

**UNIVERSITY of
STIRLING**



**The Challenges of Applying the Principle of Proportionality in Striking a Balance in
the Investor-State Relationship**

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From the International and Chinese Perspectives

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Declaration

I, Cheng Chen, do hereby declare that the thesis entitled "The Challenges of Applying the Principles of Proportionality in Striking a Balance in the Investor-State Relationship – From the International and Chinese Perspectives", or any part of the thesis has been composed solely by myself for the award of Doctor of Philosophy at the University of Stirling. The thesis, or any portion thereof, has not been submitted for the award of any other degree or qualification of this or any other university or institution.

Signature Cheng Chen

Date 30/06/2022

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Abstract

One significant concern in the current international investment is the imbalance between foreign investors' interests and the host state's right to regulate in the public interest. Broad investment protections are enjoyed by foreign investors, such as the protection of legitimate expectations included in fair and equitable treatment, whereas the host state's regulatory power for the public interest is somewhat restricted. How to strike a balance in such an imbalanced investor-state relationship is being considered by states, including China, to deliver their sustainable foreign investment.

Proportionality, which first originated in Germany, has been noted by scholars as an appropriate tool to strike a balance between private rights and the state's regulatory power by three consecutive assessments of suitability, necessity, and proportionality *stricto sensu*, respectively. However, how to bring this method into the settlement of investor-state disputes and how to apply it to balance conflicting values between foreign investors and the host state raise debates. Due to its failure to fulfil the requirements of Article 38 (1) of the Statute of the International Court of Justice, the application of proportionality depends on the interpretation of each case. Proportionality can be applied if it is expressed in the case-related treaty or included in the host state's domestic law, which is the applicable legal instrument of the case. A systemic interpretative method is then needed to apply proportionality in investor-state arbitration.

This research tests the possibility and practicability of applying proportionality in striking a balance between the investor-state relationship from the international and Chinese perspectives to ascertain an appropriate method to balance the investor-state relationship in international investment, particularly in Chinese international investment. Due to its dual role in international investment, a balanced investor-state relationship is in China's interest. The

approach it adopts may also benefit the capital importer and exporter.

Abbreviations

Abs-Shawcross Draft Convention	Draft Convention on Investments Abroad
ASEAN	Association of Southeast Asian Nations
BIT	Bilateral Investment Treaty
BLEU	Belgium-Luxembourg Economic Union
CETA	Comprehensive Economic and Trade Agreement
CSR	Corporate Social Responsibility
FDI	Foreign Direct Investment
FET	Fair and Equitable Treatment
FTA	Free Trade Agreement
FTC	Free Trade Commission
GATT	General Agreement on Tariffs and Trade
ICCPR	International Covenant on Civil and Political Rights
ICESCR	International Covenant on Economic Social and Culture Rights
ICJ	International Court of Justice
ICJ Statute	The Statute of the International Court of Justice
ICSID	International Centre for Settlement of Investment Disputes
ICSID Arbitration Rules	Rules of Procedure for Arbitration Proceedings
ICSID Convention	Convention for the Settlement of Investment Disputes between States and Nations of Other States
IIA	International Investment Agreement
ILA	International Law Association
ILC	International Law Commission
ISA	Investor-State Arbitration
ISD	Investor-State Dispute
ISDS	Settlement of Investor-State Disputes
MFN	Most-Favored-Nation
MOFCOM	Ministry of Commerce of the People's Republic of China
MST	Minimum Standard of Treatment
NAFTA	North American Free Trade Agreement
NPC	National People's Congress
NT	National Treatment
OBOR	One Belt One Road
OECD	Organisation for Economic Co-operation and Development
OECD Draft Convention	Draft Convention on the Protection of Foreign Property
PRC	People's Republic of China
PSB	Public Security Bureau
SAR	Special Administrative Regions
SCNPC	Standing Committee of the National People's Congress
SPC	Supreme People's Court
TIT	Trilateral Investment Treaty
UDHR	Universal Declaration of Human Rights
UN	United Nations
UNCITRAL	United Nations Commission on International Trade

	Law
UNCTAD	United Nations Conference on Trade and Development
US	United States
US PPI	United States Producer Price Index
Vienna Convention	Vienna Convention on the Law of Treaties
Wrongful Act	ILC's Articles on Responsibility of States for Internationally Wrongful Act
WTO	World Trade Organisation

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Chapter 1

Introduction

1.1 The Conflicting Values between Foreign Investors and the Host State

With the development of globalisation, international investment has dramatically increased. States play a dual role at the international level. As a sovereign country, a state wields the inherent power to regulate in the public interest.¹ At the same time, a host state participating in international investment has obligations *vis-à-vis* foreign investors. A balance between the values of foreign investors and the host state is needed to deliver sustainable foreign investment.

States aim to enhance foreign investors' confidence in making investments and attract more investment and capital by providing various treatments. Their obligations include the protection and promotion of foreign investments provided and guaranteed in relevant legal instruments, like the concluded international investment agreements (IIAs). However, as clarified by the United Nations Conference on Trade and Development (UNCTAD), no definitive causal link exists between the conclusion of IIAs and the attracted foreign direct investment (FDI).² Beyond the concluded treaties, other factors, such as the labour force and the market size in a state, also affect foreign investors' decisions on investment.³ By contrast, based on practice, investment protections granted to foreign investors can restrict the host state's right to regulate in the public interest, to a greater or lesser extent.⁴ The host state can face the risk of being accused by foreign investors of a violation of its treaty obligations for measures it takes to react to its changing circumstances.

The primary example here is a set of Argentinian cases arising from the country's economic crisis of 2001/2.⁵ As reflected in these cases, conflicts occurred when the state took measures to respond to the crisis. Although the implemented measures aimed to protect public interest, they were regarded as violations of treaty obligations *vis-à-vis* foreign investors. Such conflicts between the rights of foreign investors and the host state may be accentuated due to Covid-19, which raises a set of issues and various (sometimes extreme) measures taken by each state to respond to the pandemic, such as lockdown and export bans.⁶ For example, affected French investors initiated a claim under the Convention on the

¹ J. E. Viñuales, 'Sovereignty in Foreign Investment Law' in Zachary Douglas, Joost Pauwelyn, & Jorge E. Viñuales (eds), *The Foundations of International Investment Law: Bringing Theory into Theory* (OUP 2014) 327.

² UNCTAD, *The Role of International Investment Agreements in Attracting Foreign Direct Investment to Developing Countries* (2009) xiii.

³ *ibid* 6.

⁴ *ibid* xiv.

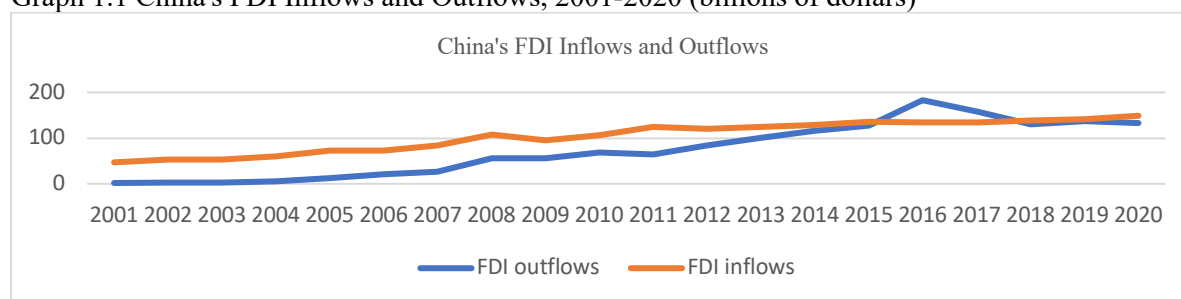
⁵ Based on the chronological order, these cases include *CMS v. Argentina*, ICSID Case No. ARB/01/8, Award, 12 May 2005; *LG&E v. Argentina*, ICSID Case No. ARB/02/1, Decision on Liability, 3 October 2006; *Enron v. Argentina*, ICDIS Case No. ARB/01/3, Award, 22 May 20007; *Sempra v. Argentina*, ICSID Case No. ARB/02/16, Award, 28 September 2007; *Continental v. Argentina*, ICSID Case No. ARB/03/9, Award, 5 September 2008; *El Paso v. Argentina*, ICSID Case No. ARB/03/15, Award, 31 October 2011. See generally in Chapter Five, which mainly discusses the application of the principle of proportionality in investor-state arbitration (ISA).

⁶ UNCTAD, 'Investment Policy Monitor—Investment Policy Responses to the Covid-19 Pandemic' [2020] Investment Policy Monitor 1, 2.

Settlement of Investment Disputes between States and Nations of Other States (ICSID Convention)⁷ against Chile due to the measures it taken to react to the pandemic.⁸

Meanwhile, non-investment values have also received increased attention. In this situation, a balance between the protection afforded to foreign investors and the host state's need to ensure sustainable investment must be addressed. No state is an exception to such a need for sustainable foreign investment, including China. Since it implemented the "Open Door" policy in the late 1970s,⁹ China has transitioned from a pure recipient of FDI to a leading participant from capital-importer and exporter perspectives. As presented in Graph 1.1, both China's inbound and outbound FDI have experienced dramatic development in the past two decades.

Graph 1.1 China's FDI Inflows and Outflows, 2001-2020 (billions of dollars)¹⁰



In its 2021 World Investment Report, the UNCTAD stated that China was both the world's second-largest recipient of FDI and the largest investor in 2020.¹¹ The data, which is collected by the Ministry of Commerce of the People's Republic of China (MOFCOM), present the top 15 countries or regions of China's inbound FDI¹² and the top 20 countries or regions of China's outbound FDI¹³ in 2020. This

⁷ ICSID Convention (1965).

⁸ International Institute for Sustainable Development (IISD), 'An Online Journal on Investment Law and Policy from A Sustainable Development Perspectives' (2021) 12 (1) Investment Treaty News <<https://www.iisd.org/system/files/2021-04/iisd-itn-march-2021-english.pdf>> last accessed 23 June 2022. Another example, Peru may face multiple ICSID claims brought against it due to the suspension of the collection of toll fees on the country's road network, which was one emergency measure taken by it in response to Covid-19, see Cosmo Sanderson, 'Peru Warned of Potential ICSID Claims over Covid-19 Measures' (*Global Arbitration Review*, 9 April 2020) <<https://globalarbitrationreview.com/article/peru-warned-of-potential-icsid-claims-over-covid-19-measures>> last accessed 23 June 2022.

⁹ Wenhua Shan & Norah Gallagher, *Chinese Investment Treaties Policies and Practice* (Yanru Wei & Qingling Li trs, OUP 2009) 6 [in Chinese].

¹⁰ Data collected from MOFCOM, 'Statistic-Foreign Investment' (*MOFCOM*) <<http://english.mofcom.gov.cn/article/statistic/foreigninvestment/>> [in Chinese] last accessed 23 June 2022.

¹¹ UNCTAD, *World Investment Report 2021—Investing in Sustainable Recovery* (2021) 4-7.

¹² MOFCOM, *Statistical Bulletin of Foreign Direct Investment in China* (2021) 8 [in Chinese]. The total inflow is \$ 140.8 billion. According to the descending order, the top 15 countries or regions of China's inbound FDI include, Hong Kong (China), Singapore, Br. Virgin Is., the Republic of Korea, Japan, Cayman Is., Netherlands, United States (US), Macao (China), Germany, Taiwan (China), United Kingdom (UK), Samoa, Switzerland, France.

¹³ MOFCOM, National Bureau of Statistics & State Administration of Foreign Exchange, *2020 Statistical Bulletin of China's Outward Foreign Direct Investment* (China Commerce and Trade Press 2021) 17 [in Chinese]. The total outflow is \$ 141.14 billion. According to the descending order, the top 20 countries or regions of China's outbound FDI include, Hong Kong (China), Cayman Is., Br. Virgin Is., US, Singapore, Netherlands, Indonesia, Sweden, Thailand, Vietnam, United Arab Emirates, Laos, Germany, Malaysia, Australia, Switzerland, Cambodia, Pakistan, UK, Macao (China).

clarifies the current situation and general trend of China's international investment from the dual role of the host state and investor perspectives.

The significance of China in international investment can also be observed in its concluded IIAs and investor-state disputes (ISD). From its first bilateral investment treaty (BIT) concluded with Sweden in 1982¹⁴ to its latest BIT signed with Turkey in 2015,¹⁵ China has signed 145 BITs with almost 130 countries.¹⁶ As listed in Tables 1.2 and 1.3 below, by the end of February 2022, China has been involved in 28 ISDs, including 19 cases brought by Chinese investors and 9 cases brought against China.¹⁷

Table 1.2 Investor-State Disputes (China as the Home State of Investors)

No.	Case Name	Case No.	Year of Initiation	Status of the Case	Respondent State	Applicable Instrument
1	Huawei v. Sweden	ICSID Case No. ARB/22/2	2022	Pending	Sweden	China-Sweden BIT (1982)
2	Qiong Ye and Jianping Yang v. Cambodia	ICSID Case No. ARB/21/42	2021	Pending	Cambodia	ASEAN-China Investment
3	Alpene Ltd v. Malta	ICSID Case No. ARB/21/36	2021	Pending	Malta	China-Malta BIT (2009)
4	Beijing Everyway Traffic Ghana v. Ghana	N/A	2021	Pending	Ghana	China-Ghana BIT (1989)
5	Wang Jiazhu v. Finland	N/A	2021	Pending	Finland	China-Finland BIT (2004)
6	Shift Energy v. Japan	N/A	2020	Pending	Japan	Hong Kong-Japan BIT (1997)
7	Wang and others v. Ukraine	N/A	2020	Pending	Ukraine	China-Ukraine BIT (1992)
8	Fengzhen Min v. Korea	ICSID Case No. ARB/20/26	2020	Pending	Korea	China-Korea, Republic of BIT (2007)
9	Jetion and T-Hertz v. Greece	N/A	2019	Withdrawn	Greece	China-Greece BIT (1992)

¹⁴ China-Sweden BIT (signed 29 March 1982, entered into force 29 March 1982).

¹⁵ China-Turkey BIT (signed 29 July 2015, entered into force 11 November 2020).

¹⁶ 'China's Bilateral Investment Treaty' (MOFCOM)

<<http://tfs.mofcom.gov.cn/article/Nocategory/201111/20111107819474.shtml>> [in Chinese] last accessed 2 May 2022.

'China-Bilateral Investment Treaties (BITs)' (*Investment Policy Hub*) <<https://investmentpolicy.unctad.org/international-investment-agreements/countries/42/china>> last accessed 2 May 2022. These data are provided by the MOFCOM of China and the UNCTAD, but they are not exactly identical. The MOFCOM of China provides statistics as to China's enforced BITs. However, the Chinese BITs provided by the UNCTAD are not only enforced but also merely signed and terminated. The lists of Chinese BITs are provided in Chapter Six, see Tables 6.1, 6.2, and 6.3.

¹⁷ 'China' (*Investment Policy Hub*) <<https://investmentpolicy.unctad.org/investment-dispute-settlement/country/42/china>> last accessed 23 June 2022. 'China' (ICSID) <<https://icsid.worldbank.org/cases/case-database>> last accessed 23 June 2022.

10	Sanum v. Laos (II)	ICSID Case No. ADHOC/17/1	2017	Pending	Laos	China-Laos BIT (1993)
11	Zhongshan Fucheng v. Nigeria	N/A	2017	Decided in favour of investor	Nigeria	China-Nigeria BIT (2001)
12	Standard Chartered Bank v. Tanzania	ICSID Case No. ARB/15/41	2015	Decided in favour of investor	Tanzania	Contract
13	Beijing Urban Construction v. Yemen	ICSID Case No. ARB/14/30	2014	Settled	Yemen	China-Yemen BIT (1998)
14	Sanum v. Laos (I)	PCA Case No. 2013-13	2012	Decided in favour of State	Laos	China-Laos BIT (1993)
15	Ping An v. Belgium	ICSID Case No. ARB/12/29	2012	Jurisdiction declined	Belgium	BLEU-China BIT (1984) BLEU-China BIT (2005)
16	Philip Morris v. Australia	PCA Case No. 2012-12	2011	Jurisdiction declined	Australia	Australia-Hong Kong BIT (1993)
17	Standard Chartered Bank v. Tanzania Electricity Supply Company Limited	ICSID Case No. ARB/10/20	2010	Decided in favour of investor	Tanzania	Contract
18	Beijing Shougang and others v. Mongolia	PCA Case No. 2010-20	2010	Jurisdiction declined	Mongolia	China-Mongolia BIT (1991)
19	Tza Yap Shum v. Peru	ICSID Case No. ARB/07/6	2007	Decided in favour of investor	Peru	China-Peru BIT (1994)

Table 1.3 Investor-State Dispute (China as the Respondent State)

No.	Case Name	Case No.	Year of Initiation	Status of the Case	Home State of Investor	Applicable Instrument
1	Eugenio Montenero v. China	N/A	2021	Pending	Switzerland	China-Switzerland BIT (2009)
2	Goh Chin Soon v. China (II)	PCA Case Np. 2021-30	2020	Pending	Singapore	China-Singapore BIT (1985)
3	AsiaPhos v. China	ICSID Case No. ADM/21/1	2020	Pending	Singapore	China-Singapore BIT (1985)
4	Goh Chin Soon v. China (I)	ICSID Case No. ARB/20/34	2020	Concluded	Singapore	China-Singapore BIT (1985)

5	Macro Trading v. China	ICSID Case No. ARB/20/22	2020	Concluded	Japan	China-Japan BIT (1988)
6	Jason Yu Song v. China	PCA Case No. 2019-39	2019	Pending	United Kingdom	China-United Kingdom BIT (1986)
7	Hela Schwarz v. China	ICSID Case No. ARB/17/19	2017	Pending	Germany	China-Germany BIT (2003)
8	Ansung China v. China	ICSID Case No. ARB/14/25	2014	Decided in favour of State	Korea	China-Korea BIT (2007)
9	Ekran China v. China	ICSID Case No. ARB/11/15	2011	Settled	Malaysia	China-Malaysia BIT (1988) China-Israel BIT (1995)

The "One Belt One Road" (OBOR) initiative, which was launched by China's President Xi in 2013 to enhance Chinese international cooperation, provides a clear context and reasoning for China to act more proactively in the protection and promotion for both its inbound and outbound FDI. It is also in China's interest to find a fair balance between the rights of foreign investors and those of the host state, quite simply because it has such a big stake in both roles. In other words, a balance in the investor-state relationship is not only significant for the context of international investment as a whole but also vital for participating states, not least China.

Based on states' practices, proportionality, an approach rooted in the domestic legal system, has been noted as a possible tool to balance the conflicting values of foreign investors and host states.¹⁸ However, due to its domestic origin, the debate has centred on whether proportionality can be applied in international investment and accepted by domestic courts and how it should be adopted to balance the conflicts. In this study, the researcher aims to clarify the challenges of applying the principle of proportionality in striking such a balance first and then address relevant issues, particularly considering Chinese international investment. Due to the undefined legal status of proportionality in the Chinese domestic legal system, it is also described as a notion or concept in the current research.

1.2 Literature Review

¹⁸ Gebhard Bücheler, *Proportionality in Investor-State Arbitration* (OUP, 2015) 2. Benedict Kingsbury & Stephan W. Schill, 'Investor-State Arbitration as Governance: Fair and Equitable Treatment, Proportionality and Emerging Global Administrative Law' [2009] New York University School of Law Public Law & Theory Research Paper Series Working Paper No. 09-46, 21-40. Benedict Kingsbury & Stephan W. Schill, 'Public Law Concepts to Balance Investors' Rights with State Regulatory Actions in the Public Interest-the Concept of Proportionality' in Stephan W. Schill (ed), *International Investment Law and Comparative Public Law* (OUP 2010) 75-104. See generally in Prabhash Ranjan, 'Using the Public Law Concept of Proportionality to Balance Investment Protection with Regulation in International Investment Law: A Critical Appraisal' (2014) 3 Cambridge Journal of International & Comparative Law 853. Caroline Henckels, 'Indirect Expropriation and the Right to Regulate: Revising Proportionality Analysis and the Standard of Review in Investor-State Arbitration' (2012) 15 Journal of International Economic Law 223, 228-9.

1.2.1 The Principle of Proportionality and Doubts

Proportionality is a principle rooted in the domestic legal system and has been utilised in many different jurisdictions. The primary debate over its application in international investment is whether and how such a tool can be brought into the settlement of investor-state disputes (ISDS) regime. Is it a provision of the case-related treaty, an international custom, or a general principle of law? In other words, the issue is whether proportionality can fulfil the requirements stipulated in Article 38 (1) of the Statute of the International Court of Justice (ICJ Statute) to be an international custom or a general principle of law.¹⁹ Alternatively, whether it can be applied in international investment depends on the specific wording of the legal instrument applicable to the case.

