

# Investment Agreements & Sustainable Development: the Non-Discrimination Standards

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# INVESTMENT AGREEMENTS & SUSTAINABLE DEVELOPMENT: THE NON-DISCRIMINATION STANDARDS

by Marcos Orellana\*

## INTRODUCTION

The approach of building mutually supportive trade, investment, and environmental regimes finds inspiration in the concept of sustainable development. Indeed, the World Summit on Sustainable Development recognized that trade and investment are necessary tools for achieving the goals of sustainable development.<sup>1</sup> Economic activities may contribute to the progressive realization of human rights and environmental protection by fostering economic development, employment, income generation, and general welfare. This potential contribution is not automatic, however, as non-sustainable investments, or unwarranted interpretations of trade and investment disciplines, may defeat such general welfare goals by exposing the population to health risks, causing environmental harm, or reducing the necessary policy space for sustainable development.

While its exact legal nature and status remain the object of controversy, at a minimum, sustainable development requires the integration of environmental issues in decision-making regarding development and investment projects.<sup>2</sup> If sustainable development requires the integration of environmental considerations in the planning and implementation of economic activities, it follows that the resolution of economic disputes concerning health, safety, and environmental (“HSE”) measures should also be integrated into the various fields involved. This process of integration in dispute settlement places an emphasis on treaty interpretation and, particularly, an emphasis on the principle of systemic integration codified in the Vienna Convention on the Law of Treaties.<sup>3</sup> In this regard, sustainable development calls for a process of normative dialogue, and the interpretive principle of systemic integration guides the conversation.

The interpretation and application of substantive investment disciplines carries intense implications for the policy space available to governments to adopt measures conducive to sustainable development. If compensation by the host government to the investor is required for the adoption of such measures, “even where regulatory action is taken in a fair and equitable manner, the potential cost to the governments may well discourage desirable or necessary environmental regulations.”<sup>4</sup> This general issue is particularly relevant in disputes concerning the relative non-discrimination standards of most-favored nation (“MFN”) treatment and national treatment (“NT”) because normal regulatory activity hinges on the construct of categories and distinctions that underlie differentiated approaches and rules attaching to particular persons, products, substances, economic sectors, etc.

This paper analyzes key issues concerning the scrutiny of HSE measures under the non-discrimination standards. It first introduces the non-discrimination standards and then examines the thorny questions of discriminatory intent and like circumstances. The paper argues that the construct of relative non-discrimination standards in investment treaties does not incorporate “necessity” requirements to justify HSE measures, in contrast to Article XX of the General Agreement on Tariffs and Trade (“GATT”) of the World Trade Organization (“WTO”). Instead, the relative non-discrimination standards of MFN and NT allow for HSE considerations in their two core operative elements: “in like circumstances” and “less favorable treatment.”

## THE NON-DISCRIMINATION STANDARDS

The relative non-discrimination standards proscribe discrimination on the basis of nationality. They require treatment no less favorable than that afforded to other national or foreign investors “in like circumstances.”<sup>5</sup> The comparison of the treatment afforded to similarly situated investors becomes the master key to the operation of the non-discrimination standards.

Given that the comparison process involves determining which investors are similarly situated, taking into account all relevant circumstances, the operation of the standards is far from a mechanical application of a mathematical formula. Instead, the application of the non-discrimination standards calls for abstract legal reasoning and involves a measure of subjective assessment. Because of this, there is a degree of uncertainty involved in their operation, which may affect the policy space available to States.

Several questions are relevant to the interpretation of non-discrimination standards through a sustainable development lens. For example: what is the meaning of “less favorable treatment,” and is it established by disparate impact alone? Does the meaning of “in like circumstances” allow authorities to differentiate among investors and/or investments on account of the dissimilar HSE threats posed by different substances, production processes, geographical conditions, etc? If so, does like circumstances operate as an element of the non-discrimination stan-

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dards, or as an exception, which would transpose the necessity test of trade law into the investment regime?

This paper addresses the non-discrimination standards of MFN and NT together, since the focus of analysis is their relation to HSE measures. In trade law, by contrast, national treatment rationales are not necessarily relevant to the interpretation of MFN disciplines,<sup>6</sup> as MFN and “non-discrimination” are not necessarily synonymous.<sup>7</sup> While differences between MFN and national treatment may be warranted in the trade regime, in the investment arena, both MFN and NT operate within the border with respect to largely similar issues. Both the *Occidental* case and the *Cross Border Trucking* case (examined below) have approached their analysis under the assumption that both the MFN and NT standards are synonymous, in the investment context.

### DISCRIMINATORY PURPOSE

Actual proof of discriminatory intent is generally not required as an element of discrimination.<sup>8</sup> This does not mean that the purpose of an HSE measure is irrelevant, however. Account of purpose allows for proper consideration of the perspectives of both the investor and the State, including the public interest underlying HSE measures, and thus overcomes unidirectional interpretations that consider investment obligations from the sole vantage point of the investor.<sup>9</sup> Moreover, the purpose of the challenged measure is relevant since less favorable treatment is not established by disparate impact alone. In practice, national treatment claims arguing that any treatment that differentially affects a foreign investor, even if the difference is not attributable to considerations of nationality, have not been successful.<sup>10</sup> If these claims were decided otherwise, the State would find itself unable to regulate in the public interest, with respect to processes or substances in a market dominated by foreign investors, without risking international liability, given that HSE measures would inevitably affect economic operators differently.

