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SHOULD INVESTMENT TREATIES CONTAIN PUBLIC POLICY EXCEPTIONS?

CAROLINE HENCKELS*

Abstract: The increasing inclusion of exceptions in newly concluded investment treaties, together with the divergent manner in which tribunals and annulment committees have approached these provisions, suggests that a greater understanding of their role and purpose is needed. In particular, the question whether exceptions operate as *permissions* or as *defenses* is a crucial but unaddressed issue that has significant implications for both litigation and practice and, in turn, implications for the stability of the regime. This Essay argues that as a starting point, exceptions should be understood as permissions that limit the scope of the substantive treaty obligations, and not as defenses invoked to justify *prima facie* unlawful conduct. Understanding exceptions as permissions has several advantages, including the avoidance of double-counting a government's motivation for its conduct or, more problematically, failing to take regulatory purpose into account when determining whether a government has complied with the treaty's substantive obligations. Understanding exceptions as permissions also sends signals to adjudicators in relation to issues such as the appropriate standard of review. The Essay also explores the desirability of including exceptions in treaties in light of recent innovations that clarify the substantive content of investment obligations. Although the uncertain analytic character of existing exceptions risks constraining rather than preserving regulatory space, they may be an important failsafe in light of current institutional arrangements for investor-state dispute settlement, which effectively preclude review for error of law. The Essay concludes that the relationship between standards of investment protection and exceptions needs further consideration, and suggests that governments negotiating investment treaties ought to more holistically consider the aims of the regime and the role of exceptions therein.

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INTRODUCTION

Public policy exceptions in investment treaties permit a government to lawfully take action directed at a particular regulatory objective, industry, or sector of the economy that would otherwise be inconsistent with its substantive treaty obligations. Exceptions have become an increasingly popular mechanism in investment treaties, appearing in 43% of investment agreements concluded between 2011 and 2016, compared to 7% of agreements signed between 1959 (when the first investment treaty was signed) and 2010.¹ The significant rise in their prevalence suggests that governments negotiating new treaties are seeking greater assurance that public welfare measures will be shielded from liability. Yet, their proliferation in recent treaties creates uncertainties in terms of how they ought to be interpreted—whether but for the exception, a government would be in breach of its substantive obligations, or whether their inclusion is for the avoidance of doubt.² In particular, the question whether the exception operates as a *permission* or a *defense* is a crucial, but unaddressed issue that has significant implications for both litigation and practice and, in turn, may have implications for the stability of the investment regime.

This Essay assesses the role and desirability of including exceptions in investment treaties in light of this interpretive uncertainty. Part I discusses two different ways of characterizing the role of exceptions—as either permissions, which limit the scope of the substantive obligations, or as defenses invoked to justify conduct that would otherwise be prohibited.³ Through this lens, Part II analyzes the manner in which investment tribunals have interpreted exceptions in terms of their analytic character, the relationship between exceptions and the regime’s substantive obligations, and any interpretive maxims that tribunals apply to construction of the exception.⁴ Part III focuses on the role of exceptions in light of recent innovations in treaty design that attempt to inject greater determinacy into the normative content of the substantive obligations, asking whether exceptions are still a neces-

¹ U.N. Conference on Trade & Development (UNCTAD), *World Investment Report 2017: Investment and the Digital Economy*, 122 tbl. III.4, U.N. Doc. UNCTAD/WIR/2017 (June 7, 2017) (including investment chapters in other economic agreements). This statistic only appears to cover Article XX GATT-like exceptions and not other types of exceptions; this Essay takes a broader approach to the concept, as discussed further below.

² See Andrew Newcombe, *The Use of General Exceptions in IIAs: Increasing Legitimacy or Uncertainty?*, in *IMPROVING INTERNATIONAL INVESTMENT AGREEMENTS* 267, 277 (Armand de Mestral & Céline Lévesque eds., 2012) (noting that it is “unclear” whether the inclusion of exceptions in international investment agreements is because the treaties are “too broad” or are there to demonstrate “an abundance of caution”).

³ See *infra* notes 7–20 and accompanying text.

⁴ See *infra* notes 21–56 and accompanying text.

sary or desirable element of investment treaties in light of these reforms.⁵ Although exceptions create some challenging questions of construction, they may be an important means of circumscribing adventurous interpretations of investment tribunals—at least in the current institutional climate, which effectively precludes review of decisions attended by legal error. This Essay concludes that the relationship between standards of investment protection and exceptions needs further consideration and suggests that states negotiating investment treaties ought to more holistically consider the aims of the regime and the role of exceptions therein.⁶

I. UNDERSTANDING THE ROLE OF EXCEPTIONS

A. A Typology of Investment Treaty Exceptions

This Essay defines an exception as a phenomenon arising from the interrelationship of two norms: the first is a command, and the second permits deviation from that command in specific circumstances.⁷ For the purpose of this Essay, I differentiate exceptions from qualifications to rules that are located within the provision itself or in an interpretive annex, such as provisions clarifying the law on indirect expropriations.⁸ I also do not include in this category open-textured or flexible norms that permit consideration of all relevant circumstances in determining whether the norm has been complied with, such as fair and equitable treatment (FET).

The following is a taxonomy of the types of provisions that this Essay will examine:

- *General and security exceptions* typically use language such as “nothing in this Agreement shall be construed to prevent the adoption of . . . ,” then impose some restrictions on the design of the measure by specifying a required nexus between the measure and the permissible objective or objectives, such as “necessary to”⁹ or “designed and ap-

⁵ See *infra* notes 57–74 and accompanying text.

⁶ See *infra* note 7–74 and accompanying text.

⁷ See Hans Kelsen, *GENERAL THEORY OF NORMS* 96 (Michael Hartney trans., 1991) (1976) (noting that “command” includes a negative-command (prohibition)).

⁸ See Claire Oakes Finkelstein, *When the Rule Swallows the Exception*, in *RULES AND REASONING: ESSAYS IN HONOR OF FRED SCHAUER* 147, 150 (Linda Meyer ed., 1999) (explaining that “[a]n exception is a qualification of a rule that stands in a certain relation to it, namely it stands *outside* the rule it qualifies. Thus, a qualification included in a statement of the rule is not properly speaking an exception to it”).

⁹ *E.g.* Reciprocal Promotion and Protection of Investments, Arg.-Qatar, art. 10, June 11, 2016 [hereinafter Argentina-Qatar BIT]; Ass’n of Southeast Asian Nations [ASEAN] Comprehensive Investment Agreement, art. 17(1)(a), Feb. 26, 2009, <http://agreement.asean.org/media/download/20140119035519.pdf> [<https://perma.cc/VZT5-7ADP>].

plied to.”¹⁰ Increasingly, investment agreements contain exceptions that incorporate by reference or are modelled on the general exceptions in Article XX of the General Agreement on Tariffs and Trade (GATT) and Article XIV of the General Agreement on Trade in Services (GATS), which both contain an additional requirement that measures not be applied in an arbitrary or discriminatory way (the *chapeau*).

