DEPARTAMENTO ACADÉMICO DE DERECHO
Av. Universitaria N° 1801, San Miguel, Lima, Perú
Teléfono: (511) 626-2000 anexos 4930 y 4901
Pontificia Universidad Católica del Perú
http://www.pucp.edu.pe/departamento/derecho/

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AUTORES
Noemí Cecilia Ancí Paredes
Mónica Barriga Pérez
Frank Roger Espinoza Laureano
Carlos Glave Mávila
Anthony Lizárraga Vera-Portocarrero
Álvaro Antonio Ocampo Grey
Richard André O'diana Rocca
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Alejandra Fiorella Zegarra Blanco

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THE ROLE OF INTERNATIONAL ENVIRONMENTAL LAW IN THE APPLICATION OF FOREIGN INVESTMENT LAW

Carlos Glave Mávila
Profesor del Departamento Académico de Derecho, PUCP*

Categoría Profesores

International Environmental Law (hereinafter, IEL) is entwined with other areas because environmental disputes are never raised in isolation of other legal fields. However, Foreign Investment Law (hereinafter, FIL) is recognized as one of the most reluctant areas when it comes to applying rules of IEL. As a consequence, it is important to remark the relevance of taking into account rules of IEL in investment disputes. In that sense, the aim of this paper is to highlight a progression in the relationship between FIL and IEL through the reasoning of decisions taken in investment arbitrations specifically dealing with expropriations. Consequently, some relevant investment arbitration awards that dealt with environmental concerns will be analyzed so as to recognize three stages of evolution. A complete lack of integration where the rules of IEL are not taken into account even though the parties have alleged them is the first period. Then, the application of concepts imported from human rights courts is the demonstration of a second phase. After that, a few more sophisticated approaches will be explained as examples of the connection between these fields of law and, finally, examples of cases where the protection of the environment is the key element of an investment dispute will be presented so as to remark that there is still a continuous evolution in progress.

1. Introduction

The aim of this paper is to highlight a progression in the relationship between IEL and FIL so as to encourage the need of achieving a balance between them. In particular, the progress will be explained through the decisions taken in investment arbitration proceedings that dealt with environmental concerns.

For the purpose of this paper, even though IEL is understood as part of international law as a whole, there is a problem if the role of international law is emphasized. International law has been basically oriented toward the freedom of states without taking into account the protection of the environment. Hence, a body of law specifically aimed at protection of the environment has been developed, and IEL is nothing else than the application of public and private international law to environmental problems.[1]

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* http://www.pucp.edu.pe/profesor/carlos-glave-mavila

1 Patricia Birnie et al., International Law & the Environment (OUP, 3rd edition, 2009) 4.

Some different forms of linking IEL with FIL will be explained. For instance, the role of the private sector in addressing environmental concerns or the fact that there are more investment treaties containing environmental regulations will be suggested as examples of the approximation between these fields of law. However, the focus of this paper will be on the case law given the fact that in recent years there are also a growing number of investment disputes with elements related to the protection of the environment. Specifically, this paper is concerned with expropriation disputes.

Sands[2] argues that usually arbitrators do not take into account rules of IEL. Although to some extent it is true, this paper will demonstrate that there is an evolution that deserves to be remarked upon.

This paper identifies four stages of this evolution. The most notable investment arbitration awards that have addressed environmental issues for the first time are the ones rendered in the Santa Elena case[3] and Metalclad case[4]. Precisely, those are the cases taken by Sands[5] as examples of the lack of integration between FIL and IEL. These cases will be described as the model of the first trend.

An interesting approach will be presented through the analysis of the Tecmed case.[6] The award rendered in this case reveals a connection between these fields of law because a concept imported from the European Human Right Courts is applied in an investment dispute.

A more sophisticated approach will be presented as the third stage in the analysis of Methanex[7] and Chemtura[8]. The former case deals with the concept of substantial deprivation of an investment as a requirement for a measure to be considered an expropriation. The latter deals with the police power doctrine to justify a regulatory measure taken by a government to protect the environment. Hence, these cases are examples of the connection that the case law is building between FIL and IEL.

Finally, as part of the evolution of this connection, two cases that are still pending to be solved will be presented. Chevron[9] and Renco[10] will be explained as examples of the final stage where the environmental considerations are not only necessarily taken into account, but also the key element of the dispute.

Consequently, this paper will demonstrate that the case law is evolving in order to connect these fields of law. The reason, as Tanzi highlights,[11] is because under international law the host state is required at the same time to protect the foreign investment and the environment.

2 Philippe Sands, 'Litigating Environmental Disputes: Courts, Tribunals and the Progressive Development of International Environmental Law' (Global Forum on International Investment VII on International Investment, March 2008) <http://www.oecd.org/investment/globalforum/40311090.pdf> accessed 10 April 2014.

3 Compañía del Desarrollo de Santa Elena S.A. v. The Republic of Costa Rica. ICSID Case No. ARB/96/1 (2000).

4 Metalclad Corporation v. The United Mexican States. ICSID Case No. ARB(AF)/97/1 (2000).

5 Sands (n 2).

6 Técnicas Medioambientales Tecmed S.A. v. The United Mexican States. ICSID Case No. ARB(AF)/00/2 (2003).

7 Methanex Corporation v. United States of America. Final Award on Jurisdiction and Merits, (2005) 44 ILM 1345, Inside US Trade, 19 August 2005, 12, IIC 167 (2005), 3rd August 2005, Ad Hoc Tribunal (UNCITRAL).

8 Chemtura Corporation v. Canada, Award, IIC 451 (2010), 2nd August 2010, Ad Hoc Tribunal (UNCITRAL).

9 Chevron Corporation and Texaco Petroleum Corporation v. The Republic of Ecuador. UNCITRAL, PCA Case No. 2009–23.

10 The Renco Group Inc. v. Republic of Peru. ICSID Case No. UNCT/13/1.

11 Atila Tanzi, 'Reducing the Gap between International Investment Law and Human Rights Law in International Investment Arbitration?' (2013) 1 Latin American Journal of International Trade Law 299.

2. A Theoretical Outline of the Relationship between FIL and IEL

2.1. The importance of foreign investment.

Since the adoption of the first Bilateral Investment Treaty (hereinafter, BIT) in 1959, the world has witnessed a continuous increase in their number.[12] Only at the end of 2008 there were 2,676 BITs around the world.[13]

The number of countries involved in the celebration of BITs has also steadily increased.[14] Currently, according to the International Centre for the Settlement of Investment Disputes Database of BITs,[15] 177 countries are parts of, at least, one BIT. In addition, it is confirmed that a higher number of BITs generates an increase in the foreign direct investments that flow to a country.[16]

The general approach of BITs is followed by multilateral agreements with the aim of promoting and protecting foreign investment. The North America Free Trade Agreement and the 1994 Energy Charter Treaty are examples of multilateral agreements with the aim of protecting foreign investors.

National laws may not provide higher standards of protection for investments. Hence, the basic aim of every foreign investment treaty is to provide an additional protection to the right of foreign investors. This could be achieved by prohibiting[17] acts or measures that expropriate or interfere with the investment and acts or measures which are supposed to be an unfair treatment.

Whereas these prohibitions imply a limitation in the sovereignty of the host state to regulate the activities performed in its own territory, it also attracts foreign investments. It has a significant importance in the economic growth and it is reflected in the number of BITs and multilateral investment agreements. Each investment treaty establishes its own provisions, but the general aim is to provide an additional protection to the foreign investor property rights. The protection of the environment is not a goal and could lead to some tensions. However, this relation can and must be balanced.

Jorge Viñuales[18] argues that the relationship between IEL and FIL has been changing since the 1960s. This author identifies three indicators or signs to explain this. Firstly, the role of the private sector in relation to the protection of the environment has moved from marginal to central. Secondly, the growing number of investment treaties with environmental considerations. Finally, an increasing number of investment disputes with environmental elements.

12 United Nations Conference on Trade and Development, 'Bilateral Investment Treaties 1959 – 1999' (United Nations New York and Geneva, 2000) 1 <http://unctad.org/en/Docs/poiteiiad2.en.pdf> accessed 26th May 2014.

13 United Nations Conference on Trade and Development, 'Recent Developments in International Investments Agreements (2008 – June 2009)' (United Nations New York and Geneva, 2009) 2 <www.unctad.org/en/docs/webdiaeia20098_en.pdf> accessed 26th May 2014.

14 UNCTAD (n 12) 4.

15 International Centre for the Settlement of Investment Disputes Database of Bilateral Investment Treaties <https://icsid.worldbank.org/ICSID/FrontServlet> accessed 27th May 2014.

16 Eric Neumayer and Laura Spess, 'Do bilateral investment treaties increase foreign direct investment to developing countries?' (London School of Economics Research Online, 2005) <http://eprints.lse.ac.uk/627/1/World_Dev_(BITs).pdf> accessed 27th May 2014.

17 Philippe Sands and others, Principles of IEL (3rd edn, CUP 2013) 871.

18 Jorge Viñuales, Foreign Investment and the Environment in International Law (CUP 2012) 9.

2.2. The role of the private sector.

The need to integrate environment and development has always been the task of IEL. The Stockholm Conference emphasizes the protection of the environment as a priority, and Viñuales[19] holds that the tension between development and environment has influenced the evolution of IEL since that moment.

A relevant point in the history of IEL is the 1992 Rio Conference where the concept of sustainable development appeared in the worldwide scene. However,[20] currently this concept could not be considered a useful instrument to solve the tension between economic development and the protection of the environment. It is perceived as a[21] "multilevel concept, with different meanings at different levels."

Then it could be appreciated that a more recent provision that sheds some light on this issue is the 2002 World Summit on Sustainable Development (WSSD) Plan of Implementation.[22] This provision requires countries to facilitate foreign direct investment with the aim of encouraging sustainable development. It means that foreign direct investment is thought of as an instrument for sustainable development. Hence,[23] there are legal instruments that connect the private sector with the protection of the environment like private-public partnerships, environmental project finance and market mechanisms such as the flexible mechanisms created by the Kyoto Protocol.

Tienhaara[24] refers to the "race to the top" when it comes to environmental performance of foreign direct investments. This author explains that a foreign investor usually deals with two decisions. A foreign investor must decide what kind of technologies will be implemented in the host state and the environmental standards that will apply.

Those decisions could have a great and long term impact on the environmental management of the host state. However, Tienhaara[25] points out that empirical evidence seems to be mixed. From that conclusion it could be appreciated that the role of foreign investment is already playing a central role even though there is still much more to be done.

In conclusion, it is clear that the private sector has been getting involved in the protection of the environment. In addition, it seems that this trend will be more intense in the future. Consequently, the role of private actors in the evolution of economic activities suggests that the apparent separate relationship between FIL and IEL could find the balance required to satisfy both interests.

2.3. An increasing number of investment treaties with environmental considerations.

Although environmental protection is not the main objective of an investment treaty, since the 1990s the number of investment treaties with environmental considerations has significantly increased. In accordance to a report[26] published by the Organisation for the Cooperation and Development (OECD),

19 Ibíd 11.

20 Ibíd 11 – 12.

21 Viñuales (n 18) 12 citing Andrew Dopson, Fairness and Futurity: Essays on Environmental Sustainability and Social Justice (OUP 1999) 23.

