V. Fair and Equitable Treatment Standard and Legitimate Expectations

The FET standard and legitimate expectations are inherently linked. This connection does not have a standardized form but the majority of investment Tribunals treat these two concepts as closely related. In such a manner they will be observed in this thesis.

A. Fair and Equitable Treatment Standard

1. General Characteristics

Most IIAs contain a clause that provides for the standard of protection known as FET. The German model BIT 2008[200], for example, contains the following provision: "Each contracting State shall in its territory in every case accord investments by investors of the other Contracting State fair and equitable treatment as well as full protection under this Treaty."[201] The FET standard is the most called upon standard of protection in investment arbitration and FET claims are deemed highly successful. Despite the standard's presence in IIAs, a surge of FET claims has been seen only since the *Metalclad* v. *Mexico* case.[202]

Historically the FET standard is rooted in the US treaties on Friendship, Commerce and Navigation.[203] Its modern manifestation was given for the first time in the Havana Charter for International Trade Organizations in 1948, where the term "just and equitable treatment" was used. Even though the Treaty which remained only a draft and which was never, in fact envisaged as an investment treaty, ensured FET its first prominent

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200 German Model Treaty-2008, Treaty between the Federal Republic of Germany and (empty space) concerning the Encouragement and Reciprocal Protection of Investments, available at: http://investmentpolicyhub.unctad.org/Download/TreatyFile/2865 (Visited last on Mar. 6, 2018) [herein after: German Model BIT].

201 *Id*, art. 2(2).

202 Rudolf Dolzer & Christoph Schreuer, Principles of International Investment Law, 1st ed., 119, (2008).

203 *Id*, at 120.

role.[204] Today FET protection is a ubiquitous standard, although it was not always present in IIAs. Over time, and especially since the conclusion of the first modern BIT between Germany and Pakistan[205], FET started to appear more regularly in IIAs.[206]

The purpose of the FET standard is to fill the gaps left by the rules on expropriation, which addresses the direct or indirect taking of property.[207] This means that an investor can sometimes count on the protection through this standard independently of the Tribunal's decision on expropriation.[208] Therefore FET protects the investor from different kinds of unfair situations.[209] The FET standard is applied as a "yardstick for the conduct of the national legislator, of domestic administrations, and of domestic courts."[210] Furthermore FET is an absolute standard. It applies to investments without regard to the State's treatment of other entities and investments.[211] It is as such a rule of international law and it cannot be based on domestic laws of the state. Therefore, violations of FET can be found even if there seems to be no breach of the national treatment obligation.[212]

However, the precise source of FET as a standard in international law is not entirely clear. It is generally accepted that FET is a part of customary international law but that is where the consensus stops.[213] Some consider the standard to be related to the customary international law standard for the treatment of aliens, as it was originally connected to it in the draft of

204 Lukas Vanhonnaeker, Intellectual Property Rights As Foreign Direct Investments: From Collision to Collaboration, 101 (2015).
205 Germany – Pakistan BIT, Supra note 50.
206 Ronald Kläger, 'Fair and Equitable Treatment' in International Investment Law, 10 (2011).
207 Dolzer & Schreuer, Supra note 202, at 122.
208 Jean Kalicki & Suzana Medeiros, Fair, Equitable and Ambiguous: What is the Fair and Equitable Treatment in International Investment Law?, 22 (1) ICSID Rev. Foreign Invs't L. J., 24, 25 (2007).
209 *Fair and Equitable Treatment,* UNCTAD Series On Issues In International Investment Agreements II, 6-7 (2012) [herein after: FET UNCTAD].
210 Stephan W. Schill, The Mulitilaterization of International Investment Law, 79 (2009).
211 FET UNCTAD, Supra note 209, at 6.
212 Dolzer & Schreuer, Supra note 202, at 123.
213 Jacob Stone, Arbitrariness, The Fair and Equitable Treatment Standard, and the International Law of Investment, 25(1) L.J.I.L. 77, 78 (2012).

the OECD convention.[214] Some however view the standard as a standalone standard without express connection to other rules of international law.[215] The qualification of the FET standard is furthermore important for its substantive content. The language of the FET provisions is often broad and vague. The arbitral Tribunals are therefore the ones who give meaning to such broadly defined provisions[216]. For that reason, the FET standard has been criticized for lacking predictability and being susceptible to expansive interpretation.[217]