Based on Barak's investigation, the application of proportionality has crossed the economic maturity divide between different states, to include both developed and developing countries.²⁰ Its application has also crossed borders, which can be seen from Germany to South Africa, from Europe to Asia.²¹ Therefore, it could appear that proportionality's general application has been ubiquitous, fulfilling the requirement of general practice. This opinion is denied by Vadi, who pointed out that the practice of certain states cannot represent the whole.²² Instead of the quantity, the quality of those states whose practices contribute to the transformation of the questioned principle is emphasised by the International Law Association (ILA) with the phrase "specially affected states".²³

The "specially affected states" vary on the basis of each particular circumstance.²⁴ In the context of international investment, they are those who have concluded most IIAs or been involved in most invest-state disputes.²⁵ Based on these criteria, leading states, including Germany, China, and the US, have been named. However, as noted by Vadi, the legal status of proportionality in the legal system of the latter two remains uncertain.²⁶ No debate arises from the widespread application of proportionality in different states, but whether it has been a general practice in the sense of Article 38 (1) of the ICJ Statute, which should be supported by the practice of sufficient specially affected states in international

¹⁹ ICJ Statute Article 38 (1).

²⁰ Aharon Barak, *Proportionality Constitutional Rights and Their Limitations* (CUP 2012) 181-202. Moshe Cohen-Eliya & Iddo Porat, *Proportionality and Constitutional Culture* (CUP 2013) 2. Moshe Hirsch, 'Sources of International Investment Law' [2011] International Law Association Study Group on the Role of Soft Law Instruments in International Investment Law 2011, 23-4 <https://papers.ssrn.com/sol3/papers.cfm?abstract_id=1892564> last accessed 26 April 2022.

²¹ *ibid.*

²² Valentina Vadi, *Proportionality, Reasonableness and Standards of Review in International Investment Law and Arbitration* (EE 2018) 120. An example for the selected legal system is the German domestic legal system.

²³ ILA, 'Final Report of the Committee Statement of Principles Applicable to the Formation of General Customary International Law' (London Conference 2000) 26. Patrick Dumberry, *The Formation and Identification of Rules of Customary International Law in International Investment Law* (CUP 2016) 133-8. UN, 'Report of the International Law Commission' (2018) UN doc. A/73/10, 136-7.

²⁴ *ibid.*

²⁵ Dumberry, *The Formation* (n 23) 136. UN (n 23) 137.

²⁶ Vadi, *Proportionality* (n 22). see also N. Jansen Calamita, 'The Principle of Proportionality and the Problem of Indeterminacy in International Investment Treaties' in Andrea K. Bjorklund (ed), *Yearbook on International Investment Law and Policy 2013-2014* (OUP 2015) 168.

investment, is questioned.

It is further argued that, in practice, the application of proportionality varies from one country to another.²⁷ As noted by Barak, some states apply proportionality in its structured approach, while others selectively utilise its components.²⁸ For example, proportionality as adopted in Germany is strictly based on the internal logical sequence of its components, namely suitability, necessity, and proportionality *stricto sensu*.²⁹ Different from others, proportionality *stricto sensu* is a value-oriented factor focusing on the real balance between conflicting values. In the limited number of Chinese administrative law cases in which proportionality was used to review the specific administrative act, it has been applied differently even in the same jurisdiction.³⁰ As reflected in these cases, importantly, proportionality was said to fail to be "consistent and uniform practice", which is required in the ICJ Statute.

Doubts also remain on whether proportionality is accepted as law and whether it, a principle that originated at the national level, can be applied at the international level. Due to such doubts, it may be too early to conclude that proportionality is an international custom or a general principle of law. Consequently, its application in international investment may have to rely on the specific wording of the applicable legal instrument.

Concerning the applicable law for the ISD, Article 42 (1) of the ICSID Convention stipulates that,

The tribunal shall decide a dispute in accordance with *such rules of law as may be agreed by the parties*. In the absence of such agreement, the tribunal shall apply *the law of the contracting state party to the dispute* (including its rules on the conflict of laws) and *such rules of international law as may be applicable*.³¹ [italic added]

Some IIAs, like the China-Mongolia BIT (1991),³² contain a similar provision of the applicable law for the ISD. As it stipulates,

The tribunal shall adjudicate in accordance with *the law of the Contracting State to the dispute accepting the investment including its rules on the conflict of laws, the provisions of this Agreement* as well as *the generally recognised principle of international law accepted by both Contracting States*.³³ [italic added]

²⁷ Barak (n 20) 132.

²⁸ *ibid*.

²⁹ See 2.5.2.2 in Chapter Two.

³⁰ See 7.5 in Chapter Seven.

³¹ ICSID Convention (n 7) Article 42 (1).

³² China-Mongolia BIT (signed 25 August 1991, entered into force 1 November 1993).

³³ *ibid* Article 8 (7).

Both provisions reflect that the applicable law includes the legal instrument agreed by the parties, the host state's law, and international law. Even though there is no such clause in the IIA, as asserted by the tribunal, the case-related BIT is the applicable law indicated by initiating an ISA under such a treaty.³⁴ In this respect, if the language of the case-related treaty either explicitly or implicitly expresses the notion of proportionality, it can be adopted in the ISDS through the systemic interpretation of the treaty. Alternatively, if proportionality is included in the host state's domestic law, it can be applied to strike a balance in the investor-state relationship.

Nevertheless, in practice, some disputes arise from selecting the applicable law for the ISD, mainly due to the interrelation between international and domestic law. The prime example here is *Wena Hotels v. Uruguay*.³⁵ In this case, the claimant reached two "Lease and Development Agreements" with EHC, a company wholly owned by the Egyptian Government, for two hotels in Egypt. Due to the omissions and actions taken by Egypt, such as the seizure of the hotels and the continual harassment, the claimant alleged that Egypt had violated its treaty obligations, like fair and equitable treatment (FET). The tribunal noted that the applicable law contained the UK-Egypt BIT (1975), the Egyptian Law (the host state's law) and international law.

One disputed point was whether Wena's claims were time-barred.³⁶ As argued by Egypt, according to Article 42 (1) of the ICSID Convention, the tribunal should apply the Egyptian law based on which Wena's claims were time-barred.³⁷ However, that was refused by the tribunal. As noted, there was no specific agreement on the applicable law for the ISD reached by the parties.³⁸ According to the logical sequence of considerations indicated by the wording "in the absence of such agreement" in Article 42 (1): The tribunal should first ascertain whether the parties achieve an agreement on the applicable law; If not, it then applies the host state's law and international law.³⁹ In *Wena*, the tribunal regarded IPPA as the primary applicable law for the dispute.⁴⁰

In the view of Egypt, the tribunal manifestly failed to apply the applicable law, the Egyptian law, and it applied for annulment. Regarding the interrelation between domestic and international law, the *ad hoc* committee introduced three different views on the role of international law in Article 42 (1).⁴¹ It further

³⁴ See an example *ADC v. Hungary*, ICSID Case No. ARB/03/16, Award of the Tribunal, 2 October 2006, para 290.

³⁵ *Wena Hotels v. Uruguay*, ICSID Case No. ARB/98/4, Award, 8 December 2000.

³⁶ *ibid* paras 102-10.

³⁷ *ibid* paras 102, 107.

³⁸ *ibid* para 79.

³⁹ ICSID Convention (n 7) Article 42 (1). Christoph H. Schreuer & others, *The ICSID Convention: A Commentary* (2nd ed, CUP 2009) 554.

⁴⁰ *Wena Hotels v. Uruguay* (n 35) paras 78-9.

⁴¹ Based on these views, international law plays (1) a broad role in the sense of Article 38 (1) of the ICJ Statute; (2) a supplemental and corrective role in applying domestic law: the former avoids lacunae while the latter avoids inconsistency; (3) a controlling role in applying domestic law to avoid conflict. *Wena Hotels v. Uruguay*, ICSID Case No. ARB/98/4, Decision (Annulment Proceeding), 5 February 2002, paras 38. Schreuer & others, *The ICSID Convention* (n 39) 626.

pointed out that the term "may" in the second sentence left some room for the tribunal to exercise its discretionary power.⁴² As emphasised by the *ad hoc* committee, "the rules of international law that directly or indirectly relate to the state's consent prevail over domestic rules that might be incommensurable with them", especially considering the host state's recognition of such rules.⁴³ Treaty provisions as *lex specialis* also prevail over *lex generalis* contained in domestic law. That was the case with the IPPA in *Wena*.⁴⁴ Consequently, the committee concluded that the tribunal did not exceed its power.

Based on the above analyses, in the context of China, there are two possible routes in which proportionality can be applied to re-balance its investor-state relationship in international investment. One is related to Chinese BITs. If the principle of proportionality is expressed in Chinese BITs, it can be applied through the systemic interpretation of treaties. Alternatively, it can be considered if it is included in the Chinese domestic legal system, which is the applicable law for the dispute. Such international and domestic law can be the applicable law for the dispute based on the parties' agreement, or on the basis of the second sentence of Article 42 (1).

However, if there are conflicts between international and domestic law in practice, some uncertainties may arise due to the lack of a definite provision of their interrelation in the Chinese Constitutional Law. The Constitution merely stipulates that the Standing Committee of the National People's Congress (SCNPC) exercises power "to decide on the ratification or abrogation of treaties and important agreements concluded with foreign states"⁴⁵ in Article 67 (15) without clarifying the domestic legal effects of such treaties. However, some Chinese laws, including the Chinese Maritime Law (1992), explicitly express the interrelation between international and domestic law. Article 268 (1) of the Law explicitly stipulates that

If any international treaty concluded or acceded to by the People's Republic of China contains provisions differing from those contained in this Law, *the provisions of the relevant international treaty shall apply, unless the provisions are those on which the People's Republic of China has announced reservations.*⁴⁶ [italic added]

As reflected in this wording, if there are conflicts between international law and the Chinese Maritime Law (1992), the former shall prevail, except China's reservations. Although there is no definite

⁴² *Wena Hotels v. Uruguay* (n 35) para 39.

⁴³ *ibid* paras 41-2.

⁴⁴ *ibid* paras 42-6.

⁴⁵ The Chinese Constitutional Law (2018) Article 67 (15) [in Chinese].

⁴⁶ The Chinese Maritime Law (1992) Article 268 (1). A similar provision can be seen in Article 142 (2) of the General Principles of the Civil Law of the People's Republic of China, which was replaced by the Chinese Civil Code (2020). The provision prescribes that "[i]f any international treaty concluded or acceded to by the People's Republic of China contains provisions differing from those in the civil laws of the People's Republic of China, the provisions of the international treaty shall apply, unless the provisions are ones on which the People's Republic of China has announced reservations". However, such clause is not referred to in the Chinese Civil Code (2020).

stipulation in the Chinese Constitutional Law, international law prevails over domestic law in particular fields as implied by the relevant Chinese laws.

1.2.2 Approaches to Treaty Interpretation and the Meaning of Proportionality

In the context of international investment, treaty interpretation plays a vital role, which is not only essential to ascertain the correct meaning and scope of investment treatments provided in ambiguous treaty provisions but also crucial to the application of proportionality in the ISDS regime. One challenge of applying proportionality is whether the interpretation of the relevant treaty provisions allows for its application to balance the conflicts between the rights of foreign investors and those of the host state. This opens the debate on how proportionality could be interpreted under Articles 31 to 33 of the Vienna Convention on the Law of Treaties (Vienna Convention).⁴⁷ Article 31 stipulates the general rule of interpretation, Article 32 provides supplementary means, while Article 33 aims to settle interpretative issues arising from two or more authentic languages.⁴⁸ As customary international law on treaty interpretation, these rules should be followed when interpreting the term of a treaty duty,⁴⁹ such as FET. They refer to all elements that should be taken into account within the process of treaty interpretation and imply the corresponding interpretative approaches.

As the general rule of treaty interpretation, Article 31 stipulates that "[a] treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose."⁵⁰ This provision presents that the essential interpretative elements are "good faith", "ordinary meaning", "context", and "object and purpose". In addition, the single word "rule" in the heading of Article 31 indicates that no hierarchy exists in those interpretative factors.⁵¹ As emphasised by Gazzini, all of them are necessary elements that should be considered to ascertain the meaning of the term in question.⁵²

Distinct from others, "good faith" also appears in Article 26 of the Vienna Convention, which requires that "[e]very treaty in force is binding upon the parties to it and must be performed by them in good faith."⁵³ In Bjorge's view, good faith is the overarching principle of treaty interpretation.⁵⁴ As asserted by Gardiner, instead of interpreting a specific word in question, good faith is applied in the whole

⁴⁷ Vienna Convention on the Law of Treaties (1969) Articles 31-33.

⁴⁸ *ibid.*

⁴⁹ Richard Gardiner, *Treaty Interpretation* (2nd ed, OUP 2015) 6-7. See also J. Romesh Weeramantry, *Treaty Interpretation in Investment Arbitration* (OUP 2012) 24-30.

⁵⁰ Vienna Convention (n 47) Article 31(1).

⁵¹ Oliver Dörr & Kirsten Schmalenbach (eds), *Vienna Convention on the Law of Treaties A Commentary* (2nd edn, Springer 2018) 561.

⁵² Tarcisio Gazzini, *Interpretation of International Investment Treaties* (Hart Publishing 2016) 63. Dörr & Schmalenbach (n 51) 561.

⁵³ Vienna Convention (n 47) Article 26.

⁵⁴ Eirik Bjorge, *The Evolutionary Interpretation of Treaties* (OUP 2014) 67.

process of the interpretation of treaties.⁵⁵ He further points out that this principle is closely linked with reasonableness and balance between interpretative elements.⁵⁶ This implies a process of weighing and balancing different values, corresponding to the notion of proportionality, especially its value-oriented factor: Proportionality *stricto sensu*.

Different approaches can be applied to interpret treaty provisions based on the emphasis on interpretative factors. As pointed out by Bos, they are grammatical, systematic, and teleological approaches, stressing the importance of "ordinary meaning", "context", and "object and purpose", respectively.⁵⁷ He asserts that the historical method, which focuses on the contracting parties' intention, is also expressed in the Vienna Convention.⁵⁸ The UNCTAD also highlights the significance of contracting parties' intention in treaty interpretation, but it emphasises the subjective approach.⁵⁹

Those interpretative approaches stress the significance of different elements that should be considered in interpreting treaty provisions. As clarified by the International Court of Justice (ICJ), "the first duty of a tribunal which is called upon to interpret and apply the provisions of a treaty, is to endeavour to give effect to them in their natural and ordinary meaning in the context in which they occur."⁶⁰ In Gardiner's view, the ordinary meaning of the text is the starting point of treaty interpretation because the text itself is the first thing that the tribunal can assess the contracting states' authentic expression from the treaty.⁶¹ Correspondingly, the textual approach aims to investigate the plain meaning of any ambiguous term, and the dictionary is the most common tool to achieve that.⁶² However, the dictionary lists all definitions of a word, some common and some rare, leading to uncertainties in treaty interpretation.⁶³ According to the principle of good faith,⁶⁴ other interpretative methods must then be considered to ascertain what the parties did mean when they used the ambiguous terms.⁶⁵

As emphasised by Villiger, no word of a treaty is drafted in isolation.⁶⁶ The context in which the interpreted term appears can confirm whether its ordinary meaning is reasonable and find its correct

⁵⁵ Gardiner (n 49) 168. Sheng Zhang, *Guo Ji Tou Zi Zhong Cai Zhong De Tiao Yue Jie Shi Yan Jiu (The Research on Treaty Interpretation in International Investment Arbitration)* (Law Press, 2016) 52 [in Chinese].

⁵⁶ Gardiner (n 49) 168, 176-9. Zhang (n 55) 53. Weeramantry (n 49) 48.

⁵⁷ Maarten Bos, 'Theory and Practice of Treaty Interpretation' (1980) 27 *Netherlands International Law Review* 135-46.

⁵⁸ *ibid.*

⁵⁹ UNCTAD, 'IIA Issues Note-Interpretation of IIAs: What States Can Do' (2011) 5. Ole Kristian Fauchald, 'The Legal Reasoning of ICSID Tribunals—An Empirical Analysis' (2008) 19 *The European Journal of International Law* 301, 315.

⁶⁰ 'Competence of the General Assembly for the Admission of a State to the United Nations' (1950) 44 *The American Journal of International Law* 582, 584.

⁶¹ UN, *Yearbook of the International Law Commission Volume II, A/CN.4/SER.A/1966/Add.1* (1967) 218. Gardiner (n 49) 165.

⁶² Zhang (n 55) 92. Gardiner (n 49) 184.

⁶³ Dörr & Schmalenbach (n 51) 581. Gardiner (n 49) 183-4, 186-9. Katayoun Hosseinejad, 'On the Nature of Interpretation in International Law' (2015) 4 *UCL Journal of Law & Jurisprudence* 225, 241.

⁶⁴ Dörr & Schmalenbach (n 51) 588.

⁶⁵ 'Competence' (n 60).

⁶⁶ Mark E. Villiger, 'The rules on Interpretation: Misgivings, Misunderstandings, Miscarriage? The 'Crucible' Intended by the International Law Commission' in Enzo Cannizzaro (ed), *The Law of Treaties Beyond the Vienna Convention* (OUP 2011) 109.

explanation from the range of definitions in the dictionary, thus contributing to ascertaining the meaning of ambiguous words. As pointed out by Orakhelashvili, the context aims to guarantee that no conflicts exist between the interpretation of the word in question and that of the rest of the treaty, ensuring the coherence of the treaty.⁶⁷ Based on Article 31 (2) and (3) of the Vienna Convention,⁶⁸ the context contains integral and extrinsic elements. The former includes the text, preamble, annexes, and any agreement and instrument that related to the conclusion of the treaty.⁶⁹ The latter refers to subsequent agreements, practices, and relevant international law.⁷⁰ This implies an internal logical order. The meaning of the ambiguous term is defined first with the remaining part of the same provision to ensure it can be understood; Then, this interpretation should be checked with other rules of the same treaty to guarantee the consistency of the treaty; Finally, the meaning of the word should be confirmed with relevant external contexts.⁷¹

The importance of "the object and purpose of the treaty" is stressed in the teleological approach, which seeks to include the meaning of the ambiguous word to achieve the desired purpose of the treaty.⁷² Unlike this approach focusing on the objective target, the subjective method focuses on the contracting parties' perceived common intention. The significance of the common intention can be seen in Article 31 (4) of the Vienna Convention, which emphasises that "[a] special meaning shall be given to a term if it is established the parties so intended."⁷³ However, investigating the common intention of contracting states is a challenge. If a special meaning is explicitly provided, then that is where the answer lies. Otherwise, the supplementary methods mentioned in Article 32,⁷⁴ such as *travaux préparatoires*, should be utilised to support the word's special meaning.⁷⁵ Issues may arise from finding *travaux préparatoires* because, as noted by Schreuer, such materials may not be publicly accessible.⁷⁶

Although no hierarchy exists between those interpretative elements, interpreting the same term, such as FET, in different approaches may lead to different interpretations in similar circumstances. The UNCTAD also stresses that all elements in Article 31 of the Vienna Convention should be considered and weighed to interpret treaty provisions, but conflicts always exist if the words in question pursue different values. If the disputed term is broadly interpreted in favour of foreign investors, the host state's values may be impaired, and *vice versa*. Therefore, there is a need to apply proportionality to balance

⁶⁷ Alexander Orakhelashvili, *The Interpretation of Acts and Rules in Public International Law* (OUP 2008) 340.

⁶⁸ Vienna Convention (n 47) Article 31 (2) and (3).

⁶⁹ *ibid* Article 31 (2).

⁷⁰ *ibid* Article 31 (3).

⁷¹ Villiger (n 66) 110. Gardiner (n 49) 222.

⁷² Oliver Morse, 'Schools of Approach to the Interpretation of Treaties' (1960) 9 *Catholic University Law Review* 36.

⁷³ Vienna Convention (n 47) Article 31(4).

⁷⁴ *ibid* Article 32.

⁷⁵ Dörr & Schmalenbach (n 51) 614.