- *Carve-outs* exempt an entire policy area or sector from the scope of a treaty. For example, Article 1108(7) of the North American Free Trade Agreement (NAFTA) provides, *inter alia*, that the national treatment and most-favored nation treatment obligations in the investment chapter “do not apply to . . . procurement by a Party or a state enterprise . . .,” and Article 22 of the investment chapter of the Australia-Singapore FTA provides that “[n]o claim may be brought . . . in respect of a tobacco control measure of a Party.”
- *Reservations* are similar to carve-outs, but permit parties to unilaterally nominate a sector or sectors in relation to which they reserve the right to adopt or maintain otherwise non-conforming measures—whether in relation to some obligations or the agreement as a whole. For example, Articles 8.2(3) and 9.2(2)(b) and (c) of the Comprehensive Economic and Trade Agreement between Canada and the European Union (CETA) provide that for the E.U., obligations regarding establishment and non-discriminatory treatment of investments “do not apply to a measure with respect to audio-visual services” and for Canada “do not apply to a measure affecting . . . cultural industries”¹¹

One might argue that general and security exceptions perform a different function to carve-outs and reservations. Carve-outs and reservations seek to quarantine specific sectors or industries (e.g. cultural industries) or policy areas (e.g. taxation) from the scope of the agreement *ex ante*, whereas exceptions preserve broad policy space across all sectors for future exigencies. Exceptions, traditionally understood, are typically more open-textured in terms of permissible objectives (“morals,” “security,” and so on). At the same time, as noted above, they generally impose greater discipline on the design of measures in order to guard against possible abuse, such as by requiring that

¹⁰ *E.g.* Investment Agreement for the COMESA Common Investment Area, art. 22(1), May 23, 2007, <http://investmentpolicyhub.unctad.org/Download/TreatyFile/3092> [<https://perma.cc/3RF2-T6PV>] [hereinafter COMESA].

¹¹ Comprehensive Economic and Trade Agreement, Can.-European Union, art. 8.2(3), 9.2(2)(c), Oct. 30, 2016, 2017 O.J. (L 11) 23 [hereinafter CETA].

measures be “necessary,” and/or by prohibiting application of the measure in such a way as to subvert the discipline of the substantive obligations.¹²

Still, there is good reason to take a broad approach to the concept of exceptions. The distinction between the different types of provisions is not always clear. Clauses that are denoted as exceptions sometimes require only that measures be (for example) “related to” or “for” a particular objective, which hardly imposes more discipline on the measure than the language of typical carve-outs and reservations. Some of the permissible objectives found in exceptions refer to specific products or issues (for example, Article XX GATT includes exceptions “relating to the importations or exportations of gold or silver” and “relating to the products of prison labour”).¹³ As I will argue below, subject always to the language of the particular provision being interpreted, exceptions, carve-outs and reservations can be understood as playing the same role: that is, giving permission to states to act in relation to the matters stipulated in the provision without violating the rules of the regime.

B. The Analytic Character of Exceptions

Exceptions signal to adjudicators, governments, and potential claimants that the purpose of the treaty is not solely to protect investment at the expense of other public policy objectives.¹⁴ Yet, a key area of uncertainty concerns the analytic character of these provisions: that is, the question whether an exception operates as a *permission* or as a *defense*. The distinction is not merely theoretical; it has significant normative and practical consequences.¹⁵

One way of describing the role of an exception is that where a government establishes that it is taking action that is comes within the scope of the provision, the treaty obligations *do not apply*. A treaty exception might

¹² I am grateful to Jürgen Kurtz for raising this issue and to Andrew Newcombe for helpful discussions.

¹³ General Agreement on Tariffs and Trade art. XX(c), (e), Oct. 30, 1947, 61 Stat. A-11, 55 U.N.T.S. 194 [hereinafter GATT].

¹⁴ See JÜRGEN KURTZ, *THE WTO AND INTERNATIONAL INVESTMENT LAW: CONVERGING SYSTEMS* 169 (2015) (noting that by including exceptions in investment treaties, “negotiators . . . are thus clearly signaling that investment liberalization and protection are not the exclusive goals of the network”); U.N. Conference on Trade & Development (UNCTAD), *World Investment Report 2015: Reforming International Investment Governance*, U.N. Doc. UNCTAD/WIR/2015, 140 (June 25, 2015) [hereinafter *World Investment Report 2015*] (noting that public policy exceptions “can also have an important signaling effect towards the general public, indicating an agreement’s compatibility with sustainable development and public policy considerations”).

¹⁵ I explore some of these issues further in Caroline Henckels, *Scope Limitation or Affirmative Defence? The Purpose and Role of Investment Treaty Exception Clauses*, in *EXCEPTIONS AND DEFENCES IN INTERNATIONAL LAW* (Lorand Bartels & Federica Paddeu eds., forthcoming 2019) [hereinafter *EXCEPTIONS AND DEFENCES IN INTERNATIONAL LAW*].

therefore be characterized as a limitation on the scope of the investment protections in the treaty, or as a permission to engage in conduct covered by the clause.¹⁶ Alternatively, an exception could be regarded as an affirmative *defense*. A state relying on the exception would not deny that it had failed to observe its treaty obligations, but would seek to avoid the consequences of its actions on the basis that it was acting to protect interests permitted by the clause. In other words, action coming within the scope of the exception would justify (that is, render lawful)¹⁷ conduct that would otherwise be prohibited by the treaty.¹⁸

Normatively, there is a difference between characterizing government action to promote public welfare as outside the scope of the obligations, compared with characterizing such action as generally prohibited but justified in exceptional circumstances. If the exception is a permission that limits the scope of the investment protections in the treaty, a state's compliance with international law is presumed, but this is not the case where a state must rely on an affirmative defense to justify otherwise unlawful conduct.¹⁹ Moreover, to characterize an exception as an affirmative defense is to view the international investment regime through a lens of prohibition: government action negatively impacting foreign investment is generally prohibited, unless a tribunal grants specific authorization after the fact, in exceptional circumstances.²⁰ Even though a finding that a state has engaged in prohibited conduct is only made as a preliminary, defeasible stage in the reasoning process, it is, nevertheless, symbolically significant from the point of view of the host state. A government might consider it more palatable to domestic constituencies for action taken to promote public welfare to be exempt from the treaty obligations, rather than to be *prima facie* in breach of those obligations.

¹⁶ Jaap Hage, Antonia Waltermann & Gustavo Arosemena, *Logical Tools for International Law*, in EXCEPTIONS AND DEFENCES IN INTERNATIONAL LAW, *supra* note 15.