However, there are some recurring concepts that Tribunals regularly consider when deciding on the violations of the standard. According to some authors five distinct points could be put under the chapeau of the FET standard:

1. Legitimate expectations – The acts or promises of the state give rise to legitimate expectations of the investor.
2. Non-discrimination – Investors are protected from discriminatory acts of the state.
3. Fair procedure – The investor is guaranteed regular access and recourse through administrative and judicial mechanisms.
4. Transparency – The investor is afforded access to clear information in regards to the domestic legal framework and procedures.
5. Proportionality – This notion requires the Tribunal to balance the interest of the investor and the state in light of the measure taken that might have resulted in the violation of the FET standard.[218]

214 OECD, The Multilateral Agreement on Investment Draft Consolidated Text, § IV, art. 1, DAFFE/MAI(98)7/REV1 (1998) available at: http://www1.oecd.org/daf/mai/pdf/ng/ng987r1e.pdf (Visited last on Mar. 6, 2018).

215 FET UNCTAD, Supra note 209, at 7-8.

216 The Tribunal made an interpretative reference to the objectives of the treaty and found that transparency should be a part of the FET standard. Metalclad Corp. v. Mexico Award, §§ 75-76, ICSID Case No. ARB(AF)/97/1 (2001)[herein after: *Metalclad v. Mexico*].

217 FET UNCTAD, Supra note 209, at 6-7.

218 Kläger, Supra note 206, at 10.

2. The Fair and Equitable Treatment Standard under NAFTA

NAFTA jurisprudence on the FET standard is somewhat specific. The provision which provides fair and equitable treatment is located under article 1105(1):

> "Each Party shall accord to investments of investors of another Party treatment in accordance with international law, including fair and equitable treatment and full protection and security."

The standard only reached a degree of uniformity after the FTC issued its seminal Note[219]. Prior to the FTC's Note *Metalclad v. Mexico* was the first award to elaborate on the standard. The follow up Tribunals after *Metalclad* v. Mexico did not however accept the same interpretative discourse.

a) Metalclad v. Mexico

In *Metalclad v. Mexico* the investor, relying on the government of Mexico's permit to run its business, was later denied the opportunity to do so by the municipality.[220] Therefore the two branches of the same government presented conflicting messages and behavior to the investor, resulting in its inability to continue the business. The Tribunal found that the violation of FET occurred in the following manner:

> "Mexico failed to ensure a transparent and predictable framework for Metalclad's business planning and investment. The totality of these circumstances demonstrates a lack of orderly process and timely disposition in relation to an investor of a Party acting in the expectation that it would be treated fairly and justly in accordance with the NAFTA."[221]

219 FTC's Note, Supra note 145.
220 *Metalclad v. Mexico,* Supra note 216, §§ 47-50.
221 Id, § 99.

b) S. D. Myers v. Canada[222]

Another NAFTA investment Tribunal found a violation of FET in the *S. D. Myers* case. The article 1105 issue was whether the violation of the national treatment standard directly indicates the violation of FET. The Tribunal left room for a possibility that a breach of the national treatment does not directly lead to a violation of FET.[223] However, what was perhaps more interesting is the definition the Tribunal provided for the threshold needed to reach a violation of FET. The Tribunal stated:

> "Article 1105(1) expresses an overall concept. The words of the article must be read as a whole. The phrases *...fair and equitable treatment...* and ...full *protection and security...* cannot be read in isolation. They must be read in conjunction with the introductory phrase *...treatment in accordance with international law*."[224]

The Tribunal considered that a breach of article 1105 occurs only when it is shown that an investor has been treated in such "an unjust or arbitrary manner that the treatment rises to the level that is unacceptable from the international perspective. That determination must be made in the light of the high measure of deference that international law generally extends to the right of domestic authorities to regulate matters within their own borders. The determination must also take into account any specific rules of international law that are applicable to the case."[225]

The departure from the *Metalclad* case was evident. The FET standard was treated in a more abstract manner and more importantly it recognized two distinct points – the breach of the standard is connected to the state's international law obligations and the deference to national law in light of the state's right to regulate.

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222 S.D. Myers, Inc. v. Canada Partial Award (2004), available at: http://www.italaw.com/sites/default/files/case-documents/ita0747.pdf (Visited last on Mar. 6, 2018) [herein after *S.D. Myers v. Canada*].

223 *Id,* § 266.

224 *Id*, § 262.