⁷⁶ Christoph Schreuer, 'Diversity and Harmonization of Treaty Interpretation in Investment Arbitration' in Malgosia Fitzmaurice, Olufemi Elias & Panos Merkouris (eds), *Treaty Interpretation and the Vienna Convention on the Law of Treaties: 30 Years on* (Brill 2020) 137-8.

different interpretative factors. As asserted by Barak, the conflicts arising from treaty interpretation can be settled by interpretative balancing, which merely focuses on the application of proportionality *stricto sensu*.⁷⁷ In his view, the questioned words have different desired objectives, and a balance can be achieved by weighing the social importance of their different purposes.⁷⁸

A proper interpretative method is a result of balancing different interpretative factors by proportionality. Meanwhile, such a proper approach is also needed to bring proportionality into the ISDS regime. In this situation, a two-tier systemic approach, which is hybrid, may be applied. To be clear, this systemic method in the current study not only stresses the treaty itself as a system but also interprets the words in question against the entire international law. In both systems, the value or purpose of each interpretative factor is weighed and balanced according to the actual circumstance, contributing to a balanced interpretation of the treaty. Such a balanced treaty interpretation is also essential for applying proportionality in ISA.

1.2.3 Unsettled Discussions on Fair and Equitable Treatment and Proportionality

Compared with other treatments provided in IIAs to foreign investors, FET is the most frequently invoked standard in treaties and practice.⁷⁹ From the perspective of concluded IIAs, this standard has been prescribed in IIAs signed by different countries, including China, to promote and protect international investments. At the time of writing, the data collected from the UNCTAD reflected that almost 95 per cent of the available IIAs (2574 in total) contain the wording "fair and equitable treatment" or equivalent terms, like "equitable treatment".⁸⁰ Meanwhile, from 697 available ISDs, 595 cases were referred for allegedly breaching the FET obligation on the basis of different applicable legal instruments.⁸¹ In 168 out of 256 cases, the host state's violation of its FET obligation *vis-a-vis* foreign investors had been found.⁸²

As demonstrated in practice, most arbitral tribunals interpreted the FET standard as favouring foreign investors.⁸³ For example, the tribunals in *Saluka v. Czech Republic*⁸⁴ interpreted FET as foreign

⁷⁷ Barak (n 20) 3-4, 71-5.

⁷⁸ *ibid.*

⁷⁹ UNCTAD, *Fair and Equitable Treatment UNCTAD Series on Issues in International Investment Agreement II*, UNCTAD/DIAE/IA/2011/5 (2012) xiii, 1.

⁸⁰ Date collected from Investment Policy Hub. 'Mapping of IIA Content-FET' (*Investment Policy Hub*) <<https://investmentpolicy.unctad.org/international-investment-agreements/ii-a-mapping>> last accessed 24 June 2022. See an example BLEU-China BIT (signed 4 June 1984, entered into force 5 October 1986, terminated 1 December 2009) Article 3.

⁸¹ 'Fair and Equitable Treatment' (*Investment Policy Hub*) <<https://investmentpolicy.unctad.org/investment-dispute-settlement>> last accessed 24 June 2022.

⁸² *ibid.*

⁸³ Thomas W. Wälde, 'Investment Arbitration under the Energy Charter Treaty: An Overview of Selected Key Issues based on Recent Litigation Experience' in Norbert Horn (eds), *Arbitrating Foreign Investment Disputes Procedural and Substantive Legal Aspects* (Kluwer Law International 2004) 206. UNCTAD, *Issues in International Investment Agreement II* (n 79) 10.

⁸⁴ *Saluka v. Czech Republic*, UNCITRAL, Partial Award, 17 March 2006.

investor-oriented, which at least should not be interpreted as a discouragement to foreign investors,⁸⁵ even though they stressed the significance of a balanced approach in which both disputing parties' values should be protected.⁸⁶ Such broad investment protection, to a certain extent, impairs the host state's right to regulate in the public interest. While FET is a standard which has been frequently invoked in both IIAs and the ISDS, it sparks the debates over whether proportionality could be adopted to address the imbalance between the conflicting values of foreign investors and the host state. In this respect, it is an excellent subject for the current research on the proper interpretative approach, namely the systemic method, and proportionality analysis in international investment.

The issues are further exacerbated by a lack of consensus on whether the nature and components of FET define itself as an international custom in the sense of Article 38 (1) (b) of the ICJ Statute. In Tudor's view, it is time for FET to be an international custom because of its prevalent application in international investment.⁸⁷ A similar view is held by Sornarajah, who regards FET as being synonymous with the minimum standard under customary international law.⁸⁸ This standard is then indirectly deemed an international custom. As denied by other scholars, such as Dumberry, FET fails to fulfil the requirements stipulated in Article 38 (1) (b) of the ICJ Statute,⁸⁹ which require that it should be broadly applied by representative states out of a sense of legal obligation to be an international custom.⁹⁰

As argued by Dumberry, FET has failed to become an international custom due to the lack of consistency and uniformity of state practice.⁹¹ Although this standard appears in almost all IIAs, its formulation varies from one treaty to another.⁹² These provisions can be generally divided into two groups: The unqualified FET with no detail and the qualified FET linked with different factors.⁹³ Consequently, the precise scope and contour of FET vary based on the provisions of each particular BIT.⁹⁴ No consensus has been reached on the precise meaning of FET. Whether it is synonymous with the international minimum standard still raises doubts.⁹⁵ States may also have different understandings

⁸⁵ *ibid* para 301.

⁸⁶ *ibid* para 300.

⁸⁷ Ioana Tudor, *The Fair and Equitable Treatment Standard in the International Law of Foreign Investment* (OUP 2008) 85.

⁸⁸ M. Sornarajah, *The International Law on Foreign Investment* (4th edn, CUP 2017) 411. Bernardo M. Cremades & David J. A. Cairns, 'Contract and Treaty Claims and Choice of Forum in Foreign Investment Disputes', in Norbert Horn (ed), *Arbitrating Foreign Investment Disputes Procedural and Substantive Legal Aspects* (Kluwer Law International 2004).

⁸⁹ 341.Graham Mayeda, 'Playing Fair: The Meaning of Fair and Equitable Treatment in Bilateral Investment Treaties' (2007) *Journal of World Trade* 273, 274.

⁹⁰ See generally in Patrick Dumberry, 'Has the Fair and Equitable Treatment Standard Become a Rule of Customary International Law?' (2017) 8 *Journal of International Dispute Settlement* 155.

⁹¹ ICJ Statute (n 19) Article 38 (1) (b). UNCTAD, *Issues in International Investment Agreement II* (n 79) 105.

⁹² Dumberry, 'Has' (n 89) 172-5.

⁹³ See 4.2.3 in Chapter Four.

⁹⁴ See 4.2.3.2 and 4.2.3.3 in Chapter Four.

⁹⁵ UNCTAD, *Issues in International Investment Agreement II* (n 79) 8, 22. 'Fair and Equitable Treatment Standard in International Investment Law' (2004) OECD Working Papers on International investment 2004/03, 40 <https://www.oecd.org/daf/inv/investment-policy/WP-2004_3.pdf> last accessed 16 June 2022.

⁹⁶ UNCTAD, *Fair and Equitable Treatment UNCTAD Series on Issues in International Investment Agreements*, UNCTAD/ITE/IIT/11 (1999) 10.

of FET due to the inherent subjectivity of "fair" and "equitable".⁹⁶

Meanwhile, inconsistent, even opposite, interpretations of FET remain in practice. The prime example of this issue is "the ultimate fiasco in investment arbitration,"⁹⁷ in terms of the opposite awards on FET between *Lauder v. Czech Republic*⁹⁸ and *CME v. Czech Republic*.⁹⁹ In both cases, the claimants alleged that the Czech Republic had violated its treaty obligations, including FET, because of its actions and omissions regarding the licence to operate broadcasting. As stipulated in the case-related applicable instruments, namely the Czech Republic-US BIT (1991)¹⁰⁰ and the Czech Republic- Netherlands BIT (1991),¹⁰¹ FET "shall in no case be accorded treatment less than that required by international law".¹⁰² If the same FET clause under these treaties were interpreted based on the rules in the Vienna Convention, the judgments on whether the Czech Republic violated its FET obligation *vis-à-vis* foreign investors should be the same.

Nevertheless, the tribunals in these cases made different decisions. The tribunal in *Lauder* stressed that the questioned term should be interpreted with consideration of the treaty's object and purpose, as well as the circumstances of its conclusion.¹⁰³ It also considered the interpretation of FET provided in the UNCTAD's document.¹⁰⁴ As stated, the prohibition of arbitrary and discriminatory measures was contained in this standard. Based on the facts, the tribunal pointed out that the reason for the actions taken by the Czech Republic was its concerns about the violation of its Media Law.¹⁰⁵ In addition, other broadcasters were treated in the same way.¹⁰⁶ Therefore, the tribunal determined that the Czech Republic had no violations of its FET obligation.¹⁰⁷

Differently, the tribunal in *CME* supported the claimant's relief.¹⁰⁸ Instead of interpreting FET based on the rules of the Vienna Convention, it considered the opinion held by Professor Vagts.¹⁰⁹ Also, in its view, the same treatment provided to other broadcasters was irrelevant to decide whether the Czech

⁹⁶ UNCTAD, *International Investments Agreements: Key Issues Volume I*, UNCTAD/ITE/IIT/2004/10 (2004) 212.

⁹⁷ August Reinisch, 'The Proliferation of International Dispute Settlement Mechanisms: The Threat of Fragmentation vs. the Promise of a More Effective System? Some Reflections from the Perspective of Investment Arbitration' in Isabella Buffard and others (eds), *International Law between Universalism and Fragmentation: Festschrift in Honour of Gerhard Hafner* (Brill, 10 December 2008) 116-7.

⁹⁸ *Lauder v. Czech Republic*, UNCITRAL, Final Award, 3 September 2001.

⁹⁹ *CME v. Czech Republic*, UNCITRAL, Partial Award, 13 September 2001.

¹⁰⁰ Czech Republic-US BIT (signed 22 October 1991, entered into force 19 December 1992).

¹⁰¹ Czech Republic-Netherlands BIT (signed 29 April 1991, entered into force 1 October 1992, terminated 10 December 2021).

¹⁰² Czech Republic-US BIT (n 100) Article II(2)(a). See also Czech Republic-Netherlands BIT (n 101) Article 3.

¹⁰³ *Lauder v. Czech Republic* (n 98) para 292.

¹⁰⁴ *ibid* para 292.

¹⁰⁵ *ibid* paras 296-9.

¹⁰⁶ *ibid* para 257.

¹⁰⁷ *ibid* paras 293-5.

¹⁰⁸ *CME v. Czech Republic* (n 99).

¹⁰⁹ *ibid* paras 526, 611.

Republic had violated its treaty obligations *vis-à-vis* CME.¹¹⁰ Because its measure altered the agreements on which foreign investors relied to invest, the Czech Republic had breached its FET obligation.¹¹¹ As reflected in these contradictory decisions, the tribunal exercised its discretionary power to interpret FET and failed to comply with the requirements of interpretative rules, expressing a gap exists between how a treaty provision should be interpreted according to the rules of interpretation provided in the Vienna Convention and what is actually interpreted in practice.

The precise contour of FET also opens up fierce debate among scholars. Although there is no defined interpretation of FET, based on the publicly documented awards of existing cases, its general scope can be depicted. As noted by Dolzer and Schreuer, the components of FET interpreted by the tribunal in *Tecmed v. Mexico*¹¹² are referred to in other cases.¹¹³ As interpreted in this case, FET includes "stability and the protection of the investor's legitimate expectations; transparency; compliance with contractual obligations; procedural propriety and due process; good faith; and freedom from coercion and harassment".¹¹⁴ At this juncture, Schill points out that "proportionality" is also an element of FET.¹¹⁵ The UNCTAD concluded that the central concepts contained in FET refer to "the prohibition of manifest arbitrariness in decision-making, the denial of justice and disregard of the fundamental principles of due process, targeted discrimination on manifestly wrongful grounds, and abusive treatment of investors" and "the host state should protect the foreign investors' legitimate expectations".¹¹⁶

Nevertheless, issues may still arise from these elements. For example, as to the protection of legitimate expectations provided by FET, one may question whether such protection is merely given to foreign investors. If it is, the approach to protecting the host state's legitimate expectations for sustainable investment is in doubt. Therefore, how to balance the expectations of foreign investors and the host state is questionable. Conflicts between both disputing parties can become more bitter when crises occur, such as the Covid-19 pandemic (2019-to date)¹¹⁷ or Argentina's economic crisis of 2001/2.¹¹⁸ Argentina saw a range of treaty-based challenges brought against it as it tried to wrestle with the severe effects of its economic crisis.¹¹⁹ Proportionality was more or less adopted by the tribunals in these cases to review

¹¹⁰ *ibid* para 611.

¹¹¹ *ibid*.

¹¹² *Tecmed v. Mexico*, ICSID ARB(AF)/00/2, Award, 29 May 2003.

¹¹³ Rudolf Dolzer & Christoph Schreuer, *Principles of International Investment Law* (2nd ed, OUP 2012) 166.

¹¹⁴ *Tecmed v. Mexico* (n 112) para 154.

¹¹⁵ Stephan W. Schill, 'Fair and Equitable Treatment under Investment Treaties as an Embodiment of the Rule of Law' (2006) International Law and Justice Working Paper 2006/6, 11 <<https://iilj.org/wp-content/uploads/2016/08/Schill-Fair-and-Equitable-Treatment-under-Investment-Treaties-as-an-Embodiment-of-the-Rule-of-Law-2006-2.pdf>> last accessed 20 June 2022.

¹¹⁶ UNCTAD, *Issues in International Investment Agreement II* (n 79) xiii. Christopher Dugan & others, *Investor-State Arbitration* (OUP 2008) 506-33.

¹¹⁷ Julien Chaisse, 'Both Possible and Impossible-Could Covid-19 Measures Give Rise to Investor-State Disputes?' (2020) 13 Contemporary Asia Arbitration Journal 99, 101-4. UNCTAD, 'Investment Policy Responses' (n 6).

¹¹⁸ See generally in Chapter Five. Argentinian cases (n 5).

¹¹⁹ *ibid*.

Argentina's actions by interpreting its textual basis in the applicable BIT, such as the exception clause under the Argentina-US BIT (1991).¹²⁰ Conflicting decisions on the measures in question were made by the tribunals based on different approaches to proportionality analysis, implying the significance of a proper way to apply proportionality in the ISDS regime.

1.2.4 Uncertainties of the Textual Basis of Proportionality in Chinese BITs

Considering the nature of proportionality, which is neither an international custom nor a general principle of law, one route to its application in the settlement of Chinese ISDs is to interpret proportionality's textual basis stipulated in the case-related treaty. In this respect, the wording of Chinese BITs signed with another contracting state is vital to the application of proportionality.

As pointed out by Kong, China's attitudes towards FDI refer to "three guiding principles": Sovereignty, equality and mutual benefit, and reference to international practice.¹²¹ He further stressed that the principle of equality and mutual benefit requires "a balance between the rights and obligations of the parties concerned",¹²² which is also a requirement in the proportionality principle. However, no "proportionality" term exists in China's 145 BITs,¹²³ with the exception of the treaty it signed with Colombia in 2008.¹²⁴ Article 12 of the China-Colombia BIT (2008)¹²⁵ prescribes that the measures to preserve public order should be "proportional to the objective they seek to achieve",¹²⁶ explicitly expressing the requirement of a rational means-end connection.

More specifically, depending on the attributes of the treaties, Chinese BITs can be generally classified into three different generations.¹²⁷ The first-generation includes 24 BITs signed by China with another contracting state from 1982 to 1989.¹²⁸ As noted by Wen and Gallagher, the Chinese Government held

¹²⁰ Argentina-US BIT (signed 14 November 1991, entered into force 20 October 1994) Article XI.

¹²¹ See from Qingjiang Kong, 'Bilateral Investment Treaties: The Chinese Approach and Practice' (2003) 8 *Asian Yearbook of International Law* 105, 110.

¹²² *ibid* 111.

¹²³ *supra* note 16.

¹²⁴ China-Colombia BIT (signed 22 November 2008, entered into force 2 July 2013).

¹²⁵ *ibid*.

¹²⁶ *ibid* Article 12.

¹²⁷ Shan & Gallagher (n 9) [in Chinese]. Yuwen Li and Cheng Bian also point out that these Chinese BITs are classified into three generations based on the provisions of substantive protection and ISDS, but they opine that first-generation Chinese BITs were concluded from 1982 to 1999, second-generation Chinese BITs were signed from 1997 to 2011, and third-generation Chinese BITs have been concluded since 2007. see in Yuwen Li & Cheng Bian, 'China's Stance on Investor-State Dispute Settlement: Evolution, Challenges, and Reform Option' (2020) 67 *Netherlands International Law Review* 503, 505; In some scholars' view, Chinese BITs that were signed from the early 2010s belong to the fourth generation, which reflects the "Americanisation" of Chinese treaties, see Guang Wang & Jinyong Lu, 'Chinese Bilateral Investment Treaties: Evolution and Development Tendency' (2019) 2 *Journal of International Economic Cooperation* 52, 53, 55 [in Chinese]. See also Heng Wang & Lu Wang, 'China's Bilateral Investment Treaties' in Julien Chaisse & others (eds), *Handbook of International Investment Law and Policy* (Springer, 2020) 2382-4. In Cohen's view, China's investment policy has experienced four different eras, see Tyler Cohen & David Schneiderman, 'The Political Economy of Chinese Bilateral Investment Treaty Policy' (2017) 5 *The Chinese Journal of Comparative Law* 110, 114.

¹²⁸ Shan & Gallagher (n 9) 36-9.

a relatively conservative attitude at this time,¹²⁹ during which it was a pure capital-importing state. It mainly signed BITs with developed countries to protect and attract the inbound FDI.¹³⁰ Due to China's late signing of the ICSID Convention until 1990, foreign investors were granted limited access to arbitration under the first-generation Chinese BITs: Only the dispute arising from the amount of compensation for expropriation could be submitted to the arbitral tribunal.¹³¹ In this respect, the ISD would finally become the state-state dispute.¹³²

In the second-generation, between 1990 and 1997, China signed 67 BITs.¹³³ At this phase, China ratified the ICSID Convention in 1992 and subsequently deposited its instruments of ratification in 1993.¹³⁴ As retained by China, only the ISD over "compensation resulting from expropriation and nationalisation" would be considered to be submitted to the jurisdiction of the ICSID.¹³⁵ Against such a background, some Chinese BITs signed in the second generation, like the China-Uruguay BIT (1993),¹³⁶ have no provision of the jurisdiction of the ICSID. Therefore, China still retained a conservative attitude.

Since 1998, China has concluded 53 third-generation BITs,¹³⁷ which differ from the treaties signed previously. Cohen and Schneiderman observed that all ISDs could be submitted to the jurisdiction of the ICSID.¹³⁸ Meanwhile, the common standards adopted in most capital-exporting countries in their treaties have also been embraced by China,¹³⁹ reflecting the remarkable change in China's international investment policy.¹⁴⁰ Han argued, however, that unlike the US, Canada and other states that have taken care to guarantee their rights to regulate in the public interest via the use of exception clauses, China has not included such provisions in the majority of its BITs.¹⁴¹

¹²⁹ *ibid* 37.

¹³⁰ *ibid*. Cohen & Schneiderman (n 127) 116. Kong (n 121) 112. According to the data from UN, the developed countries that signed BITs with China between 1982 and 1989 are Sweden, Germany, France, Belgium-Luxembourg, Finland, Norway, Italy, Denmark, Netherlands, Austria, United Kingdom, Switzerland, Australia, Japan, New Zealand.

¹³¹ See an example China-Romania BIT (signed 10 February 1983). As stipulated in Article 4 (3), "[i]f a dispute concerning the amount of compensation between an investor of a contracting party and the other contracting party in whose territory the investment was made continues to exist after the amount has been reassessed by the court or other competent body of the investment has been made, the dispute will be resolved by the two contracting parties in accordance with the provisions of article 9 of this agreement, if the investor has requested it from his government". Article 9 is about the settlement of disputes between the contracting parties.

¹³² Shan & Gallagher (n 9) 39.

¹³³ *ibid* 39-40.

¹³⁴ 'Member State—China' (*ICSID*) <<https://icsid.worldbank.org/about/member-states/database-of-member-states/member-state-details?state=ST30>> last accessed 15 May 2022.

¹³⁵ *ibid*.

¹³⁶ China-Uruguay BIT (signed 2 December 1993, entered into force 1 December 1997).

¹³⁷ Shan & Gallagher (n 9) 40-2.

¹³⁸ Cohen & Schneiderman (n 127) 122. Shan & Gallagher (n 9) 41.

¹³⁹ Stephan W Schill, 'Tearing Down the Great Wall: The New Generation Investment Treaties of the People's Republic of China' (2007) 15 *Cardozo Journal of International & Comparative Law* 73, 76. Cohen & Schneiderman (n 127) 111.