22 United Nations, 'Report of the World Summit on Sustainable Development' (Johannesburg, August 2002) <http://www.un.org/jsummit/html/documents/summit_docs/131302_wssd_report_reissued.pdf> accessed 27th May 2014.

23 Viñuales (n 18) 12 – 13.

24 Kyla Tienhaara, The Expropriation of Environmental Governance. Protecting Foreign Investors at the Expense of Public Policy (CUP 2009) 26.

25 Ibíd 26 – 27.

26 Viñuales (n 18) 14 citing K. Gordon and J. Pohl, 'Environmental Concerns in International Investment Agreements:

there is a clear contrast between investment and free trade agreements concluded before the 1990s and the ones concluded afterwards, especially from 2002 onwards. The report also shows that 89% of the new investment treaties concluded in 2008 have references to environmental considerations.

In the same sense, Schommer[27] states that environmental issues brought into spheres where it was historically precluded is an example of a positive evolution in the past fifteen years of bilateral and multilateral trade agreements.

Viñuales[28] argues that the clear contrast between earlier and recent investment treaties reflects that interactions between FIL and IEL are growing. However, concerning merely the environmental considerations in investment treaties, there is a long way to go through in order to reach a real balance between these fields.

It is important to analyze the content of those environmental provisions so as to realize that this relationship is still in progress. The OECD Report[29] of 2011 recognizes seven different types of environmental provisions in investment treaties:

(a) General language in preambles that mentions environmental concerns and establishes protection of the environment as a concern of the parties of the treaty.
(b) Reserving policy space for environmental regulation.
(c) Reserving policy space for environmental regulation for more specific, limited subject matters (performance requirements and national treatment).
(d) Provisions that clarify the understanding of the parties that non-discriminatory environmental regulation does not constitute "indirect expropriation."
(e) Provisions that discourage the loosening of environmental regulation for the purpose of attracting investment.
(f) Provisions related to the recourse to environmental experts by arbitration tribunals.
(g) Provisions that encourage and strengthen environmental regulation and cooperation.

The second is the most common of all the environmental provisions in investment treaties[30] with 62 per cent of the cases. This suggests that there is an increasing consideration of environmental concerns in investment treaties, although the approach is basically focused on broad definitions or even "to some extent uncertain clauses."[31]

One example is NAFTA. Article 1005(1) of this treaty stipulates that "Each Party shall accord to investment of investors of another Party treatment in accordance with international law, including fair and equitable treatment and full protection and security". The title of this article is "Minimum Standard of Treaty" and it is clearly related to the "fair" protection that a foreign investment shall receive from the host country. Furthermore, NAFTA article 1110, called "expropriation and compensation," provides that it is not allowed to nationalize or expropriate a foreign investment, except for a public purpose, on a non-discriminatory basis, in accordance with due process, and on payment of compensation.

A survey' OECD Working Papers on International Investment No. 2011/1 (OECD Report 2011) 8.

27 Hena Schommer, 'Environmental Standards in U.S. Free Trade Agreements: Lessons from Chapter 11' Sustainable Development Law & Policy, Fall 2007, 36, 84. <digitalcommons.wcl.american.edu/cgi/viewcontent.cgi?article=1153&context=sdlp> accessed 15th August 2015.

28 Viñuales (n 18) 14.

29 K. Gordon and J. Pohl (n 26) 15 – 16.

30 Viñuales (n 18) 16.

31 Ibíd 16.

NAFTA articles 1005 and 1110 are part of the chapter 11 section A titled "Investment." The last article of this section is article 1114, which stipulates that nothing in that chapter shall be construed to prevent a party from adopting, maintaining or enforcing any measure considered appropriate to ensure that investment activity is carried out in an environmentally sensitive manner. Moreover, this article states that parties shall not consider appropriate the encouragement of investment by relaxing domestic health, safety or environmental measures. It means that a party should not derogate any national measure, or offer its derogation, in order to attract or maintain foreign investments.

Sands argues[32] that the language used in NAFTA suggests that there is a hierarchy between article 1005 and 1110 in relation to environmental protection measures. It could be noticed because article 1110 provides, in a restricted sense, the requirements to nationalize or expropriate an investment; whereas, article 1114 refers to environmental measures in a more relaxed orientation.

According to Sands,[33] there is a similar approach in the Energy Charter Treaty of 1994. Article 10(1) refers to equitable, favorable and transparent conditions for investors and that an investment shall not be subject of any kind of unreasonable or discriminatory measures. Furthermore, if a contracting state decides to nationalize or expropriate a foreign investment, article 13(1) sets forth the same requirements provided in NAFTA.

Another example of environmental regulations in investment agreements is the USA-Peru Trade Promotion Agreement where there is a chapter exclusively dedicated to the protection of the environment. Furthermore, there is also a chapter focused on investment where the exceptions to allow an expropriation are basically the same as in NAFTA (for public purpose, in a non discriminatory manner, on payment of compensation and in accordance to due process of law). However, it is interesting that annex 10-B defines what is understood by 'expropriation' and that it specifies that a non-discriminatory action is not considered an indirect expropriation if it is designed and applied to protect legitimate public welfare objectives, such as the environment. Precisely, this annex is specifically referenced in the section where it is stipulated that a public purpose is an exception when an expropriation may be accepted.

To sum up, in general terms investment treaties regulate broad or vague environmental obligations. A state party shall adopt an appropriate measure to ensure that an investment is being carried out in an environmentally friendly manner. Also, a state party should not attract or maintain an investment through the derogation, or offer of derogation, of an environmental protective measure. On the other hand, the obligations destined to protect foreign investment properties are clear and strict. A state party cannot nationalize or expropriate an investment unless four conditions are met. This is an example of the most common approach taken by investment treaties when it comes to include environmental clauses, precisely what Viñuales[34] highlights about the OECD report.

Finally, it is interesting that since 1995 there have been some negotiations in order to agree on a worldwide Multilateral Agreement on Investment. According to Sands,[35] by 1998 there was considerable agreement on the rules relating to investment protection and the settlement of

32 Sands, Principles of IEL (n 17) 872.
33 Ibíd 873.
34 Viñuales (n 18) 16 – 17.
35 Sands, Principles of IEL (n 17) 874.

disputes. However, this author highlights[36] that negotiations were not successful in agreeing on the terms of the relation between the not expropriate or not investment interference obligation with the maintenance, adoption and enforcement of national rules concerned with the protection of the environment. Finally, by 1998 negotiations did not reach an agreement.[37]

This clearly suggests that the relation between FIL and IEL is complex. Nevertheless, the facts reveal that investment treaties are increasingly including environmental provisions. This is considerably relevant so as to achieve a balance when there is a dispute concerned with the interests protected by these fields of law. Although the most common approach taken by these environmental provisions does not provide a detailed environmental protection, the environmental provisions are already playing a significant role in the case law.

2.4. A growing number of investment disputes with elements concerning the protection of the environment.

Another factor is the growing number of investment disputes with elements related to the protection of the environment. This is not an easy task because a dispute could not be easily qualified as an environmental one as long as environmental considerations are never raised in isolation from other fields of law.

As a result, it is better to refer to a case with elements related to the protection of the environment.[38] Hence, it is possible to evaluate the types of investment disputes with these elements. Viñuales[39] has concluded that there is evidence that confirms that the number of investment disputes dealing with environmental considerations has increased in the last two decades.

This author[40] has located only one investment dispute with elements related to the protection of the environment decided before 1990, and three more decided during the 1990s. Apart from those four investment disputes, all of the other investment disputes with environmental considerations have been decided from the year 2000 onwards. In the period between 2000 and 2011, twenty-four investment disputes dealing with environmental elements were decided.[41]

In addition, it is interesting that the types of disputes are not basically concerned with first generation environmental issues such as pollution or the protection of species. Investment disputes are increasingly dealing with second-generation environmental issues like climate change or the production of electricity from renewable sources. Viñuales argues that this kind of investment case law suggests that the relationship between these fields is evolving.

In conclusion, there is sufficient evidence to argue that environmental law is playing a role in the foreign direct investment field. The trend suggests that this role is evolving so as to achieve a balance. Having mentioned that, the aim of this paper will be to demonstrate this evidence with the analysis of some specific investment disputes.

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36 Ibíd 875.

37 According to Philippe Sands, in 2001 the issue was addressed again by the Doha WTO Ministerial Declaration. These negotiations were established with the vision of reaching an agreement by January 2005, but it failed again. However, this author suggests that it is possible that environmental concerns may appear again in the context of WTO negotiations with the aim of agreeing on a Multilateral Investment Agreement. Sands Principles of IEL (n 17) 876.

38 Sands, 'Litigating Environmental Disputes: Courts, Tribunals and the Progressive Development of International Environmental Law' (n 2).

39 Viñuales (n 18) 17 – 23.

40 Ibíd 17 – 18.

41 Some of them were solved in different ways such as settlement or discontinuance. Ibíd 18.

3. The Focus of the Analysis on Cases Dealing with Alleged Foreign Investment Expropriation Measures

From the first chapter, it is clear that IEL is progressively getting entwined with FIL. To exemplify that, the analysis will be focused on the evolution of the investment disputes decisions dealing with expropriations.

Investment disputes dealing with expropriation measures and concerning the protection of the environment is one of the particular areas where the balance between these fields is reaching maturity.[42] Because of that reason, the focus of this paper will be on this particular kind of investment disputes. Nevertheless, before analysing the case law that has marked this evolution, some concepts of investment property expropriation must be mentioned.

Investment treaties and the case law show that a distinction between direct expropriation and indirect expropriation is widely recognized. The former supposes an immediate transfer of the property in favour of the host state, and the latter does not imply any transfer of property.

A decision made in an investment dispute dealing with a direct expropriation usually should decide whether the measure was valid or not. In other words, the discussion would be focused on the lawfulness or unlawfulness of the expropriation decision. A good example is whether the decision is based on an authentic public purpose, environmental reasons or not.

However, besides the validity of the measure, the environmental discussion could have a relevant impact on one consequence of the expropriation. The amount of compensation deserved by the foreign investor affected with this measure is what an arbitral tribunal could decide in a direct expropriation investment dispute dealing with environmental concerns. This determination has been the focus of widely known investment arbitrations.[43]

On the other hand, an indirect expropriation measure is classified in two different ways. Firstly, a regulatory expropriation means a measure of general application with the consequence of depriving the value of the private property. As a form of indirect expropriation, the property is not transferred. The only consequence is the deprivation of its value due to a measure of general application. In principle,[44] a general regulation should not be considered as an expropriation given the fact that it is recognized that states have the sovereign power of adopting general regulations.

Sornarajah[45] also confirms that idea. This author explains that the law has always recognized the category of regulatory measures such as taxation, export controls or the creation of regimes in areas like antitrust, consumer protection, securities and environmental protection. According to this author,[46] it is recognized that the interference of these measures is not identified as a compensable expropriation where public harm has already resulted or is anticipated. This is confirmed in the evolution of the investment case law that will be presented.

