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Paris Arbitration Week Recap: The Fair and Equitable Treatment Standard – Update and Perspectives

Ioana Knoll-Tudor (Jeantet) · Thursday, April 14th, 2022

As part of the 2022 Paris Arbitration Week, Jeantet organised a round table on "*The Fair and Equitable Treatment Standard: Update and Perspective*". The panel was composed of Yuriy Pochtovyk *(Legal Official, Energy Charter Secretariat)*, Prof. Kaj Hobér *(Associate Member, 3 Verulam Buildings)*, Barton Legum *(Partner, Honlet Legum Arbitration)*, Irena Alajbeg *(Croatian Ministry of Foreign and European Affairs)*, Nir Deutsch *(Legal Adviser, Israeli Ministry of Justice)*, and Lucia Raimanová *(Partner, Allen & Overy)* and was moderated by Dr Ioana Knoll-Tudor *(Partner, Jeantet)*.

In recent years, the drafting of "Fair and Equitable Treatment" (FET) provisions has considerably evolved. While the first-generation FET clauses only referred to the FET standard alone, or sometimes in connection with international law and/or other standards of treatment, today's clauses are more diverse and sophisticated. This evolution is illustrated both by new BITs as well as the ongoing modernization process of the Energy Charter Treaty (ECT). Our understanding of these changes increases in time, however despite the impact of these changes on the outcome of cases, certainty regarding both the level of protection provided to investors by FET articles and the method of their interpretation by tribunals has not been reached yet. These and other topics were put forward before the panel and addressed by the speakers as summarized below.

Status of the ECT Modernization Negotiations

The ECT is the most frequently invoked investment agreement. Currently the ECT Secretariat is aware of 145 ECT-based cases, concluded or still pending. From the 83 cases on which such information is available, a FET breach is alleged in 77 of them. A study conducted by the ECT Secretariat concerning investor grievances in the renewable energy sector identifies 119 publicly known cases brought based on IIAs. From the 60 cases on which public information is available, a breach of FET is alleged in 51. The FET is, undeniably, the most litigated substantive protection standard.

The current text of the FET clause in the ECT (Article 10.1) is open-ended and neither links the FET to international law nor to the minimum standard of international law. Some tribunals, especially when scrutinising in the context of legitimate expectations, found that the ECT put a particular emphasis on the stability of the business and legal framework, mainly by reference to

Article 2 ECT as well as to the first sentence of Article 10.1. A number of tribunals also found that denial of justice, breach of due process, discrimination on wrongful grounds, arbitrariness, harassment and coercion may amount to violations of the FET.

In November 2019, the Energy Charter Conference established the Modernisation Group to start negotiations on the modernisation of the ECT, including the topic of the definition of FET. 11 negotiation rounds already took place (in 7 of them the definition of FET was discussed) and two more rounds are scheduled for April and May, before Contracting States will try to reach an agreement in principle in June.

At this stage, only the EU has made available its text proposal for Article 10. The Contracting Parties keep moving forward with the negotiations of the definition of FET. Recently, the Modernisation Group agreed to discuss FET in conjunction with the umbrella clause, as well as advanced their discussions on the introduction of a stand-alone article on the right to regulate.

Historical Perspective on the ECT

During the negotiations, parties intended to craft a *magna carta* for energy, covering not only investment protection but also trade (which has now been replaced by the WTO treaties), environment (provisions not really enforceable under the ECT) and transit.

However, despite such a broad scope, negotiations were wrapped up in a haste, resulting in many provisions remaining unclear or lacking thorough legal analysis, like Article 10. The panel welcomed the current modernization negotiations, while noting that no treaty is perfect. The provisions of the Charter will thus continue to be interpreted on the basis of the Vienna Convention (VCLT), in conformity with the purpose of the treaty (Article 2 ECT).

Evolution of FET in the First NAFTA Cases

The panel has then drawn attention to the evolution of the FET standard in f the first NAFTA cases. Until the *Loewen*, *Mondev* and *Methanex* cases brought against the U.S., no formal position had been taken by the U.S. government on the content of NAFTA's Article 1105. In these arbitrations, each claimant used the ordinary meaning approach of Article 31 VCLT. In the absence of any case law, at the time, the task of the arbitral tribunals was therefore to assess the fairness of the incriminated measures.

To the extent that Article 1105 framed the FET as subordinate to international law and the international minimum standard, NAFTA parties used it as a basis for resisting the ordinary meaning approach that was not generally available for contemporaneous European investment treaties. The Notes of Interpretation of Article 1105 adopted by the NAFTA Free Trade Commission in 2001 confirmed this position in a binding instrument. Although this interpretation did not end the debate on the obligations imposed by Article 1105, it provided an analytically rigorous structure for debating the content of the FET – a debate that continues until today.

Approach of a EU Member State (Croatia) and a Non-EU Country (Israel) Regarding Drafting Formulations of FET Clauses

Drafting of FET Clauses in Croatian BITs

Croatia concluded most of its BITs in the mid-90's when there was neither sufficient awareness of the content of the FET nor case law to clarify its meaning. Indeed, it was only through case law that Croatia realized that an open-ended FET clause could be interpreted broadly.

