party autonomy, in particular the appointment of arbitrators and the choice of the applicable law, remain key components, when applying the substantive law in question, the determination of contentious legal questions must preserve the foundational premise of preserving balance between investor rights and the host States' sovereign regulatory authority. If a host State has acted unlawfully in contravention of property rights under an investment treaty compensation should unequivocally be granted. Inversely, if the State has acted in a manner which furthers a compelling public interest and clearly fulfils other requirements under investment treaties for resorting to their police powers, the investor must potentially accept the harms to his or her investment which follow.[44]

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[41] Meg Kinnear, "Continuity and Change in the ICSID System: Challenges and Opportunities in the Search for Consensus", 2019 *John E.C. Brierley Memorial Lecture*, published March 10, 2020: "The outcome of cases has [...] been fairly steady over time. About 35% of cases are resolved before going to a final award; States continue to win slightly more than half of cases; and investors receive on average about 40% of what is claimed when they are successful."

[42] The very recent amendments of the ICSID rules for arbitration and conciliation, approved in March 2022 by the ICSID Administrative Council, and entering into force on 1 July 2022, are a very welcome step in the direction of enhancing and strengthening the integrity, transparency and legitimacy of the system. The amendment's aim is first to further reduce the time and cost of cases, including mandatory timeframes for rendering orders and awards. New expedited arbitration rules are also made available, which would cut case times in half when adopted by parties. Entirely new procedural rules have been developed for mediation and fact-finding. The mediation rules offer a process to support a negotiated resolution of a dispute between parties, while fact-finding provides an impartial and targeted assessment of facts related to an investment. Both may be used as stand-alone procedures or in combination with an arbitration proceeding. See ICSID press release, 21 March 2022, available on icsid.worldbank.org.

[43] Meg Kinnear, ibid.

[44] In fact, this statement flows naturally from the third of the established criteria in investor-state arbitral practice applied in determining the concept of "investment", i.e. (i) a contribution, (ii) of a certain duration, and (iii) with an element of risk. Of course, subject to the wording of the provision in the treaty for dispute resolution, the legality of the investment and the investor's good faith may be relevant as elements of the definition of investment or as a bar to the exercise of jurisdiction or to investment protection on the merits, see, for example *Electrabel S.A.*, ibid, note __, § 5.43.

58. So, to conclude ladies and gentlemen, in this years' Kaplan Lecture, for which I again thank my good friend Neil and the organisers for inviting me to deliver, I have firstly tried to demonstrate that the wholesale transposition of the doctrine of the margin of appreciation to the investment treaty field is not, as such, justified as matter of principle. Secondly, and without myself taking any firm position on this issue, I have hopefully managed to contribute to this debate by reflecting on the arguments for and against the relevance of some of the conceptual elements of the doctrine for investor-state arbitration and in particular by explaining, from my vantage point as a former President of the Strasbourg Court, how the doctrine actually operates in the ECHR system. I hope that my contribution can inform the work of arbitrators, counsel and investment-treaty scholars in the difficult and challenging times ahead.

59. Thank you very much indeed.