The second type of indirect expropriation is a targeted measure. There is not a transfer of property, but in this case the measure is not of general application. The measure is individually focused on the foreign investment property. According to Viñuales,[47] case law suggests that

42 Viñuales (n 18) 294.
43 One notable example is the Santa Elena case that will be analyzed.
44 Viñuales (n 18) 298, 305.
45 Muthucumaraswamy Sornarajah, The International Law on Foreign Investment (3rd edn, CUP 2010) 374.
46 Ibíd 374.
47 Viñuales (n 18) 297.

whilst in general terms regulatory measures are not considered tantamount to expropriation, targeted measures are. When a public harm has already occurred or is anticipated, a regulatory measure is necessary and is easier to justify that it is not an act of compensable expropriation. On the other hand, it is more difficult to support the legitimacy of a targeted measure on public policy grounds or necessity. However, the progressive approach between investment and environmental law in the case law indicates that it is possible.

Sornarajah[48] has evaluated the concept of property in the context of foreign investment expropriation. The different forms of takings or expropriations have been grouped by this author as follows: (1) forced sales of products; (2) forced sales of shares in an investment through a corporate vehicle; (3) indigenisation measures; (4) taking over management control of the investment; (5) inducing others to take over the property physically; (6) failure to provide protection when there is interference with the property of the foreign investor; (7) administrative decisions which cancel licences and permits necessary for the foreign business to function within the state; (8) exorbitant taxation; (9) expulsion of the foreign investor contrary to international law; (10) acts of harassment such as the freezing of bank accounts or promoting strikes, lockouts and labour shortages.

Viñuales[49] argues that in that classification only taxation could be identified as a regulatory measure. All of the other forms of property takings are targeted measures. This confirms that targeted measures are more likely to be considered as compensable expropriations than regulatory measures. Some other reasons presented by Viñuales[50] to hold this idea are that the effects of targeted measures are similar to the ones of direct expropriations. Moreover, it is more difficult to use defences based on the power of the state such as emergency and necessity clauses to support targeted measures. The investment case law nevertheless suggests that targeted measures could also be taken as part of the policy powers of a state.[51]

4. A First Trend in the Case Law: a Complete Separation

As we mentioned, there are only four identified investment disputes dealing with environmental concerns concluded in the 1990s. Then the number increased since the year 2000. Two awards rendered in the year 2000 are the ones identified as the cases that have marked the beginning of environmental considerations in investment disputes. These are the awards rendered in Compañia del Desarrollo de Santa Elena S.A. v. Republic of Costa Rica (ICSID Case ARB/96/1) and Metalclad Corporation v. United Mexican States (ICSID Case ARB (AF)/97/1).

4.1. *Compañia del Desarrollo de Santa Elena S.A. v. Republic of Costa Rica* (ICSID Case ARB/96/1).

4.1.1. The origins and characteristics of the dispute.

On June 2nd, 1995, Compañia del Desarrollo de Santa Elena (hereinafter, Santa Elena or the claimant) submitted a request for arbitration to ICSID to determine the valuation of the compensation owed to the claimant by the Republic of Costa Rica (hereinafter, Costa Rica or the respondent). The award was rendered on February 17th, 2000.

48 Sornarajah (n 45) 375.
49 Viñuales (n 18) 297.
50 Ibíd 298.
51 The Chemtura case is the example that will be presented to demonstrate it.

Santa Elena was a Costa Rican corporation, and most of its stakeholders were citizens of the United States of America[52] (hereinafter, USA), and since 1973 it owned a property located in the Guanacaste Province of Costa Rica.

On May 5th, 1978, the government of Costa Rica issued a decree expropriating Santa Elena. The reason provided in the decree is that Santa Rosa National Park, which is adjacent to the property of Santa Elena, was insufficient to maintain the population of some special animals. Thus, a substantial area was needed to be added to the National Park for conservational requirements.

In the decree it was explained that the purpose of the government had been previously communicated to Santa Elena and that the president of the company did agree with the expropriation, but he expressed his disagreement with the price offered as compensation. According to Santa Elena, in that moment the price of the property was approximately US$ 6.4 million. Although the government acknowledged this disagreement, the decree was issued and the property expropriated. The price ordered to be paid in the decree as compensation was 16'450,000 colones.[53]

It should be highlighted that, to some extent, Costa Rica suffered a different form of pressure by Santa Elena.[54] In 1994, USA issued an enactment known as the Helms Enactment. The award recognized that, in application of this enactment, a USA US$ 175'000,000 Inter-American Development Bank loan destined to Costa Rica was delayed until Costa Rica consented the dispute to international arbitration. Regarding the discussion on the merits, the Helms Enactment is important because Costa Rica relied on it to argue that the parties had an agreement on the applicable law.

Although there were some discussions between the parties about the ICSID jurisdictional requirements,[55] then both parties consented to the arbitration without conditions, and the award strictly focused on the merits. As it could be noticed, the measure of the expropriation was not discussed. The only disagreement was on the value of the compensation owed to Santa Elena.

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52 Charles N. Brower and Jarrod Wong, 'General Valuation Principles: The Case of Santa Elena' in Todd Weiler (ed), International Investment Law and Arbitration: Leading Cases from the ICSID, NAFTA, Bilateral Treaties and Customary International Law (Cameron May 2005) 748.

53 This amount was approximately US$ 1.9 million in accordance to the then-current exchange. Ibíd 750.

54 The conflict took so long because in the following years Santa Elena retained the possession, and the parties were involved in unsuccessful negotiations. In 1987 the government of Costa Rica issued a second degree that expanded the area of Santa Rosa National Park and thus incorporated Santa Elena as part of this National Park. It was done because in accordance to Costa Rican law, if an expropriated land has not been used for its purpose for ten years, the expropriated owners can claim for the return of the property. Then, Costa Rica commenced judicial proceedings before their national courts in order to determine the value of the compensation. On the other hand, Santa Elena brought two claims before Costa Rican national courts. One sought the annulment of the 1978 decree, and the second attacked the 1987 decree arguing that it was an indirect expropriation. The effect of the proceedings initiated by Santa Elena was that the one initiated by Costa Rica was suspended. The Costa Rican Supreme Court rejected the claims brought by Santa Elena. Thus, the judicial proceeding initiated by the state was reactivated in September 1992. In that moment, the parties reassumed negotiations, but again they did not reach an agreement. By that time, a third valuation of the property was made by Costa Rica fixing the property at approximately US$ 4.4 million. Charles N. Brower and Jarrod Wong, Ibíd 754 – 757.

55 The questions around the jurisdiction arose because it was not clear if Santa Elena had always been owned by a majority of 50% USA citizens. Had it not been the case, the USA rule known as 'Helms Enactment' would have not been applicable to the case. However, Costa Rica never made an objection to the jurisdiction of the tribunal. For a full description of this issue review Charles N. Brower and Jarrod Wong, Ibíd 754 – 757.

This case is concerned with a direct expropriation. The 1978 decree directly expropriated the foreign investor property, and the discussion was not focused on the legitimacy or validity of that measure but on the value of the compensation. Regarding this paper, the question was whether or not environmental concerns related to the expropriation could play a role when it comes to determining the value of the compensation.

4.1.2. The parties' allegations and the decision.

The only relevant issue brought before the arbitrators was the amount of the compensation. To address this issue, it was relevant for the tribunal to determine the applicable law. Article 42(1) of the ICSID Convention had to be applied. According to this article, arbitrators shall apply the rules agreed to by the parties. Only if there is not an agreement, the tribunal shall apply the rules of the contracting state party to the dispute, and the rules of international law as may be applicable.

Santa Elena held that the parties did not have an agreement on the applicable law. Hence, the applicable law should have been the Costa Rican laws. This was extremely favorable to the interests of Santa Elena given the fact that under the national laws of Costa Rica, the valuation shall be based on a fair market value when the compensation is provided. The year of the award was in 2000.

On the other hand, Costa Rica claimed that the parties had implicitly agreed on the applicable law. To support that hypothesis, Costa Rica argued that parties consented to arbitration on the base of the Helms Amendment. In application of the Helms Amendment, USA prohibits foreign aid to a country that has expropriated the property of a USA citizen or company with at least 50% of USA stakeholders. This prohibition included USA approval of financing in an international finance organization. The only way to change that was if the country accomplished some requirements. One of them was to provide an adequate and effective compensation as required by international law. As a result, Costa Rica requested the tribunal not to apply Costa Rican laws but international law.

The tribunal rejected this argument. The award states[56] that article 42(1) of the ICSID Convention does not require that the agreement must be in writing or even expressly. However, the tribunal considered that if the agreement was implied, its substance had to be clear. According to the tribunal, that is not the case. Consequently, the tribunal pointed out that the dispute did not have to be solved solely in accordance to international law.

Given that the tribunal held that there is not an agreement, in application of article 42(1) of the ICSID Convention, the arbitrators had to apply the laws of Costa Rica and the rules of international law that may be applicable. The tribunal stated that the rules of Costa Rica regarding this dispute were clear enough and consistent with[57] "accepted principles of international law on the subject matter." Furthermore, the tribunal remarked that if there were inconsistencies, the rules of public international law must prevail.

Then, the conclusion was that rules of public international law must be applied to determine the value of the compensation. However, the question is what are the applicable principles and rules to determine the compensation under the umbrella of public international law. Here is one of the most important consequences of the award in regards to this research because the tribunal stated:[58]

56 Santa Elena case (n 3) para 63.
57 Ibíd para 64.
58 Ibíd para 71 – 72.

> While an expropriation or taking for environmental reasons may be classified as a taking for a public purpose, and thus may be legitimate, the fact that the Property was taken for this reason does not affect either the nature or the measure of the compensation to be paid for the taking. That is, the purpose of protecting the environment for which the Property was taken does not alter the legal character of the taking for which adequate compensation must be paid. The international source of the obligation to protect the environment makes no difference.
>
> 72. Expropriatory environmental measures—no matter how laudable and beneficial to society as a whole—are, in this respect, similar to any other expropriatory measures that a state may take in order to implement its policies: where property is expropriated, even for environmental purposes, whether domestic or international, the state's obligation to pay compensation remains.

In a footnote of this fragment of the award, the tribunal expressly noted: "For this reason, the Tribunal does not analyse the detailed evidence submitted regarding what Respondent refers to as its international legal obligation to preserve the unique ecological site that is the Santa Elena Property."

As a result, the tribunal only took into account the international principles of full compensation for a fair market value.

Parties did not agree on the date of the valuation, even under the application of international law. Costa Rica argued that it should be on the date of the decree of expropriation in 1978 while Santa Elena claimed that it must be on the date of the award. The tribunal concluded that the date for the valuation was the date of the expropriation. Then, arbitrators took into account the appraisals made at that time by the two parties and reached[59] a "reasonable and fair approximation of the value at the date of its taking."

However, the relevance for this paper is that the tribunal carried out all this analysis without considering that environmental elements could affect the principle of full compensation for a fair market value.