¹⁷ A justification permits a party to engage in conduct that would otherwise be prohibited by the regime, meaning that the conduct is lawful. *See generally* Kent Greenawalt, *Distinguishing Justifications from Excuses*, 49 L. & CONTEMP. PROBS. 89 (1986) (providing further discussion regarding how to distinguish between an excuse and a justification).

¹⁸ *See* KURTZ, *supra* note 14, at 217–18 (explaining how the exception operates to “save” a *prima facie* breach of a state's obligations).

¹⁹ *See generally* CAROLINE E. FOSTER, SCIENCE AND THE PRECAUTIONARY PRINCIPLE IN INTERNATIONAL COURTS AND TRIBUNALS: EXPERT EVIDENCE, BURDEN OF PROOF AND FINALITY 213 (2011) (discussing how the invocation of an exception removes the presumption of compliance with international law).

²⁰ *See* Frederick Schauer, *Exceptions*, 58 U. CHI. L. REV. 871, 872–73 (1991) (describing the relationship between rules and their exceptions); Foster, *supra* note 19, at 214 (noting how in exceptions, the party claiming the exception bears the burden of proof).

II. THE TREATMENT OF EXCEPTIONS IN INVESTMENT DISPUTES

Any analysis of the decided investment cases is hindered by the fact that in no case has an investment tribunal or annulment committee explained how it arrived at its characterization of an exception—whether as a matter of treaty interpretation, or based on normative considerations. Moreover, the parties’ submissions are not always available, or are not directed to this issue. However, a careful parsing of the decisions permits their categorization into defenses and permissions.

A. The Character of the Exception

1. Exception as Defense

Early tribunals determining claims involving the security exception in the U.S.-Argentina BIT²¹—*CMS Gas Transmission Company v. Argentine Republic* in 2004,²² *Enron Corporation Ponderosa Assets L.P. v. Argentine Republic* in 2007,²³ and *Sempra Energy International v. Argentine Republic* in 2007²⁴—appeared to view the provision as an affirmative defense, although their characterization of the exception is difficult to untangle from their mistaken understanding of the relationship between the exception and the defense of necessity at customary international law. Two further tribunals hearing claims against Argentina—*El Paso Energy International Company v. Argentine Republic* in 2011 and *LG&E Energy Corporation v. Argentine Republic* in 2006—adopted a similar approach, based on an apparent misapprehension that the exception was a *lex specialis* expression of the necessity defense.²⁵

²¹ Treaty Concerning the Reciprocal Encouragement and Protection of Investment, U.S.-Arg., art. XI, Nov. 14, 1991, S. TREATY DOC. 103-2 (1993) [hereinafter U.S.-Argentina BIT] (“This Treaty shall not preclude the application by either Party of measures necessary for . . . the [p]rotection of its own essential security interests.”).

²² *CMS Gas Transmission Co. v. Argentine Republic*, ICSID Case No. ARB/01/08, Award, ¶¶ 320–324, 329, 355–356, 374 (May 12, 2004).

²³ *Enron Corp. & Ponderosa Assets L.P. v. Argentine Republic*, ICSID Case No. ARB/01/3, Award, ¶¶ 334, 339 (May 22, 2007) [hereinafter *Enron Award*].

²⁴ *Sempra Energy Int’l v. Argentina Republic*, ICSID Case No. ARB/02/16, Award, ¶¶ 376, 388 (Sept. 28, 2007) [hereinafter *Sempra Award*].

²⁵ *El Paso Energy Int’l Co. v. Argentine Republic*, ICSID Case No. ARB/03/15, Award, ¶ 552 (Oct. 31, 2011); *LG&E Energy Corp. v. Argentine Republic*, ICSID Case No. ARB/02/1, Decision on Liability, ¶¶ 229, 257, 261 (Oct. 3, 2006) [hereinafter *LG&E Award*]. See generally Henckels, *supra* note 15 (providing further discussion on the analytic character of exceptions); Caroline Henckels, *Investment Treaty Security Exceptions, Necessity & Self-Defence in the Context of Armed Conflict*, EUR. Y.B. INT’L ECON. L. (forthcoming 2018) (for further discussion on the relationship between security exceptions and the circumstances precluding wrongfulness). *Lex specialis* is an interpretive maxim in international law which provides that whenever two or more

In 2017, the *Bear Creek Mining Corporation v. Republic of Peru* tribunal appeared to view a general exceptions provision, akin to Article XX GATT, as operating to justify otherwise unlawful conduct, referring to the exception being invoked to “justify” government conduct.²⁶ The tribunal in *Fireman’s Fund Insurance Company v. United Mexican States* in 2006 took the same approach in relation to an exception for prudential measures (“Nothing in this Part . . . shall be construed to prevent a Party from adopting or maintaining reasonable measures for prudential reasons.”)²⁷

2. Exception as Permission

Other tribunals and annulment committees have viewed the same or similar provisions as permissions that limit the scope of investment protections in the treaty.

The *CMS v. Argentina* annulment committee held in 2007 that where the U.S.-Argentina BIT security exception applied, the “substantive obligations under the Treaty do not apply,”²⁸ and in 2008, the *Continental Casualty Company v. Argentine Republic* tribunal held that this provision “reserved rights” of state parties under the treaty: where it applied, the substantive obligations would be “set[] aside or suspend[ed]” and measures coming within the exception would “lie outside the scope of the Treaty.”²⁹

Likewise, in 2016, the *Copper Mesa Mining Corporation v. Republic of Ecuador* tribunal, deciding a claim involving a general exception clause substantially similar to Article XX GATT, held that an expropriation would be proven, in part, by the “non-application” of the exception.³⁰ This interpretation suggests that the tribunal viewed the provision as limiting the scope of the treaty, in the sense that the claimant would have to prove that the impugned measure did not come within the scope of the treaty protections.

norms deal with the same subject matter, priority should be afforded to the more specific norm. See Dorota Marianna Banaszewska, *Lex specialis*, in MAX PLANCK ENCYCLOPAEDIA OF PUBLIC INTERNATIONAL LAW (Rüdiger Wolfrum ed., 2008).

²⁶ *Bear Creek Mining Corp. v. Republic of Peru*, ICSID Case No. ARB/14/21, Award, ¶ 475 (Nov. 30, 2017) [hereinafter *Bear Creek Award*].

²⁷ *Fireman’s Fund Ins. Co. v. United Mexican States*, ICSID Case No. ARB(AF)02/01, Award, ¶¶ 158, 168 (July 17, 2006); see North American Free Trade Agreement, Can.-Mex.-U.S., art. 1410, Dec. 17, 1992, 32 I.L.M. 289 [hereinafter NAFTA]; KURTZ, *supra* note 14, at 188–89.

²⁸ *CMS Gas Transmission Co. v. Argentine Republic*, ICSID Case No. ARB/01/08, Decision on Annulment, ¶ 129 (Sept. 25, 2007).