But how can tribunals determine the real purpose behind a measure? And, how should tribunals address situations of mixed intent, i.e., situations where a legitimate HSE objective co-exists with an impermissible motive? The difficulties involved in identifying regulatory purpose are compounded in the modern regulatory State, where legislatures and administrations respond to a number of often-competing interests, and where so much economic and social activity is highly regulated. In light of the fact that States are hardly monolithic entities, the determination of protectionist purpose may become a formidable challenge to a discrimination claim or defense. The *Methanex* Tribunal, hearing an arbitration involving groundwater contamination in California, aptly expressed the problem:

In particular, decrees and regulations may be the product of compromises and the balancing of competing interests by a variety of political actors. As a result, it may be difficult to identify a single or predominant purpose underlying a particular measure. Where a single governmental actor is motivated by an improper purpose, it does not necessarily follow that the motive can

be attributed to the entire government. Much if not all will depend on the evidential materials adduced in the particular case.<sup>11</sup>

Several observations may be warranted in respect to the difficulties involved in identifying and proving intent. First, although in international law States may be said to express but one voice, democracies in practice respond to different, often competing, political interests. This political feature of democracy is not to be condemned, especially when international law recognizes that democracy, human rights, and development are “interdependent and mutually reinforcing.”<sup>12</sup> It may well be that different purposes co-exist and explain why a given measure was adopted.

In such cases, issues of mixed intent will introduce severe tensions between economic and HSE considerations. In this regard, once evidence reveals the existence of HSE risks, the parallel presence of illicit protectionist intent in some governmental organ should not *ipso facto* render a measure illegal. If HSE risks are real, then the HSE protective purpose should in principle prevail over other purposes, given the paramount importance of safeguarding health, safety, and the environment.

Second, HSE measures cannot be presumed to be discriminatory. On the contrary, where national authorities have applied due process and based their findings of risks and determination of the level of protection on the basis of available scientific evidence, the specificity of HSE measures warrants qualified deference. It is for the claimant to prove discriminatory treatment, and not incumbent upon the government to demonstrate its public purpose. That said, the “smell test,” discussed below, the uncertainties as to the location of the threshold involved in making a *prima facie* case, and the dangers of negative inferences should lead cautious governments to be forthcoming in adducing evidence demonstrating the legitimacy of their HSE measures.

With regard to the evidence underlying a HSE measure, the country of origin of the scientific evidence is not necessarily a material reason for either accepting or rejecting it.<sup>13</sup> The origin of the scientific evidence cannot sustain a presumption of discriminatory intent because if it could, then most governments would risk attracting international responsibility for their efforts in assessing risks. Furthermore, the level of detail or specificity required of the scientific evidence underlying HSE measures needs to take into account real world considerations and the substantial costs involved in producing a science-based analysis of the risks presented by the multiple substances, processes, and activities that interact in society. The burden on developing countries of producing tailored and specific scientific studies, in light of their limited budget for scientific research and more pressing priorities such as sanitation and food security, illustrates the tensions surrounding the role of science in investment law.<sup>14</sup>

Third, in facing the challenges involved in determining protectionist intent, especially when considering facially neutral measures, tribunals are often tempted to adopt a “smell-test.”<sup>15</sup> The degree of circumstantial evidence pointing to protectionist intent may acquire a critical role, especially where direct evidence is unavailable. Thus, claimants will be drawn to

statements from different interests groups active in the political arena, figures on the expected benefits accruing to competitors in the marketplace, statements and memos from public officials, and any other piece of evidence that may serve to raise doubts as to the legitimacy of purpose. In *S.D. Myers*, which involved a ban on the export of hazardous PCB waste from Canada to the United States, the “smoking gun” tactic proved effective in convincing the tribunal that at stake was not a legitimate HSE measure, but rather a sham cover for protectionist purposes.<sup>16</sup> In the *Methanex* case, the claimant even hired a private investigator to inspect the garbage of ethanol lobbying firms and to trespass into their offices.<sup>17</sup>

Fourth, resort to consistency and necessity could also provide indirect evidence of governmental intent. Such indirect evidence, however, only offers limited assistance because of the specific nature of HSE measures as well as the absence of actual obligations for consistency or necessity. Most often governments regulate in response to public perception of threats as they arise, and as scientific progress reveals what were until then “invisible” risks. Also, sustainable development calls for adaptive management and evolving norms in order to incorporate new scientific insights and lessons learned regarding the operation and effectiveness of legal tools. Thus, requiring overall consistency in levels of protection and attaching liability for failure to achieve consistency would have the law operate in fictitious conditions.

The parallel between Bilateral Investment Treaties (“BITs”) and the Agreement on Sanitary and Phytosanitary Measures (“SPS”)<sup>18</sup> of the WTO illustrates the different roles of harmonization and consistency requirements in the trade and investment regimes. The protection of health in a society via sanitary measures that impede market access for goods that pose SPS risks will normally impose costs on other countries; to address this situation and secure market access to foreign goods, the SPS Agreement pursues harmonization of standards and even presumes conformity when international standards are utilized.<sup>19</sup> Investors and their investments, by contrast, are fully immersed in the diversity of national and local regulatory requirements, and it would have been quite far-reaching indeed if international investment agreements (“IIAs”) pursued harmonization of HSE standards across legal cultures and across differing levels of development.