4.1.3. A conclusion of the decision in regards to the relationship between FIL and IEL.

Regarding the different types of expropriation, this one is clearly a direct expropriation. One decree directly expropriated a foreign investor property. Then, the discussion was not related to the legitimacy or validity of that measure but the value of the compensation.

Environmental legal arguments could be applied alongside other principles of international law, such as full market value, in order to determine the value of the compensation. For instance, Sands[60] remarks that Costa Rica requested the arbitrators to evaluate that a high compensation would be a disincentive, especially for developing countries, to take measures destined to protect the environment such as the creation or expansion of a national park. This author[61] also highlights that Costa Rica claimed that the expropriation was decided so as to

59 At the time of the expropriation, Costa Rica had valued the property approximately at US$ 1.9 million and Santa Elena in approximately US$ 6.4 million. The tribunal decided that the reasonable and fair value would be US$ 4.15 million. Then, an interest rate was applied and the value which comprised the principal and interest to the date of the award was US$ 16 million.

60 Sands, Principles of IEL (n 17) 844.

61 Ibíd 844.

comply with international environmental obligations, in particular the 1940 Western Hemisphere Convention.

It is important to remark that the award states that[62] "an expropriation or taking for environmental reasons may be classified as a taking for a public purpose, and thus may be legitimate […]." This could be classified as the first step taken in investment disputes addressing the relationship between FIL and IEL. Hence, a first conclusion could be that in order to accomplish environmental obligations, an expropriation may be legitimate. Nonetheless, this award was not addressing that discussion. As it has been explained the award had to analyze the value of the compensation, and in regards to that issue it states that environmental concerns did not play any role.

This approach reflects the first trend in investment disputes addressing environmental concerns. From what the award had to solve, Sands[63] explains that rules of FIL appear to be of a superior level than IEL rules.

4.2. *Metalclad Corporation v. United Mexican States* (ICSID Case No. ARB(AF)/97/1).

4.2.1. The origins and characteristics of the dispute.

Metalclad Corporation (hereinafter, Metalclad or the claimant) and ECO-Metalclad Corporation (hereinafter, ECO) were two USA corporations. Ecosistemas Nacionales S.A. de C.V. (hereinafter, ECONSA) was a Mexican corporation. ECONSA is wholly owned by ECO and Metalclad wholly owns this one.

Confinamiento Tecnico de Residuos Industriales, S.A. de C.V. (hereinafter, COTERIN), another Mexican company, was the owner of a landfill property in the Valley of La Pedrera in the Municipality of Guadalcazar in the Mexican State of San Luis de Potosi. In 1993 ECONSA purchased COTERIN, which included the landfill property.

In October 1996, Metalclad, on behalf of COTERIN, initiated arbitration under NAFTA article 1117 against the government of the United States of Mexico (hereinafter, Mexico or the respondent). The claimant argued that Mexico had breached its international obligations recognized in articles 1105 and 1110 of NAFTA.

Given the fact that Mexico is not a contracting state of the ICSID Convention, in accordance to NAFTA article 1120, the arbitral proceeding was administered by ICSID Secretariat and governed by the ICSID Additional Facility Rules. The award was rendered on August 30th, 2000.

Sands[64] describes that COTERIN had two federal government authorizations to construct and operate a hazardous waste transfer station in the site, two environmental impact authorizations concerning the construction, and a land-use permit issued by the state of San Luis de Potosi. These permits were granted before USA investors purchased COTERIN.

Metalclad claimed that shortly after purchasing COTERIN, the municipal governor embarked on a public campaign against the landfill. The award describes[65] that, in accor-

62 Santa Elena case (n 3) para 71.

63 Sands, 'Litigating Environmental Disputes: Courts, Tribunals and the Progressive Development of International Environmental Law' (n 2) 9.

64 Sands, Principles of IEL (n 17) 878.

65 Metalclad case (n 4) para 36.

dance to Metalclad's explanation, this company would not have purchased COTERIN without the apparent approval and support offered by federal and state officials.

In May 1994, Metalclad began the construction of the landfill. In October 1994, due to the lack of a municipal construction permit, the municipality interrupted the construction. Metalclad claimed[66] that federal authorities assured that the company could construct and operate the landfill, and that the municipality did not have the authority to deny the construction permit. The company also asserted[67] that federal authorities assured that Metalclad should apply to the municipality permit so as to facilitate an amicable relationship with the municipality, and that the permit would be issued.

On the other hand, Mexico claimed that a federal authority could not tell a company that a municipal permit construction is not required. Mexico asserted[68] that Metalclad knew that this permit was required or should have known it.

In November 1994, the company recommenced the construction of the landfill and applied to this municipal permit, but in December 1995 it was denied again. By March 1995, the landfill was finished and was inaugurated, but Metalclad claimed that since the inauguration day it was prevented from operating due to social agitations organized in part by Mexican state and local governments.

One year later, in November 1995, Metalclad reached an agreement with two federal sub agencies. According to this agreement, scientific studies recognized that the lands were suitable for the operation of the landfill. Some deficiencies were detected, though. Thus, the parties agreed on an action plan that included a site remediation plan.[69] As a result, Metalclad was allowed to operate the landfill for an initial period of five years.

The municipality initiated administrative and judicial proceedings seeking the annulment of the agreement reached by Metalclad and Mexican federal authorities. These complaints were dismissed.

After the beginning of the investment arbitration proceeding, the governor of the State of San Luis de Potosi issued an ecological decree declaring a natural area for the protection of cacti. This natural area included the landfill. There was some discussion about the consideration of this ecological decree by the tribunal. Mexico argued that it is not part of its jurisdiction because it was enacted after Metalclad's Notice of Intent to Arbitration. The tribunal dismissed that claim given the fact that Mexico had enough opportunity to respond to the allegations related to that decree. Thus, the tribunal held that the analysis of the ecological decree was within its jurisdiction. However, it was not considered relevant to decide on the merits.

In the award the tribunal held that Mexico was in breach of its obligations contained in NAFTA articles 1105 and 1110, and thus ordered Mexico to pay US$16,685 million to Metalclad.

In summary, this case is concerned with an indirect expropriation. The property was never transferred to the government, but it is argued that there is an expropriation because of an interference with the use of the property. According to Viñuales,[70] Mexico is found responsible for two measures that amount for an indirect expropriation. The first is classified as a targeted measure be-

66 Metalclad case (n 4) para 41.

67 Metalclad case (n 4) para 41.

68 Metalclad case (n 4) para 41.

69 Sands remarks that, before 1991, 20,000 tons of waste were deposited on the site without treatment or separation. This suggests that before the participation of foreign investors, there were some environmental concerns related to this site. According to this explanation, the action plan contained in the agreement reached in 1994 also included a site remediation plan. Sands, Principles of IEL (n 17) 878.

70 Viñuales (n 18) 300.

cause Metalclad was denied to operate the landfill in spite of the existence of the required permits. The second is the enactment of the ecological decree that is identified as a regulatory measure.

4.2.2. The considerations made in the award.

First of all, the award established that under international law, the conduct of an agency or state organ shall be considered as an act of the state. Thus, Mexico could be responsible for the acts of the municipality, and those acts were covered by NAFTA.

Then, the tribunal noted that under NAFTA Preamble, Mexico is obliged to ensure a predictable commercial framework for business planning an investment. Regarding this obligation, the tribunal considered that Mexico violated NAFTA article 1105, which provides that there is an obligation to treat a foreign investor in accordance to international law, including fair and equitable treatment and full protection and security.

The tribunal asserted that the requirements, practice and procedures to issue a municipal construction permit were not clear, and thus Mexico infringed NAFTA article 1105.

In relation to the purpose of this paper, it is important to remark that the award[71] remarks that this conclusion is not affected by NAFTA article 1114. In accordance to this article, a NAFTA party shall ensure that an investment in its territory is carried out in a manner that is sensitive to environmental concerns. The tribunal concluded that Mexico ensured that the landfill operations had been executed in an environmentally friendly manner. To support this conclusion, the tribunal relied on the agreement between the claimant and some environmental federal agencies, which included a plan for the landfill operation, and on the issuance of federal permits. The existence of this agreement and the federal permits suggested that Mexico considered that the landfill had been and would be conducted in a manner sensitive to the environment.

It is relevant for this paper because, as Sand asserts,[72] the language of NAFTA implies a hierarchy in favor of the foreign property rights, and does not suggest that environmental aims could shed some light on the interpretation of NAFTA articles 1105 and 1110 obligations. This case is an example of that hypothesis because although the agreement between Metalclad and the environmental federal agencies existed, it was not analyzed in the award in order to conclude that the landfill had been operating and could continue to operate in a manner sensitive to environmental concerns.

Precisely, the reason so as to not analyse the environmental considerations of that agreement could be the language of NAFTA article 1114. The reference to the protection of the environment is too vague and broad. According to that language, the tribunal held that the mere existence of an agreement addressing environmental concerns is enough to conclude that Mexico agreed on the apparently environmentally friendly manner in which the landfill had been performing its activities.

This was confirmed by the definition of 'expropriation' provided in paragraph 103 of the award:

> Thus, expropriation under NAFTA includes not only open, deliberate and acknowledged takings of property, such as outright seizure or formal or obligatory transfer of title in favour of the host State, but also covert or incidental interference with the use of property which has the effect of depriving the owner, in whole or in significant part, of the use or reasonably-to-be-expected economic benefit of property even if not necessarily to the obvious benefit of the host State.

71 Metalclad case (n 4) para 98.

72 Sands, Principles of IEL (n 17) 872 – 873.

A direct consequence of this analysis was that Mexico also failed to comply with the obligation stated in NAFTA article 1110. The award clearly states that an expropriation could also be an "incidental interference with the use of the property." As it can be appreciated, this is a broad definition of expropriation.

Then, the tribunal addressed the effects of the ecological decree. The arbitrators explained that this analysis is not essential to conclude that Mexico failed to comply with its obligations under NAFTA articles 1105 and 1110, but it was a[73] "further ground for a finding of expropriation."

What is relevant for this purpose is that the tribunal expressly asserted that it was not necessary to evaluate the motivation or intent of the ecological decree, and that the ecological decree would be in itself an act tantamount to expropriation, and thus a violation of NAFTA article 1110.

Exactly like in Santa Elena, in this award the arbitrators implied that it is not necessary to take into account the rules of IEL. The importance of this hypothesis is that, again,[74] the rules of FIL appear to be of a superior level than the rules of IEL.

4.2.3. The relevance of this decision in the relationship between foreign investment and the protection of the environment.

Two conclusions could be highlighted from the decision in Metalclad.

In regards to the targeted measure, it must be noticed that the analysis and decision is a consequence of the language used in investment treaties dealing with environmental concerns. The language of NAFTA generates that[75] "the awards made under NAFTA are more intent on property protection and have constructed more rigorous theories of absolute property rights than even decisions of US Courts."

As it has been explained, NAFTA article 1114 has a broad and, to some extent, vague reference to the protection of the environment. Thus, it would be difficult for a state party to demonstrate that an action has been taken to ensure that an investment activity is being carried out in a manner sensitive to environmental concerns.