²⁹ *Continental Casualty Co. v. Argentine Republic*, ICSID Case No. ARB/03/9, Award, ¶¶ 164, 168 (Sept. 5, 2008).

³⁰ *Copper Mesa Mining Corp. v. Republic of Ecuador*, PCA No. 2012-2, Award, ¶ 6.58 (Mar. 15, 2016).

Tribunals in some sixteen decisions to date³¹ have interpreted carve-outs and reservations (for taxation, cultural industries, government procurement, and performance requirements) as permissions that exclude certain measures from the scope of the treaty obligations. The provisions in question variously state:

- “[T]he provisions of this Treaty . . . shall apply to matters of taxation only with respect to . . .”,³²
- “Except as otherwise provided in this Article, nothing in this Treaty shall create rights or impose obligations with respect to Taxation Measures of the Contracting Parties . . .”,³³
- “Except as set out in this Article, nothing in this Agreement shall apply to taxation measures”,³⁴
- “[A]ll matters relating to taxation . . . shall be excluded from this Treaty”,³⁵
- “The provisions of this Agreement shall not apply to taxation”,³⁶

³¹ As of September 11, 2018 (as far as the author is aware).

³² The Encouragement and Reciprocal Protection of Investment, U.S.-Ecuador, art. X(2), Aug. 27, 1993, S. TREATY DOC. 103-15 (1993) [hereinafter U.S.-Ecuador BIT]; U.S.-Argentina BIT, *supra* note 21, art. XII(2); *see* Treaty Concerning the Treatment and Protection of Investments, U.S.-Pan., art. XI(2), Oct. 27, 1982, S. TREATY DOC. 99-14 (1982), 21 I.L.M. 1227; Pan American Energy LLC v. Argentine Republic, ICSID Case No. ARB/03/13, Decision on Preliminary Objections, ¶¶ 135, 139 (July 27, 2006); El Paso Energy Int’l Co. v. Argentine Republic, ICSID ARB/03/15, Decision on Jurisdiction, ¶¶ 115–116 (Apr. 27, 2006). *But see* El Paso Energy, ICSID Case No. ARB/03/15, Award, ¶¶ 448–449 (hinting that the tribunal may have viewed the provision, like the security exception, as a defense).

³³ Energy Charter Treaty art. 21(1), Dec. 17, 1998, 2080 U.N.T.S. 95, 34 I.L.M. 360 [hereinafter ECT]; *see* Antaris Solar GmbH v. Czech Republic, PCA Case No. 2014-01, Award, ¶¶ 215–217 (May 2, 2018); Eiser Infrastructure Ltd. & Energia Solar Luxembourg S.á.r.l. v. Kingdom of Spain, ICSID Case No. ARB/13/36, Award, ¶ 270 (May 4, 2017); Hulley Enters. Ltd. (Cyprus) v. Russian Federation, PCA Case No. AA 226, Final Award, ¶¶ 1405, 1430, 1433 (July 18, 2014); Yukos Universal Ltd. (Isle of Man) v. Russian Federation, PCA Case No. AA 227, Final Award, ¶¶ 1405, 1430, 1433 (July 18, 2014); Veteran Petroleum Ltd. (Cyprus) v. Russian Federation, PCA Case No. AA 228, Final Award, ¶¶ 1405, 1430, 1433 (July 18, 2014); Plama Consortium Ltd. v. Republic of Bulgaria, ICSID Case No. ARB/03/24, Award, ¶ 266 (Aug. 27, 2008).

³⁴ Agreement for the Promotion and Reciprocal Protection of Investments, Can.-Ecuador, art. XII(1), Apr. 29, 1996, 2027 U.N.T.S. 196 [hereinafter Canada–Ecuador BIT 1996], <http://investmentpolicyhub.unctad.org/Download/TreatyFile/609> [<https://perma.cc/7WZN-55N2>]; NAFTA, *supra* note 27, art. 2103; *see* Resolute Forest Prod. Inc. v. Gov’t of Canada, PCA Case No. 2016-13, Decision on Jurisdiction and Admissibility, ¶ 328 (Jan. 30, 2018); Cargill, Inc. v. United Mexican States, ICSID Case No. ARB(AF)/05/2, Award, ¶ 297 (Sept. 18, 2009); Marvin Feldman v. Mexico ICSID Case No. ARB(AF)/99/1, Award, ¶ 141 (Dec. 16, 2002); EnCana Corp. v. Republic of Ecuador, LCIA UN3481, Award, ¶¶ 140–148 (Feb. 3, 2006) (London Ct. of Int’l Arb.).

³⁵ Treaty Concerning the Reciprocal Encouragement and Protection of Investments, Egypt-U.S., art. XI, Mar. 11, 1986, S. TREATY DOC. 99-24 (1986); *see* Ampal-American Israel Corp. v. Arab Republic of Egypt, ICSID Case No. ARB/12/11, Decision on Jurisdiction, ¶ 267 (Feb. 1, 2016).

- Certain obligations “do not apply to . . . procurement by a Party or a state enterprise . . . ”;³⁷
- The prohibition on performance requirements “do[es] not apply to . . . any existing non-conforming measure”;³⁸ and
- “[A]ny measure adopted or maintained with respect to cultural industries . . . shall be governed under this Agreement exclusively in accordance with the provisions of the *Canada-United States Free Trade Agreement*.”³⁹

As is evident from the wording of these provisions, by their typical stipulation that the treaty obligations do “not apply” in certain contexts, their intended effect is far more precise than Article XX GATT-type exceptions, by more clearly directing tribunals to construe these provisions as permissions.

B. The Relationship Between the Exception and the Substantive Treaty Obligations

In recent years, many tribunals have considered the purpose, subject-matter, design and application of a challenged measure in the context of determining the state’s compliance with the substantive obligations in the treaty. These are also considerations that are usually relevant in determining whether an exception would apply.⁴⁰ Because these factors are germane to both the threshold question of compliance with the substantive obligations in the treaty and to the question whether an exception is applicable, it is arguable that the presence of an exception can give rise to certain interpretive

³⁶ Agreement on the Promotion and Reciprocal Protection of Investments, Den.-Russ., art. 11(3), Dec. 11, 1993, <http://investmentpolicyhub.unctad.org/Download/TreatyFile/1028> [https://perma.cc/BYQ9-R2K7]; see *RosInvestCo UK Ltd. v. Russian Federation*, SCC Case No. V079/2005, Final Award, ¶¶ 618, 628 (Sept. 12, 2010).