¹⁴⁰ *ibid*.

¹⁴¹ Xiuli Han, 'On the Application of the Principle of Proportionality in the ICSID Arbitration and Proposals to the Government of the People's Republic of China' (2006) 13 *James Cook University Law Review* 233, 248-9.

These changes in three generations of Chinese BITs, to a certain extent, express the general trend of the development of Chinese IIAs. In addition, considering the changes in its role (a transition from the pure recipient to a capital-importing and exporting state) in international investment, it is in China's interest to establish a balanced investor-state relationship via the application of proportionality. The problem is that only the China-Colombia BIT (2008)¹⁴² explicitly refers to the notion of "proportionality".¹⁴³ The interpretation and application of proportionality still depend on the language of each case-related treaty, which should be interpreted in the systemic approach.

1.2.5 Doubts on the Legal Status of Proportionality in China

The investigation of proportionality's legal status in China may contribute to understanding the nature of proportionality and its application in the ISDS in which China is involved. Proportionality can be applied if it is provided in the host state's domestic law, which is the applicable legal instrument of the case.

The absence of the word "proportionality" and its equivalent terms in Chinese laws and regulations raise debates and doubts on whether such a principle is included in the Chinese domestic legal system. As noted by Han, although *Zhong Yong Zhi Dao* (中庸之道, moderation in all things), which expresses the concept of proportionality, is referred to in Chinese traditional culture, both the Chinese Constitutional Law and administrative laws have no provision of proportionality.¹⁴⁴ Arriving from the positive law approach, he points out that no principle of proportionality exists in China because of the lack of explicit stipulation.¹⁴⁵ However, this view is rejected by others, who argue that the notion of proportionality can be observed from the wording of Chinese laws, regulations, and policy documents.¹⁴⁶

In the view of those scholars who regard proportionality as a constitutional principle in China, it can be deduced from "the rule of law"¹⁴⁷ and "human rights".¹⁴⁸ As pointed out by Jiang, similar to its position

¹⁴² China-Colombia BIT (n 124).

¹⁴³ *ibid* Article 12.

¹⁴⁴ Han, 'On the Application' (n 141) 254.

¹⁴⁵ Xiuli Han, 'The Application of the Principle of Proportionality in *Tecmed v. Mexico*' (2007) 6 *Chinese Journal of International Law* 635, 650. Jinguang Hu, *Zhong Guo Shi Da Xian Zheng Shi Li Yan Jiu* (*The Research on China's Top Ten Constitutional Cases*) (China Renmin University Press 2009) 130 [in Chinese].

¹⁴⁶ Xin Jiang, 'Bi Li Yuan Ze De Li Lun Ji Chu Tan Xi-Yi Xian Zheng Zhe Xue Yu Gong Fa Jing Shen Wei Shi Jiao' (The Theoretical Foundation for the Principle of the Proportionality—From the Angle of Constitutional Government Philosophy and Public Law Spirit) (2008) 26 *Hebei Law Science* 77 [in Chinese]. Longfei Rao & Jianhui Chen, 'Bi Li Yuan Ze De Zhong Guo Xian Fa Yi Ju' (Basis of Chinese Constitutional Norms of Principle of Proportionality) (2016) 18 *Journal of Shandong University of Science and Technology* 37, 44 [in Chinese].

¹⁴⁷ Jiang (n 146).

¹⁴⁸ Hongchang Jiao, "'Guo Jia Zun Zhong He Bao Zhang Ren Quan" De Xian Fa Fen Xi' (A Constitutional Analysis on "State Respects and Protect Human Rights") (2004) *China Legal Science* 42, 46-7 [in Chinese]. Zhongjing Men, 'Bi Li Yuan Ze De Xian Fa Di Wei Yu Yi Ju Gui Fan—Yi Xian Fa Yi Yi Shang De Kuan Rong Li Nian Wei Fen Xi Shi Jiao' (The Constitutional Position and Norm Basis of the Principle of Proportionality-Taking the Concept of Tolerance in Constitutional Sense as the Analysis View) (2014) 29 *Legal Forum* 94, 101 [in Chinese]. Zhongjing Men, 'Han Yi Yu Yi Yi Gong Gong Li Yi De Xian Fa Jie Shi'

in German law, proportionality in the Chinese domestic legal system is inherently required by the substantive rule of law.¹⁴⁹ Instead, others assert that proportionality is derived from human rights, but they have divergencies on its precise textual basis.¹⁵⁰ For example, in Jiao's view, the provision of human rights, which first appeared in the Chinese Constitutional Law (2004),¹⁵¹ expresses the notion of proportionality.¹⁵² Differently, Rao and Chen point out that such a concept should be deduced from the restrictions on the limits on fundamental rights,¹⁵³ which can be expressed by interpreting Article 33 of the Chinese Constitution Law in conjunction with Article 51. However, doubts on whether proportionality is a constitutional principle in the Chinese domestic legal system remain because it has never been approved or tested by the competent authority.

Unlike its position in the Constitution, proportionality can be observed and argued for its application in both theory and practice of Chinese administrative law. The rules of Chinese administrative laws and regulations, in particular, Articles 23 and 43 of the Chinese Administrative Compulsion Law, reflect the concept of proportionality.¹⁵⁴ They express a balance between the achievement of public authorities' desired purpose and the protection of individuals' rights, which can be struck by applying proportionality.¹⁵⁵

However, proportionality's relationship with the principle of reasonableness raises doubts over whether it is an independent principle in Chinese administrative law. Scholars hold different views on their relationship.¹⁵⁶ As pointed out by Wang, the current mainstream view in China is that proportionality is a sub-element of the principle of reasonableness.¹⁵⁷ This is denied by Chen, who regards proportionality as a synonym with reasonableness.¹⁵⁸ In his view, their only difference is that, compared with proportionality, the principle of reasonableness has been invoked more frequently.¹⁵⁹ However, as argued by Hu, even though proportionality and reasonableness have similarities, they are different

(Meaning and Significance: The Constitutional Interpretation of Public Interest) (2012) *Tribune of Political Science & Law* 151, 158 [in Chinese].

¹⁴⁹ Jiang (n 146) 77-80.

¹⁵⁰ *supra* note 148.

¹⁵¹ The Chinese Constitutional Law (2004) Article 33 (3) [in Chinese].

¹⁵² Jiao (n 148).

¹⁵³ Rao & Chen (n 146).

¹⁵⁴ The Chinese Administrative Compulsion Law (2011) Articles 23 and 43 [in Chinese].

¹⁵⁵ Xuexian Huang & Hong Yang, 'Wo Guo Xing Zheng Fa Zhong Bi Li Yuan Ze De Li Lun Yan Jiu Yu Shi Jian Fa Zhan' (On the Theoretical Study and The Development of Practice of the Principle of Proportionality about Chinese Administrative Law) (2017) *Law & Economy* 5, 13 [in Chinese].

¹⁵⁶ Haocai Luo & Zhongle Zhan, *Xing Zheng Fa Xue (Administrative Law)* (3rd edn, PUP 2012) 31-4 [in Chinese]. Xinmin Chen, *Zhong Guo Xing Zheng Fa Yuan Li (Principles of Chinese Administrative Law)* (China University of Political Science and Law Press 2002) 42 [in Chinese]. Jingchun He, 'Xing Zheng Bi Li Yu He Li Xing Yuan Ze De Bi Jiao Yan Jiu' (Comparative Study on Principle of Proportionality and Principle of Rationality) (2004) *Administrative Law Review* 33, 35 [in Chinese].

¹⁵⁷ Jing Wang, 'Bi Li Yuan Ze Zai Xing Zheng Shi Jian Zhong De Shi Yong' (Application of Proportionality Principle in Administration in China) (2017) *Law & Economy* 19, 23-4 [in Chinese]. Luo & Zhan (n 156).

¹⁵⁸ Chen (n 156).

¹⁵⁹ *ibid*.

principles.¹⁶⁰ Their differences can be observed in several aspects:¹⁶¹ For instance, from the natural perspective, proportionality is objective, whereas reasonableness is subjective.¹⁶²

Meanwhile, concluded from practice, proportionality has been explicitly or implicitly adopted by the Chinese courts as the basis of their verdicts on the specific administrative act implemented by the public authorities, but its application varies from one case to another. As noted by Chen, some courts regard proportionality as a shortcut,¹⁶³ referring to it in their decisions without any detail.¹⁶⁴ Other courts review the impugned measures by the all-compassing proportionality, which includes three consecutive tests of suitability, necessity, and proportionality *stricto sensu*.¹⁶⁵ The suitability and necessity tests ascertain the disputed measure itself, while proportionality *stricto sensu* is a value-oriented assessment stressing the real balance between conflicting values. However, some courts selectively apply the tests included in proportionality analysis, such as the necessity test or the assessment of proportionality *stricto sensu*.¹⁶⁶ Consequently, proportionality's muddled relationship with the principle of reasonableness and its chaotic application in practice cast doubt on its legal status in the Chinese domestic legal system.

1.3 The Aim and Objectives of the Research

This thesis will investigate the challenges of applying the principle of proportionality in striking a balance in the investor-state relationship from the international and Chinese perspectives and provide the corresponding recommendations to address such issues. The general objectives of this study are firstly to ascertain whether proportionality as a tool can generally be adopted in international investment to balance the conflicting legitimate expectations of foreign investors and host states. Secondly, this study will explore the possibility and practicability of applying proportionality to re-balance the investor-state relationship in a particular circumstance, namely Chinese international investment.

1.3.1 Specific Objectives

In order to interpret and advise on the challenges and reach the objectives of the study, a set of specific related questions are answered in this research to understand comprehensively the application of proportionality in general, settle the main issues as to the possibility and practicability of this tool in the context of international investment, and strike a fair balance in the investor-state relationship. They are:

¹⁶⁰ He (n 156).

¹⁶¹ *ibid.* Dengfeng Yang, 'Cong He Li Yuan Ze Zou Xiang Tong Yi De Bi Li Yuan Ze' (From the Reasonable Principle to A Unified Principle of Proportionality) [2016] China Legal Science 88, 89 [in Chinese].

¹⁶² *ibid.*

¹⁶³ Cenbo Chen, 'Bi Li Yuan Ze Zai Fa Yuan Shen Li Zhong De Shi Yong Kun Jing' (The Dilemma of the Application of the Principle of Proportionality in Court Trial) (2018) Academic Search for Truth & Reality 77, 79-81 [in Chinese].

¹⁶⁴ *ibid.*

¹⁶⁵ See 7.5.3 in Chapter Seven.

¹⁶⁶ See 7.5.1 and 7.5.2 in Chapter Seven.

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1. Explore why proportionality should be applied to weigh and balance competing values.
 2. Examine the nature of proportionality to demonstrate the approach in which this tool can be generally applied in international investment.
 3. Investigate proportionality's precise components and structure, contributing to its application in balancing the conflicting legitimate expectations of foreign investors and the host state.
 4. Identify the appropriate approach to interpreting treaty provisions, which contributes to a balanced interpretation of treaties and the application of proportionality.
 5. Highlight the conflicts between the legitimate expectations of foreign visitors and the host state.
 6. Consider the appropriate approach to the application of proportionality in the ISDS regime to settle ISDs based on different examinations.
 7. Scrutinise how proportionality has been applied by the arbitral tribunals.
 8. Investigate the legal status of proportionality in the Chinese domestic legal system.
 9. Explore and identify the textual basis of proportionality in Chinese BITs.
 10. Explore Chinese routes to the application of proportionality.

1.4 The Rationale of the Research

The issue of imbalanced investor-state relationships that affect international investments has drawn states' attention. As a leading participant in international investment, China cannot be exempted. Against this background, it is in China's interest to re-address such conflicts of values, like the conflicting legitimate expectations of foreign investors and the host state of the stable legal framework.

Nevertheless, a gap between the protections of both parties' rights provided in Chinese BITs and what is needed in practice raises questions over how their conflicting values can be re-balanced. As mentioned in 1.2.4, most Chinese BITs were concluded when China, a pure recipient of FDI, sought to provide investment protection and attract foreign investors and capital.¹⁶⁷ Based on Argentinian cases, which will be discussed in Chapter Five, broad investment protections more or less impair China's right to regulate in the public interest when it is a host state. This conflict between its value and foreign investors may be fiercer in times of emergency, like the pandemic. Also, these old BITs fail to provide sufficient protection to Chinese investors in the current context of international investment due to the limited access to investment arbitration. However, during the past four decades, only 17 Chinese BITs have been amended or replaced by new treaties.¹⁶⁸ Therefore, identifying a useful tool, like proportionality, to establish a balanced investor-state relationship has its own significance in Chinese

¹⁶⁷ Shan & Gallagher (n 9) 35-42.

¹⁶⁸ These 17 BITs are the treaty signed by China with Germany, France, BLEU, Finland, Netherlands, Singapore, Switzerland, Russia, Turkey, the Czech Republic, Portugal, Spain, Uzbekistan, the Republic of Korea, Chile, Mauritius, and Nigeria, respectively.

international investment policy.

Moreover, applying proportionality based on its internal logical order contributes to achieving China's desired purpose, providing sufficient support and guarantee to its FDI whilst trading off investment and non-investment values. With its dual role in international investment, the measures that can be used to strike such a balance are considered by China from both perspectives of the host state and the home state of investors, which may be more balanced and unbiased.

1.5 The Research Methodology

A combination of comparative and doctrinal legal methodology will be adopted in this study to investigate the possibility and practicability of applying proportionality to strike a balance in the investor-state relationship, especially in Chinese international investment. Various primary and secondary sources regarding proportionality, treaty interpretation, FET, the protection of legitimate expectations, and the textual basis of proportionality in Chinese BITs and its domestic legal system will be examined to answer the research question.

The primary methodology applied in this thesis is comparative legal research.¹⁶⁹ As Kzweigert and Kötz clarified, "[t]he basic methodological principle of all comparative law is that of functionality."¹⁷⁰ Rather than the structure or doctrine of different legal systems, the functional comparative method focuses on their functions, which means what social problem is solved by the law and how the institution deals with the issue. Moreover, the comparatists postulate that different countries stipulate different laws to deal with similar real-life problems with similar results.¹⁷¹ This highlights the intrinsic similarity between the institutions of different states, that although they are doctrinally different, this similarity leads to a correct settlement of the issue.¹⁷² As pointed out by Michaels, in the functional comparative approach, different legal systems can be compared when they deal with similar societal needs, and the objects of the comparison are often judicial decisions as responses to problems.¹⁷³

In the current research, the practices of different jurisdictions will be first compared to determine the utility and advantage of proportionality as a tool to weigh and balance competing values. This approach will be utilised in Chapter Two to investigate why proportionality, rather than other principles such as reasonableness, has been noted as a preeminent and flexible tool to strike a balance between the legitimate expectations of foreign investors and those of the respective host state. This question will be

¹⁶⁹ The application of comparative legal methodology can be seen in Chapters Two, Four, and Six.

¹⁷⁰ Konrad Kzweigert & Hein Kötz, *An Introduction to Comparative Law* (Tony Weir tr, 3rd edn, OUP 1998) 34.

¹⁷¹ Ralf Michaels, 'The Functional Method of Comparative Law' in Mathias Reimann & Reinhard Zimmermann (eds), *The Oxford Handbook of Comparative Law* (OUP, 2006) 347.

¹⁷² *ibid.*

¹⁷³ *ibid* 342.

answered by comparing different tactics used by states to weigh competing values and reviewing the various questioned measures taken by the public authority.

Article 38 (1) of the ICJ Statute serves as further evidence supporting the use of comparative legal research methodology, which will be discussed in Chapters Two and Four.¹⁷⁴ According to this rule, states' practices need to be compared to investigate whether the applications of proportionality in states are sufficient to be a general practice and whether it has been consistently and uniformly adopted. Similarly, the nature of FET should also be investigated based on a comparison between different states' practices. All this will feed the further discussion on balancing the conflicts between the values of foreign investors and the host state.

Furthermore, this methodology will address the issue arising from the limited ISDs in which China is involved. The role and application of proportionality in Chinese international investment cannot be tested based on China's own disputes. This is due to the lack of Chinese cases which refer to proportionality and the ambiguous perception of Chinese scholars. Learning from the international debates, the discussion on the application of proportionality in typical cases, such as those arising from the Argentinian economic crisis of 2001/2,¹⁷⁵ and the current debates among Chinese scholars are critical to remedy such a paucity. One noteworthy point here is that considering the differences in applicable instruments and factual backgrounds of each case, how to fill the gap existing between the application of proportionality analysed in this thesis and that applied by China in its future practice must be considered.

Meanwhile, the doctrinal methodology will also be applied in this study, where the meaning of the law is examined, focusing on the legislation, awards, case law, and other legal sources.¹⁷⁶ The doctrinal methodology will be used to ascertain the legal status of proportionality in international investment law and the Chinese domestic legal system.¹⁷⁷ Alongside the international awards, which will be discussed in Chapter Five, the wording of different versions of the Chinese Constitutional Law and its administrative laws and regulations will be analysed in Chapter Seven to answer whether proportionality is included in China. The Chinese administrative law cases in which proportionality was referred to as a basis of the decisions, which allude to its legal status in the Chinese domestic legal system, will also be scrutinised. In order to eliminate the gap between theory and practice, legitimate

¹⁷⁴ The application of this methodology in identifying the nature of proportionality can be seen in Chapter Two, while its application in the identification of FET can be observed in Chapter Four.

¹⁷⁵ Argentinian cases (n 5).

¹⁷⁶ Terry Hutchinson, 'Doctrinal Research: Researching the Jury' in Dawn Watkins & Mandy Burton (eds), *Research Methods in Law* (2nd edn, Routledge 2018) 13. Amrit Kharel, 'Doctrinal Legal Research' (2018) 2 <https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3130525> last accessed 26 April 2022.

¹⁷⁷ Chapter Five aims to analyse proportionality at the international level, while Chapters Six and Seven discuss proportionality from Chinese perspective.

expectations and proportionality analysis are closely examined and analysed to aid the discussion in this research.

The current research relies on both primary and secondary sources regarding the principle of proportionality, treaty interpretation, and the FET standard, such as books, articles, online sources and some legal databases, like the UNCTAD Investment Policy Hub, Westlaw, Kluwer Arbitration, HeinOnline, PKULAW, and China Judgement Online. Other in-printed materials relating to law and practice have been collected from different libraries and jurisdictions, mainly in China. Chinese documents, books, and other materials have been collated and translated.

1.6 The Originality and Significance of the Research

This research contributes to ascertaining the general application of the principle of proportionality in international investment and its application in a particular circumstance Chinese international investment. The investigation corresponds with Vadi's call for a wider application of proportionality, who stated: "more studies are needed to identify the legal status of proportionality in international law".¹⁷⁸ More specifically, the contribution of the current study can be seen in its originality and contributions to (1) fulfilment of a further systemic investigation of the principle of proportionality required for the academic scholarship, (2) knowledge, understanding and clarification of the legal status of proportionality in China contributing to further identification of proportionality's legal status in international law, and (3) research-based recommendations for the review of the outdated Chinese BITs as well as how proportionality could be brought into the ISDS via the interpretation of the new generation of BITs.

Concluded from the research on arbitral awards of existing ISDs, it is evident that some treaty interpretations made by the tribunals imply the preference for one party, worsening the already imbalanced investor-state relationship.¹⁷⁹ Therefore, based on the rules of interpretation provided in the Vienna Convention and current research, this thesis delivers a hybrid systemic interpretative approach that can be utilised to interpret treaty provisions in a balanced method, with the aim of striking a critical balance in international investment.

Meanwhile, this study will draw a map of balancing competing values on the basis of Chinese BITs and its domestic law. More details on the investment environment in China will also be presented. The findings in the current study, such as the analysis of the textual basis of proportionality, will provide a legal basis for China's much-needed sustainable investment policy and the appropriate measures to

¹⁷⁸ Vadi, *Proportionality* (n 22) 120-1.

¹⁷⁹ Zhang (n 55) 43-5.

balance the conflicts between foreign investors and the host state in its international investment.

1.7 The Structure of the Thesis

In order to answer the research question of whether the conflicting legitimate expectations of foreign investors and the host state in Chinese international investment can be balanced by applying proportionality based on the comparison between international practices of proportionality analysis and FET as well as analyses of the changes in Chinese domestic laws and BITs, the current study proceeds as below.

Chapter One: Introduction

Chapter Two: Proportionality—A Structured and Flexible Tool to Balance Conflicting Values

Chapter Three: The Interaction between Treaty Interpretation and Proportionality

Chapter Four: Fair and Equitable Treatment, Legitimate Expectations, and Proportionality

Chapter Five: The Application of the Principle of Proportionality in Balancing the Conflicting Legitimate Expectations of Foreign Investors and the Host State in the Argentinian Cases

Chapter Six: Can Proportionality Be Applied Based on Chinese Bilateral Investment Treaties?