In this case, the existence of an agreement between Metalclad and some environmental federal agencies of Mexico was enough for the arbitrators to conclude that Mexico was satisfied with the environmental concerns related to the operation of the landfill. Hence, it is clear that the environmental analysis was, at least, superficial in comparison to the rigorous attention given to the foreign investment property rights.

The second conclusion that could be taken from Metalclad is that rules of FIL are implicitly considered of a superior level than rules of IEL. The evaluation of the ecological decree reveals this conclusion because the tribunal argued that its only existence constituted an indirect expropriation and an infringement to NAFTA article 1110. According to the arbitrators, the motivations or reasons for the existence of the ecological decree did not have any relevance to determine that a compensable expropriation occurred.

Unlike Santa Elena, this is an indirect expropriation. However, the consequence is the same because international environmental obligations are not considered. Nevertheless, in San-

73 Metalclad case (n 4) para 109.

74 Sands, 'Litigating Environmental Disputes: Courts, Tribunals and the Progressive Development of International Environmental Law' (n 2) 9.

75 Sornarajah (n 45) 372 citing V. Bean and J. Beauvais, "The Global Fifth Amendment? NAFTA's Investment Protection and the Misguised Quest for an International 'Regulatory Takings' Doctrine" (2003) 78 New York University Law Review 30.

ta Elena, the tribunal stated that environmental reasons could be the ground for a legitimate expropriation, but are irrelevant to determine the valuation of the compensation.

In Metalclad, the consideration of environmental concerns was even worse. The arbitral tribunal held that the ecological decree was an act tantamount to expropriation in itself without evaluating its environmental reasons. Its mere existence was an indirect expropriation. Thus, environmental reasons were not considered to evaluate the legitimacy of an expropriation or to determine the valuation of the compensation.

4.3. Conclusions.

Santa Elena and Metalclad are good examples to demonstrate that in the case law, the starting point in the relationship between FIL and IEL was a complete disconnection. The conclusion from this first approach is that rules of FIL are superior to environmental ones. As Sands[76] claims, this is a mistake.

It could also be concluded at this point that a soft and vague language of environmental regulations in investment treaties could trigger superficial environmental analysis in comparison to a rigorous and protective property rights interpretation.

Finally, it could be stated that environmental concerns exist in investment disputes and, from the first moment, they are considered, at least, as legitimate reasons to support the validity of an expropriation of foreign investment rights.

In the next chapters, some investment arbitration awards enacted after Santa Elena and Metalclad will be referred to in order to demonstrate that the distance between FIL and IEL is getting closer.

5. A First Approach. The *Tecmed* Case

To some extent, the facts are similar to those of Metalclad because it involves the allegation of an expropriation measure taken in the same country and in the same economic sector. Although the outcome of the dispute is also equal, the reasoning is different. Precisely, that difference is the relevance of Tecmed, which constitutes a new path for the relationship between IL and IEL.

5.1. A brief description of the dispute.

The proceeding was conducted under the ICSID Additional Facility Rules in accordance to the Agreement on the Reciprocal Promotion and Protection of Investments signed by the Kingdom of Spain and Mexico.

Tecnicas Medioambientales de Mexico, S.A. de C.V. (hereinafter, Tecmed or the claimant) was a Mexican corporation controlled by the Spanish corporation named Tecnicas Medioambientales Tecmed S.A. Tecmed owned 99% of the shares of Cytar S.A. de C.V., a Mexican company which took place through the investment of this case.

The dispute was related[77] to a landfill built in 1998 on a land purchased by the government of the State of Sonora. At that time, the landfill had a renewable license to operate for five years. Then the landfill was transferred to another public agency. On May 4th, 1994, a new authorization was issued to operate the landfill for an indefinite period. The Hazardous Materi-

76 Sands, 'Litigating Environmental Disputes: Courts, Tribunals and the Progressive Development of International Environmental Law' (n 2)

77 Tecmed case (n 6) para 36.

als, Waste and Activities Division of the National Ecology Institute of Mexico (hereinafter, INE), an environmental federal agency of Mexico, is the public entity that enacted this authorization.

The public entities, which owned the landfill, transferred it to Promotora Inmobiliaria del Ayuntamiento de Hermosillo (hereinafter, Promotora) a decentralized municipal agency of the Municipality of Hermosillo, located in the State of Sonora. Tecmed created Cytar S.A. de C.V. with the aim of conducting the operations of this landfill, given the fact that Tecmed was awarded by Promotora with the landfill in a public auction concluded on February 16th, 1996.

On November 11th, 1996, INE confirmed that the name of the license to operate the landfill had been changed, and that the name of Cytar S.A. de C.V. was indicated as the new owner. This authorization could be extended every year. It was the case when it was extended to November 19th, 1998.

On November 25th, 1998, INE rejected the application presented by Cytar S.A. de C.V. for renewal of the authorization, and requested this company to submit a program to close the landfill. According to Tecmed, this measure constituted an unjustifiable expropriation of its investment without any compensation.

5.2. The arguments of the parties on the merits and the relevant parts of the award for the purpose of this paper.

The claimant holds[78] that the extension of the authorization of the permit to operate the landfill was refused due to political pressures. The measure was qualified as arbitrary and unjustifiable because Cytar S.A. de C.V. had not violated the terms under which the landfill was supposed to be operated.

The claimant, nonetheless, recognizes[79] some breaches of the conditions of the expired permit, but holds that an extreme decision like the closure of the landfill was not justifiable and constituted a breach of Mexican international obligations. According to Tecmed, the federal Environmental Protection Attorney's Office, which is also an environmental federal agency of Mexico, had investigated the breaches of the conditions of the expired permit without deciding a revocation of the license. Moreover, the claimant points out that this environmental agency did not find violations that might threaten the environment or the population's health. Thus, this public entity only fined Cytar S.A. de C.V. even though it had the authority to revoke the permit.

On the other hand, Mexico[80] claims that the decision was a control measure undertaken in a regulated sector closely linked to public interests, and thus is not an act of expropriation or an infringement of investment international obligations.

The award[81] explained that the investment agreement between Spain and Mexico neither define the concept of expropriation nor does it classify the measures or actions that would be considered as an act of expropriation. However, the arbitrators base their understanding on Metalclad. Thus, they assert that expropriation is not only a taking of property by the government, but also actions that deprive persons of their ownership without allocating their assets to third parties or the government itself.[82]

Having classified the dispute as one that involves an alleged indirect expropriation, the

78 Tecmed case (n 6) para 42.
79 Tecmed case (n 6) para 43.
80 Tecmed case (n 6) para 46.
81 Tecmed case (n 6) para 113.
82 Tecmed case (n 6) para 113.

tribunal stated[83] that it was relevant to determine if the assets related to the investment had lost their value. According to the award,[84] this determination was of great importance because it would clarify whether the measure was an ordinary exercise of the state power's policy or a de facto expropriation that deprived the investment assets of any real substance.

The arbitrators concluded that the measure had destroyed the investment value, and thus it was an indirect or de facto expropriation. To confirm that analysis, the award remarks that in the investment treaty between Spain and Mexico, there was no principle that excludes an action of being classified as an expropriation even if it is beneficial to society or the environment. In order to support that opinion, the arbitrators quoted the award enacted in Santa Elena.[85]

However, this award is relevant for the purpose of this paper because it adds an important element in the approach between FIL and IEL. The arbitrators did not simply conclude their analysis claiming that there was no relation between these fields. In spite of qualifying the measure as an act of expropriation on the basis of Santa Elena and Metalclad, the arbitrators considered that it was required to evaluate the proportionality of the measure in order to find out if Mexico had breached a foreign investment obligation.

The award relies upon the jurisprudence of the European Court of Human Rights[86] and states that "There must be a reasonable relationship of proportionality between the charge or weight imposed to the foreign investor and the aim sought to be realized by any expropriatory measure." As it could be noticed, even though the act was qualified as an expropriation, the arbitrators explained that their decision must consider[87] "a reasonable relationship of proportionality."

In this case, the arbitrators concluded that the measure was not proportional because it was based on community and political pressures that could not to lead to an emergency situation. In particular, the award stated that the measure was not proportional because in this case it was clear that the alleged infringements of the claimant did not pose a present or imminent risk to the ecological balance and people's health. As a result, the award determined that Mexico was responsible for an act of expropriation and must be compensated.[88]

5.3. Conclusions from the *Tecmed* award.

Tecmed award was rendered only three years after Santa Elena and Metalclad awards, but it demonstrates that the distance between FIL and IEL is getting closer. In accordance to some authors[89], a rule of proportionality was imported from the European Court of Human Rights, and the consequence is that under this principle[90] "regulation that would otherwise constitute indirect expropriation will not be considered a violation of international law if it is a proportion-

83 Tecmed case (n 6) para 115.
84 Tecmed case (n 6) para 115.
85 Tecmed case (n 6) para 121.
86 Tecmed case (n 6) para 122 citing Mellacher and Others v. Austria (1989) ECtHR; Pressos Compañía Naviera and Others v. Belgium (1995) ECtHR; Matos e Silva Lda, and others v. Portugal (1996) ECtHR.
87 Tecmed case (n 6) para 122.
88 The award ordered Mexico to pay the amount of US$ 5,533,017.12 plus an interest rate.
89 Jack J. Coe and Noah Rubins, 'Regulatory Expropriation and the Tecmed case: Content and Contributions' in Todd Weiler (ed), International Investment Law and Arbitration: Leading Cases from the ICSID, NAFTA, Bilateral Treaties and Customary International Law (Cameron May 2005) 664.
90 Ibíd 664.

al response to a legitimate public concern."

Consequently, the first conclusion is that, unlike the previous approach, this award provides a guidance to deal with foreign investment disputes regarding environmental concerns.

From this analysis, it is not possible to argue that foreign investment disputes must be decided without taking into consideration different fields of law such as IEL. This award relies upon what international human rights courts have been doing when it comes to taking a decision regarding government measures that have affected property rights. Then, the concept of proportionality is vital in this regard because rules of FIL and rules of IEL are not absolute.

Surely, it implies that there is not a unique solution and that there must be a case-by-case approach. However, Tecmed provides an important element for the development of foreign investment disputes. Arbitrators could use the concept of proportionality just like human rights courts have been doing so. As a consequence, unlike Metalclad and Santa Elena, environmental international obligations must be taken into account in order to conclude whether a measure is proportional and an act of compensable expropriation or not.

6. On the Way of Achieving a Balance

6.1. Methanex Corporation v. United States of America. Award rendered in the international arbitration under chapter 11 of the NAFTA and UNCITRAL arbitration rules.

6.1.1. A brief description of the dispute.

Methanex Corporation (hereinafter, Methanex) was a Canadian company and was the largest producer of methanol, a feedstock for a gasoline additive known as MTBE (methyl tertiary-butyl ether). The claim was related to a ban on the sale and use of MTBE issued by the State of California. Methanex argued that this ban constitutes a USA infringement of NAFTA obligations.

The award was rendered on 3rd August, 2005. The arbitrators decided that they did not have jurisdiction to determine the claims made by Methanex. However, they also stated that if they had jurisdiction they would decide to dismiss the claims made on the merits by Methanex.