225 Id, § 263.

c) Pope & Talbot v. Canada[226]

Another prominent case, after which the FTC's Note was eventually issued, was the *Pope & Talbot* case. The Tribunal took on an "additive" approach, thus holding that the FET standard contained in 1105(1) goes beyond the minimum standard of treatment of aliens found in international customary law. The Tribunal stated:

> "Accordingly, the Tribunal interprets Article 1105 to require that covered investors and investments receive the elements of the fairness benefits under ordinary standards applied in the NAFTA countries without any threshold limitation that the conduct complained be of 'egregious,' 'outrageous,' or 'shocking,' or otherwise extraordinary."[227]

The interpretation gave way for an open-ended direction in the development of jurisprudence on the FET standard. Therefore, the FTC's Note can be seen as a pre-emptive move to defer future Tribunals from further widening the FET standard. The FTC's interpretative Note stated:

> "The concepts of 'fair and equitable treatment' and 'full protection and security' do not require treatment in addition to or beyond that which is required by the customary international law minimum standard of treatment of aliens."[228]

A clear signal was sent. The Note did not address just one issue. More interpretative guidance was given in the Note. Under article B(3) of the Note the following is pronounced:

> "A determination that there has been a breach of another provision of the NAFTA, or of a separate international agreement, does not establish that there has been a breach of Article 1105(1)."[229]

This interpretative rule prohibited a direct causal link between breaches of international law and the FET standard. Therefore, when a breach of international or other NAFTA obligation is found, it should be treated from a case specific viewpoint. What comes from this is that an investor cannot solely rely on proving the breach of the international legal norm, rather it

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226 *Pope & Talbot Inc. v. Canada*, UNCITRAL,Award on the Merits of Phase II, (2001), available at: http://www.italaw.com/sites/default/files/case-documents/ita0678.pdf (Visited last on Mar. 6, 2018) [herein after: *Pope & Talbot v. Canada*].

227 *Id*, § 118.

228 FTC's Note, Supra note 145, art. B(2).

229 *Id*, art. B(3).

needs to be placed into context of the conduct amounting to the breach of the possible FET standard.

d) Mondev v. USA[230]

The first case after the FTC's Note was the *Mondev v. USA* case. It was the first time a NAFTA investment Tribunal applied the Note in practice. The Tribunal accepted the connection to the international law standard. However, it firstly rejected the standard set in the *Neer* case as currently applicable.[231] The Tribunal made a further clarification that the standard evolves over time and that the Note's language points to the contemporary standard of customary international law. The Tribunal stated:

"But in its view, there can be no doubt that, by interpreting Article 1105(1) to prescribe the customary international law minimum standard of treatment of aliens as the minimum standard of treatment to be afforded to investments of investors of another Party under NAFTA, the term 'customary international law' refers to customary international law as it stood no earlier than the time at which NAFTA came into force. It is not limited to the international law of the 19th century or even of the first half of the 20th century, although decisions from that period remain relevant. In holding that Article 1105(1) refers to customary international law, the FTC interpretations incorporate current international law, whose content is shaped by the conclusion of more than two thousand bilateral investment treaties and many treaties of friendship and commerce."[232]

After *Mondev v. USA* the NAFTA investment Tribunals decided on a number of cases where the designated interpretation of article 1105(1) was used. However even this circumscribed version of article 1105 left room for various application of the standard, owing to the specific factual situation of the cases.

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230 Mondev I'ntl Ltd. v. USA, ICSID (Additional Facility) Award, Case No. ARB(AF)/99/2 (2002), available at: http://www.italaw.com/sites/default/files/case-documents/ita1076.pdf (Visited last on Mar. 6, 2018) [herein after: *Mondev v. USA*].

231 *Id*, § 116.

232 *Id*, § 125.

e) Waste Management v. Mexico[233]

Despite the Note´s limiting effect NAFTA´s FET jurisprudence kept on evolving even after *Mondev v. USA*. In the *Waste Management v. Mexico* the Tribunal made way to what was to become the basis for legitimate expectations, although a clear distinction was not made at the time. The Tribunal stated:

> "[T]hat the minimum standard of treatment of fair and equitable treatment is infringed by conduct attributable to the State and harmful to the claimant if the conduct is arbitrary, grossly unfair, unjust or idiosyncratic, is discriminatory and exposes the claimant to sectional or racial prejudice, or involves a lack of due process leading to an outcome which offends judicial propriety—as might be the case with a manifest failure of natural justice in judicial proceedings or a complete lack of transparency and candor in an administrative process. In applying this standard it is relevant that the treatment is in breach of representations made by the host State which were reasonably relied on by the claimant."[234]

The FET standard definition given by the *Waste Management* Tribunal relied primarily on the denial of justice and transparency. However, the last sentence introduced, very clearly, the concept of legitimate expectations as a part of the FET standard. The jurisprudential influence of *Metalclad v. Mexico* is likewise evident. Its reference to the establishment of a transparent and predictable legal system very well corresponded with the concept of legitimate expectation.