Before Croatia's accession to the EU, Croatian BITs incorporated four different approaches to the FET: (i) 6% did not contain a FET clause, (ii) 30% contained a FET clause without reference to international law or other criteria, (iii) 25% connected the FET to the national treatment or MFN standards, and (iv) 39% referred to the FET in accordance with international law.

During the EU accession process, two arbitrations were initiated against Croatia, both invoking a FET breach. As a consequence, Croatia reconsidered its investment policy aiming at (i) clarifying existing standards; (ii) ensuring more consistency and predictability in the tribunals' interpretation and (iii) the right balance between protecting investors' rights and preserving the State's right to regulate.

One of the questions that remains open is the way in which FET clauses of old BITs should be dealt with. Two solutions are under consideration: amending these provisions in order to narrow their scope, or adopting an interpretative statement.

Drafting of FET Clauses in Israeli BITs

Moving on to the position of a non-EU Member State, the example of Israel and its position towards the FET also confirmed a clear evolution in terms of drafting technique. Israel's existing FET article formulations were discussed in connection with their interpretation by arbitral tribunals. The first example was the FET clause of the Israel-Georgia BIT (1995) which could be considered as one of the "first-generation" style articles. On the basis of this BIT, in the *Fuchs v. Georgia case*, the tribunal mentioned that Georgia claimed that the FET was synonymous with the customary international law standard while the investor claimed that the FET could be breached by a conduct of a "*less egregious nature*" and decided that the FET clause allowed the investor to develop legitimate expectation that the State "*would conduct itself vis-à-vis his investment in a manner that was reasonably justifiable and did not manifestly violate basic requirements of consistency, transparency, even-handedness and non-discrimination*".

A second example related to the Israel-Guatemala BIT (2006) which contained a more "modern" version FET clause, referring in its drafting to what could be considered a rather vague notion of providing the FET standard "*in accordance with the provisions of this agreement*". In *IC Power v. Guatemala*, the arbitral tribunal was asked to determine whether actions of national courts could amount to a FET breach under the Israel-Guatemala BIT, even if they could not be considered as "denial of justice". The tribunal decided that "*such conclusion cannot be extended to the FET standard in the Treaty, which is agreed sets a lower threshold for a violation than customary minimum…*". With doubts raised regarding the aforementioned agreement, the award could be read in a manner the renders the FET standard in the BIT, when not directly qualified to the minimum standard of treatment, as perhaps containing more than the customary minimum standard.

Israel's most recent BITs contain a variety of drafting formulations: the Israel-Japan BIT (2017)

contains a FET clause referring to customary international law, the Israel-South Korea BIT (2020) contains a FET clause referring to denial of justice and the Israel-UAE BIT (2021), took over the CETA model drafting, with a closed list approach. These examples of drafting styles and tribunals decisions containing various positions by disputing parties raises the question of whether these drafting formulations differ from each other in the level of protection that they provide or if they mean the same and governments were just reacting to the tribunals' interpretation. As suggested by the speakers, a possible answer may be found in the dynamics of treaty negotiations, and the understanding that international relations and cultural elements add a challenge to the question of renegotiating treaties and clarifying what previous treaties have meant.

Different Drafting Formulations and the Impact on Case Outcome

The final intervention proposed to look at three drafting formulations of FET clauses and apply each of them to a mock scenario, with an aim to consider the effects of these drafting formulations on the outcome of the case.

The first drafting formulation was extracted from the Albania-Israel BIT (1996) and reads: "*Investments* (…) *shall be accorded fair and equitable treatment*". This unqualified clause gives the tribunal some leeway to balance the State and investor's interest when determining what is fair and equitable.

In the second drafting formulation**,** the Canada-China BIT (2012), the FET clause was linked to the minimum standard of treatment. Tribunals have neither searched for general State practice nor for *opinio juris* to determine the content of minimum standard of treatment, as this is very difficult to do in practice. Rather, on the whole, they ascribed a meaning to the minimum standard of treatment. Although tribunals have not been consistent in their approach, the interpretation of the minimum standard of treatment tends to be narrower and the liability threshold higher.

The third drafting formulation was that of the CETA Article 8.10, favoured by the EU. Here, the intent is to limit the tribunals' interpretative function and move away from the FET as a standard to the FET as a closed list of possible behaviours. At the same time, CETA Article 8.9 exempts a Contracting Party from liability if it regulates in pursuit of legitimate policy objectives. Therefore, a breach would be potentially more difficult to establish than under the minimum standard of treatment.

Conclusion

The panel concluded that the wording of FET clauses will continue to be of utmost importance.

Finally, the speakers were asked whether one should aim for a uniform level of protection or rather a uniform method of interpretation, with clearly identified criteria, providing more predictability in the interpretation of the FET standard, both for investors and for States. A more uniform method of interpretation was favoured by the majority of panellists.

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