6.1.2. The relevant arguments of the parties and the considerations of the award regarding the purpose of this paper.

Methanex claims that all methanol producers were in similar circumstances than USA domestic ethanol producers. Methanol and ethanol are oxygenates used to produce reformulated gasoline. Thus, methanol and ethanol producers competed for customers in the oxygenate market. As a consequence, the ban on the sale of MTBE and methanol was a discriminatory measure and an act tantamount to expropriation.

According to Methanex, the burden of proof bore on USA so as to justify that the ban was a valid environmental measure.[91] As a result, USA had to demonstrate that the California measure: (i) was necessary to fulfil an environmental objective; (ii) was proportionate; (iii) was the least restrictive of foreign investment; and (iv) was not a disguised restriction of foreign investment.

Methanex argues that the measure did not satisfy these criteria. Moreover, Methanex claims that it was an act tantamount to expropriation that was not intended to serve a public

91 According to the award, Methanex relied upon the award rendered in the United States—Standards for Reformulated and Conventional Gasoline, (US v. Braz.), WT/DSZ/AB/R (WTO 1996). Methanex case (n 7) pt IV, ch B, para 9.

purpose;[92] that the measure did not comply with the due process of law given the fact that it was discriminatory, and that Methanex was not compensated.[93]

On the other hand, USA asserts that 47% of methanol producers in this country were domestic.[94] Hence, the measure was supposed to have the same effect on foreign and domestic investors and did not constitute a discriminatory measure. Moreover, USA holds that methanol and ethanol are chemically different, have distinct end uses, and are not interchangeable. Hence, USA claims that these products did not directly compete. In that sense, USA argues that the ban was not an act tantamount to expropriation because it was not discriminatory and was made for a public purpose.

As it has been mentioned, the award rejects Methanex's claims. According to the arbitrators, the ban on the use and sale of MTBE issued by the State of California was not discriminatory or an act tantamount to expropriation.

The tribunal did agree with Methanex in terms of considering this one an act of international discrimination as an expropriation. However, the tribunal[95] explained that a consequence of that conclusion is that a non-discriminatory regulation for a public purpose, issued in accordance with the due process of law, is not an act of compensable expropriation.

In the interpretation of NAFTA article 1110, the tribunal[96] suggested that a regulatory measure is not an act tantamount to expropriation unless the host state was previously committed with the foreign investors to refrain from issuing this regulation. If that is not the case, a regulatory measure, which is not discriminatory, in accordance to the due process of law and issued for a public purpose, is not an act of expropriation.

The arbitrators[97] concluded that regarding the facts brought before them, USA had not previously committed with Methanex to refrain from changing the regulation. Finally, in regards to the requirements to consider an act as an expropriation (such as the discriminatory measure, the absence of a public purpose or the infringement of the due process of law), the tribunal[98] held that Methanex had been unable to demonstrate them.

6.1.3. Conclusions from the **Methanex** *case.*

This award is an example of progress in the considerations of environmental concerns in investment disputes. It confirms that a regulatory measure is not considered a compensable expropriation if it was taken for a public purpose.

As it has been explained, an indirect expropriation could be classified as a regulatory measure or as a targeted measure. They are indirect expropriations because there is not a direct transfer of property to the state or third parties. However, they may account for an expropriation because they deprive the value of the foreign investor property.

92 Methanex asserts that the measure was planned to hand the profit of the market directly to domestic investors. Methanex case (n 7) pt IV, ch D, para 2.

93 Methanex also relies on the definition of expropriation under NAFTA given in the Metalclad award, which includes "incidental interference with the use of property which has the effect of depriving the owner, in whole, or in significant part, of the use of reasonably-to-be-expected economic benefit of property even if not necessarily to the obvious benefit of the Host state." Methanex case (n 7) pt IV, ch D, para 4.

94 Methanex case (n 7) pt IV, ch B, para 18.

95 Methanex case (n 7) pt IV, ch D, para 7.

96 Methanex case (n 7) pt IV, ch D, para 7.

97 Methanex case (n 7) pt IV, ch D, para 9.

98 Methanex case (n 7) pt IV, ch D, para 12, 13, 14.

In Metalclad, a regulatory measure (such as the ecological decree) was considered an expropriation without taking into account its reasons. Then, in Tecmed, a targeted measure (such as the refusal of a renewable permit) was considered an act of compensable expropriation even though a test of proportionality imported from human rights courts was applied.

In Methanex, a regulatory measure was not considered as an expropriation. It was understood as part of a valid exercise of the policy powers of a sovereign state with the aim of protecting the environment. This implies a clear rejection of Metalclad conclusions.[99]

In particular, it is interesting that this analysis has an effect in the allocation of the burden of proof.[100] The previous case law suggests that a regulatory measure, which does not account for a compensable expropriation, is an exception. Thus, it is the host state that must establish that its measure is an exception. However, this award departs from that view and understands that a regulatory change is the rule. Specifically, Vinuales[101] notes that it is the case in highly regulated markets like the energy, mining or chemical sectors.

In the Methanex award,[102] it is explained that the claimant knew that the market for MTBE in the USA was the result of continuous regulatory process. That is why[103] "the normal course of a regulated market is that general regulations will evolve over time."

As a result, from the analysis made in Methanex, a regulatory measure could be considered the rule, and only under exceptional circumstances, it would be an act of compensable expropriation. This implies that the foreign investor bears the burden of proving that its investment has lost its value and that the changes introduced by the regulatory measure are not part of its commercial risks or, if they were, that the measure was taken in contradiction to previous host state commitments.

As it could be noticed, this award means clear progress in the proximity between FIL and IEL. It recognizes the value of sovereign states to regulate the activities performed in their jurisdictions so as to protect the environment as a rule instead of an exception.

6.2. Ad hoc NAFTA Arbitration under UNCITRAL Rules between *Chemtura Corporation v. Canada*.

6.2.1. A brief description of the dispute.[104]

Chemtura Corporation (hereinafter, Chemtura or the claimant) was a USA company based under the laws of the State of Delaware. This company was registered in Canada for the use of lindane-based pesticides. Lindane is a pesticide used to treat canola. The Pest Management Regulatory Agency (hereinafter, PMRA) is the federal agency responsible for the regulation of pest control products in Canada.

Regarding an international concern in the use of lindane and the restrictions imposed in the USA since 1998, the claimant and other lindane registrants in Canada did agree on removing this product in the treatment of canola. This was known as the withdrawal agreement. Chemtura confirmed its agreement subjecting it to a number of conditions. For instance, that all

99 Surya P. Subedi, International Investment Law. Reconciling Policy and Principle (2nd edn, Hart Publishing 2012) 162.

100 Viñuales (n 18) 306.

101 Ibíd 306.

102 Methanex case (n 7) pt IV, ch D, para 9.

103 Viñuales (n 18) 306.

104 Chemtura case (n 8) para 6 – 49.

other registrants also agree to withdraw it by the same date. However, then Chemtura decided not to voluntary remove the use of lindane in the treatment of canola unless it had alternative products registered to replace it.

A Special Review of Pest Control Products Containing Lindane was launched by the PMRA. In October 2001, they concluded that in regards to the risk assessment findings, a regulatory action had to be taken in the form of suspending or terminating lindane registrations. Hence, in December 2001 and January 2002, PMRA offered to Chemtura a phase out of the use of lindane through voluntary discontinuation. Chemtura did not accept it, and on February 21st, 2002 PMRA informed Chemtura that its registrations had been terminated through suspension. The PMRA also argued that under the withdrawal agreement, a registration of replacement products was not promised.

Following a request made by Chemtura, a Board of Review was established by the Canadian Minister of Health and began its work in May 2004. The Board Review Report recommended PMRA to reconsider possible opportunities for the use of lindane as well as seek input from Chemtura.

The PMRA launched a re-evaluation process in which Chemtura and other registrants participated and provided information. Nevertheless, the Re-evaluation Note (REN) found similar conclusions than the Special Review. Chemtura did not agree with it and claimed that it was in contrast with the findings of the Board of Review.

6.2.2. The considerations of the award regarding the purpose of this paper. Chemtura argues that Canada had infringed its international obligations recognized in NAFTA articles 1105, 1003 and 1110.

NAFTA article 1105 refers to the minimum standard of treatment that a foreign investor deserves in the host state. A key question that the tribunal addressed[105] was if there is a margin of appreciation in domestic regulatory measures that could diminish the protection granted under this NAFTA regulation. The award suggested that it exists because it recognized an international minimum standard of treatment that must be evaluated regarding all the circumstances of the case. These include[106] "the fact that certain agencies manage highly specialized domains involving scientific and public policy determinations."

Consequently, the award analyzes all the circumstances alleged by Chemtura to support the existence of an unfair treatment to its investment. Among the different factual basis on which Chemtura based its claim, the award bases its analysis on the considerations related to the review process launched by the PMRA.

Among the reasons given to dismiss Chemtura's claim, the tribunal showed that since the 1970s, there has been a worldwide concern related to the use of lindane.[107] As a result, in contrast to the opinion of Chemtura, the award asserted that PMRA launched the Special Review as part of its mandate as a regulatory agency and in accordance to a Canadian international commitment to the Aarhus Convention and Protocol to the Convention on Long-Range Transboundary Air Pollution on Persistent Organic Pollutants.

Furthermore, Chemtura claimed that they had a legitimate expectation under the withdrawal agreement. Chemtura held that PMRA would accept that lindane products could be

105 Chemtura case (n 8) para 23.
106 Ibíd para 23.
107 Ibíd para 135 – 137.

used to treat canola until July, 2001 and that there were no restrictions on when the products could be sold or planted.

The award asserts that the mere existence of the withdrawal agreement was a regulatory fairness expression and that PMRA fulfilled Canadian NAFTA obligations when facilitating the conclusion of the withdrawal agreement. Moreover, the award[108] holds that the content of the withdrawal agreement did not suggest to Chemtura a "reasonable" or "legitimate" expectation to be treated without considering the deadline.

Chemtura[109] also held that PMRA should have secured a phase-out under the Pesticide Control Products Regulations of Canada. Chemtura argued that they were deprived of that right and that the cancelation of its registration was a punitive measure.

The arbitrators disagreed with that argument. They asserted[110] that, under Canadian regulation, the Minister of Health is allowed to cancel a registration if, on the basis of current information, the safety of that product is no longer acceptable. The arbitrators held that PMRA was not legally obliged to assure a voluntary phase-out procedure.[111] Moreover, they explained that PMRA satisfied the standard treatment required by NAFTA when offering twice a voluntary phase-out discontinuation procedure.[112]

The most relevant part of the decision regarding the purpose of this paper is the alleged infringement of NAFTA article 1110. According to Chemtura, the decision of cancelling the lindane registration was an indirect expropriation because it implied a substantial deprivation of its investment. Moreover, Chemtura argued that the reason of the measure was irrelevant.

There are two significant arguments presented by the tribunal so as to reject the claim made by Chemtura. Firstly, the tribunal explained that it was indispensable to analyze if the cancellation of the registration meant a substantial deprivation of the Chemtura investment.