Chapter Seven: Can Proportionality Be Applied Based on the Chinese Domestic Law?

Chapter Eight: Conclusion and Recommendations

The general application of proportionality at the national level will be introduced and analysed in Chapter Two, clarifying why and how it should be applied in the ISDS. The process of proportionality analysis and relevant factors that should be considered will also be presented, preparing for its application in a particular circumstance, namely international investment.

Considering issues arising from the application of proportionality and ambiguous treaty provisions, Chapter Three will investigate the proper interpretative approach that can be utilised to make a balanced treaty interpretation. The rules of interpretation stipulated in the Vienna Convention, particularly Articles 31 and 32, will be mainly analysed, followed by examining their applications in interpreting the FET standard in Chapter Four. On the one hand, many disputes, in practice, arise from the ambiguous FET clause; On the other hand, evident changes can be seen in the provision of FET by comparing different generations of Chinese BITs.¹⁸⁰ As proved by the data related to its prominence in IIAs and investment arbitration, FET, compared with other investment treatments provided to foreign investors, is the more suitable standard for examining proportionality analysis in treaty interpretation and application.¹⁸¹ The interpretations of FET via different interpretative approaches will be critically

¹⁸⁰ Text to 6.3.1 in Chapter Six.

¹⁸¹ Text to 1.2.3. At the time of writing, the FET standard is contained in almost 95 per cent of the available IIAs; The breach of FET has been referred to in over 85% ISDS.

examined and compared to present the primary trend of FET in IIAs. Also, the general contour of FET will be presented, which prepares for further discussion on the protection of legitimate expectations, one of its essential elements.

With the analyses of the legitimate expectations of foreign investors and the host state in Chapter Four, Chapter Five will focus on how the tribunals interpreted FET, particularly the protection of legitimate expectations in practice. Then, how proportionality was adopted by them to balance the disputing parties' conflicting legitimate expectations and relevant issues will be discussed. This chapter will mainly discuss and analyse a set of representative and influential ISDs arising from Argentina's economic crisis of 2001/2.¹⁸² This will focus on the possibility of striking a balance between investment protection and the protection of non-investment values in the host state by applying proportionality. Consequently, the textual basis of applying proportionality in the ISDS can be clarified. The tribunals' interpretations of treaty provisions and application of proportionality will also be presented. All these examinations and comparisons will underscore the establishment of a benchmark that can be utilised to examine whether proportionality can be adopted to settle Chinese ISDs.

From Chapter Six, the focus of this research will move to the application of proportionality in Chinese international investment. The languages of different generations of Chinese BITs will be expounded on and compared to understand whether the textual basis of proportionality is contained in treaties.

In order to seek an answer from its domestic context in Chapter Seven, Chinese domestic law, in particular the Chinese Constitutional Law¹⁸³ and Administrative Compulsion Law,¹⁸⁴ will be analysed to investigate whether the principle of proportionality is included in the Chinese domestic legal system. The findings in this Chapter will clarify the legal status of proportionality in China, contributing to ascertaining Chinese alternative routes to the application of proportionality in balancing conflicting values. They will further supplement the discussion on the nature of proportionality in Chapter Two, presenting a more precise account of this principle.

The analyses and examinations of the research will be concluded with an answer to the challenges of applying proportionality to strike a balance between the opposing values of foreign investors and the host state. From the international perspective, although proportionality cannot be universally applied to settle ISDs because it is neither an international custom nor a general principle of law, it can be brought into the ISDS regime by interpreting the case-related treaty through the two-tier systemic approach.

¹⁸² Argentinian cases (n 5).

¹⁸³ The Chinese Constitutional Law (n 45).

¹⁸⁴ The Chinese Administrative Compulsion Law (n 154).

From the Chinese perspective, applying proportionality as a principle in its domestic legal system is currently not available, considering the absence of "proportionality" in its domestic laws. However, if the present trend continues, proportionality is highly likely to be a principle, at least in Chinese administrative law. Although only the China-Colombia BIT (2008)¹⁸⁵ explicitly stresses the application of proportionality in balancing conflicting values, the language of other treaties, particularly the more recent Chinese BITs, implies the notion of proportionality. Compared with older treaties, the recent Chinese BITs stipulate clarified provisions of substantive treatment provided to foreign investors. They also emphasise the significance of non-investment values in the treaty preamble and main text and even provide foreign investors' obligations. All of these present the textual basis of proportionality in the ISDS.

With consideration of the relevant issues arising from the application of proportionality in the ISDS, the recommendations for a balanced paradigm of Chinese BITs can be suggested by the researcher. This strikes a balance between investment and non-investment values in Chinese international investment and sufficiently supports and protects China's outbound and inbound FDI.

¹⁸⁵ China-Colombia BIT (n 124).

Chapter 2

Proportionality—A Structured and Flexible Tool to Balance Conflicting Values

2.1 Introduction

It can be concluded from practice that different tools, such as reasonableness in China and balancing in the US, have been applied to review the measures taken by public authorities to weigh competing values. Compared with other legal principles, proportionality, which first originated in Germany, has been utilised at both national and international levels. By dictionary definition, "proportionality" describes "the quality, character, or fact of being proportional",¹⁸⁶ and "proportional" means "in due proportion, corresponding in degree or amount".¹⁸⁷ In this respect, the principle of proportionality optimises conflicting values, such as the public interest and private rights, by balancing the means-end relationship.¹⁸⁸ Although its application may vary from one state to another, proportionality has been adopted in many countries, like South Africa.¹⁸⁹ Meanwhile, it has appeared in several fields of international law, such as human rights law.¹⁹⁰

Due to its prevalence, proportionality has been noted by scholars as a valuable tool to strike a balance between the conflicting values of foreign investors and the host state in international investment.¹⁹¹ A typical example to present its significance in the ISDS is the Argentinian cases arising from the economic crisis of 2001/2.¹⁹² In these cases, the measures taken by Argentina to react to its crisis were challenged by investors as violations of its treaty obligations, expressing the conflicts between investment and non-investment values.¹⁹³ Proportionality had been utilised by the tribunals to balance

¹⁸⁶ 'Proportionality' (*OED*) <<https://www-oed-com.ezproxy-s1.stir.ac.uk/view/Entry/152773?redirectedFrom=proportionality#eid>> last accessed 6 October 2021.

¹⁸⁷ H. W. Fowler & F. G. Fowler (eds), *The Concise Oxford Dictionary of Current English* (J. B. Sykes, 7th edn, OUP 1982) 826.

¹⁸⁸ 'Proportionality' in Jonathan Law (ed), *A Dictionary of Law* (9th edn, OUP 2018) <<https://www.oxfordreference.com/view/10.1093/acref/9780198802525.001.0001/acref-9780198802525-e-3094?rsk=B3NRnC&result=3413>> last accessed 15 November 2020. Han, 'The Application of the Principle of Proportionality' (n 145) 636. Han, 'On the Application' (n 141) 234. Qinglin Zhang & Haiou Yu, 'On the Application of the Principle of Proportionality in the International Investment Arbitration' (2015) 13 *Presentday Law Science* 3, 4 [in Chinese]. Vadi, *Proportionality* (n 22) 54.

¹⁸⁹ Barak (n 20) 182. According to the map, the countries or districts that mention the principle of proportionality include: Germany, Canada, South Africa, Israel, Turkey, Brazil, the United States, New Zealand, Australia, Western European Countries (Austria, Portugal, Ireland, Spain, Belgium, The Netherlands, Switzerland, the UK., Greece), Latin American countries (Colombia, Peru, Mexico, Chile), All Central and Eastern European countries (Russia, Hungary, Poland, Lithuania, Slovenia, Czech), Asian countries or districts (the Republic of Korea, Hong Kong, India). As listed by Cohen-Eliya & Porat, the prevalent application of proportionality can be seen in Germany, Continental Europe, the UK, Canada, Israel, South Africa, Australia, New Zealand, Brazil, India, and the Republic of Korea. They call the spread of proportionality as "an undisputed fact" and point out that the US may be "the sole exception" to the application of proportionality. Concluded from practice, they also point out that proportionality may be contained in the US Constitutional Law. However, there is no any discussion on the legal status of proportionality in China. See Moshe Cohen-Eliya & Iddo Porat, 'Proportionality and the Culture of Justification' (2011) 59 *The American Journal of Comparative Law* 463, 465.

¹⁹⁰ Barak (n 20) 202-6.

¹⁹¹ Bücheler (n 18) 1, 194. Kingsbury & Schill (n 18) 79. Stephan W. Schill & Vladislav Djanic, 'Wherefore Art Thou? Towards a Public Interest-Based Justification of International Investment Law' (2018) 33 *ICSID Review-Foreign Investment Law Journal* 29, 46. Calamita, 'The Principle' (n 26). Barak (n 20) 131. Aikaterini Titi, *The Right to Regulate in International Investment Law* (Hart Publishing 2014) 35.

¹⁹² See generally in Chapter Five.

¹⁹³ Argentinian cases (n 5).

the conflicting values.¹⁹⁴ Unfortunately, the application of proportionality in these Argentinian cases had been affected by the lack of consensus on this principle, leading to different decisions on the challenged means.¹⁹⁵

In the current context of international investment, non-investment values in the host state can be limited by foreign investors' values, and such conflicts may be worse due to the pandemic, expressing that proportionality plays an increasingly important role in the ISDS. However, no universal consensus has been reached on proportionality, in particular, on its nature.¹⁹⁶ The approach in which proportionality can be brought into the ISDS regime is also uncertain because it is rooted in the domestic legal system and has not been explicitly expressed in IIAs.

The heated debates are mainly over whether proportionality is an international custom or a general principle of law. If proportionality falls into these two categories, it can be universally applied in treaty interpretation and application.¹⁹⁷ Bücheler regards proportionality as a general principle of law because it has been applied in various domestic legal systems.¹⁹⁸ At the same time, its application in several fields of international law reflects that it is transposable into international law.¹⁹⁹ However, it is argued by Vadi,²⁰⁰ who contends that any conclusion would be premature, and further study is required.²⁰¹ She asserts that the legal status of proportionality in some main legal systems, like China, is uncertain.²⁰² More specifically, no term "proportionality" has been stipulated in Chinese laws and regulations. Instead, the principle of reasonableness is currently applied in China.²⁰³ Proportionality's relationship with reasonableness is also convoluted and raises debates in China.²⁰⁴ Due to those uncertainties, identifying proportionality's nature is still an open-ended question.²⁰⁵

Meanwhile, problems arise from applying proportionality in practice, which can be observed in its structure and practical approach. Scholars agree on the relevant considerations that should be taken into account within proportionality analysis, but they diverge on the precise sequence of these factors.²⁰⁶

¹⁹⁴ See generally in Chapter Five.

¹⁹⁵ See generally in Chapter Five.

¹⁹⁶ Valentina Vadi, 'The Migration of Constitutional Ideas: The Strange Case of Proportionality in International Investment Law and Arbitration' in Andrea K. Bjorklund (ed), *Yearbook on International Investment Law and Policy 2013-2014* (OUP 2015) 337, 340.

¹⁹⁷ *ibid.*

¹⁹⁸ Bücheler (n 18) 31-63.

¹⁹⁹ *ibid* 33-4.

²⁰⁰ Vadi, *Proportionality* (n 22).

²⁰¹ *ibid* 120-1.

²⁰² *ibid* 120.

²⁰³ See 7.4.2 in Chapter Seven.

²⁰⁴ As discussed later in Chapter Seven, Chinese scholars can be divided into groups based on their different views on the relationship between proportionality and reasonableness.

²⁰⁵ Vadi, *Proportionality* (n 22) 120-1.

²⁰⁶ Lu Pan, 'The Origin and Feature of Proportionality' (*People's Court Daily*, 30 October 2020) (footnote omitted) <http://www.rmfb.com/paper/html/2020-10/30/content_173343.htm?div=-1> [in Chinese] last accessed 23 June 2022.

The mainstream view, for example, suggests that the application of proportionality contains four assessments, examining the legitimacy of the pursued purpose, the suitability and necessity of the questioned measure, and the relation between the benefits and the encumbrances, respectively.²⁰⁷ This opinion is supported by Barak.²⁰⁸ Other scholars hold the three-test view, in which the assessments of suitability, necessity, and proportionality *stricto sensu* are mentioned.²⁰⁹ Some of them, such as Bücheler, regard the legitimate purpose as a relevant consideration in the suitability test.²¹⁰ In the restrictive view, which is held by Chen, only the necessity test and the assessment of proportionality *stricto sensu* are referred to in the application of proportionality.²¹¹

The debates on whether it is a structured tool can also be observed in the practice of proportionality in different states. For example, South Africa has applied proportionality in a horizontal approach, in which its constituent elements are put at the same level, and no sequence exists between them.²¹² This approach, in Barak's view, expresses the application of proportionality as a recommendation.²¹³ Differently, Germany has adopted this tool vertically, applying its sub-tests successively.²¹⁴ Moreover, based on the later discussion in Chapter Seven, when reviewing the questioned specific administrative acts, some Chinese courts adopted the all-encompassing proportionality containing consecutive tests of suitability, necessity, and proportionality *stricto sensu*, whereas others merely applied the necessity test or the assessment of proportionality *stricto sensu*.²¹⁵

All the above uncertainties affect the application of proportionality in balancing the conflicting values of foreign investors and the host state, including their conflicting legitimate expectations of the latter's stable legal framework. This chapter will analyse the application of proportionality in weighing different values in general, in preparation for further investigation of how an investor-state relationship could be re-balanced by such a structured and flexible tool.

People's Court Daily is a daily newspaper owned by the People's Republic of China (PRC) Supreme People's Court (SPC).

²⁰⁷ Barak (n 20) 131. Im Rautenbach, 'Proportionality and the Limitation Clauses of the South African Bill of Rights' (2014) 17 Potchefstroom Electronic Law Journal 2229, 2233. Yossi Nehushtan, 'The Non-Identical Twins in UK Public Law: Reasonableness and Proportionality' (2017) 50 Israel Law Review 69, 74.

²⁰⁸ Barak (n 20) 131. Rautenbach (n 207) 2233.

²⁰⁹ Bücheler (n 18) 2. Kingsbury & Schill (n 18) 86. Robert Alexy, 'Proportionality and Rationality' in Vicki C. Jackson & Mark Tushnet (eds), *Proportionality-New Frontiers, New Challenges* (CUP 2017) 14. In Yang's view, the principle of proportionality has three sub-principles, which are suitability, necessity, and proportionality *stricto sensu*. In addition, a prerequisite for triggering the application of proportionality is that the fundamental rights are limited by the public authority. Dengjie Yang, 'Zhi Zhong Xing Quan De Xian Fa Bi Li Yuan Ze: Jian Yu Mei Guo Duo Yuan Shen Cha Ji Zhun Bi Jiao' (The Constitutional Principle of Proportionality of Executive Power: A Comparison with American Multivariate Review Benchmarks) (2015) 27 Peking University Law Journal 367, 370 [in Chinese].

²¹⁰ Bücheler (n 18) 2. Kingsbury & Schill (n 18) 86.

²¹¹ Chen (n 156).

²¹² Bücheler (n 18) 45. Barak (n 20) 132.

²¹³ Barak (n 20) 132.

²¹⁴ Bücheler (n 18) 45.

²¹⁵ See 7.5 in Chapter Seven.

The advantages of proportionality in balancing competing values will be introduced first to reflect its particularity. Proportionality and other tools, namely reasonableness and balancing, will be examined and compared in 2.2 to ascertain why proportionality should be applied to re-balance the investor-state relationship. The nature of proportionality will be examined in 2.3. This will investigate whether proportionality fulfils the requirements stipulated in Article 38 (1) of the ICJ Statute and how it can be brought into the ISDS regime: A treaty-based provision, an international custom, or a general principle of law.²¹⁶ The component of proportionality will be discussed in 2.4, followed by the analysis of its structure and the approach to its application in 2.5. Both horizontal and vertical methods of applying proportionality will be examined and compared to see which one prevails. The uncertainties regarding its application in practice, such as the decision-maker who has the power to decide whether the state interest is at stake and needs to be protected by particular measures, will be briefly discussed in this chapter. More details will be provided in Chapter Five, which chiefly focuses on the particular role of proportionality in the context of international investment.²¹⁷

2.2 Proportionality—A Structured and Flexible Tool

The tools utilised to review the measures taken by public authorities vary according to each circumstance. As shall be discussed in Chapter Seven, for instance, reasonableness and proportionality are obfuscated in Chinese administrative laws and policies.²¹⁸ Instead of proportionality, balancing is applied in the US. Thus, one may question why proportionality is the most appropriate tool with which to strike a balance in the conflicting legitimate expectations of foreign investors and the host state to settle ISDs. These different tools will be examined and compared below to present, in the researcher's view, the advantage of proportionality in weighing competing values: A compromise between structure and flexibility.

2.2.1 Proportionality and Reasonableness—"the Non-Identical Twins"

As evaluated by Nehushtan, proportionality and reasonableness are "the non-identical twins",²¹⁹ indicating they are different with certain similarities. Some factors are included in both principles. For instance, discerning between competing values, which is considered in proportionality analysis, is also taken into account in the test of reasonableness.²²⁰ Their unclear relationship can be seen in the Chinese domestic legal system, particularly administrative law.²²¹ As pointed out by He, however, despite their similarities, proportionality differs from reasonableness in several aspects: From components to nature, from structure to function.²²²

²¹⁶ ICJ Statute (n 19) Article 38 (1).

²¹⁷ See generally in Chapter Five.

²¹⁸ See 7.4.2 in Chapter Seven.

²¹⁹ Nehushtan (n 207) 69.

²²⁰ *ibid* 76.

²²¹ See 7.4.2 in Chapter Seven.

²²² He (n 156). Yang (n 161). Xuexian Huang, 'Xing Zheng Fa Zhong De Bi Li Yuan Ze Yan Jiu' (The Research on the Principle of

Compared with reasonableness, proportionality has more detailed constituent elements. Consequently, more specific guidance on judging conflicting values is provided within proportionality analysis.²²³ As asserted by Barak, no consensus has been reached on the components of reasonableness, which vary from one circumstance to another.²²⁴ Some Chinese scholars point out that the factors that should be considered in the test of reasonableness include the legitimate purpose, the consideration of relevant factors, and the equal application of the law.²²⁵ Any consideration of irrelevant factors will lead to the violation of the reasonableness principle.²²⁶ However, based on the later discussion in 2.4, the application of proportionality refers to different factors, containing the legitimate purpose, the rational means-end connection, the less restrictive means, and a balance between the achieved benefit and the infringed interest (proportionality *stricto sensu*).²²⁷ That is to say, proportionality and reasonableness have different components. In Nehushtan's view, their critical difference is the factor of "necessity".²²⁸ As required by necessity, the measures taken by any public authority should achieve the pursued purpose with less limit on the protected rights,²²⁹ which is not required in the test of reasonableness.

The difference between proportionality and reasonableness can also be reflected in their nature. Proportionality is objective, while reasonableness is subjective.²³⁰ Consequently, compared with that of the test of reasonableness, the result of proportionality analysis is more straightforward and definite. Whether a measure in question is proportionate to the achieved purpose is expressed by a number or portion.²³¹ As put by Li, such a specific number reflects that proportionality is objective and cannot be affected by an individual's understanding.²³² On the contrary, the term "reasonable" is open to ambiguity, and its meaning varies from one person to another.²³³ Besides, no defined criterion can be used to describe what action is reasonable.²³⁴ Compared with that of proportionality analysis, the result of the reasonableness test, to a certain extent, may be affected by the decision-maker's understanding of "reasonable".

Proportionality in Administrative Law) (2001) Science of Law 72, 78 [in Chinese].

²²³ Nehushtan (n 207) 81.

²²⁴ Barak (n 20) 373-4.

²²⁵ Luo & Zhan (n 156) 31-2. Linyun Yu, 'Lun Xing Zheng Fa Shang De Bi Li Yuan Ze' (On the Principle of Proportionality in Administrative Law) (2002) The Jurist 31, 37 [in Chinese]. He (n 156). Nehushtan (n 207) 70.

²²⁶ Yu (n 225) 37.

²²⁷ Text to 2.4. He (n 156) 36.

²²⁸ Nehushtan (n 207) 75-8, 85.

²²⁹ Text to 2.4.3.

²³⁰ Yan Li, 'Lun Bi Li Yuan Ze' (On the Principle of Proportionality) [2012] Administrative Law Review 37, 41 [in Chinese].