B. Legitimate Expectations

1. General Characteristics

The root of the concept of legitimate relates to the "phenomenon of 'change'". An investment, whatever form it assumes, usually persists for a prolonged period of time. It is very rarely an instantaneous and "one-off" business act. During this time the investment might be affected by adverse

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233 Waste Management Inc. v. Mexico, ICSID (Additional Facility) Award, Case No. ARB(AF)/00/3 (2004), available at: http://www.italaw.com/sites/default/files/case-documents/ita0900.pdf (Visited last on Mar. 6, 2018) [herein after: *Waste Management v. Mexico*].

234 *Id*, § 98.

changes coming from different sources. Some are a result of economic factors or technological development. However, some acts of the state like regulatory measures and the implementation of a law can affect investments as well. The second type of situation is the one legitimate expectations address.[235] The core notion of legitimate expectations is that an investor is able to rely on certain state acts when making its investment decisions. However not all expectations are considered protectable under international investment law.[236]

The concept of legitimate expectations is usually accepted as falling under the chapeau of the FET standard, which is on the one hand clearly worded in IIAs. On the other hand, there rarely seems to be clear wording in FET provisions pointing to the protection of legitimate expectations.[237] So how exactly does a concept like legitimate expectations persist in investment arbitration jurisprudence? As some authors suggest legitimate expectations can be viewed as a general principle of law.[238] General principles of law are usually supplementary means of interpretation used for gap filling of provisions[239] or as means to resolve conflicts between overlapping provisions and rules.[240] Nevertheless in establishing the link one needs to look to existing legal systems where legitimate expectations are firmly grounded. Therefore, some authors suggest looking at municipal law[241] and public law[242] in different jurisdictions as possible sources. By taking the core of the concept, based on the recurring characteristic of the principle in the observed jurisdictions, which would be "suited for the international environment", could provide a source to the principle.[243] From the perspective of legal theory this line of reasoning has some standing. In

235 FET UNCTAD, Supra note 209, at 63-64.
236 Christoph Schreuer & Ursula Kriebaum, At What Time Must Legitimate Expectations Exist? in A Liber Amicorum: Thomas Wälde - Law Beyond Conventional Thought, 265, 265 (Jacques Werner & Arif Hyder Ali 1st ed. 2009).
237 Michele Potesta, Legitimate Expectations in Investment Treaty Law: Understanding the Roots and the Limits of a Controversial Concept, 28(1) ICSID - For. Inv. L.J., 88, 90 (2013).
238 Elizabeth Snodgrass, Protecting Investor's Legitimate Expectations: Recognizing and Delimiting the General Principle, 21(1) ICSID - For. Inv. L.J., 1, 11 (2006).
239 *Id*, at 13.
240 *Id,* at 19.
241 *Id,* at 18.
242 *Id,* at 21.
243 *Id,* at 23.

practice though, investment Tribunals do not apply this approach. According to some authors there seems to be little regard for real state practice.[244] Likewise the Tribunals are likely to look at previous decisions of other Tribunals, thus effectively creating a rule of precedent in international investment arbitration.[245]

The substantive content of legitimate expectations varies, although there seems to be a general understanding of which notions they carry. In essence the investor is able to base its expectations on certain conditions attributable to the state provided at the time of the investment. The conditions cannot be established on a unilateral basis, they must exist in law and be enforceable by it. If the state has failed to respect its promises it is required to compensate the investor expect in cases of state necessity. The investor cannot disregard parameters such as industry patterns and business risk when creating its expectations.[246]

The question to be asked here is – what type of condition can the investor rely on and which expectations can be legitimate? Three distinct approaches can be found.