Chemtura's claim was based on the definition of expropriation given in Metalclad, and the tribunal highlighted that this award was challenged before the Supreme Court of British Columbia. Although it was not set aside on the ground of the definition of expropriation, the tribunal noticed that Justice Tysoe asserted that the definition was extremely broad. As a result, the tribunal argued that[113] "Metalclad v. Mexico has given rise to some controversy as to the degree of the required deprivation."

Consequently, instead of applying a broad definition of expropriation, the tribunal asserted that the circumstances of each case must determine the existence of a substantial deprivation.[114] Under the circumstances of the case, the tribunal concluded that there was not a substantial deprivation of the investment because lindane products represented a small portion of Chemtura investments.[115] This was confirmed by the fact that Chemtura sales were reduced

108 Chemtura case (n 8) para 179.
109 Ibíd para 182.
110 Ibíd para 185.
111 Ibíd para 190.
112 The award also dismisses the allegation made by Chemtura in regards to the delays in the registration of Gaucho as an alternative product. The tribunal holds that it did not have an economic impact on Chemtura, and that the time used by PMRA was not different from the usual practice in the USA in the same circumstances. Thus, this fact is not part of a pattern of unfair conduct as was argued by Chemtura. Ibíd para 194 – 225.
113 Ibíd para 248.
114 Ibíd para 249.
115 Ibíd para 260 – 262.

in 2002 even though it performed an ascending trend between 2002 and 2007.[116] Consequently, the cancellation could not be identified as a substantial deprivation of the investment.

The valid exercise of the government policy powers doctrine was another reason given by the tribunal to explain that the cancelation was not an infringement of NAFTA article 1110. The tribunal[117] stated:

> 266. Irrespective of the existence of a contractual deprivation, the Tribunal considers in any event that the measures challenged by the Claimant constituted a valid exercise of the Respondent's police powers. As discussed in detail in connection with article 1105 of NAFTA, the PMRA took measures within its mandate, in a non-discriminatory manner, motivated by the increasing awareness of the dangers presented by lindane for human health and the environment. A measure adopted under such circumstances is a valid exercise of the State's police powers and, as a result, does not constitute an expropriation.

6.2.3. Conclusions from the Chemtura *case.*

This award reflects other important developments in reducing the gap between FIL and IEL. For instance, regarding the alleged infringement of the minimum standard of treatment, the tribunal not only took into account the international concern related to the use of lindane, but also remarked that Canada was committed to accomplish the Aarhus Convention and the Protocol to the Convention on Long-Range Transboundary Air Pollution on Persistent Organic Pollutants.

Furthermore, the award recognizes that the definition of expropriation made in Metalclad is, at least, in controversy. The arbitrators asserted that the concept of expropriation couldn't be too broad.

In order to evaluate the application of this concept, the award held that a substantial deprivation is required, and that it must be evaluated under the circumstances of each case. In this case, the award decided that the deprivation of the investment was not substantial given the fact that lindane products were only a small part of Chemtura's investment. However, what is relevant is that the concept of 'substantial deprivation' is applied[118] to evaluate if a measure could be an act of expropriation. This clearly limits the broad definition of expropriation suggested in Metalclad where an expropriation is an[119] "incidental interference with the use of property."

Moreover, Chemtura confirms the application of the policy powers doctrine to justify the regulations of a state. In particular, it confirms the application of this doctrine to justify the

116 Ibíd para 264.

117 Ibíd para 266.

118 In *Pope & Talbot Inc. v. Canada* Award (2000), 7th August 2000, Ad Hoc Tribunal (UNCITRAL), there are criteria to determine if there is an act of indirect expropriation. The elements of this test are: (i) whether the investor remained in control of its investment, (ii) whether it directed its day-to-day operations, (iii) whether its officers and employees were detained by the state, (iv) whether the state supervised the work of the investor's officers and employees or not, (v) whether the state had taken the proceeds of sales other than through taxation, (vi) whether the state interfered with management or shareholders' activities, (vii) whether the state prevented the distribution of dividends to shareholders, (viii) whether the state interfered with the appointment of directors or management, and (ix) whether the state had taken any other actions ousting the investor from full ownership and control of the investment. In the *Chemtura* case, the parties tried to highlight only some of these elements in regards to their interests. That is why the tribunal held that the concept of substantial deprivation is a matter of degree and not one of specific conditions. However, these elements are important because under the circumstances of each case they could be useful to determine if a measure has deprived an investment in a substantial form, and could be considered an act of expropriation for that reason.

119 *Metalclad* case (n 4) para 103.

enactment of environmental regulations.[120] This award verifies this doctrine because it had been already applied in Methanex.

However, in Methanex the measure was one of general application. In the terms detailed in chapter 2, it was a regulatory measure. In Chemtura, the measure is not one of general application. It is the cancellation of a registration, so it is a targeted measure because it directly affects the investment. Thus, this award supposes not only a confirmation of the policy powers doctrine but also an improvement of it. Now the police powers doctrine supports the issuance of environmental measures that are only focused on the foreign investment property.

7. The Protection of the Environment as the Key Element of an Investment Dispute

7.1. *Chevron v. Ecuador*.

Texaco Petroleum Company is an affiliate of Chevron Corporation. Both are from the USA and the claimants in one investment arbitration against the Republic of Ecuador that is part of a complex national and international dispute. For the purpose of this paper, some aspects of the investment arbitration will be described to demonstrate that currently the protection of the environment could be a key element of an investment dispute.

It is an arbitration proceeding under UNCITRAL rules pursuant to the BIT between USA and Ecuador. The case is basically concerned with the legal effects of the 1995 Settlement Agreement signed between Ecuador, Petroecuador and TexPet.

To date, TexPet is owned by Chevron, but it was not the case in 1995. According to the preamble of this agreement,[121] TexPet agreed to take environmental remedial work in consideration for being released and discharged of all its legal and contractual obligations and liability for environmental impact arising out of the consortium's operations.

Article 5.1 of the Settlement Agreement stipulates:

> On the execution date of this contract, and in consideration of TexPet's agreement to perform the Environmental Remedial Action Plan, the Government and Petroecuador shall hereby release, acquit and forever discharge TexPet, Texaco Petroleum Company, Compañía Texaco de Petroleos del Ecuador S.A., Texaco Inc, and all their respective agents, servants, employees, officers, directors, legal representatives, insurers, attorneys, indemnitors, guarantors, heirs, administrators, executors, beneficiaries, successors, predecessors, principals, and subsidiaries, (hereinafter referred as the Releasees) of all the Government's and Petroecuador's claims against the Releasees for Environmental Impact arising from the operations of the Consortium, except for those related to the obligations contracted hereunder for the performance by TexPet of the Scope of Work (Annex A).

In turn, article 5.2 stipulates what are the government's and Petroecuador's claims that are discharged in favor of the releasees. In that sense, a relevant aspect of the dispute is in relation to the interpretation of what is understood by a "Third Party" of the agreement. Article 9.1

120 Viñuales (n 18) 310.

121 Chevron Corporation and Texaco Petroleum Corporation v. The Republic of Ecuador. UNCITRAL, PCA Case No. 2009–23. First Partial Award on Track 1, 17th September para 19.

sets forth that the agreement shall not be construed to confer any benefit on any third party, nor shall it provide any rights to such third party.

It is relevant for the dispute because between October 2000 and November 2001 Chevron became TexPet's indirect owner. Thus, the question is whether or not Chevron is a third party of the Settlement Agreement. If Chevron is a third party, it could not be considered a releasee and shall be responsible of all the eventual claims related to the operations of the Consortium.

This discussion has been identified for the purpose of this paper because it is an investment dispute where the definition of the environmental claim is essential to determine whether or not Chevron is a releasee under the Settlement Agreement.

Chevron claims[122] that the causes of action in the Settlement Agreement include all "collective" or "diffuse" environmental rights,[123] but does not include causes of action available to private individuals making claims for their own personal harm caused by environmental pollution.

This differentiation is important because Chevron's aim is not to be considered responsible in a multimillionaire lawsuit known as the Lago Agrio Litigation, which was initiated by private individuals who are pleading for compensation for environmental harm. Chevron holds that this lawsuit is related to the protection of diffuse environmental rights, and thus under the Settlement Agreement this company is released as a matter of res judicata and collateral estoppel under Ecuadorian law applicable to settlements.

Chevron states[124] that Lago Agrio litigation in Ecuador is different from Aguinda Litigation in New York because the latter involved only individual rights and consequently it is a litigation that was not covered by the Settlement Agreement. Nonetheless, Chevron argues that the Settlement Agreement covers the Lago Agrio litigation in the Ecuadorian courts because private individuals who are seeking the protection of environmental diffuse rights initiated it.

The reasoning of this position is that in 1995 (when the Settlement Agreement was signed) no private individual had legal standing to bring environmental claims in respect of collective or diffuse rights. Although collective and diffuse rights existed under Ecuadorian law, only the government on behalf of the people could exercise them. Consequently, in the Settlement Agreement the government was capable of releasing environmental diffuse or collective claims, but individual claims could not be released. The private individuals had legal standing to vindicate their individual rights.

A partial award on track I enacted on 17th September 2013 concluded in favor of Chevron that this company was a releasee under the Settlement Agreement in the same terms as TexPet. Furthermore, this partial award stated that the scope of the release does not extend to any environmental claim made by an individual for personal harm. However, it also concluded that this scope precludes any diffuse claim against Chevron made by the government or by any individual not claiming personal harm.

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122 Ibíd. para 45.

123 Regarding the jurisdictional access to the protection of the environment, it can be mentioned that there is a Model Code of Collective Processes elaborated by the Iberoamercan Institute of Procedure Law. It is a proposal of a systematic regulation for iberoamerican countries that was inspired in the regulation passed in Brazil. In accordance to this model code of collective processes, there is a classification of collective rights that are differentiated between diffuse or collective and individuals. Unfortunately, in many Latin American countries there is an insufficient regulation of collective processes with many loopholes, which constitutes a denial to the access of justice (including environmental protection rights). See: Carlos Glave 'Modelos incompletos de procesos colectivos en el Perú' (2011) 38 Revista de Análisis Especializado de Jurisprudencia RAE Jurisprudencia 111.

124 Chevron case (n 121) para 47.

However, a following partial award enacted on 12th March 2015 decided[125] in favor of Ecuador that the Lago Agrio litigation was not wholly barred at its inception by res judicata, under Ecuadorian law by virtue of the Settlement Agreement. The reason is that the tribunal found that the Lago Agrio litigation included individual claims resting upon individual rights in a substantially similar way than the Aguinda plaintiff in New York.

Regardless of the characteristic of the claims and protection sought in the Lago Agrio litigation, what could be appreciated is that this is an investment dispute where the solution is based on the understanding of an environmental claim. It is an investment dispute where the analysis is focused on the characterization of environmental rights whether diffuse, collective or individual so as to evaluate the scope of a release contract in relation to an environmental claim.

As a consequence, this case reveals that currently investment disputes are not only taking into account environmental considerations, but also focusing their main analysis on environmental matters.