³⁷ NAFTA, *supra* note 27, art. 1108(7)(a); see *Mesa Power Grp., LLC v. Gov’t of Canada*, UNCITRAL, PCA Case No. 2012-17, Award, ¶ 427 (Mar. 24, 2016); *United Parcel Serv. of Am. Inc. v. Gov’t of Canada*, UNCITRAL, ICSID Case No. UNCT/02/1, Award on the Merits, ¶ 127 (May 24, 2007) [hereinafter *UPS Award*]. *But see UPS Award, supra*, at Separate Statement of Arbitrator Cass, ¶ 133 (referring to the provision as an “affirmative defense[]”); *ADF Grp. v. United States of America*, ICSID Case No. ARB(AF)/00/1, Award, ¶ 170 (Jan. 9, 2003).

³⁸ NAFTA, *supra* note 27, art. 1108(1)(a); see *Mobil Invs. Canada & Murphy Oil Corp. v. Canada*, ICSID Case No. ARB(AF)/07/4, Decision on Liability and on Principles of Quantum, ¶¶ 247, 266 (May 22, 2012).

³⁹ NAFTA, *supra* note 27, Annex 2106; see *id.*, art. 2106. Article 2005 of the Canada-United States Free Trade Agreement (1987) provides: “Cultural industries are exempt from the provisions of this Agreement” See Free Trade Agreement, Can.-U.S., art. 2005, Dec. 22, 1987, 27 I.L.M. 281; *UPS Award, supra* note 37, ¶¶ 161–162, 167; *UPS Award, supra* note 37, at Separate Statement of Arbitrator Cass, ¶ 141.

⁴⁰ See, e.g., *Bilcon of Del., Inc. v. Gov’t of Canada*, PCA Case No. 2009-04, Award on Jurisdiction and Liability, ¶ 723 (Perm. Ct. Arb. 2015) [hereinafter *Bilcon Award*].

dilemmas that may, paradoxically, reduce states' regulatory space under investment treaties, depending on the character of the exception.

If an exception is treated as an affirmative defense, the principle of effectiveness in treaty interpretation would suggest that the challenged measure's objective should be considered only in the context of determining whether the exception applies, rather than in determining compliance with the substantive obligations—otherwise, the effect of the exception would be diminished or redundant.⁴¹ Arbitrators appear to have taken this approach in the *LG&E v. Argentina* and in *Bear Creek v. Peru* cases. In *LG&E v. Argentina*, the tribunal found Argentina in breach of fair and equitable treatment, but ultimately not liable due to successful invocation of the security exception.⁴² Although the analytical process undertaken by the tribunal is less than clear, the presence of the exception seemingly directed it to analyze the circumstances surrounding Argentina's actions (the emergency situation imperiling Argentine society) only as a question of justification, rather than in the context of determining compliance with fair and equitable treatment. In *Bear Creek v. Peru*, the tribunal suggested that the general exceptions provision (discussed above) and an annex clarifying states' police powers in the context of indirect expropriation⁴³ would both operate to justify otherwise unlawful conduct.⁴⁴ The tribunal, however, then went on to find that the presence of the general exception clause meant that “no other exceptions [e.g., police powers] from general international law or otherwise can be considered applicable in this case.”⁴⁵ That is to say, the tribunal held that the factors that would otherwise have been taken into account in the determination of whether a measure was an indirect expropriation or an exercise

⁴¹ See Bradly J. Condon, *Treaty Structure and Public Interest Regulation in International Economic Law*, 17 J. INT'L ECON. L. 333, 342–43 (2014) (noting that “the presence of general exceptions that explicitly address public interest regulation makes it inappropriate to address public interest regulation in general scope provisions or specific limitations on the scope of specific obligations” because doing so would “diminish” exceptions' impact and render them “redundant”); Céline Lévesque, *The Inclusion of GATT XX Exceptions in IIAs: A Potentially Risky Policy*, in PROSPECTS IN INTERNATIONAL INVESTMENT LAW & POLICY: WORLD TRADE FORUM 363, 366–67 (Roberto Echandi & Pierre Sauvé eds., 2013) (noting that the presence of an exception would narrow tribunals' approaches to the substantive obligations, as a broader approach like that currently taken by NAFTA tribunals in relation to national treatment run contrary to the principle of effectiveness).

⁴² *LG&E Award*, *supra* note 25, ¶¶ 132–139.

⁴³ Agreement for the Promotion and Protection of Investments, Can.-Peru, Annex 812.1(c), May 29, 2008, <http://international.gc.ca/trade-commerce/trade-agreements-accords-commerciaux/agr-acc/peru-perou/fta-ale/08.aspx?lang=eng> [<https://perma.cc/Q949-YVLZ>].

⁴⁴ See *Bear Creek Award*, *supra* note 26, ¶ 473.

⁴⁵ *Id.*

of police powers were only relevant insofar as they were embodied in the exception clause.

These cases highlight the problems that can arise from the inclusion of an exception clause in a treaty where the substantive investment protection obligations already permit an assessment of the circumstances of the measure's adoption and/or implementation. The *LG&E v. Argentina* decision can, in this respect, be contrasted with the *Total S.A. v. Argentine Republic* decision in 2010.⁴⁶ In *Total*, the tribunal found that the same measures did not breach fair and equitable treatment in the context of the France-Argentina BIT, which does not contain an exception.⁴⁷ Relatedly, the presence of exceptions in some treaties but not others may send a signal to tribunals that treaties without exceptions do not permit tribunals to examine whether a challenged measure is directed to promoting public welfare at all when determining whether a state has complied with its investment treaty obligations. Although this might sound a little far-fetched, the tribunal in *BG Group Plc. v. Republic of Argentina* in 2007 effectively refused to consider whether Argentina's emergency measures had a legitimate public welfare objective, on the basis that the U.K.-Argentina BIT contained no security exception.⁴⁸

C. Application of Exception May Restrict Regulatory Flexibility

When exceptions are interpreted as defenses, their effect may be to restrict, rather than enhance, states' regulatory flexibility.⁴⁹ Exceptions typically contain an exhaustive list of permissible objectives that, depending on how the provision is drafted, risks failing to keep pace with developments in governments' regulatory priorities. It has been argued that the general exceptions in the WTO agreements, for example, might not authorize the adoption of certain measures adopted to protect human rights or to deal with climate change.⁵⁰ In *Bear Creek*, the tribunal held that only the enumerated

⁴⁶ Compare *LG&E Award*, *supra* note 25, ¶¶ 132–139, with *Total S.A. v. Argentine Republic*, ICSID Case No. ARB/04/1, Decision on Liability ¶¶ 163–165, 309, 429 (Dec. 27, 2010) [hereinafter *Total Award*].

⁴⁷ *Total Award*, *supra* note 46, ¶¶ 163–165, 309, 429.

⁴⁸ *BG Group Plc. v. Republic of Argentina*, UNCITRAL, Final Award, ¶¶ 373, 385–387 (Dec. 24, 2007).