a) Legitimate Expectations Arising out of Contractual Basis

An investor's legitimate expectations can arise out of a contract concluded with the state. Contracts are widely recognized as pillars of "legal stability and predictability" and thus present a good basis for legitimate expectations.[247] Nevertheless a pure breach of contractual obligations does not in itself amount to an automatic frustration of legitimate expectations. An additional factor is needed to amount to a breach of treaty obligations. As some author see it the additional factor would be "'a breach involving a sovereign power' (*pussiance publique*), or 'outright and unjustified repudiation of the transaction' or 'substantial breach' 'under certain limited circumstances. '"[248]

244 Potesta, Supra note 237, at 90.
245 *Id*, at 91.
246 The Oxford Handbook of International Investment Law, 496 (Peter Muchlinski, Federico Ortino & Christoph Schreuer eds., 2008)
247 Potesta, Supra note 237, at 101-2.
248 *Id.*, at 102.

b) Legitimate Expectations Arising out of Representations of State

A basis for legitimate expectations can be found in the promises and representations made by the state which the investor relied on, while making decisions regarding the investment.[249] However not all promises and representations give rise to legitimate expectations. Legitimate expectations in this case require a certain level of specificity. What is usually required is that the promise or representation is individualized and unambiguous. The promise must accordingly be addressed directly at the investor and not at the general public.[250]

c) Legitimate Expectations Arising out of State's Regulatory Framework

The investor can at times base its legitimate expectations on the state's regulatory and legislative framework at the time when it made its investment. The frustration of legitimate expectations can arise when the state changes its laws or the way they are applied. These changes need to bring economic loses to the investor. However, this approach is not commonly accepted in investment arbitration jurisprudence. The premise of such a wide interpretative approach lies in the dedication to stability envisaged by the treaty itself. Often the basis is found in the treaty language and when the Tribunals are willing to expand the interpretation of legitimate expectations. So, in which circumstances can legitimate expectations arise out of a requirement of the state not to change its laws? As some authors suggest a general reference to stability in the treaty language is insufficient to give rise to legitimate expectations. Only an explicit reference in the form of a "stability clause" should give rise to legitimate expectations. Furthermore, there can be no standardized "yardstick of good governance", rather the decision should be evaluated on a factual, case to case basis.[251] Some of the arbitral awards demonstrate how the standard should be evaluated. One Tribunal stated that legitimate expectations cannot exist where it is expected that the implementation, interpretation and application of the law has changed over time. Another Tribunal points to the

249 *Id.*, at 103.
250 *Id.*, at 105-6.
251 *Id.*, at 113.

"unreasonableness" of the changes in the law as something that might frustrate legitimate expectations.[252]

2. Legitimate Expectations under NAFTA

NAFTA article 1105 express connection to international law creates specific circumstances not found in other IIAs. Nevertheless, even despite the FTC's circumscribed seeing of the article, legitimate expectations have found their way into NAFTA investment arbitration jurisprudence. The case law demonstrates that legitimate expectations are observed as a part of the FET.

a) Thunderbird v. Mexico[253]

Thunderbird was the first case under NAFTA to fully investigate legitimate expectations, although *Metalclad v. Mexico* and other previous awards had previously touched upon the issue.[254]

Thunderbird is a game facilities operator. The company tried opening a business outpost in Mexico and received an opinion for operating such an establishment by the adequate state authority, confirming its legality.[255] However upon inspecting the establishment, Thunderbird was not allowed to continue its business. The authorities stated that the gaming machines were contrary to Mexico's gambling laws.[256] It was determined by the Mexican authorities and later confirmed by the Tribunal that Thunderbird did not truthfully disclose the functionality of the machines. They were characterized as "games of chance."[257] However Thunderbird claimed that its legitimate expectations were nevertheless frustrated.

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252 *Id.*, at 117.

253 International Thunderbird Gaming Corp. v. Mexico, Award, (2007) available at: http://www.italaw.com/sites/default/files/case-documents/ita0431.pdf (Visited last on Mar. 6, 2018) [herein after: *Thunderbird v. Mexico*].

254 Patrick Dumberry, The Protection of Investors' Legitimate Expectations and the Fair And Equitable Treatment Standard under NAFTA article 1105, 31 (1) J. Int'l Arb. 47, 51 (2014).

255 *Thunderbird v. Mexico,* Supra note 253, § 55.

256 *Id,* §§ 73-4.

257 *Id*, §§ 151-53.