7.2. *Renco v. Peru.*

Renco is a legal entity organized under the laws of New York, USA. Doe Run Peru (hereinafter, DRP) is a legal entity organized under the laws of Peru, and a subsidiary of Renco. Centromin (a public company from Peru) owned a metallurgical smelting and refining complex in the town of La Oroya in the Andes region of Peru, and in October 1997 DRP acquired the shares of Centromin pursuant to the Stock Transfer Agreement.

Before the acquisition of the complex by DRP, in January 1997 the Programa de Manejo Ambiental (PAMA) was approved and Centromin became obligated to meet certain environmental goals so as to remediate decades of environmental harm during the operation of the complex. The PAMA has an initial period of ten years.

Renco claims[126] that as part of the Stock Transfer Agreement, Centromin retained some of PAMA's obligations. Specifically, those related to the remediation of the area in and around the town of La Oroya as long as there was environmental impact produced from seventy-five years of gaseous and particle emissions from the operation of the complex by Centromin and its predecessors. This is the reason why Renco holds[127] that Peru and Centromin accepted and assumed liability for any and all claims that third parties might bring after DRP acquired the complex. Renco remarks[128] that the complex would not have been acquired without this commitment made by Centromin and Peru. This is relevant for the dispute because citizens of La Oroya sued Renco and DRP before the courts of Missouri seeking damages, and this lawsuit is stalled until the investment arbitration determines whether or not Renco is responsible.

Renco also states[129] that Peru breached its contractual obligations by failing to grant DRP adequate extensions of time to complete its PAMA obligations. According to Renco,[130] there were circumstances of force majeure, including economic alterations during 2002-2008, and the economic crisis in 2009 as well as impositions upon DRP by Peru of additional and

125 Chevron Corporation and Texaco Petroleum Corporation v. The Republic of Ecuador. UNCITRAL, PCA Case No. 2009–23. Decision on Track I–B, 12th March 2015 para 186.

126 The Renco Group Inc. v. Republic of Peru. ICSID Case No. UNCT/13/1. Claimant's Notice of intent to commence arbitration, 29th December 2010 para 3.

127 Ibíd para 3.

128 Ibíd para 52.

129 Ibíd para 7.

130 Ibíd para 46.

onerous environmental and operational obligations. Renco holds[131] that in 2009 this situation caused DRP's lending institution to refuse to renew operational financing, forcing DRP to cease its operations of the complex. Moreover, Renco claims[132] that Peru's unfair treatment might lead to an expropriation of the complex given the fact that DRP was unable to pay its creditors, and in 2010 DRP was placed into an involuntary bankruptcy process where the government of Peru has become the largest creditor.

As it could be noticed, this investment arbitration dispute deals directly with environmental matters. Like in the Chevron case, the arbitration tribunal will decide whether or not the government has breached investment obligations for not assuming the defence and liability in lawsuits initiated by citizens claiming environmental harm and seeking for damages.

Furthermore, in Renco the tribunal must determine if the foreign investor has accomplished environmental obligations. The tribunal will evaluate the fulfillment of DRP PAMA's obligations and the reasons why the original ten years period was extended as well as the consequences of a bankruptcy proceeding entwined with the cost of fulfilling its environmental obligations. Everything will be evaluated in order to determine whether or not DRP suffered an indirect expropriation and unfair treatment.

What it reveals is that this is an investment case where the accomplishment of environmental obligations is the key element of the dispute. Moreover, it could be stated that the alleged unilateral impositions upon DRP of onerous environmental obligations are, in fact, regulations applicable to all investors performing economic activities in Peru. For example, the environmental quality standards of the air regulated with the aim of providing a progressive protection of the environment.[133]

It is interesting because the USA-Peru Trade Promotion Agreement stipulates that a non-discriminatory action is not considered an expropriation when it is designed and applied to protect legitimate public welfare objectives like the environment. Therefore, the tribunal will determine if the impositions of regulations aimed at protecting the environment could be considered a breach of investment obligations.

Therefore, the analysis of the tribunal will be necessarily focused on the accomplishment of environmental obligations and regulations passed with the objective of conserving the environment. This demonstrates that investment disputes cannot be decided without taking into account environmental law as long as the protection of the environment becomes the key element of the dispute.

Renco and Chevron are examples of cases where the foreign investor acquired a business activity with serious environmental liabilities. As a consequence, any problem in relation to the failure to fulfill investment obligations requires a decision on the accomplishment of environmental obligations.

For example, unlike the Santa Elena case where the legal measure was taken so as to prevent environmental or ecological harm (like maintaining the population of species), in the Renco case the environment had been previously damaged for years. Thus, the evaluation is

131 Ibíd para 46.

132 Ibíd para 57.

133 In 1996 (R.M. 315-96-EM/VMM), before DRP acquired the complex, the environmental quality standards for the air were 572 ug/m3 (0.2 ppm) per day and 172 ug/m3 (0.06 ppm) per year. Then in 2001 (Decreto Supremo N° 074-2001-PCM) they were fixed in 365 ug/m^3 per day and 80 ug/m^3 per year. In 2008 (Decreto Supremo N° 003-2008-MINAM) they were fixed again in 80 ug/m^3 per day, and 20 ug/m^3 per day (to be applicable since 2014). However, in 2013 Decreto Supremo N° 006-2013-MINAM), the standards for some specific zones (included La Oroya) were fixed in 80 ug/m^3 per day.

focused on the accomplishment of environmental obligations and regulations related to adaptation and mitigation. This situation reveals that the facts of current investment disputes are based on the application of environmental law.

8. Conclusions

It is a fact that IEL is entwined with other areas of law because environmental disputes are never raised in isolation of other legal fields. FIL is not an exception. As a result, this paper has remarked that in recent years, more investment treaties contain environmental regulations and the number of investment disputes dealing with environmental concerns is continuously increasing.

Through the explanation of some investment case law, this paper has presented an evolution in the connection between FIL and IEL.

A first trend marked by the awards rendered in Santa Elena and Metalclad suggests that environmental concerns do not need to be addressed in investment disputes. A direct expropriation measure, as the one taken in Santa Elena, is a breach of foreign investment rules and must be compensated without regarding the reasons given to take the measure while in Metalclad the definition of expropriation is too broad that it even covers an incidental interference with the use of the property. Moreover, in Metalclad only the mere creation of a National Park is directly considered an expropriation.

Sands highlights the mistake of this trend[134] because it implies that rules of FIL appear to be of a superior level than rules of IEL.

This apparent disconnection is the beginning of an authentic approach between these fields. In accordance to the analysis made in Tecmed, a measure that is claimed as an indirect expropriation could not amount as an infringement of foreign investment obligations if it is a proportional response to a legitimate public concern. It also reveals that investment arbitrators can apply concepts imported from human rights courts that have addressed disputes dealing with measures that affect property rights.

According to Professor Tanzi,[135] other arbitration awards have also focused their analysis on trying to achieve a balance between the foreign investment interests and the public interest of the host state. Professor Tanzi highlights that it happens in Suez v. Argentina in 2010, Glamis Ltd. v. USA in 2009, Azurix Corp. v. Argentina in 2006, LG&E Energy v. Argentina in 2006 and in Tecmed.

Furthermore, in Methanex and Chemtura there is a more sophisticated analysis that implies a connection and balance between FIL and IEL. In Methanex, a sovereign state could issue a regulatory measure that affects an investment, but it is not a compensable expropriation because it is a valid exercise of its policy powers. Precisely, it would be a valid exercise of its powers if the objective of the measure is to protect the environment. This is clearly a rejection of the broad definition of expropriation made in Metalclad.[136]

Moreover, in Chemtura, the policy powers doctrine is also applicable when it comes to analyzing targeted measures. The cancellation of a registrant is a measure that directly affects

134 Sands (n 2), 'Litigating Environmental Disputes: Courts, Tribunals and the Progressive Development of International Environmental Law' 9.

135 Atila Tanzi 'Recent Trends in International Investment Arbitration and the Protection of Human Rights in the Public Services Sector' in N Boschiero et al. (eds), International Courts and the Development of international Law (TMC Asser Press 2013) 595.

136 Subedi (n 99) 162.

an investment, but could not be a compensable expropriation and an infringement of foreign investment rules if it was taken by a state as a valid exercise of its policy powers.

Furthermore, Chevron and Renco reveal that recent investment disputes are based on the determination of environmental rights and the analysis of environmental obligations. Currently, foreign investors are performing economic activities with several environmental liabilities, and thus the terms of its investment obligations are taken in regards to environmental regulations and obligations. As a consequence, any dispute that might arise out of these activities is intrinsically related to the application of environmental law. This reveals that the current characteristics of investment disputes are taking the application of environmental law in investment disputes to a next level where the evaluation of environmental considerations are a key element to decide on the merits of the investment dispute.

As part of the conclusion of this paper, it is important to mention some consequences of the described progressive connection between FIL and IEL developed in the case law. Firstly, it could lead to the creation of stronger environmental regulations in investment treaties. Subedi[137] notes that after Methanex, some investment treaties and negotiations of investment treaties are evaluating to narrow the scope of indirect expropriations in regards to the protection of the environment.

Secondly, the consideration of IEL is important for the success of the foreign investment mechanisms of disputes resolutions. Sometimes arbitration awards are challenged before national courts on the grounds of public policy reasons. Even under the rules of ICSID, where awards are considered to be automatically enforced, there are some problems with the recognition and enforcement of arbitration awards by national courts.[138] When the environmental obligations are not taken into account, these problems could be more frequent.[139] Then it could be argued that one consequence of applying IEL in foreign investment disputes is to secure the recognition, validation and enforcement of investment arbitration awards.

Finally, the consideration of IEL in investment disputes contributes to a more inclusive investment dispute resolution mechanism. As a result, it is not strange that recent academic papers[140] are proposing new procedural forms in international investment arbitrations that include the participation of affected populations.

137 Some examples mentioned by Subedi are the Canada – Peru BIT of 2006 and the draft between EU and Pacific members of the ACP countries of June 2006. According to this author, the former goes much further narrowing the scope of indirect expropriations while the latter admits regulatory measures as non-compensable expropriations. Ibíd 162.

138 To review the problems of enforcement of investment awards, and in particular the problems in the recognition and enforcement of ICSID awards, see: Julian Lee, Loukas Mistelis and Stefan Kroll Comparative International Commercial Arbitration (Kluwer Law International 2003) 187; Edward Baldwin, Mark Kantor and Michale Nolan, 'Limits to Enforcement of ICSID Awards' (2006) Journal of International Arbitration 23; James Barrat and Michael Margarita 'The Automatic Enforcement of ICSID Awards: The Elephant in the Room?' (2014) The European, Middle Eastern an African Arbitration Review. <http://globalarbitrationreview.com/reviews/58/sections/202/chapters/2274/> accessed 15 June 2014.

139 Precisely part of Metalclad award was annulled by the Supreme Court of British Columbia.

140 Jose Daniel Amado, 'From Investors' Arbitration to Investment Arbitration; A Mechanism for Allowing the Participation of Host State Populations in the Settlement of Investment Conflicts' (2014) University of Cambridge Legal Studies Research Paper Series 8/2014 <http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2385776> accessed 16 June 2014.

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