Nehushtan (n 207) 70. He (n 156) 36.

²³¹ Li (n 230) 41.

²³² *ibid.*

²³³ *ibid.* Nehushtan (n 207) 70.

²³⁴ *ibid.*

Meanwhile, proportionality is quantitative, while reasonableness is qualitative.²³⁵ Whether the questioned measure satisfies the principle of proportionality can be evaluated by a set of examinations and finally expressed by a particular proportion or number.²³⁶ Within this process, both the achieved benefit and the impaired value are considered.²³⁷ However, the test of reasonableness aims to answer whether or not the measure in question is reasonable.²³⁸ This assessment merely focuses on the impugned measure itself without any consideration of the counterpart's rights affected by it.²³⁹

Moreover, the internal logical order of its constituent elements should be followed when applying proportionality, which is one of its advantages.²⁴⁰ The application of proportionality refers to a structured approach and stricter threshold to review the measures in question, whereas the process of identifying whether it is reasonable is not structured.²⁴¹ As pointed out by Barak, the test of reasonableness is carried out with no reference to the sequence of suitability, necessity, and proportionality *stricto sensu*, which is emphasised in proportionality analysis.²⁴² Therefore, based on the application of proportionality, the questioned measure can be assessed with more precise tests.²⁴³ In other words, as a tool, proportionality, in comparison with reasonableness, provides more objective and stricter guidance as well as a structured approach to reviewing the means taken by public authorities. Consequently, as asserted by Nehushtan, the proportional measure is also reasonable, but the reasonable means may be not proportionate in relation to the desired purpose.²⁴⁴

2.2.2 Proportionality and Balancing

Despite its implied rigidity, proportionality also has flexibility. This advantage can be observed by comparing it with balancing, which is utilised in the US to review governmental actions.²⁴⁵ The latter contains three fixed levels, including minimal security, intermediate security, and strict security.²⁴⁶

Compared with the relatively flexible application of proportionality, these three levels included in

²³⁵ He (n 156). Yubiao Liu, 'Xing Zheng Bi Li Yuan Ze Zai Zhong Guo De Yan Bian' (The Evolution of the Principle of Proportionality in Chinese Administrative Law) [2017] Legal System & Society 17 [in Chinese]. Linhong Yang, 'Xing Zheng Fa Zhong De Bi Li Yuan Ze Yan Jiu' (The Research on the Principle of Proportionality in Administrative Law) [2001] Law & Social Development 42, 46 [in Chinese].

²³⁶ Li (n 230) 41.

²³⁷ Text to 2.4. Barak (n 20) 132, 460-7. He (n 156) 36.

²³⁸ He (n 156). Liu (n 235) 17. Yang (n 235) 46.

²³⁹ He (n 156) 36.

²⁴⁰ Nehushtan (n 207) 75-8, 85. Barak (n 20) 132. More detailed analyses can be seen in 2.4.

²⁴¹ Nehushtan (n 207) 84. Barak (n 20) 375, 377.

²⁴² Barak (n 20) 375.

²⁴³ *ibid* 376.

²⁴⁴ Nehushtan (n 207) 76-7. Barak (n 20) 377.

²⁴⁵ Moshe Cohen-Eliya & Idoo Porat, 'American Balancing and German Proportionality: The Historical Origins' (2010) 8 International Journal of Constitutional Law 263, 264.

²⁴⁶ Quan Liu, 'Mu Di Zheng Dang Xing Yu Bi Li Yuan Ze De Chong Gou' (The Legitimacy of Pursued Purpose and the Reconstruction of Proportionality) (2014) 4 China Legal Science 133, 142 [in Chinese]. Jud Mathews & Alec Stone Sweet, 'All Things in Proportion? American Rights Doctrine and the Problem of Balancing' (2010) 60 Emory Law Journal 797, 836. Aharon Barak, 'Proportionality and Principled Balancing' (2010) 4 Law & Ethics of Human Rights 1, 9.

balancing are strictly adhered to in reviewing the impugned measures that are pre-classified according to different circumstances.²⁴⁷ More specifically, strict scrutiny is the highest level of review, which refers to the governmental actions that fall into the category of "suspect classifications", such as race and religion.²⁴⁸ In order to meet the requirements, the pursued purpose must be a "compelling state interest".²⁴⁹ If the affected values are related to the "quasi-suspect classifications" like gender, the governmental actions are then reviewed according to intermediate scrutiny.²⁵⁰ At this level, the pursuant value is deemed "an important state interest".²⁵¹ A substantive connection between the limits and the achieved benefit should be fulfilled.²⁵² Lower order measures that impair rights in other fields, such as economic rights, are reviewed according to minimal scrutiny,²⁵³ the lowest threshold.²⁵⁴ As it requires, the state interest should be "legitimate", and the means-end connection should be rational.²⁵⁵

Both proportionality and balancing refer to weighing different values. More specifically, as evaluated by Cohen-Eliya and Porat, only the proportionality *stricto sensu*, the last factor contained in proportionality emphasising the real balance between conflicting values, is similar to balancing.²⁵⁶ However, their differences can be seen in other aspects. The scope of proportionality is broader than that of balancing. As analysed later, the whole process of applying proportionality can be generally divided into two stages: The rational means-end connection and the utilitarian trade-off between the conflicting values.²⁵⁷ Conversely, the trade-off only focuses on the stage at which the competing values are weighed and balanced against each other. Therefore, the aim of balancing may be fulfilled by proportionality, but it cannot achieve what proportionality pursues. Cohen-Eliya and Porat further clarify that the aim of balancing differs from that of proportionality.²⁵⁸ The former decreases unnecessary protections provided to the rights, while the latter prevents the rights from the unnecessary limit.²⁵⁹

The difference between balancing and proportionality can also be observed from their practical applications. The objectives of balancing have been explicitly pre-set with clear thresholds.

²⁴⁷ *ibid.*

²⁴⁸ Aaron Baker, 'Proportional, Not Strict, Scrutiny: Against a US "Suspect Classifications" Model under Article 14 ECHR in the UK' (2008) 56 *The American Journal of Comparative Law* 847, 868.

²⁴⁹ *ibid.*

²⁵⁰ *ibid* 869.

²⁵¹ *ibid.*

²⁵² *ibid.*

²⁵³ *ibid* 870.

²⁵⁴ *ibid.*

²⁵⁵ *ibid.*

²⁵⁶ Cohen-Eliya & Porat, 'American Balancing' (n 245) 268.

²⁵⁷ See in 2.4, the suitability and necessity tests aim to ascertain a means-end connection, while the assessment of proportionality *stricto sensu* is a value-oriented real balance between conflicting values. Cohen-Eliya & Porat, 'American Balancing' (n 245) 268. Barak (n 20) 461.

²⁵⁸ Cohen-Eliya & Porat, 'American Balancing' (n 245) 266.

²⁵⁹ *ibid* 266, 284.

Consequently, the questioned measure can be reviewed by reference to the fixed values criteria. However, such classifications are not provided for applying proportionality. The whole process of proportionality analysis depends on the actual circumstances, namely the means-end connection in each case. Different factors are considered to balance the conflicting values to decide whether the implemented measure is proportionate to the achieved benefit. In this regard, proportionality is more flexible than balancing, leaving some room for review. As shall be discussed later, although some issues may arise from the decision-maker, in the application of proportionality, this tool contributes to a balanced investor-state relationship in matters of international investment.²⁶⁰

As suggested by the above examinations and comparisons, proportionality is between the two ends of the spectrum: Reasonableness and balancing. The principle of reasonableness allows the reviewers to exercise discretionary power without guidance on the sequence of considerations. On the other end, the balancing provides details on considerations but restricts the reviewers' discretion. Compared with them, proportionality has characteristics from both ends of the spectrum, reflecting the compromise between delegation and restriction, yet indicating a balance. Therefore, by applying proportionality, the reviewers can review the impugned measure according to the actual circumstances; Meanwhile, they are provided with a logical order based on which the review should be carried out.

2.3 The Legal Status of Proportionality in International Law

As rooted in the domestic legal system, one may question whether the source of proportionality lies in the phrase "rules of international law as may be applicable" in Article 42 (1) of the ICSID Convention.²⁶¹ The term "international law", as clarified in the Report of the Executive Directors on the ICSID Convention, should be understood as it is defined in Article 38 (1) of the ICJ Statute.²⁶² That is to say, proportionality, which is a useful tool to weigh and balance competing values, can be universally applied if it falls into the categories of the rules of customary international law or general principles of law in Article 38 (1) of the ICJ Statute.²⁶³ Otherwise, its application depends on the legal instrument applicable to the case. This issue, arising from the nature of proportionality, lies in the divergences that require treaty interpretation in international investment.

However, no consensus has been reached on the legal status of proportionality in international law. To add to the confusion, proportionality has been applied by the tribunals in the ISDS via treaty interpretation, or application, if the term or its equivalent appears in the case-related treaty, implicitly

²⁶⁰ See generally in Chapters Five and Six.

²⁶¹ ICSID Convention (n 7) Article 42 (1). This can also be seen from some BITs, see an example China-Tanzania BIT (signed 24 March 2013, entered into force 17 April 2014) Article 13 (6).

²⁶² 'Draft Convention: Working Paper for the Legal Committee' Article 45 (1) in ICSID, History of the ICSID Convention Volume II-1 (1968) 630.

²⁶³ ICJ Statute (n 19) Article 38 (1).

or explicitly.²⁶⁴ As proportionality has been examined in the more recent arbitral awards, it is essential to understand the debates surrounding its nature as an international custom or a general principle of law.

2.3.1 Is Proportionality an International Custom?

According to Article 38 (1) (b) of the ICJ Statute, the international custom is "evidence of a general practice accepted as law".²⁶⁵ As reflected, the requirements of becoming an international custom refer to "general practice" (state practice) and "accepted as law" (*opinio juris*).²⁶⁶

2.3.1.1 Inconsistent and Non-Uniform Application of Proportionality

"State practice" is an objective requirement,²⁶⁷ requiring that the practice in question be applied consistently and uniformly by the most representative states.²⁶⁸ Besides, in Dumberry's view, a temporal element, closely linked to the generality and consistency of the questioned practice,²⁶⁹ should also be satisfied.²⁷⁰ As he ascertained, the more general and consistent a practice is, the shorter period is needed.²⁷¹ Equally, the less widespread and the more inconsistent, the more time is required for the universal application.²⁷² However, as clarified by the UN, the duration in which the principle is applied contributes to the formation of an international custom, but it is not a *sine qua non*.²⁷³ In other words, the time requirement is supplemental, instead of an essential element to form an international custom. Therefore, this section will mainly examine whether proportionality fulfils the requirements of state practice from its generality and consistency perspectives.

Nevertheless, the absence of a definite criterion for a state's representativeness, as well as the consistency and uniformity of its practice leads to heated debates. In Villiger's view, the representative states come from "all major political and social-economic systems".²⁷⁴ He links a state's representativeness to its national strength: The more powerful the state, the more representative it is.²⁷⁵ One may doubt the reliability of this criterion because powerful states may not be outstanding in all

²⁶⁴ As shall be discussed later, especially in Chapter Six, the concept of proportionality is explicitly expressed in China-Colombia BIT (n 124), which requires the disputed measures should be "proportional to the desired purpose it pursues" to be justified.

²⁶⁵ ICJ Statute (n 19) Article 38 (1) (b).

²⁶⁶ Dumberry, *The Formation* (n 23) 31. James Crawford, *Brownlie's Principles of Public International Law* (8th edn, OUP 2012) 23.

²⁶⁷ Dumberry, *The Formation* (n 23) 31, 128. ILC, 'Second Report on Identification of Customary International Law', by Michael Wood, Special Rapporteur, ILC Sixty-sixth Session, Geneva, 5 May-6 June and 7 July-8 August 2014, UN doc. A/CN.4/672, 8.

²⁶⁸ *ibid.* Andreas Zimmermann, Christian Tomuschat & Karin Oellers-Frahm (eds), *The Statute of International Court of Justice-A Commentary* (OUP 2012) 752.

²⁶⁹ Dumberry, *The Formation* (n 23) 128, 138. Zimmermann, Tomuschat & Oellers-Frahm (n 268) 753.

²⁷⁰ Dumberry, *The Formation* (n 23) 138.

²⁷¹ *ibid.* 138-9. Mark E. Villiger, *Customary International Law and*

Treaties—A Manual on the Theory and Practice of the Interrelation of Sources (2nd edn, Kluwer Law International 1997) 46.

²⁷² *ibid.*

²⁷³ ILC, 'Second Report on Identification of Customary International Law' (n 267) 40.

²⁷⁴ Villiger, *Customary International Law* (n 271) 29. Dumberry, *The Formation* (n 23) 134.

²⁷⁵ *ibid.*

fields, *vice versa*. As clarified by the ILA, "the representative state" is a qualitative rather than a quantitative requirement.²⁷⁶ Instead of a powerful country, the state whose interests are "specially affected" by the practice in question plays a significant role in the formation of an international custom.²⁷⁷

On account of fluidity in the "specially affected states" status, such states vary very much by circumstance.²⁷⁸ Consequentially, as observed by the Dumberry, the "specially affected states", in the context of international investment are those who are the most active participants.²⁷⁹ The activity level can be reflected by the amount of concluded IIAs as well as the number of investor-state activities and disputes in which they are involved.²⁸⁰ Therefore, the leading investment countries, such as Germany, China, and the US, fall into this category, since they have concluded most IIAs or been involved in most ISDs.²⁸¹ Whether proportionality has been consistently and uniformly utilised by these states needs to be unambiguous to ascertain whether it is an international custom or not.

Regarding the standard for its consistent application, the ILA stressed that instead of a complete universal consistency, the practice "must be *virtually uniform*, both *internally* and *collectively*",²⁸² reflecting national and international requirements. At the national level, the state, in general, should keep the same attitude when acting.²⁸³ In other words, the same approach should also be required by different administrative organs of a state acting consistently and uniformly in relevant circumstances.²⁸⁴ At the international level, no substantive differences should exist in those states' practices that contribute to forming an international custom.²⁸⁵

Concluded from practice, it is not the time to regard proportionality as an international custom. Different from Germany, where proportionality first originated, whether the US and China refer to this principle in domestic legal systems, as noted by Vadi, is still questioned.²⁸⁶ As she stressed, the current research on proportionality mainly focuses on certain selected legal systems, which cannot represent the

²⁷⁶ *supra* note 23.

²⁷⁷ UN (n 23) 137.

²⁷⁸ ILA (n 23).

²⁷⁹ Dumberry, *The Formation* (n 23) 136.

²⁸⁰ *ibid*.

²⁸¹ Data collected from Investment Policy Hub. 'International Investment Agreements Navigator-IIAs by Economy' (*Investment Policy Hub*) <<https://investmentpolicy.unctad.org/international-investment-agreements/by-economy>> last accessed 24 June 2022. 'Investment Dispute Settlement Navigator-Countries' (*Investment Policy Hub*) <<https://investmentpolicy.unctad.org/international-investment-agreements/by-economy>> last accessed 24 June 2022. More detail as to China please see Chapter Six.

²⁸² ILA (n 23) 21 [italic added]. Dumberry, *The Formation* (n 23) 130.

²⁸³ *ibid*.

²⁸⁴ *ibid*.

²⁸⁵ ILA (n 23) 21. Dumberry, *The Formation* (n 23) 129-31.

²⁸⁶ Vadi, *Proportionality* (n 22). Calamita, 'The Principle' (n 26). Cohen-Eliya & Porat, 'Proportionality' (n 189) 465.

whole.²⁸⁷ The ILA Final Report also commented that if the principle in question fails to be accepted by significant actors, it is not yet sufficiently mature to be considered as an international custom.²⁸⁸

China is a vital player in modern international investment, but its practice of proportionality has never been taken into account by those scholars who regard such a principle as an international custom or a general principle of law.²⁸⁹ Although some Chinese courts have utilised it as a basis for their decisions, proportionality has not been stipulated in Chinese laws and regulations.²⁹⁰ As a result, even if Chinese practice is considered, its contribution to the transformation of proportionality as an international custom is limited. However, the underlying trend of applying proportionality in the Chinese domestic legal system cannot be ignored, this will be further discussed in Chapter Seven.²⁹¹

Furthermore, Kulick opines that proportionality has not been uniformly applied even in those countries whose domestic legal systems include this principle.²⁹² Based on the later discussion in 2.5.2, the application of proportionality varies according to each particular circumstance.²⁹³ The typical examples can be seen in the practice of proportionality in Germany and South Africa. The former applies proportionality according to its internal logical order, whereas the latter selectively utilises its components.²⁹⁴ This observation also corresponds with the interpretation provided in Chapter Seven, where the application of proportionality varies based on circumstances in which the Chinese courts apply it to review specific administrative acts.²⁹⁵ Considering its inconsistent and non-uniform application, proportionality fails to be a general practice.²⁹⁶

2.3.1.2 Is Proportionality Accepted as Law?

Apart from the above objective requirement, concerns are also raised over whether proportionality is "accepted as law" to be an international custom.²⁹⁷ If so, proportionality is adopted by the specially affected states out of "a sense of legal obligation".²⁹⁸ This requirement is closely linked to the intention of the party who utilises it in practice. As pointed out by the International Law Commission (ILC), a

²⁸⁷ Vadi, *Proportionality* (n 22). One selected legal system is German domestic legal system. Even when discussing the uncertainties as to the application of proportionality in different jurisdictions, that is the US rather than China has been mentioned. See in Cohen-Eliya & Porat, 'Proportionality' (n 189) 463, 465. Barak (n 20) 181-202, 206-10.

²⁸⁸ ILA (n 23).

²⁸⁹ For the example Barak (n 20).

²⁹⁰ Han, 'The Application of the Principle of Proportionality' (n 145) 635. See generally in Chapter Seven.

²⁹¹ See generally in Chapter Seven. The trend of applying proportionality in Chinese administrative law is relatively evident.

²⁹² Andread Kulick, *Global Public Interest in International Investment Law* (CUP 2012) 169.

²⁹³ Text to 2.5.2. Barak (n 20) 460-2.

²⁹⁴ Text to 2.5.2. Bücheler (n 18) 45. Barak (n 20) 132.

²⁹⁵ See 7.5.1 in Chapter Seven.

²⁹⁶ Text to 2.3.2. Another specially affected state, the US, adopts balancing instead of proportionality to review governmental actions.

²⁹⁷ ICJ Statute (n 19) Article 38 (1) (b).

²⁹⁸ UN (n 23) 138. ICJ Statute (n 19) Article 38 (1) (b). Dumberry, *The Formation* (n 23) 31, 128. ILC, 'Second Report on Identification of Customary International Law' (n 267) 8.

state's intention can be investigated from two perspectives: positive and negative.²⁹⁹ If a state takes some positive action, such as explicitly recognising the practice in question as a legal obligation, *opinio juris* then exists.³⁰⁰ From the negative perspective, there is no such intention if the questioned practice is denied by the state.³⁰¹

Nevertheless, Dumberry notes that the problem is that those states in international investment have seldom expressed their intentions.³⁰² Considering the complex structure of a state, which consists of different organs, the difficulties in understanding its intention as a unit are increased because the reason for one authority's action may differ from others.³⁰³ Such a difficulty is reemphasised when ascertaining the intention of the parties in the interpretation of disputed words.³⁰⁴ As highlighted by Schreuer, the problems are in accessing *travaux préparatoires* of BITs, which may not be documented and may not be available to the public.³⁰⁵ Due to the vital role of *travaux préparatoires* in treaty interpretation, more detail will be analysed and discussed in Chapter Three, which chiefly concentrates on the appropriate approach to treaty interpretation.³⁰⁶ The historical materials related to the negotiations of IIAs, which reflect treaty parties' common intention, are not freely available to the public.³⁰⁷ For example, in *Pope & Talbot v. Canada*,³⁰⁸ even though the tribunal requested the contracting parties to provide documents of the negotiating history to understand further the inconsistencies between provisions of BITs and Article 1105 of the North American Free Trade Agreement (NAFTA), they denied the existence of such materials.³⁰⁹

In response to that situation, Tudor opines that although a state's intention is not explicitly expressed in IIAs, it can still be extrapolated from the repeated treaty provisions.³¹⁰ As argued by the UN, the same rule that appears in many treaties "*may, but does not necessarily*" reflect an international custom.³¹¹ This evaluation recognises the contribution of repeated clauses to forming an international custom; However, it also emphasises that these two factors have no necessary connection.³¹² One prime example to illustrate such a "may, but not necessary" relation is the provision of FET, which has been stipulated in almost 95 per cent of the available IIAs (2574 in total).³¹³ Although FET is a prevalent standard

²⁹⁹ ILC, 'Second Report on Identification of Customary International Law' (n 267) 59.