⁴⁹ See Lévesque, *supra* note 41, at 364 (arguing that the inclusion of exceptions in investment treaties creates the “risk that such provisions could reduce rather than improve” the regime’s balance “between investment protection and other public policy objectives”); Newcombe, *supra* note 2, at 278–81 (noting that the inclusion of exceptions in investment treaties “might have the unintended consequence of limiting the range of legitimate objectives available to the state”).

⁵⁰ Although a “public morals” exception may be sufficiently open-textured as to accommodate measures that do not come within one of the other exceptions: as a WTO panel remarked, the content of the concepts “public morals” and “public order” “can vary in time and space, depending upon a range of factors including prevailing social, cultural, ethical and religious values.” Panel

policy areas in the general exceptions clause would be relevant to defeat a *prima facie* claim of indirect expropriation.⁵¹ In doing so, the tribunal viewed the exception as subsuming the police powers doctrine, which does not limit permissible objectives (whether as a rule of customary law or as clarified in recent treaties). Likewise, when determining compliance with other substantive investment norms such as fair and equitable treatment and national treatment, tribunals can, in theory, consider an unlimited list of legitimate regulatory objectives.

For that matter, exceptions may well have a more stringent nexus requirement than investment tribunals have applied in the context of relevant substantive norm. For example, exceptions that require that government action be “necessary” to achieve the particular objective arguably demand a form of least restrictive means analysis that is akin to the WTO Appellate Body’s approach to the general exceptions in GATT and GATS (as the *Continental Casualty v. Argentina* tribunal held, extensively relying on WTO jurisprudence when determining the applicability of the security exception in the U.S.-Argentina BIT).⁵² By comparison, many investment tribunals have used a less rigorous test in determining whether fair and equitable treatment and national treatment have been complied with. These other decisions often require only a *rational* or *reasonable* connection between a non-discriminatory public welfare objective and the challenged measure.⁵³ Quarantining consideration of the nature of the challenged measure to the context of the exception (à la *LG&E v. Argentina*, for example) risks applying a more stringent legal test than would otherwise apply.

D. Narrow Interpretation of Exception and Strict Standard of Review

Another potential issue that arises when viewing an exception as a defense is the prospect that a tribunal might adopt a narrow construction of the exception based on the view that exceptions are derogations from the general rule(s) that ought to be given a restrictive interpretation. We see this

Report, *United States—Measures Affecting the Cross-Border Supply of Gambling and Betting Services*, ¶ 6.461, WT/DS285/R (adopted Nov. 10, 2004).

⁵¹ See *Bear Creek Award*, *supra* note 26, ¶ 473; *id.* at Partial Dissenting Opinion of Professor Phillippe Sands QC, ¶ 41.

⁵² *Cont’l Cas. Co. v. Argentine Republic*, ICSID Case No. ARB/03/9, Award, ¶¶ 181, 223 (Sept. 5, 2008). See generally, Andrew D. Mitchell & Caroline Henckels, *Variations on a Theme: Comparing the Concept of “Necessity” in International Investment Law and WTO Law*, 14 CHI. J. INT’L L. 93, 127 (2013) (examining investment tribunals and the WTO Appellate Body’s approaches to determining whether a measure is “necessary”).

⁵³ See CAROLINE HENCKELS, *PROPORTIONALITY & DEFERENCE IN INVESTOR-STATE ARBITRATION: BALANCING INVESTMENT PROTECTION & REGULATORY AUTONOMY* 115–22 (2015) (discussing various methods of review that tribunals have employed).

occurring in *Enron Corporation Ponderosa Assets L.P. v. Argentina Republic* and in *Sempra Energy International v. Argentine Republic*, where both tribunals stated that “the object and purpose of the Treaty is . . . [to apply] in situations of economic difficulty and hardship that require the protection of the internationally guaranteed rights of its beneficiaries . . . any interpretation, resulting in an escape route from the defined obligations cannot be easily reconciled with that object and purpose. Accordingly, a restrictive interpretation of any such alternative is mandatory.”⁵⁴ In 2006, in *Canfor Corporation v. United States*, the tribunal reviewed a number of exceptions in NAFTA (including reservations for existing non-conforming measures, a carve-out for government procurement, and exclusions from dispute settlement), holding that, as a general interpretive maxim, exceptions should “be interpreted narrowly.”⁵⁵

Viewing an exception as an affirmative defense might, alternatively, result in a tribunal affording less restraint in its scrutiny of a host state’s arguments defending its actions than it otherwise would. In other words, a tribunal might be tempted to employ a stricter standard of review than it would have applied in the context of determining compliance with a substantive obligation or viewing the exception as a permission. In 2007, in *UPS v. Canada*, for example, one of the arbitrators opined that in determining whether Canada had breached the national treatment obligation, “a more deferential—though certainly not a wholly deferential—review [is] in order” than determining whether an exception was made out; in this context, “I do not believe a similar deference is appropriate.”⁵⁶

III. GREATER PRECISION IN TREATY DRAFTING: IMPLICATIONS FOR EXCEPTIONS

A. Specific Obligations Versus Exceptions

Whether an exception to a rule is needed depends in part on the linguistic tools that are available to the rule-drafter.⁵⁷ A precisely drafted norm that is clear about the conduct that is and is not permitted might remove the

⁵⁴ *Sempra Award*, *supra* note 24, ¶ 373; *Enron Award*, *supra* note 23, ¶ 331. Nevertheless, as noted above, these tribunals conflated the exception with the defense of necessity at customary international law. Viewing these norms as separate might have led to a less narrow interpretation of the exception clause.

⁵⁵ *Canfor Corp. v. United States, Terminal Forest Prods. Ltd. v. United States*, UNCITRAL, Decision on Preliminary Question, ¶ 187 n.198 (June 6, 2006).

⁵⁶ *UPS Award*, *supra* note 37, at Separate Statement of Arbitrator Cass, ¶ 149; *see Noble Ventures, Inc. v. Romania*, ICSID Case No ARB/01/11, Award, ¶ 55 (Oct. 12, 2005).

⁵⁷ *See Schauer*, *supra* note 20, at 874–75 (describing the language limitations a rule-drafter faces).

need to have recourse to an exception. As such, it is arguable that the introduction of exceptions into new investment treaties creates uncertainty, and that a preferable approach would be for treaty parties to clarify the substantive obligations so as to better reflect a balance between regulatory freedom and investment protection.⁵⁸ This approach—embedding consideration of the purpose and tailoring of the challenged measure within the substantive obligation—is also preferable based on the normative considerations referred to above. The challenge is to draft a provision that is sufficiently precise, but not so rigid as to be unable to adapt to all possible contingencies.