With respect to necessity requirements, could less-trade restrictive alternatives provide indirect evidence of protectionist intent? In addressing this question, it must first be noted that the prerogative of countries to establish their levels of protection stems from their sovereignty, expressed in constitutional mandates to safeguard fundamental rights and to protect the population, *inter alia*, from HSE risks and that these duties cannot be surrendered or abandoned.<sup>20</sup> Second, countries are not obligated to justify their measures on the basis of necessity, absent explicit, conventional commitments to that effect. Third, any inquiry on less-trade restrictive alternatives should consider that reasonably available measures should achieve the same level of protection, involve the same regulatory costs, and restrict trade significantly

less. Fourth, the textual differences between the SPS Agreement, which explicitly refers to necessity,<sup>21</sup> on the one hand, and non-discrimination disciplines in investment agreements, which do not usually include such requirement, on the other, must be given effect.

Fifth and perhaps decisively, in WTO law the remedy for a measure that offends the less-trade restrictive standard is cessation, i.e., removal of the offending measure and adoption of the reasonably available less-trade restrictive measure.<sup>22</sup> By contrast, investment treaties contemplate monetary damages as the remedy of choice, which highlights the need to avoid automatic transposition of trade law into the investment field. Thus, less-trade restrictive criteria as indirect evidence is of limited value and could not by itself render sufficient light on illicit motive.

Therefore, arbitral tribunals inclined to employ less-trade restrictive criteria as indirect evidence should be careful not to transform them into a substantive necessity requirement. In claims involving trade and investment issues, the importation of a necessity test could involve investment arbitration adjudicating trade law claims, in excess of jurisdiction. Further, importing a necessity test into the non-discrimination standards in investment law would intrude much further into the regulatory autonomy of host States and potentially “lead to odd results.”<sup>23</sup>

Finally, with respect to “less favorable treatment,” the purpose of a science-based HSE measure should prevail over NT or MFN claims, including *de facto* discrimination. A claimant alleging disguised protectionism in HSE measures will need to submit compelling evidence proving that the science is a sham, that no HSE risk exists, or that the government is operating solely for protectionist purposes. Admittedly, this is a high threshold. Still, the alternative could allow successful challenges to legitimate HSE measures, thereby compromising the abilities of governments to fulfill their environmental and human rights obligations.

## LIKE CIRCUMSTANCES AND NON-DISCRIMINATION

As the UN International Law Commission observed, even absent explicit reference to “like circumstances” or “like situations,” such comparative context is implicit in the essence of the MFN clause.<sup>24</sup> The operation of “like circumstances” is not an easy task, however, given the elasticity of the terms and, thus, its ability to cast too wide or too narrow a net, depending on the level of abstraction or detail.

The application of non-discrimination standards raises difficulties where, as a result of local environmental conditions or the structure of a specific market, the operator that is treated or affected differently by the HSE measure is also a foreign investor. A hypothetical example presented by the United States Trade Representative in the context of the failed Multilateral Agreement on Investment (“MAI”) clarifies the point:

One concern which was raised was the possibility that measures entirely consistent with MFN and national treatment may provide differing treatment to investors depending on the particular circumstance. For example,

a foreign investor whose investment is situated on a wetland may legitimately be treated differently than another foreign or domestic investor due to the location of the investment, rather than the nationality of the investor. To address this issue, we included language in our proposal that would clarify the MAI's definition of "in like circumstances," in order to ensure that legitimate environmental measures will not be challenged purely on the grounds of such differential treatment.<sup>25</sup>

The application of the non-discrimination standards to HSE measures raise at least two intertwined questions concerning the operation of the phrase "in like circumstances." First, whether like circumstances operates as an exception to non-discrimination disciplines or alternatively as an operative element of the MFN and NT standards. Second, whether like circumstances refer only to operators in the same economic sector or whether it includes other differentiating criteria. In addition to these two questions, it remains open to question whether like circumstances could otherwise safeguard HSE measures that by design differentiate between investors on the basis of nationality.

#### LIKE CIRCUMSTANCES: AN OPERATIVE ELEMENT OR AN EXCEPTION?

Investment jurisprudence is divided as to whether "like circumstances" constitutes an operative element of the non-discrimination standards or an exception that could justify differential treatment on policy grounds. Analysis of the *Cross-Border Trucking* case, concerning U.S. restrictions on cross-border trucking services as well as restrictions on Mexican investment in the U.S. trucking industry, is useful in approaching this issue. The NT and MFN issues before the *Cross-Border Trucking* NAFTA Chapter 20 Arbitral Panel turned on the meaning and scope of the phrase "in like circumstances."<sup>26</sup> The Arbitral Panel sought guidance from other agreements that use similar language, such as the Canada-U.S. FTA. As the Panel noted, this agreement contains an exception to NT in services trade,<sup>27</sup> where "the difference in treatment is no greater than that necessary for prudential, fiduciary, health and safety, or consumer protection reasons," and explicitly imposes the burden of satisfying the exception on the party according different treatment.<sup>28</sup> The Panel then observed that the phrase "like circumstances" may properly include differential treatment, under the conditions specified in the Canada-U.S. FTA.<sup>29</sup>