³⁰⁰ *ibid.*

³⁰¹ *ibid.*

³⁰² Dumberry, *The Formation* (n 23) 295-6.

³⁰³ *ibid.* 296.

³⁰⁴ See 3.3.5 and 3.3.6 in Chapter Three.

³⁰⁵ Schreuer, 'Diversity' (n 76) 137.

³⁰⁶ See in Chapter Three.

³⁰⁷ Zhang (n 55) 120-2.

³⁰⁸ *Pope & Talbot v. Canada*, UNCITRAL, Award in Respect of Damages, 31 May 2002.

³⁰⁹ *ibid.* paras 26, 28.

³¹⁰ Tudor (n 87) 82-3, 85.

³¹¹ UN (n 23) 143, 146 [*italic added*].

³¹² *ibid.* 146.

³¹³ *supra* note 84. See in Chapter Four.

provided in most IIAs, as discussed later in Chapter Four, whether it is viewed or accepted as an international custom is still subject to debate.³¹⁴

Moreover, Tudor's view may not hold the whole truth in the case of proportionality because most IIAs have no provision that refers to proportionality, or its constituent elements, such as necessity.³¹⁵ At the time of writing, in 2574 signed IIAs, the provision of "essential security exception" is stipulated in 394 treaties,³¹⁶ the "public health and environment exceptions" clause is prescribed in 240 treaties,³¹⁷ and the provision of "other public policy exceptions" is provided in 236 treaties.³¹⁸ The actual number would be less because a treaty may contain several exception clauses: From general to particular exceptional situations.³¹⁹ Even if these repeated provisions can reflect a state's intention, they may actually indicate otherwise: It is a treaty-based obligation instead of a rule of customary international law.³²⁰ If the principle of proportionality had enjoyed universal applicability as an international custom, there would be no need to prescribe such a clause in treaties. Therefore, proportionality should not be viewed as an international custom because it fails to satisfy the above requirements of "state practice" and "*opinio juris*" stipulated in Article 38 (1) (b) of the ICJ Statute.

2.3.2 Is Proportionality a General Principle of Law?

Nevertheless, proportionality can still be universally applied in balancing competing values if it fulfils the requirements of general principles of law, which are also prescribed in Article 38 (1) of the ICJ Statute.³²¹ However, there are heated debates over its acceptance as a "general principle of law recognised by civilised nations". As pointed out by Bermúdez in the First Report on General Principles of Law, the term "law" in Article 38 (1) (c) of the ICJ Statute is not limited by any adjective,³²² indicating two potential routes to the formation of a general principle of law.³²³ One is the origination from

³¹⁴ See 4.3 in Chapter Four.

³¹⁵ Text to see 2.4.3.

³¹⁶ "Essential Security Exception" included in BITs' (*Investment Policy Hub*) <<https://investmentpolicy.unctad.org/international-investment-agreements/iia-mapping#section-91>> last accessed 24 June 2022.

³¹⁷ "Public Health and Environment" included in BITs' (*Investment Policy Hub*) <<https://investmentpolicy.unctad.org/international-investment-agreements/iia-mapping#section-91>> last accessed 24 June 2022.

³¹⁸ "Other Public Policy Exceptions" included in BITs' (*Investment Policy Hub*) <<https://investmentpolicy.unctad.org/international-investment-agreements/iia-mapping#section-91>> last accessed 24 June 2022.

³¹⁹ See an example China-Mauritius BIT (signed 4 May 1996, entered into force 8 June 1997) Article 11, which reads that '[t]he provisions of this Agreement shall not in any way limit the right of either Contracting Party to apply prohibitions or restrictions of any kind or take any other action which is directed to the protection of its essential security interests, or to the protection of public health or the prevention of diseases and pests in animals or plants or the protection of its environment'. This BIT was replaced by China-Mauritius FTA (signed 17 October 2019, entered into force 1 January 2021).

³²⁰ UN (n 23) 146.

³²¹ ICJ Statute (n 19) Article 38 (1) (c).

³²² ILC, 'First Report on General Principles of Law', by Marcelo Vázquez-Bermúdez, Special Rapporteur, ILC Seventy-first Session, Geneva, 29 April-7 June and 8 July-9 August 2019, UN doc. A/CN.4/732, 46.

³²³ *ibid* 52. Vadi, *Proportionality* (n 22) 122.

domestic legal systems, while the other is the formation within the international legal system.³²⁴

2.3.2.1 Derived from Domestic Legal Systems?

According to Article 38 (1) (c) of the ICJ Statute, to be a general principle of law, the principle in question should be "general" and "recognised" by "civilised nations".³²⁵ Clearly, the term "civilised nations" is unhelpful, on account of its irrelevance in modern discourse.³²⁶ As clarified by Sloan, this term was previously aimed to distinguish the civilised countries from those that are not.³²⁷ Only European Christian states were deemed civilised and therefore allowed to participate in the formation of international law when the term "civilised nation" was meaningful.³²⁸ However, as the modern age ushered in greater diversity, this outdated perspective became irrelevant.³²⁹ In Bassiouni's view, except extreme situations, this requirement "civilised nations" is no longer considered because all member-states of the UN, including China, are "civilised" because they have mature legal systems.³³⁰ In the ILC Second Report, Bermúdez also highlights that "civilised nations", as an anachronistic term, has no contribution to identifying general principles of law, stressing that all nations "must" be considered to be civilised.³³¹

As a consequence of reimagining the "civilised nation" standard, the process of identifying general principles of law refers to two steps.³³² Firstly is the principle of proportionality common at the national level?³³³ Secondly, if so, is it still applicable at the international level? Thus, its transportability is tested.³³⁴ A comparison between domestic legal systems is necessary to examine whether the principle in question has been broadly applied at the national level.³³⁵

³²⁴ *ibid.* M. Cherif Bassiouni, 'A Functional Approach to "General Principles of International Law"' (1990) 11 *Michigan Journal of International Law* 768, 772.

³²⁵ ICJ Statute (n 19) Article 38 (1) (c).

³²⁶ James Sloan, 'Civilised Nations' (*Oxford Public International Law*, April 2011)

<<https://opil.ouplaw.com/view/10.1093/law:epil/9780199231690/law-9780199231690-e1748#law-9780199231690-e1748-div1-1>> last accessed 24 June 2022. ILC, 'First Report on General Principles of Law' (n 322) 52.

³²⁷ *ibid.*

³²⁸ *ibid.*

³²⁹ ILC, 'First Report on General Principles of Law' (n 322) 54.

³³⁰ Bassiouni (n 324) 768. As he exemplified, one special situation is that a country has no longer a civilised legal system due to some peculiar historical circumstances.

³³¹ ILC, 'Second Report on General Principles of Law', by Marcelo Vázquez-Bermúdez, Special Rapporteur, ILC Seventy-second Session, Geneva, 27 April-5 June and 6 July-7 August 2020, UN doc. A/CN.4/741, 2, para 2 (d), para 3.

³³² Bücheler (n 18) 32.

³³³ *ibid.* Michael Wood, 'Customary International Law and the General Principles of Law Recognised by Civilised Nations' (2019) 21 *International Community Law Review*, 307, 318. ILC, 'First Report on General Principles of Law' (n 322) 8.

³³⁴ Bücheler (n 18) 32.

³³⁵ ILC, 'First Report on General Principles of Law' (n 322) 8, 65. Wood (n 333) 317. See also Christopher A Ford, 'Judicial Discretion in International Jurisprudence: Article 38 (1) (c) and General Principles of Law' (1994) 5 *Duke Journal of Comparative & International Law* 38, 66. Zakiyyu Muhammad & Usman Suleiman Jahun, 'An Examination of Article 38 (1) of the Statute of the International Court of Justice 1945 as a Source of International Law' (2017) 7 *International Journal of Scientific & Research Publication* 427, 429.

However, there is no definite number of the states whose recognitions can prove a broad application.³³⁶ Brazil expressed its opinion in the 72nd session of the UN General Assembly, stating that the questioned principle should be identified on the basis of "all legal systems of the world".³³⁷ Such an overly broad view is challenged by scholars.³³⁸ As argued by Bermúdez, a principle has been broadly applied if it is common to a sufficiently large number of domestic legal systems.³³⁹ In addition, Bücheler stresses the significance of the state's representativeness.³⁴⁰ As opined by him, a principle has broad application if recognised by "a fair number of representative legal systems".³⁴¹ A similar view is held by Schreuer, who emphasises that the principle in question should be common, at least, in "the most important major representative systems".³⁴² Therefore, whether the application of proportionality is broad can be tested by two similar but different criteria: Recognition by most states or by prominent and representative states.

Based on the first criterion, proportionality is common because of its prevalent application in enough domestic legal systems to be considered sufficiently widespread. As mapped by Barak, since 1958, this principle has been adopted in both developed and developing states.³⁴³ It is also prevalent from Europe to Asia, from Germany to South Africa.³⁴⁴ In this regard, proportionality has been utilised widely at the national level.³⁴⁵

According to the second criterion, proportionality is required to be established in the most representative states, which can indicate the formation of an international custom.³⁴⁶ As we have seen, representative states are those who are especially active in international investment.³⁴⁷ However, proportionality fails to meet this requirement due to the uncertainties regarding its domestic legal status in some leading international investors, including China.³⁴⁸

Those two criteria leading to different results on the universality of the application of proportionality

³³⁶ ILC, 'First Report on General Principles of Law' (n 322) 49-50, 64. Rumiana Yotova, 'Challenges in the Identification of the General Principles of Law Recognised by Civilised Nations: The Approach of the International Court' (2017) 3 *Canadian Journal of Comparative & Contemporary Law* 269, 282.

³³⁷ UN, 'Sixth Committee Summary Record of the 21st Meeting', 25 October 2017, UN doc. A/C.6/72/SR.21, para 15. ILC, 'First Report on General Principles of Law' (n 322) 59.

³³⁸ Bücheler (n 18) 32. Bassiouni (n 324).

³³⁹ ILC, 'First Report on General Principles of Law' (n 322) 49-51. Wood (n 333) 317.

³⁴⁰ Bücheler (n 18) 32, 51.

³⁴¹ *ibid* 32.

³⁴² Schreuer & others, *The ICSID Convention* (n 39) 610. Valentina Vadi, *Analogies in International Investment Law and Arbitration* (CUP 2015) 123.

³⁴³ Barak (n 20) 182. Cohen-Eliya & Porat, 'Proportionality' (n 189) 463, 465.

³⁴⁴ Barak (n 20) 182. Cohen-Eliya & Porat, *Proportionality and Constitutional Culture* (n 20) 2. Hirsch (n 20).

³⁴⁵ Bücheler (n 18) 62.

³⁴⁶ Text to see 2.2.1.1.

³⁴⁷ *ibid*.

³⁴⁸ Text to see 2.2.1.1 and 2.3.2. The legal status of Proportionality in the Chinese domestic legal system can be seen in Chapter Seven. Another specially states, the US, applies balancing rather than proportionality.

leave room for doubts on whether proportionality is a general principle of law. The fact is that even if proportionality has been generally applied at the national level, it cannot automatically become a general principle of law in the sense of Article 38 (1) of the ICJ Statute because of the variance between national and international legal systems.³⁴⁹ Bermúdez stresses that due to such differences, the principle applied at the national level may not be applicable at the international level.³⁵⁰ He further clarifies that, in order to be used at the international level, a principle *in foro domestic* should be compatible with fundamental principles of international law, and the condition for its application in the international legal system occurs.³⁵¹

Nevertheless, no consensus has been reached on the transportability of proportionality to the context of international investment. The application of proportionality can be seen in many fields of international law, from the law of the sea to human rights law.³⁵² In Bücheler's view, such prevalent applications support the applicability of proportionality at the international level.³⁵³ However, this view is doubted by Orakhelashvili,³⁵⁴ who notes that proportionality has not been universally applied in the entire international law.³⁵⁵ Consequently, proportionality's application in some fields of international law cannot transpose it to others, such as international investment, with certainty. In addition, he points out that the real meaning and function of proportionality are different even in those certain fields where it is adopted.³⁵⁶ For example, in the law of the sea, proportionality is part of equity and plays a corrective role,³⁵⁷ while in the European Convention on Human rights, it is linked to the margin of appreciation.³⁵⁸ Even the relationship between necessity and proportionality varies from one circumstance to another.³⁵⁹ As shall be discussed in 2.4, necessity is one essential element of proportionality,³⁶⁰ but in international humanitarian law they are separate concepts.³⁶¹

As suggested by Wood, if a principle's nature still raises doubts and debates, it should not easily be deemed a general principle of law.³⁶² Bermúdez also emphasises the stringent identification of general principles of law, whose existence "cannot and should not be easily assumed".³⁶³ Seen in this sense, as

³⁴⁹ ILC, 'First Report on General Principles of Law' (n 322) 65. Hirsch (n 20).

³⁵⁰ ILC, 'Second Report on General Principles of Law' (n 331) 22, para 73. Wood (n 333) 318.

³⁵¹ ILC, 'Second Report on General Principles of Law' (n 331) 23, para 74, 26, para 83.

³⁵² Vadi, *Proportionality* (n 22) 119.

³⁵³ Bücheler (n 18) 68, 78-9.

³⁵⁴ Orakhelashvili (n 67) 266.

³⁵⁵ *ibid.*

³⁵⁶ *Ibid.* Thomas Cottier & others, 'The Principle of Proportionality in International Law' (2012) Swiss National Centre of Competence in Research Trade Working Paper No 2012/38, 4, 30.

³⁵⁷ Orakhelashvili (n 67) 266-8.

³⁵⁸ *ibid* 268-70.

³⁵⁹ *ibid* 270-4.

³⁶⁰ Based on the analysis and discussion, the principle of proportionality in the current study contains three consecutive factors, which are suitability, necessity, and proportionality *stricto sensu*. More detailed discussion can be seen in 2.4.

³⁶¹ Orakhelashvili (n 67) 271-2.

³⁶² Wood (n 333) 324.

³⁶³ ILC, 'Second Report on General Principles of Law' (n 331) 6 para 20.

a principle that originated from the domestic legal system, proportionality should not be regarded as a general principle of law, due to the uncertainties as to its broad application at the national level and its appropriateness to be transposed to the international level.

2.3.2.2 Formed from the International Legal System?

By dictionary definition, "law" means "a rule of conduct imposed by authority".³⁶⁴ No limitations are provided in Article 38 (1) (c) of the ICJ Statute on the source of general principles of law. Such an absence of qualifying language, as asserted by Bermúdez, reflects that a general principle of law can also form within the international legal system.³⁶⁵ Also, considering its gap-filling function, the general principle of law should not be limited in the scope of domestic legal systems.³⁶⁶

Nevertheless, problems emerge around which requirements should be satisfied by proportionality to form a general principle of law within the international legal system. In the ILC First Report, Bermúdez emphasises the significance of recognition.³⁶⁷ Such recognition is closely linked to states' consensus, which can be deduced from rules of international conventions and customary international law and reflected in the measures taken by international organisations.³⁶⁸ In this regard, states' recognition plays an essential role in the formation of proportionality as a general principle of law.³⁶⁹ However, as mentioned previously, the ambiguous attitude to the principle of proportionality of some notably influential states, such as China, remains uncertain.³⁷⁰ Even though the application of proportionality can be seen in certain fields of international law, it has different functions. Those applications somewhat reflect states' recognition of proportionality, but whether such recognition implies their consensus on the nature of proportionality, as a general principle of law, is questioned due to the different function of proportionality in each particular circumstance.

Based on the above considerations on the nature of proportionality, the legal basis of its application in international investment is mutable, essentially on a case-by-case basis. This is because it is neither an international custom nor a general principle of law in the sense of Article 38 (1) of the ICJ Statute. Consequently, the application of proportionality in balancing the conflicting values of foreign investors and the host state, such as their legitimate expectations of the stable legal framework, can be seen in two situations. Proportionality can be used if the applicable law is the host state's domestic law in which

³⁶⁴ 'Law' (*OED*) <https://www-oed-com.ezproxy-s1.stir.ac.uk/search?searchType=dictionary&q=LAW&_searchBtn=Search> accessed 15 November 2021.

³⁶⁵ ILC, 'First Report on General Principles of Law' (n 322) 47.

³⁶⁶ *ibid* 48, 67.

³⁶⁷ *ibid* 48, 68.

³⁶⁸ *ibid*.

³⁶⁹ *ibid* 51.

³⁷⁰ Vadi, *Proportionality* (n 22). See generally in Chapter Seven, which concludes that although there is no term "proportionality" in Chinese laws, regulations, and policy documents, there is a visible trend of the application of proportionality in the Chinese domestic legal system, at least in Chinese administrative law.

the principle of proportionality is included. However, this approach is currently unavailable to China because the legal status of proportionality in the Chinese domestic legal system remains uncertain.³⁷¹ Alternatively, if this principle is expressed in the treaty applicable to the case, either explicitly or implicitly, proportionality analysis can be carried out through treaty interpretation and application.

2.4 The Constituent Elements of Proportionality

As stressed by Jans, one crucial point of proportionality is "what must be proportionate to what".³⁷² The factors that should be taken into account within the process of proportionality analysis play a vital role in answering this question. The prime example of the constituent elements of proportionality is Article 36 of the South African Constitution with the heading "limitation of rights", which provides a detailed list of considerations.³⁷³ As stipulated,

1. The rights in the Bill of Rights may be limited only in terms of law of general application to the extent that the limitation is reasonable and justifiable in an open and democratic society based on human dignity, equality and freedom, taking into account all relevant factors, including
 - (a) the nature of *the right*;
 - (b) the importance of *the purpose* of the limitation;
 - (c) the nature and extent of *the limitation*;
 - (d) *the relation between the limitation and its purposes*; and
 - (e) *less restrictive means* to achieve the purpose.
2. Except as provided in subsection (1) or in any other provision of the Constitution, no law may limit any right entrenched in the Bill of Rights.³⁷⁴ [*italic added*]

This provision explicitly expresses that proportionality generally includes three elements and describes three relations. The factors are the implemented means, the pursued purpose, and the infringed right. The means-end connection from both positive and negative perspectives and a real balance between the achieved benefit and the impaired right can also be seen in this provision. Especially the phrase "the relation between the limitation and its purposes" which explicitly describes a means-end connection, further clarified by the wording "less restrictive". As required, the implemented measure should not only contribute to fulfilling the desired purpose but also achieve it with less cost, corresponding to one criterion for necessity, "the less restrictive means".

Like each measure can lead to positive and negative results, a limitation contributing to achieving its desired purpose also inflicts the impairment of fundamental rights. Such costs, as pointed out by Alexy, cannot be avoided.³⁷⁵ A balance needs to be struck to optimise the values on both sides.³⁷⁶ Although

³⁷¹ See generally in Chapter Seven.

³⁷² Jan H. Jans, 'Proportionality Revisited' (2000) 27 *Legal Issues of Economic Integration* 239.

³⁷³ The Constitution of the Republic of South Africa (1996) Article 36.

³⁷⁴ *ibid.*

³⁷⁵ Alexy, 'Proportionality and Rationality' (n 209) 16.

³⁷⁶ *ibid.*

Alexy and Barak hold different views on the specific approach to balance the conflicts, both recognise that "the importance of the purpose" should be compared against "the importance of preventing the limitation on the rights".³⁷⁷ The former factor can be seen in Article 36 (1) (b). Barak further asserts that "the extent of the limitation", which is prescribed in Article 36 (1) (c), should also be considered to weigh the conflicting values.³⁷⁸ That is to say, the considerations and relations referred to in the process of applying proportionality are expressed in the list provided in Article 36 (1) of the South African Constitution.³⁷⁹

A similar list can be seen in the China-Colombia BIT (2008),³⁸⁰ the only Chinese BIT in which the term "proportional" appears. As prescribed in Article 12 (1) (d), the measure in question should be "proportional to the objective they seek to achieve",³⁸¹ reflecting a rational means-end connection. These factors and relations will be analysed in-depth below to ascertain the considerations that should be referred to in the application of proportionality.

2.4.1 A Legitimate Desired Purpose

The notion of "proportionality" first originated from Germany,³⁸² but the requirement of legitimate purpose did not draw attention until the concept of "the substantive rule of law" appeared in the German Basic Law of 1949.³⁸³ The emphasis on the legitimacy of pursued purpose reflects the transition of the German domestic legal system from the formal rule of law to the substantive rule of law. A similar transition can be observed in the Chinese domestic legal system, which will be analysed in detail in Chapter Seven.³⁸⁴

Article 10 (II) (17) of the Prussian General Law of 1794, which stipulated that "[t]he office of the police is to take the *necessary* measures for the maintenance of public peace, security, and order",³⁸⁵ is regarded as the first textual basis of proportionality.³⁸⁶ The term "necessary" appears in this provision, but as asserted by Pan this requirement is different from the necessity included in proportionality, as we think of it today.³⁸⁷ In her view, the former can be regarded as the current requirement of suitability, which

³⁷⁷ *ibid.* Barak (n 20) 6.