In this regard, developments in treaty drafting that attempt to inject greater determinacy into the substantive obligations have taken place primarily in relation to fair and equitable treatment and indirect expropriation. In relation to fair and equitable treatment, following several early decisions that took extremely broad approaches to interpreting the obligation, in 2001 the North American Free Trade Agreement (NAFTA) parties adopted a binding interpretation of the fair and equitable treatment clause stating that it “prescribes” and does not require “treatment in addition to or beyond” the customary international law minimum standard of treatment of aliens.⁵⁹ This clarification has had some impact on NAFTA tribunals, which have generally accepted that the threshold for breach is a high one.⁶⁰ However, there is a lack of consensus concerning what the customary minimum standard of treatment actually requires of states in the regulatory context.⁶¹ As such, this clarification may not provide sufficient certainty as to the conduct that is permitted and proscribed.

The fair and equitable treatment (FET) clause in the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) attempts to address this issue, providing some limited references to the normative content of the obligation in relation to denials of justice, investors’ expectations, and subsidies and grants.⁶² Otherwise, the clause refers to the custom-

⁵⁸ See Newcombe, *supra* note 2, at 269 (arguing that “the better way forward is . . . through states clarifying the scope of investment obligations in their investment treaty practice”).

⁵⁹ NAFTA Free Trade Commission, Notes of Interpretation of Certain Chapter 11 Provisions (July 31, 2001). Article 1133(2) NAFTA provides that notes of interpretation issued by the NAFTA Free Trade Commission (comprising ministerial representatives of each party) are binding on arbitral tribunals. See NAFTA, *supra* note 27, art. 1132(2).

⁶⁰ Although certain cases, such as the recent *Bilcon v. Canada* decision, demonstrate that tribunals are not immune from taking an expansive approach to when a state will be in breach of the customary international law minimum standard. See *Bilcon Award*, *supra* note 40, ¶¶ 441–454.

⁶¹ See, e.g., ROLAND KLÄGER, ‘FAIR AND EQUITABLE TREATMENT’ IN INTERNATIONAL INVESTMENT LAW 48–61, 71–72, 75–76, 87–88 (2011) (discussing various understandings of the minimum standard treatment).

⁶² See Trans-Pacific Partnership Agreement, arts. 9.6 (2)(a), (4), (5), Feb. 4, 2016 (no longer in effect), <https://ustr.gov/trade-agreements/free-trade-agreements/trans-pacific-partnership/tpp->

ary international law minimum standard of treatment without further concretization. Another approach is taken in Comprehensive Economic and Trade Agreement (CETA), where the fair and equitable treatment clause states that a government breaches fair and equitable treatment only where it engages in certain specified conduct.⁶³ Some of the elements of the definition of FET permit consideration of both public and private interests and any legitimate public policy basis for the measure in the determination of breach (“fundamental breach of due process,” and, perhaps, “manifest arbitrariness”).⁶⁴ Other elements would seemingly not permit an exception to rescue the conduct, namely “targeted discrimination on manifestly wrongful grounds” and “abusive treatment.” What is clear is the parties’ intent that *bona fide* regulatory or administrative measures, adopted in order to promote public welfare, would not be captured within this definition. Arguably, this could have been spelled out more explicitly.⁶⁵

This attempt to more precisely define proscribed government action is relevant to the scope of the CETA’s general exceptions provision,⁶⁶ which does not apply to fair and equitable treatment or to expropriation,⁶⁷ suggesting that the parties’ preference was to clarify the substantive obligations rather than relying on exceptions to maintain regulatory flexibility. This approach is somewhat undermined by the fact that the exception clause applies to CETA’s investment chapter in relation to national treatment and most-favored nation treatment. Investment tribunals have almost invariably considered a government’s reasons for its actions in the context of determining whether a measure complies with national treatment, in circumstances where the treaty provision is silent as to the role of the regulatory purpose in the discrimination inquiry.⁶⁸ Providing an exception for the non-discrimination sug-

full-text [<https://perma.cc/3884-68WK>] [hereinafter TPP]. Article 1 of the Comprehensive and Progressive Agreement for Trans-Pacific Partnership incorporates the TPP by reference.

⁶³ CETA, *supra* note 11, art. 8.10(2).

⁶⁴ *See id.*, art. 8.10(2)(b)–(c) (providing that a breach of fair and equitable treatment includes a “fundamental breach of due process,” and “manifest arbitrariness”).

⁶⁵ *See generally* Caroline Henckels, *Protecting Regulatory Autonomy Through Greater Precision in Investment Treaties: The TPP, CETA, and TTIP*, 19 J. INT’L ECON. L. 27 (2016) (arguing for more precise terminology in treaties to limit arbitral discretion).

⁶⁶ *See* CETA, *supra* note 11, art. 28.3 (outlining the general exceptions to CETA).

⁶⁷ *See id.*, Annex 8-A (defining expropriation). CETA clarifies that “except in rare circumstances . . . non-discriminatory measures of a Party that are designed and applied to protect legitimate public welfare objectives, such as health, safety and the environment, do not constitute indirect expropriations.” *Id.*; *see also* TPP, *supra* note 62, Annex 9-B (stating that “[n]on-discriminatory regulatory actions by a Party that are designed and applied to protect legitimate public welfare objectives, such as public health, safety and the environment, do not constitute indirect expropriations . . .”).

⁶⁸ *See generally* Andrew D. Mitchell, David Heaton & Caroline Henckels, NON-DISCRIMINATION AND THE ROLE OF REGULATORY PURPOSE IN INTERNATIONAL TRADE AND

gests that the intention may be to jettison the body of decided cases in favor of justifying differential treatment under the exception provision. The parties could have provided more clarity in the national treatment clause itself as they have done for fair and equitable treatment and indirect expropriation. The drafters of the CPTPP, for instance, provided in an explanatory note that the question whether treatment has been accorded in like circumstances “depends on the totality of the circumstances, including whether the relevant treatment distinguishes between investors or investments on the basis of legitimate public welfare objectives” and noted that to avoid liability, any differential treatment must be plausibly or reasonably “connected to [a] legitimate public welfare objective[.]” and be applied in a non-discriminatory manner.⁶⁹ Again, these criteria appear to incorporate considerations relevant to an exception into the substantive obligation itself.

B. Do Precisely Defined Obligations Obviate the Need for Exceptions?

While it is difficult to see how a measure that failed to comply with CETA’s fair and equitable treatment provision (for example) could be saved by an exception, it is arguable that exceptions still have a role to play even where the substantive obligations are drafted with greater precision. Under current institutional arrangements for investor-state dispute settlement, which effectively preclude review of tribunal decisions attended by legal error, it would be overly optimistic to rely on arbitrators to “get it right” in every case. My analysis of WTO decisions dealing with Article XX GATT or Article XIV GATS demonstrate that forty-seven percent of panel findings concerning these provisions were fully or partially reversed on appeal.⁷⁰ This suggests that institutional reform could have a significant role to play in correcting erroneous interpretations of exceptions.