Upon this reading of "like circumstances" and under the light of NAFTA's trade liberalization objectives,<sup>30</sup> the Panel reached the conclusion that the "in like circumstances" language constitutes an exception to the non-discrimination disciplines and should thus be interpreted narrowly.<sup>31</sup> The Panel explained that "differential treatment should be no greater than necessary for legitimate regulatory reasons such as safety, and that such different treatment be equivalent to the treatment accorded to domestic service providers."<sup>32</sup>

The *Cross-Border Trucking* Panel's analysis highlights the difficulties involved in the operation of non-discrimination disciplines. In particular, the Panel's reading of "like circumstances"

as an *exception* to differential treatment could serve to avoid unreasonable results, considering that NAFTA's investment chapter does not explicitly contain prudential exceptions for the protection of health, safety, and the environment that could *justify* departure from its substantive obligations, unlike trade in goods and services.<sup>33</sup>

Other NAFTA arbitral tribunals have confronted similar issues and adopted a similar rationale in the context of national treatment. The *S.D. Myers* Tribunal, for example, noted that the "assessment of like circumstances must also take into account circumstances that would *justify* governmental regulation that treat them differently in order to protect the public interest."<sup>34</sup>

In a similar jurisprudential vein, the *Parking* Tribunal considered environmental criteria in its application of the non-discrimination standards.<sup>35</sup> This case involved parking works and operations within the old city of Vilnius, Lithuania, which was protected by the UNESCO Convention concerning the Protection of the World Cultural and Natural Heritage.<sup>36</sup> The investor claimed that other parking works and operations had been treated differently.<sup>37</sup> The *Parking* Tribunal applied a binary construct to the non-discrimination standard: it compared certain economic operators, on the one hand, and it examined the policy underlying the differential treatment, on the other.<sup>38</sup> In this reading, the non-discrimination standard implicitly incorporates an exception for measures justified by legitimate governmental policies.

It would appear at first sight that this formula could avoid excessive outcomes by taking into account HSE considerations to justify differential treatment. However, the practical effect of such reading reduces the policy space available to governments, as the meaning of "like circumstances" is narrowed down by the IIA's economic objectives. Such a narrow reading of the object and purpose of IIAs risks frustrating mutually supportive trade and environment regimes, as the legitimacy of public policy goals is solely or predominantly evaluated through the lens of the investment liberalization goals. Moreover, by defining the purpose of investment agreements as tools for protecting investors, all doubts and ambiguities are resolved in the investors' favor. To overcome this apparent lack of balance, IIAs should be appreciated as instruments for sustainable development—embracing its three pillars: economic, social, and environment—and properly placed in the broader international law universe.

The reading of "like circumstances" as an exception also suffers from deficiencies relating to scope and the burden of proof. In regards to the burden of proof, the interpretation that treats "like circumstances" as an exception requires the respondent government to justify its regulations, relieving the applicant of establishing relevant, material facts and proving all the elements of its claim.<sup>39</sup> Then in regards to scope, the "exceptional" formulation of "in like circumstances" hinges on "necessity" considerations, where arbitral tribunals run the risk of second-guessing government regulators by testing potentially available least trade restrictive measures against investment liberalizing objectives. The deficiencies of such "exceptional" readings are

amplified by the complexity and dynamism of market structures, as well as by evolving scientific knowledge and changing social preferences in the modern regulatory State.

Instead, in the investment context, “like circumstances” should be read in light of its role as the key operative element of the non-discrimination standards, rather than as a *defense*, *exception*, or *justification* against MFN or NT obligations. In such role, “like circumstances” does not involve presumptions, narrow interpretations, or transfers in the burden of proof. Similarly, such reading does not transpose the WTO necessity test into the operation of investment non-discrimination disciplines.

As an operative element of the standard, the “like circumstances” test requires the identification of *all* relevant circumstances that serve to distinguish among foreign investors, including HSE considerations. In that context, as clarified by the Organization for Economic Co-operation and Development (“OECD”), analysis of conditions of competition in specific economic sectors provide a point of departure, but neither exhaust the task of establishing the category of actors that should be compared, nor the policy objectives that can be taken into account to define relevant parameters for comparison.<sup>40</sup> It appears that the objective relevance of the circumstances for each specific case seems to be the correct standard of reference,<sup>41</sup> including circumstances pertaining to HSE risks. Particular circumstances with respect to HSE issues should constitute a valid basis for distinguishing among otherwise similar investments or investors.<sup>42</sup>

Reading “like circumstances” as an operative element of the NT and MFN standards would do greater justice to the text and context of IIAs and would have positive systemic effects. This reading would not presume discrimination in the face of differential treatment or effects. Furthermore, this reading would also avoid a mechanical transposition of WTO law and jurisprudence into IIAs, both of which are different treaties with different parties, history, practice, text and context, structure, obligations, and remedies, thereby also avoiding the application of a goods analysis, or a services analysis, to investment matters. Finally, the scope of like circumstances would not be narrowed by the sole consideration of trade and investment objectives, thereby contributing to building mutually supportive environment and investment regimes.