The Tribunal applied the following definition:

> "The concept of 'legitimate expectations' relates, within the context of the NAFTA framework, to a situation where a Contracting Party's conduct creates reasonable and justifiable expectations on the part of an investor (or investment) to act in reliance on said conduct, such that a failure by the NAFTA Party to honor those expectations could cause the investor (or investment) to suffer damages."[258]

The Tribunal held that the intentional failure to provide truthful information, on which the representation was based, cannot give rise to legitimate expectations. When the legality of the investment is doubtful there can be no legitimate expectations.[259]

b) Glamis Gold v. USA[260]

This NAFTA case was about a mining endeavor of a Canadian company, whose attempts at open pit mining were stopped by the state of California.[261]

The Tribunal considered legitimate expectations a constituent part of the FET standard. It set the legal standard for determining the threshold of legitimate expectations' violations:

> "Tribunal has explained in its discussion of the 1105 legal standard, a violation of Article 1105 based on the unsettling of reasonable, investment backed expectation requires, as a threshold circumstance, at least a quasi-contractual relationship between the State and the investor, whereby the State has purposely and specifically induced the investment."[262]

A strong message came out of this award as the Tribunal showed deference to the states right to regulate. Legitimate expectations for the Tribunal arise only when specific "quasi-contractual" representations are made to the investor. Even reasonable expectations made at the moment of

258 Id, § 147.
259 Dumberry, Supra note 254, at 51.
260 Glamis Gold, Ltd. v. USA, ICSID Award (2009) available at: http://www.italaw.com/sites/default/files/case-documents/ita0378.pdf (Visited last on Mar. 6, 2018) [herein after: *Glamis Gold v. USA*].
261 Dumberry, Supra note 254, at 54.
262 *Glamis Gold v. USA,* Supra note 260, § 766.

the investment should not be protected if there is no concrete representation.

c) Grand River v. USA[263]

In this case the Tribunal had to resolve an issue related to an economic burden imposed on foreign cigarette importers and distributors.[264]

The Tribunal addressed the issue of the relationship of external international law sources as a basis for the violation of a treaty standards. The interpretation set by FTC's Note was accordingly put into practice.[265] The Tribunal clearly rejected the importation of norms from other treaties in establishing standards for the violation of article 1105. It referred to the express linkage with international law and rejected the practice of "looking beyond". However, this rejection was aimed at establishing direct breaches of other international norms as direct violation of the investment treaty standards.[266] The Tribunal did not however dismiss the possibility to analyze the international sources of law as a matter of fact. Indeed, it entertained the possibility of other sources of law creating legitimate expectations but determined that, in the case itself, the legislation did not create legitimate expectations even if they had been pertinent to the case.[267]

d) Mobil v. Canada[268]

Mobil v. Canada was a case where the government of Canada implemented regulatory changes in relation to two companies in the business of off-

263 Grand River Enterprises Six Nations Ltd., et al. v. USA, ICSID Award (2011) available at: http://www.italaw.com/sites/default/files/case-documents/ita0384.pdf (Visited last on Mar. 6, 2018) [herein after: *Grand River v. USA*].
264 *Id,* §§ 18-19.
265 *Id,* § 176.
266 *Id,* § 219.
267 *Id,* §§ 141-142.
268 Mobil Investments Canada Inc. & Murphy Oil Corp. v. Canada, ICSID Decision on Liability and on Principles of Quantum, Case No. ARB(AF)/07/4 (2012) available at: http://www.italaw.com/sites/default/files/case-documents/italaw4399_0.pdf (Visited last on Mar. 6, 2018) [herein after: *Mobil v. Canada*].

shore oil drilling.[269] The measures required the companies to spend a certain percentage of their income on R&D, which they claimed violated their rights under the NAFTA Investment Chapter.[270]

In addressing the article 1105 issue, the Tribunal stated:

> "This applicable standard does not require a State to maintain a stable legal and business environment for investments, if this is intended to suggest that the rules governing an investment are not permitted to change, whether to a significant or modest extent. Article 1105 may protect an investor from changes that give rise to an unstable legal and business environment, but only if those changes may be characterized as arbitrary or grossly unfair or discriminatory."[271]

Likewise, the Tribunal created the standard which gave a "road map" for determining whether legitimate expectations were in fact frustrated. First of all, a clear representation needs to be made by the state to induce the investments. Second, the investor reasonably needs to rely on it. Third, the state must rescind on the representation.[272] The *Mobil* Tribunal thus took a very clear stance on how to approach regulatory changes in light of legitimate expectations.