INVESTMENT LAW (2016) (analyzing the decided WTO and investment cases in terms of the role of regulatory purpose in the discrimination inquiry).

⁶⁹ TPP Drafters, *Drafters’ Note on Interpretation of “In Like Circumstances” Under Article 9.4 (National Treatment) and Article 9.5 (Most-Favoured-Nation Treatment)*, Nov. 5, 2015, <https://www.mfat.govt.nz/assets/Trans-Pacific-Partnership/Other-documents/Interpretation-of-In-Like-Circumstances.pdf> [<https://perma.cc/8Q5Y-ZVQ4>]; see also COMESA, *supra* note 10, art. 17(2) (stating that when determining whether a claimant’s investment and domestic investments are “in like circumstances” a tribunal should regard circumstances including the effects of the investment on third persons, the local community and the environment; the relevant sector; the “aim of the measure” and “the regulatory process generally applied in relation to the measure”).

⁷⁰ See TRADE LAW GUIDE (Oct. 15, 2017), <http://www.tradelawguide.com/index.asp?toc=content&id=88> [<https://perma.cc/U66Y-S9K3>] (source for the author’s analysis for finding the percentage of WTO decisions that dealt with Article XX GATT or Article XIV GATS that were fully or partially reversed on appeal).

There are many different ways of approaching the drafting of exceptions, and I will not address them in detail here. To begin, drafters need to have a clear idea of what they are trying to achieve. States could clarify that exceptions are to be understood as limiting the scope of investment obligations in the treaty and/or stipulate that the burden would rest with the claimant to establish that the measure did not comply with the exception, if this is what is intended.⁷¹ States ought to consider the likely longevity of permissible objectives and whether they would keep pace with developments in, for example, technology.⁷² The required nexus between a measure and permissible policy objectives is also an important consideration, as it effectively sets the desired level of protection of the objective (for example, an exception can require that a measure be “necessary” to achieve its objective, or a less strict nexus such as “related to”). The more lenient the nexus, the more it risks being circumvented by measures that are protectionist or otherwise hostile to foreign investors or investments. Language akin to the WTO general exceptions’ *chapeaux* (which prohibit arbitrary, discriminatory or other application of measures that undermines the treaty’s objectives) is one way of addressing these concerns.⁷³ An unresolved question is whether the incorporation by reference or the practice of transplanting WTO exceptions to investment treaties would enliven tribunals to follow WTO jurisprudence on these provisions.⁷⁴ Although the Appellate Body has, over the years, interpreted the general exceptions in a way that is sensitive to governments’ reg-

⁷¹ The question of which disputing party has (or should have) the burden of proving that the exception applies is an important practical consideration, as the default position in international adjudication is that the party making an assertion must prove that assertion. See generally Henckels, *supra* note 15 (providing a more detailed discussion on the burden of proof in relation to exceptions).

⁷² See, e.g., 2015 Norway Model Agreement for the Promotion and Protection of Investments, art. 24(v), <http://investmentpolicyhub.unctad.org/Download/TreatyFile/2873> [https://perma.cc/2UFY-TH2P] (including the phrase “for the protection of the environment” in the general exceptions). This appears to be broader than “the conservation of exhaustible natural resources” in Article XX(g) GATT. See GATT, *supra* note 13, art. XX(g). UNCTAD suggests exceptions should include the provision of “essential social services (e.g. health, education, water supply); the prevention of tax evasion; the protection of . . . cultural heritage . . . cultural diversity; and media diversity.” *World Investment Report 2015*, *supra* note 14, at 140–41.

⁷³ See, e.g., Agreement for the Promotion and Protection of Investments, Can.-Slovak., art. IX(1), July 20, 2010 (prohibiting “arbitrary or unjustifiable discrimination between investments or between investors, or a disguised restriction on international trade or investment”); Agreement for the Promotion and Protection of Investments, Can.-Romania, art. XVII(3), May 8, 2009; Agreement for the Promotion and Protection of Investments, Can.-Latvia, art. XVII(3), May 5, 2009 (prohibiting “measures . . . applied in a manner that would constitute arbitrary or unjustifiable discrimination”); ECT, *supra* note 33, art. 24(2) (prohibiting measures that constitute “a disguised restriction on Economic Activity in the Energy Sector, or arbitrary or unjustifiable discrimination between . . . [investors]”).

⁷⁴ KURTZ, *supra* note 14, at 198–99.

ulatory autonomy, it has also (problematically in my view) consistently interpreted these provisions as affirmative defenses and, as a result, generally quarantined examination of regulatory purpose to this context, rather than in the context of determining compliance with the relevant substantive obligation.

CONCLUSION

This Essay argues that there are good reasons to view exceptions (in their various manifestations) as permissions that limit the scope of the investment protections in the relevant treaty, rather than as defenses that are invoked to justify what would otherwise be unlawful conduct. Viewed as permissions, exceptions signal to adjudicators and to potential claimants that states retain regulatory capacity in the areas covered by the provision and take regulatory purpose as central to the question of breach. The analysis of decided cases involving exceptions in this Essay shows that investment adjudicators have not thoroughly considered this crucial issue. This is evidenced by their frequently terse and impressionistic reasoning regarding the purpose and effect of exceptions.

Exceptions are one of a number of tools available to drafters. Given the stark lack of unanimity among tribunals concerning their analytic character and their relationship with the treaty's investment protections, a continuation of current drafting approaches may, problematically, signal to tribunals that the regulatory purpose of a challenged measure should be quarantined to the context of determining whether the exception applies once a *prima facie* breach of investment obligations has been established. This approach also creates the risk that tribunals will adopt a narrow interpretation of the exception or apply a stricter standard of review than it would otherwise have applied in considering a state's reasons for its actions.

If we are to accept the orthodox view that the purpose of the investment regime is to engender sustainable economic development, it follows that investment protection should be viewed as a means to that end, to be balanced with governmental autonomy to pursue other welfare-enhancing objectives, such as protection of health and the environment. Viewing laws and other government actions taken to promote public welfare as *exceptional*, rather than something that takes place in the ordinary course of governance, undermines this objective. Moreover, exceptions may not be the most effective way to shield *bona fide* public welfare measures from liability. It may be preferable to frame the substantive obligations in such a way as to provide greater clarity about the types of government action that are permitted and proscribed. Still, at least as long as current institutional arrangements for investor-state dispute settlement persist, exceptions may be an

important failsafe against erroneous interpretations of the substantive obligations.

Reading exceptions in their various forms across the body of investment treaties leaves one with the impression that the reasons for including particular exceptions and the form and coverage that these provisions take has not been well thought out. Rather than simply copy-pasting exceptions from previous investment and/or trade agreements, governments would do well to devote fuller consideration to the reasons why particular types or categories of measures ought to be shielded from liability under the regime, and the most fitting mechanism or mechanisms to achieve this purpose.