The *GAMI* Tribunal confirmed the role of policy considerations in the determination of “likeness,” and not as an “exception” to non-discrimination disciplines:

The Arbitral Tribunal has not been persuaded that GAM’s circumstances were demonstrably so “like” those of non-expropriated mill owners that it was wrong to treat GAM differently. The Government may have been clumsy in its analysis of the relevant criteria for the cutoff line between candidates and non-candidates for expropriation. Its understanding of corporate finance may have been deficient. But ineffectiveness is not discrimination. The arbitrators are satisfied that a reason exists for the measure which was not itself discriminatory. That measure was plausibly connected with a legitimate goal of policy (ensuring that the sugar

industry was in the hands of solvent enterprises) and was applied neither in a discriminatory manner nor as a disguised barrier to equal opportunity.<sup>43</sup>

Following the reasoning of the *GAMI* Award, differential treatment based on HSE considerations would not be on the basis of nationality, but on the basis of legitimate regulatory objectives. This rationale applies with particular force with respect to HSE measures of general application. But what about HSE measures that call for differential treatment on the basis of the nationality of the investor?

Governmental measures implementing multilateral environmental agreements (“MEAs”) may well have implications for the NT and MFN standards in IIAs.<sup>44</sup> For example, an MEA allowing performance requirements to transfer environmentally sound technology might place greater burdens on a foreign as compared to domestic investors, and environmental controls arising out of the Clean Development Mechanism established under the Kyoto Protocol may require countries to discriminate between different categories of investors on the basis of nationality.<sup>45</sup> In these situations, is the phrase “in like circumstances” broad enough to safeguard nationality-based discrimination based on an MEA?

Markedly, the *Pope & Talbot* Tribunal presented a “like circumstances” formulation that purports to go beyond discrimination on the basis of nationality: “[a] formulation focusing on the like circumstances question, on the other hand, will require addressing *any* difference in treatment, demanding that it be justified by showing that it bears a reasonable relationship to rational policies not motivated by preference of domestic over foreign owned investments.”<sup>46</sup> Further, the *Pope & Talbot* Tribunal explicitly noted that differences in treatment will *presumptively* violate the non-discrimination standards, “unless they have a reasonable nexus to rational government policies that (1) do not distinguish, on their face or *de facto*, between foreign owned and domestic companies, and (2) do not otherwise unduly undermine the investment liberalizing objectives of NAFTA.”<sup>47</sup>

According to this reading, “in like circumstances” can safeguard HSE measures expressing rational government policies but not if HSE measures, by design, distinguish between investors on the basis of nationality. Thus, under this construct, MEA-based requirements would fail the non-discrimination test.

This solution may not contribute to mutual supportiveness between investment law and international environmental law because it could frustrate the objectives of MEAs. Three alternative options provide for a solution whereby the MEA-based, nationality requirement can co-exist with the non-discrimination standards. First, “in like circumstances” could consider the fact that the HSE measure is based on an MEA. Second, a conflict of norms analysis could apply to the conflict between the investment norm and the MEA norm, giving priority to the MEA obligation on account of the *lex specialis* principle. Third, general exceptions for HSE measures, where available, could safeguard nationality-based distinctions effected by HSE measures pursuant to MEAs. These three options would not frustrate the objectives of investment law because the nationality-based

distinctions would not be arbitrary or a disguise for an impermissible motive. Further, their rational basis and legitimate policy goals are underscored by the fact that they have been established by the international community in an international treaty—the MEA—seeking solutions to global HSE risks.

#### IN LIKE CIRCUMSTANCES & THE RELEVANT COMPARATORS

Then on the question of the determination of relevant comparators for the operation of the “like circumstances” test, the *Occidental* case, involving discrimination claims by an oil producer against the application of Ecuadorean tax law, provides a platform for analysis.<sup>48</sup> The key issue before the tribunal turned on the meaning of “in like situations.”<sup>49</sup> *Occidental* argued that “in like situations” did not refer to companies in the same sector of activity, such as oil producers, but to companies that were engaged in exports, even if encompassing different sectors.<sup>50</sup> *Occidental* further argued that a number of companies involved in the export of flowers, mining, seafood products, lumber, bananas, and African palm oil were entitled to receive Value Added Tax (“VAT”) refunds and continuously enjoyed that benefit.<sup>51</sup> Ecuador responded that “in like circumstances” could not extend to sectors other than oil producers because the whole purpose of the VAT refund policy was to ensure that the conditions of competition were not changed.<sup>52</sup> Ecuador further noted that with respect to VAT refunds, all oil producers were treated alike, including the national State oil company, Petroecuador.<sup>53</sup>

The *Occidental* Tribunal found in favor of the claimant on the basis of thin reasoning and doubtful propositions, two of which will be noted here. First, the Tribunal noted that “the purpose of national treatment is to protect investors as compared to local producers, and this cannot be done by addressing exclusively the sector in which that particular activity is undertaken.”<sup>54</sup> Such formulation is problematic, not least because it neglects the essence of non-discrimination principles in securing equal access to opportunity, particularly in respect to the conditions of competition.<sup>55</sup> Further, the public interest implications of such an unbalanced reading are readily apparent, including with respect to HSE measures, as governments will differentiate among different sectors for entirely legitimate reasons.<sup>56</sup>