3. Legitimate Expectations and Intellectual Property in Investment Arbitration

The relationship between legitimate expectations and the IPRs was up to very recently a matter of purely scholarly conjecture. However, cases started appearing that have addressed the issue.

a) Philip Morris v. Australia

The first case to establish a link between TRIPS, an international IP treaty, and an investment claim was the *Philip Morris v. Australia* case.

Australia enacted regulatory changes that require cigarettes to be sold in a particular type of packaging. This affected the way in which the trade-

269 *Id*, § 1.
270 *Id,* § 100.
271 *Id,* § 153.
272 *Id,* §152 (3).

mark of the cigarette brand could be displayed. The changes were implemented as a public health measure with a view of decreasing smoking.[273]

Philip Morris claimed that Australia had frustrated its legitimate expectations by failing to observe its international obligations from the TRIPS. It claimed that the measures unjustifiably encumbered its trademarks. Philip Morris claimed that it made the investment legitimately expecting Australia to comply with its international obligations.[274] However the Tribunal never got to addressing the legitimate expectations issue as the case was resolved by the Tribunal declining jurisdiction.[275]

Even though the investment claim did not succeed Australia still has to defend its legislation in an international forum. Currently there is an ongoing WTO case where the same plain packaging legislation was challenged under the TRIPS.[276] The outcomes remains to be seen.

b) Philip Morris v. Uruguay

So far, the only publicly available investment arbitration award that addressed the issue of legitimate expectations and IP laws is *Philip Morris v. Uruguay* case.

The factual background of the case is very similar to *Philip Morris v. Australia*. In 2005 Uruguay enacted regulatory changes affecting the tobacco industry.[277] The measures were envisaged as a public health measure to combat smoking.[278] Restrictions on advertising, mandatory health warnings, elevated taxation on tobacco products and banning smoking in public places were the steps the Uruguayan government undertook to fight smoking.[279] The claim put forward by Philip Morris was that Uruguay´s measures affected their IPRs, which are under the Switzerland – Uruguay

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273 *Philip Morris v. Australia,* Supra note 107, Australia's Response to Notice of Arbitration, §§ 20-23.
274 *Id*, §§ 6.5-6.8.
275 *Philip Morris v. Australia*, Supra note 107, Award, § 588.
276 The panel report is pending. *Australia — Certain Measures Concerning Trademarks, Geographical Indications and Other Plain Packaging Requirements Applicable to Tobacco Products and Packaging*, WT/DS467/20 (2013).
277 *Philip Morris v. Uruguay*, Supra note 107, Award, § 67.
278 *Id*, § 74-77.
279 *Id*, § 78.

BIT[280] protected as investments.[281] The measures in effect limited the way their registered trademarks are displayed.[282] Uruguay, as the respondent state, justified its measures on public policy grounds.[283]

The Tribunal agreed with Uruguay and recognized both the right of the state to regulate and the acceptable limits to regulation:

> "On this basis, changes to general legislation (at least in the absence of a stabilization clause) are not prevented by the fair and equitable treatment standard if they do not exceed the exercise of the host State's normal regulatory power in the pursuance of a public interest and do not modify the regulatory framework relied upon by the investor at the time of its investment "outside of the acceptable margin of change."[284]

The Tribunal accepted the position that for legitimate expectations to arise a direct representation needs to be made by the state to the investor. Legislation directed at the general public cannot create legitimate expectations.[285] The Tribunal concluded that the manifest absence of a representation made by the state shows that there can be no legitimate expectations.[286] The Tribunal further recognized that the legislation which imposed the restrictions on Philip Morris' trademark rights were a legitimate policy measure. For these reasons the Tribunal dismissed the legitimate expectation claims of Philip Morris.[287]

The focus of the Tribunal was almost exclusively on the domestic legislation. The only time international treaties were mentioned in addressing this particular claim was as supporting proof for the justification of the measures undertaken by Uruguay.[288] Therefore international treaties were used merely for interpretative guidance. Even more importantly the treaties referred to, were not IP treaties.

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280 The Agreement between the Swiss Confederation and the Oriental Republic of Uruguay on the Reciprocal Promotion and Protection of Investment, Oct. 7, 1988, 1976 U. N. T. S. 413.
281 *Philip Morris v. Uruguay*, Supra note 107, Award, § 9.
282 *Id*, § 11
283 *Id*, § 13.
284 *Id*, § 423.
285 *Id*, § 426
286 *Id,* § 429.
287 *Id*, § 432.
288 *Id,* § 423.