A more balanced approach to non-discrimination has been elaborated by the OECD, a forum convening the most heavily regulated States in the world, in the context of the 1976 Declaration on International Investment and Multinational Enterprises.<sup>57</sup> In its 1993 interpretation of the NT standard included in the 1976 Declaration, the OECD observed that:

As regards the expression “in like situations”, the comparison between foreign-controlled enterprises established in a Member country and domestic enterprises in that Member country is valid only if it is made between firms operating in the same sector. . . . More general considerations, such as the policy objectives of Member countries, could be taken into account to define the circumstances in which comparison between foreign-controlled and domestic enterprises is permis-

sible inasmuch as those objectives are not contrary to the principle of National Treatment.<sup>58</sup>

A second doubtful proposition underlying the *Occidental* Tribunal’s extremely broad reading of “in like situations” relates to the linkages between disparate treatment and protectionism. The *Occidental* Tribunal noted that it was “convinced” that *Occidental*’s less favorable treatment, i.e., the fact that unlike flower exporters it was denied VAT refunds, was not the result of discriminatory intent.<sup>59</sup> Without more, this statement equates disparate impact with discrimination, and this interpretation dramatically compromises a government’s ability to regulate in the public interest, including by way of differential and incremental policy approaches.<sup>60</sup> In this regard, it may be useful to recall the attempt by the Chair of the OECD’s Multilateral Agreement on Investment Negotiating Group to put together a package of proposals to address member States’ concerns on the impact on regulatory autonomy of the NT and MFN standards:<sup>61</sup>

The fact that a measure applied by a government has a different effect on an investment or investor of another Party would not in itself render the measure inconsistent with national treatment and most favoured nation treatment. The objective of “in like circumstances” is to permit the consideration of all relevant circumstances, including those relating to a foreign investor and its investments, in deciding to which domestic or third country investors and investments they should appropriately be compared.<sup>62</sup>

This approach is more nuanced and recognizes both the close link between discrimination and equal opportunity. It also recognizes the fact that a government may treat economic operators differently for entirely legitimate policy reasons.

#### CONCLUSION

The operation of the relative non-discrimination standards can penetrate deeply into the regulatory sphere of the State, since they require the State to adduce a coherent explanation of the relevant categories and distinctions underlying the content and scope of application of an internal measure. Policy rationales for disparate treatment can involve a number of public interest regulations, including with respect to the environment, health, and safety. In this regard, interpreting “in like circumstances” as an operative element of the non-discrimination standards in IIAs that accounts for all relevant circumstances relating to the investment, rather than as a narrow exception that transfers to the State the burden of justifying its policy preferences, contributes to preserving the policy space necessary for the exercise of governmental authority in respect of health, safety, and the environment. Thus, the interpretation of “in like circumstances” as an operative element of the non-discrimination standards ultimately contributes to building channels of dialogue between legal regimes relevant to sustainable development. 

- <sup>1</sup> World Summit on Sustainable Development, 26 Aug. – 4 Sept. 2002, *Plan of Implementation of the World Summit on Sustainable Development*, ¶ 84, *passim*, U.N. Doc. A/CONF.199/20 (Sept. 23, 2002).
- <sup>2</sup> Iron Rhine Railway (Belg. v. Neth.), ¶ 59 (Perm. Ct. Arb. 2005) [hereinafter Iron Rhine Railway].
- <sup>3</sup> Vienna Convention on the Law of Treaties, art. 31.3.c, 1155 U.N.T.S. 331, 8 I.L.M. 679 (1969).
- <sup>4</sup> David Gantz, *Potential Conflicts Between Investor Rights and Environmental Regulation Under NAFTA's Chapter 11*, 33 GEO. WASH. INT'L L. REV. 651, 656 (2001).
- <sup>5</sup> General Agreement on Tariffs and Trade, Oct. 30, 1947, 61 Stat. A-11, 55 U.N.T.S. 194 [hereinafter GATT], [http://www.wto.org/english/docs\\_e/legal\\_e/gatt47\\_02\\_e.htm](http://www.wto.org/english/docs_e/legal_e/gatt47_02_e.htm).
- <sup>6</sup> Appellate Body Report, *European Communities – Regime for the Importation, Sale, and Distribution of Bananas*, ¶ 231, WT/DS27/AB/R (Sept. 9 1997).
- <sup>7</sup> Robert E. Hudec, “Like Product”: *The Differences in Meaning in GATT Articles I and III*, in REGULATORY BARRIERS AND THE PRINCIPLE OF NON-DISCRIMINATION IN WORLD TRADE LAW 101-23 (Thomas Cottier & Petros Mavroidis eds., 2000); Edward Laing, *Equal Access/Non-Discrimination and Legitimate Discrimination in International Economic Law*, 14 WIS. INT'L L.J. 246, 273 (1996).
- <sup>8</sup> Barnali Choudhury, *Recapturing Public Power: Is Investment Arbitration's Engagement of the Public Interest Contributing to the Democracy Deficit?*, 41 VAND. J. TRANSNAT'L L. 775, 828 (2008).
- <sup>9</sup> *Id.*
- <sup>10</sup> Andrea Bjorklund, *National Treatment*, in STANDARDS OF INVESTMENT PROTECTION 29, 49 (August Reinisch ed., 2008).
- <sup>11</sup> First Partial Award *Methanex Corp. v. United States*, ¶ 158 (NAFTA Ch. 11 Arb. Trib. Aug. 7, 2002).
- <sup>12</sup> World Conference on Human Rights, June 14-25, 1993, *Vienna Declaration and Programme of Action*, ¶ 8, U.N. Doc A/CONF.157/23 (July 12, 1993).
- <sup>13</sup> See Mitsuo Matsushita, *Some Issues of the SPS Agreement*, in THE ROLE OF THE JUDGE IN INTERNATIONAL TRADE REGULATION 193, 202 (Thomas Cottier & Petros Mavroidis eds., 2003).
- <sup>14</sup> See generally Marcos Orellana, *The Role of Science in Investment Arbitrations Concerning Public Health in the Environment*, 17 YB. INT'L ENV'L L. 48 (2006).
- <sup>15</sup> ROBERT E. HUDEC, *ESSAYS ON THE NATURE OF INTERNATIONAL TRADE LAW* 376 (1999).
- <sup>16</sup> First Partial Award, *S.D. Myers v. Canada*, ¶¶ 130, 137 (NAFTA Ch. 11 Arb. Trib. Nov. 13, 2000).
- <sup>17</sup> *Methanex Corp. v. United States*, Part II, Chapter I (NAFTA Ch. 11 Arb. Trib. Dec. 5, 2003). Such practice certainly raises questions on standards of evidence, and it was strongly condemned by the *Methanex* Tribunal.
- <sup>18</sup> Agreement on the Application of Sanitary and Phytosanitary Measures, Apr. 15, 1994, Marrakesh Agreement Establishing the World Trade Organization, Annex 1A, 1867 U.N.T.S. 493 [hereinafter SPS Agreement].
- <sup>19</sup> *Id.*
- <sup>20</sup> Kojo Yelpaala, *Fundamentalism in Public Health and Safety in Bilateral Investment Treaties (Part II)*, 3 ASIAN J. WTO & INT'L HEALTH L. & POL'Y 465, 466, 475-79, 492-93 (2008).
- <sup>21</sup> SPS Agreement, *supra* note 18.
- <sup>22</sup> *Id.*
- <sup>23</sup> Nicholas DiMasio & Joost Pauwelyn, *Nondiscrimination in Trade and Investment Treaties: Worlds Apart or Two Sides of the Same Coin?*, 102 AM. J. INT'L L. 48, 87-88 (2008).
- <sup>24</sup> See Report of the International Law Commission on the Work of its Thirtieth Session, 33 UN GAOR Supp. (No. 10) at 31, commentary arts. 9-10, ¶ 18, UN Doc. A/33/10 (1978), [http://untreaty.un.org/ilc/documentation/english/A\\_33\\_10.pdf](http://untreaty.un.org/ilc/documentation/english/A_33_10.pdf).
- <sup>25</sup> John Wickham, *Toward a Green Multilateral Investment Framework: NAFTA and the Search for Models*, 12 GEO. INT'L ENVTL. L. REV. 617, 631 (2000) (referring to United States Trade Representative (“USTR”), Briefing Paper for Staff of the U.S. Trade and Environment Policy Advisory Committee, TEPAC at 1, 5 Aug. 1998).
- <sup>26</sup> Cross-Border Trucking Services (U.S. v. Mex.), ¶ 247 (NAFTA Ch. 20 Arb. Trib. Feb. 6, 2001) [hereinafter Cross-Border Trucking Services]; see also Wickham, *supra* note 25, ¶ 276.
- <sup>27</sup> The fact that the *Cross Border Trucking Services* case involved issues of services trade and investment may have influenced the panel's reading of the operation of the exception clause in the NAFTA services chapter. See Cross-Border Trucking Services, ¶122 (NAFTA Ch. 20 Arb. Trib.).
- <sup>28</sup> *Id.* ¶ 250.
- <sup>29</sup> *Id.* ¶¶ 122, 258. Article 1402 of the U.S.-Canada FTA contains other requirements besides the one quoted above, including prior notification of proposed treatment and that such different treatment is equivalent in effect to the treatment accorded by the Party to its persons for such reasons. See *id.* ¶ 250.
- <sup>30</sup> The Panel also noted that the Preamble reflects a recognition that the Parties intended to “preserve their flexibility to safeguard the public welfare.” See *id.* ¶ 219.
- <sup>31</sup> *Id.* ¶ 260.
- <sup>32</sup> *Id.* ¶¶ 258-59 (“With regard to objectives, it seems unlikely to the Panel that the ‘in like circumstances’ language in Articles 1202 and 1203 [NT & MFN in Services] could be expected to permit maintenance of a very significant barrier to NAFTA trade, namely a prohibition on cross-border trucking services. Similarly, the Panel is mindful that a broad interpretation of the ‘in like circumstances’ language could render Articles 1202 and 1203 meaningless”).
- <sup>33</sup> In this regard, NAFTA Article 1114 on Environmental Measures is rather circular in that it allows what it does not prohibit. But see, NAFTA Article 2103 concerning taxation.
- <sup>34</sup> First Partial Award, *S.D. Myers v. Canada*, ¶ 250 (NAFTA Ch. 11 Arb. Trib. Nov. 13, 2000) (emphasis added).
- <sup>35</sup> *Parkerings-Compagniet AS v. Lithuania*, ICSID Case No. ARB/05/8, ¶¶ 371, 392 (Sept. 11, 2007) (decided by the International Centre for Settlement of Investment Disputes (“ICSID”) based on a treaty between the Government of the Republic of Lithuania and the Government of the Kingdom of Norway).
- <sup>36</sup> *Id.*
- <sup>37</sup> *Id.*
- <sup>38</sup> *Id.*
- <sup>39</sup> See *Avena and Other Mexican Nationals (Mex. v. U.S.)*, 2004 I.C.J. 12, ¶ 55 (Mar. 31); *Military and Paramilitary Activities in and against Nicaragua (Nicar. v. U.S.)*, 1984 I.C.J. 392, ¶ 101 (Nov. 26).
- <sup>40</sup> See OECD, NATIONAL TREATMENT FOR FOREIGN-CONTROLLED ENTERPRISES 22 (1993).
- <sup>41</sup> Giorgio Sacerdoti, *Foreign and Foreign-Owned Corporations in International Economic Law*, in FOREIGN INVESTMENT IN THE PRESENT AND A NEW INTERNATIONAL ECONOMIC ORDER 289, 302 (Detlev Chr. Dicke ed., 1987).
- <sup>42</sup> Cf. Appellate Body Report, *European Communities – Measures Affecting Asbestos and Asbestos-Containing Products*, WT/DS135/AB/R (Mar. 12, 2001).
- <sup>43</sup> *Gami Inv., Inc. v. United Mexican States*, ¶ 114 (NAFTA Ch. 11 Arb. Trib. Nov. 15, 2004).
- <sup>44</sup> PETER MUCHLINSKI, MULTINATIONAL ENTERPRISES AND THE LAW 571 (2d ed. 2007).
- <sup>45</sup> *Id.*
- <sup>46</sup> Award on the Merits of Phase 2, *Pope & Talbot Inc. v. Canada*, ¶ 79 (NAFTA Ch. 11 Arb. Trib. Apr. 10, 2001), <http://www.appletonlaw.com/cases/P&T-Merits%20Award-April%2010,%202001.pdf> (“A formulation focusing on the like circumstances question, on the other hand, will require addressing any difference in treatment, demanding that it be justified by showing that it bears a reasonable relationship to rational policies not motivated by preference of domestic over foreign owned investments.”).
- <sup>47</sup> *Id.* ¶ 78 (stating that differences in treatment will presumptively violate Article 1102(2)).
- <sup>48</sup> *Occidental Exploration and Prod. Co. v. Ecuador*, Case No. UN 3467 (London Ct. Int'l. Arb. July 1, 2004) [hereinafter *Occidental Exploration*]. Ultimately, the *Occidental* Tribunal found that Ecuador breached its non-discrimination and fair and equitable obligations and awarded compensation in the amount of US\$71,533,649.00 plus 55% of the arbitration costs (US\$326,724.40).
- <sup>49</sup> *Id.* ¶¶ 167-79. The *Occidental* Tribunal addressed both the MFN and NT standards under the same heading, perhaps due to the fact that both standards are included in the same article II(1) of the BIT.
- <sup>50</sup> *Id.* ¶ 167-68.
- <sup>51</sup> *Id.* ¶ 168.
- <sup>52</sup> *Id.* ¶ 171.
- <sup>53</sup> *Id.* ¶ 172.
- <sup>54</sup> *Id.* ¶ 173.

<sup>55</sup> See Fabrizio Pagani & Marie-France Houde, *Most-Favored-Nation Treatment in International Investment Law* 16 (OECD, Working Paper No. 2004/2), <http://www.oecd.org/dataoecd/21/37/33773085.pdf>.

<sup>56</sup> See Jürgen Kurtz, *National Treatment, Foreign Investment and Regulatory Autonomy: The Search for Protectionism or Something More?*, in *NEW ASPECTS OF INTERNATIONAL INVESTMENT LAW* 311 (Philippe Kahn & Thomas Wälde eds., 2007).

<sup>57</sup> OECD, *1976 Declaration and Decisions on International Investment and Multinational Enterprises*, DAF/IME(2000)20 (Nov. 9, 2000), [http://www.oecd.org/officialdocuments/displaydocumentpdf?cote=daffe/ime\(2000\)20&doclanguage=en](http://www.oecd.org/officialdocuments/displaydocumentpdf?cote=daffe/ime(2000)20&doclanguage=en).

<sup>58</sup> Pagani & Houde, *supra* note 55.

<sup>59</sup> Occidental Exploration, *supra* note 48, ¶ 177.

<sup>60</sup> Aloysius Llamzon, *The Final Award in Occidental v. Ecuador*, in *THE REASONS REQUIREMENT IN INTERNATIONAL INVESTMENT ARBITRATION* 211, 227 (Guillermo Aguilar Alvarez & Michael Reisman eds., 2008).

<sup>61</sup> See Kurtz, *supra* note 56.

<sup>62</sup> OECD, *Chairman's Note on Environment and Related Matters and on Labour*, at 5 DAF/MAI(98)10 (Mar. 9, 1998), <http://www1.oecd.org/daf/mai/pdf/ng/ng9810e.pdf>.