³⁷⁸ Barak (n 20) 6.

³⁷⁹ *supra* note 373.

³⁸⁰ China-Colombia BIT (n 124).

³⁸¹ *ibid.* Article 12.

³⁸² Barak (n 20) 182.

³⁸³ Cohen-Eliya & Porat, 'Proportionality' (n 189) 475-6.

³⁸⁴ See 7.2.1 in Chapter Seven.

³⁸⁵ See from Alec Stone Sweet & Jud Mathews, 'Proportionality Balancing and Global Constitutionalism' (2008) 47 *Columbia Journal of Transnational Law* 73, 101 [*italic added*]. Cohen-Eliya & Porat, 'American Balancing' (n 245) 271.

³⁸⁶ Pan (n 206) (footnote omitted). Sweet & Mathews, 'Proportionality Balancing' (n 385) 101. Cohen-Eliya & Porat, 'American Balancing' (n 245) 271.

³⁸⁷ Pan (n 206).

merely focuses on a rational means-end connection.³⁸⁸ Based on Article 10 (II) (17),³⁸⁹ the state's actions explicitly prescribed under the law were valid.³⁹⁰ It was neither necessary nor possible to assess the legitimacy of the purpose pursued by the legislature because of the supremacy of law.³⁹¹ However, that has been changed since the stipulation of Article 1 in the German Basic Law of 1949,³⁹² which emphasises that

- (1) Human dignity shall be inviolable. To respect and protect it shall be the duty of *all* state authorities.
- (2) The German people therefore acknowledge inviolable and inalienable human rights as the basis of every community, of peace and of justice in the world.
- (3) The following basic rights shall bind *the legislature, the executive, and the judiciary* as directly applicable law.³⁹³ [italic added]

As evaluated by Cohen-Eliya and Porat, this rule has brought the notion of "the substantive rule of law" into the German domestic legal system,³⁹⁴ stressing the importance of the legitimacy of the pursued purpose.³⁹⁵ The wording emphasises that all state organs, from the legislature to the judiciary, have the duty to respect and protect "human rights" and "human dignity". The imperative "shall" further expresses that such duties are mandatory. If any questioned action infringes on fundamental rights, the pursued object is illegitimate, even if the measure itself is lawful.³⁹⁶ In Liu's view, the aim of testing the legitimacy of the desired purpose is to ascertain the authority's real intention when acting.³⁹⁷ As put by Yang, according to this test, the measures that manifestly infringe fundamental rights would be excluded,³⁹⁸ and the situation in which illegal purposes are concealed under the guise of legal measures would also be prevented.

The significance of a legitimate purpose is recognised, but whether it is an independent element of proportionality raises debates among scholars. For this view are those who regard the legitimate purpose as independent factor stress its significance from the structural and functional perspective. As they point out, although the considerations of proportionality include the pursued purpose, its current components, from suitability to proportionality *stricto sensu*, merely focus on the implemented action itself and its effects.³⁹⁹ Therefore, an independent test of legitimate purpose is needed to fill this deficiency in proportionality's structure. Liu also points out that there are potential risks in which the protection of

³⁸⁸ *ibid.*

³⁸⁹ See from Cohen-Eliya & Porat, 'American Balancing' (n 245) 271. Bücheler (n 18) 35.

³⁹⁰ Cohen-Eliya & Porat, 'American Balancing' (n 245) 271.

³⁹¹ Liu (n 246) 137.

³⁹² Basic Law for the Federal Republic of Germany (entered into force 1949, amended 2019) Article 1.

³⁹³ *ibid.*

³⁹⁴ Cohen-Eliya & Porat, 'Proportionality' (n 189) 475-6.

³⁹⁵ *ibid.*

³⁹⁶ Liu (n 246) 138. Barak (n 20) 254-5.

³⁹⁷ Liu (n 246) 144.

³⁹⁸ Yang (n 209) 371.

³⁹⁹ See from Pan (n 206).

public interest is used as an excuse to limit relative parties' fundamental rights.⁴⁰⁰ In his view, the assessment of the legitimacy of the purpose can close such a gap in the function of proportionality.⁴⁰¹

Nevertheless, as argued by those against this view of legitimate purpose, including the legitimacy test in proportionality may lead to the expansion of this principle.⁴⁰² A similar opinion is held by Alexy, who asserts that the legitimacy of the desired purpose is a superfluous requirement, which may diminish proportionality's rationality.⁴⁰³ In his opinion, whether the desired purpose is legitimate would be assessed at the final assessment of proportionality *stricto sensu*, which is value-oriented and optimise both values based on the legal possibility.⁴⁰⁴ Therefore, there is no need to set an individual test of the nature of the pursued purpose. Other scholars recognise the significance of the legitimate purpose, but they assert that it should be considered before applying proportionality to balance conflicting values.⁴⁰⁵ As highlighted by Cohen-Eliya and Porat, a legitimate purpose is a foundation and prerequisite for applying proportionality.⁴⁰⁶ Chen also points out that the function of the legitimate purpose test is to investigate whether the desired purpose accords with the Constitution.⁴⁰⁷ Only when the impaired value falls into the category of fundamental rights will further analysis be triggered, and the competing values will be weighed.⁴⁰⁸

2.4.2 Suitability: A Rational Means-End Relationship

Suitability describes a rational means-end connection. As required, the adopted measure should contribute to achieving the pursued purpose.⁴⁰⁹ Chen puts that instead of the achieved aim, the disputed measure is the object of the suitability test.⁴¹⁰

Although there is no defined criterion for "contribution", scholars have reached a consensus that no extreme contribution is required.⁴¹¹ Yang argues that the measure at hand does not need to wholly or mainly achieve the desired purpose to satisfy the requirement of suitability.⁴¹² In Alexy's view, such

⁴⁰⁰ Liu (n 246) 135.

⁴⁰¹ *ibid.*

⁴⁰² Pan (n 206).

⁴⁰³ Alexy, 'Proportionality and Rationality' (n 209) 14.

⁴⁰⁴ *ibid.*

⁴⁰⁵ Cohen-Eliya & Porat, 'Proportionality' (n 189) 464. Hongwei Cai, 'Zuo Wei Xian Zhi Gong Quan Li Lan Yong De Bi Li Yuan Ze' (The Principle of Proportionality-Limiting the Abuse of Public Power) (2019) *Law & Social Development* 127, 135-6 [in Chinese]. Jinghui Chen, 'Bi Li Yuan Ze De Pu Bian Hua He Ji Ben Quan Li De Xing Zhi' (The Universality of Proportionality and the Nature of Fundamental Rights) (2017) *Chinese Legal Science* 279, 284 [in Chinese].

⁴⁰⁶ *ibid.*

⁴⁰⁷ Chen (n 405) 284. Cai (n 405) 135.

⁴⁰⁸ Kevin Iles, 'A Fresh Look a Limitations: Unpacking Section 36' (2007) 23 *South African Journal on Human Rights* 68, 71.

⁴⁰⁹ Cohen-Eliya & Porat, 'Proportionality' (n 189) 464.

⁴¹⁰ Chen (n 405) 284.

⁴¹¹ Benedikt Pirker, *Proportionality Analysis and Models of Judicial Review a Theoretical and Comparative Study* (Europa Law Publishing 2013) 27.

⁴¹² Yang (n 209) 371.

contribution to the achievement of the desired purpose suffices for suitability.⁴¹³ As he asserts, the function of the suitability test is to preclude the measures that have no any promotion to the achievement of the desired purpose.⁴¹⁴ Moreover, as noted by Kingsbury and Schill, such a rational means-end connection is always established in practice.⁴¹⁵ As they clarify, if a state or its organ acts in good faith, the implemented means would more or less further the achievement of the pursued purpose.⁴¹⁶ A situation in which the measure taken by the authority is entirely invalid is rare.⁴¹⁷

The degree to which a measure can achieve the desired purpose can be investigated from the relevant facts. However, one may question what circumstances should be taken into account to ascertain the suitability of such means. As put by Andenas and Zleptnig, such circumstances may refer to the facts when the measures were taken and those at the time of review.⁴¹⁸ Considering similar issues appear within the process of applying proportionality, both in the tests of suitability and necessity, further discussion on how the implemented measures were reviewed is essential. More detail will be analysed in Chapter Five based on the available awards of existing ISDs, for instance, the cases arising from the Argentinian economic crisis of 2001/2.⁴¹⁹

2.4.3 Necessity: Equal Effect with Less Limit

Like suitability, necessity also describes a means-end connection and mainly tests the measure in question. However, compared with suitability, necessity relies upon a closer connection, requiring that the implemented means should be necessary to achieve the pursued purpose.⁴²⁰ Unlike other constituent elements of proportionality, the requirement of necessity can be seen in provisions of both domestic laws and international legal instruments, including IIAs. For example, the Canada-China BIT (2012) explicitly stipulates that the host state's measures necessary for particular purposes shall not be precluded.⁴²¹

Nevertheless, issues arise from assessing the necessity of the disputed measures due to the lack of a defined criterion for "necessity". Concluded from provisions in which the term "necessary" appears, two criteria can be used for such an assessment: "The only one test" and "the less restrictive means test".

⁴¹³ Alexy, 'Proportionality and Rationality' (n 209) 15.

⁴¹⁴ *ibid.* Yang (n 209) 371.

⁴¹⁵ Kingsbury & Schill (n 18) 86. Alec Stone Sweet & Giacinto Della Cananea, 'Proportionality, General Principles of Law, and Investor-State Arbitration: A Response to Jose Alvarez' (2014) 46 *New York University Journal of International Law & Politics* 911, 917. Alec Stone Sweet & Jud Mathews, *Proportionality Balancing and Constitutional Governance: A Comparative and Global Approach* (OUP 2019) 36.

⁴¹⁶ Kingsbury & Schill (n 18) 86.

⁴¹⁷ *ibid.*

⁴¹⁸ Mads Andenas & Stefan Zleptnig, 'Proportionality and Balancing in WTO Law: a Comparative Perspective' (2007) 20 *Cambridge Review of International Affairs* 71, 74-5.

⁴¹⁹ See in Chapter Five.

⁴²⁰ Pirker (n 411) 29. Chen (n 405) 284.

⁴²¹ See an example Canada-China BIT (signed 9 September 2012, entered into force 1 October 2014) Article 33.

"The only one test" can be observed in Article 25 of the Responsibility of States for Internationally Wrongful Act (2001) (Wrongful Act).⁴²² As stipulated in this provision, the means necessarily taken by the state should be "the only way" to achieve the desired purpose.⁴²³ In other words, if other available measures can fulfil the same purpose, the one identified is unnecessary. As stressed by the ILC, the disputed means can be replaced by alternatives even if they are more costly or more difficult to be implemented.⁴²⁴ This threshold of necessity is commonly criticised as too strict to be met because the alternative measures are always there regardless of their costs.

Alternatively, "the less restrictive means test" can be seen in Article 36 of the South African Constitution which prescribes "*less restrictive means* to achieve the purpose".⁴²⁵ As reflected in this language, the necessity of the measure in question is proved by excluding its alternative means.⁴²⁶ Barak points out that the prerequisite for the necessity test is the existence of alternative measures.⁴²⁷ If no other means can be utilised to pursue the same purpose, the adopted measure then is proved as the only one. Consequently, it is the means necessary to achieve the desired purpose. If the alternatives exist, the questions are whether those measures are excluded and in which way are they excluded.

Compared with "the only one test", it is the researcher's view that "the less restrictive means test", which has a broader scope, may be more reasonable. Based on the earlier discussion, in particular circumstances, the less restrictive means may be the only one to achieve the desired purpose. In this respect, "the only one test" is implicitly included in the contour of "the less restrictive means test". Moreover, in practice, "the less restrictive means test" is more widely applicable due to its lower threshold. The irreplaceability of a measure cannot be fulfilled unless in extreme situations. Besides, considerations from the cost and benefit perspectives, rather than alternative measures themselves, can prove the necessity of the impugned means with more solid evidence. Therefore, instead of "the only one test", "the less restrictive means test" should be utilised to assess whether the implemented measure is necessary to achieve the pursued purpose.

Nevertheless, as expressed by the Argentinian cases discussed in Chapter Five,⁴²⁸ issues arise from the exclusion of alternative measures. Some tribunals in those cases denied the necessity of the proposed

⁴²² Responsibility of State for Internationally Wrongful Acts (2001) Article 25. More detail as to Article 25 can be seen in Chapter Five.

⁴²³ *ibid.*

⁴²⁴ UN, *Yearbook of the International Law Commission Volume II Part Two, A/CN.4/SER.A/2001/Add.1 (Part 2)* (2007) 83. *CMS v. Argentina* (n 5) para 324.

⁴²⁵ *supra* note 373.

⁴²⁶ Barak (n 20) 317.

⁴²⁷ *ibid* 321.

⁴²⁸ See generally in Chapter Five. Argentinian cases (n 5).

measures merely based on the existence of alternatives.⁴²⁹ Those decisions differ from the views held by scholars. As emphasised by Regan, both the cost and benefit of a measure should be considered to investigate whether it satisfies the necessity test.⁴³⁰ Similarly, Andenas and Zleptnig put that the alternative measures should fulfil both requirements of "equal effects on the purpose pursued" and "less limitation on the interest affected".⁴³¹ Otherwise, they would be excluded. As emphasised by Barak, the proposed measure is necessary if its alternative measures fail to achieve the same purpose or lead to more impairment of the affected value.⁴³² Despite applying the term "least" instead of "less", as asserted by Liu, necessity is a relative rather than an absolute requirement.⁴³³ Therefore, in order to be a measure necessary to achieve the desired purpose, the proposed means should not make the same contribution to the pursued purpose but also have less limit on the affected value.

Similar to the suitability of the measure in question, its necessity should be tested based on the relevant facts.⁴³⁴ However, the circumstances in which the implemented means should be reviewed are uncertain. Questions also arise from the decision-maker who has the power to decide whether the state interest is at stake and needs to be protected by any particular means.⁴³⁵ As evaluated by Rivers, proportionality "is not specifically designed for implementation by courts but forms a general rational test for the limitation of rights".⁴³⁶ In this respect, proportionality as a tool is not merely adopted by the courts or tribunals. Instead, it can be applied by any player who can review the measure in question. Those issues will be analysed later in light of actual incidences in which proportionality has been applied to strike a balance between the conflicting legitimate expectations of foreign investors and the host state.⁴³⁷

2.4.4 Proportionality *Stricto Sensu*: Achieved Benefits v. Impaired Interests

A vital factor in proportionality analysis is discerning between competing values. This test mainly evaluates the pursued purpose itself.⁴³⁸ Barak asserts that in order to fulfil the requirement of proportionality *stricto sensu*, namely the real balance between conflicting values, to justify the questioned measures, a proper relationship should exist between the achievement of the desired purpose and the infringement of the limited rights.⁴³⁹ Rivers describes this process as a cost-benefit analysis.⁴⁴⁰

⁴²⁹ See 5.4.2 in Chapter Five. See an example *CMS v. Argentina* (n 5).

⁴³⁰ Donald H. Regan, 'The Meaning of 'Necessary' in GATT Article XX and GATT Article XIV: The Myth of Cost-Benefit Balancing' (2007) 6 *World Trade Review* 347, 349.

⁴³¹ Andenas & Zleptnig (n 418) 75.

⁴³² Barak (n 20) 323.

⁴³³ Quan Liu, 'Xing Zheng Pan Jue Zhong Bi Li Yuan Ze De Shi Yong' (The Application of Proportionality Principle in Administrative Judgment) (2019) *Chinese Legal Science* 84, 95 [in Chinese]. It is also described as "less restrictive measures" by some scholars.

⁴³⁴ Nehushtan (n 207) 77.

⁴³⁵ Calamita, 'The Principle' (n 26) 171.

⁴³⁶ Julian Rivers, 'Proportionality and Variable Intensity of Review' (2006) 65 *Cambridge Law Journal* 174, 182.

⁴³⁷ See generally in Chapter Five.

⁴³⁸ Chen (n 405) 284.

⁴³⁹ Barak (n 20) 340. Kingsbury & Schill (n 18) 87.

⁴⁴⁰ Rivers (n 436) 200.

In Leonhardsen's view, the benefits should exceed or, at least, equal the limits on the relevant values.⁴⁴¹

Different from other components of proportionality, this one is weighed based on the value or a result-oriented test.⁴⁴² As pointed out by Rivers, unlike the necessity test, which aims to preclude the measures that cannot achieve the same purpose with less restriction, proportionality *stricto sensu* focuses on the evaluation of the value.⁴⁴³ In order to ascertain whether the benefits go beyond the costs or not, the straightforward way is to weigh and balance them. However, some values may not be comparable. In this situation, they can be weighed and balanced indirectly. Alexy stresses their "importance for the constitution",⁴⁴⁴ while Barak chooses a similar way, "marginal social significance".⁴⁴⁵ If the competing values cannot be weighed directly, the social importance of each value can be tested first. Then, a real balance can be struck between these values by weighing their social importance.

2.5 The Application of Proportionality in Balancing Conflicting Values

Based on the above discussion, the relevant considerations within the process of proportionality analysis include the legitimacy of the pursued purpose, the rational means-end connection, the equal effective means with less limit, and the balance between conflicting values. However, the interaction among these factors, namely the precise structure of proportionality analysis, is as yet undefined. Confusion persists as to the approach in which proportionality should be applied to review the impugned means. This section will examine the appropriate structure of proportionality analysis and its practical approach, in preparation for a later in-depth analysis of the application of proportionality as a fulcrum in the investor-state relationship.

2.5.1 The Structure of Proportionality Analysis-Three Consecutive Tests

Scholars can be divided into three distinct groups according to their divergent opinions on the structure of proportionality analysis. In the mainstream view,⁴⁴⁶ which is held by Barak, the application of proportionality consists of four tests, which review the legitimacy of the desired purpose, the suitability and necessity of the implemented measure, and a real balance between the conflicting values, respectively.⁴⁴⁷ Chen, at the other end of the spectrum, holds the restrictive opinion that only the assessments of necessity and proportionality *stricto sensu* are included in proportionality analysis.⁴⁴⁸ In

⁴⁴¹ Erlend M. Leonhardsen, 'Looking for Legitimacy: Exploring Proportionality Analysis in Investment Treaty Arbitration' (2012) 3 *Journal of International Dispute Settlement* 95. Han, 'The Application of the Principle of Proportionality' (n 149) 635.

⁴⁴² Nehushtan (n 207) 77. Barak (n 20) 342.

⁴⁴³ Rivers (n 436) 200.

⁴⁴⁴ Robert Alexy, 'On Balancing and Subsumption, A Structural Comparison' (2003) 16 *Ratio Juris* 433, 442.

⁴⁴⁵ Barak (n 20) 350-2.

⁴⁴⁶ Rautenbach (n 207) 2233. Sweet & Mathews, *A Comparative and Global Approach* (n 415) 30. Cai (n 405) 136. Francisco J. Urbina, 'A Critique of Proportionality' (2012) 57 *American Journal of Jurisprudence* 49.

⁴⁴⁷ Barak (n 20) 131.

⁴⁴⁸ Chen (n 156).

others' views, the process of applying proportionality refers to the tests of suitability, necessity, and proportionality *stricto sensu*,⁴⁴⁹ but they have divergences on the legitimate pursued purpose. Kingsbury and Schill regard the legitimacy of the desired purpose as a sub-element of suitability.⁴⁵⁰ In this respect, as noted by Arnould, no substantive differences exist between the three-element view and the mainstream view.⁴⁵¹ However, Chen argues that the legitimate purpose is not part of proportionality analysis.⁴⁵² Instead, it should be considered as a prerequisite for applying proportionality.⁴⁵³

Although scholars have recognised that both tests of necessity and proportionality *stricto sensu* are included in proportionality analysis, they disagree on the suitability test. As stated by Chen, suitability is a superfluous element from both functional and practical perspectives.⁴⁵⁴ In his view, the function of the suitability test, which aims to examine the rational means-end connection, can also be achieved by the necessity test.⁴⁵⁵ The latter assessment even requires a higher threshold: The relationship should be not only rational but also necessary to the pursued purpose. In this respect, the actions necessary to pursue the purpose undoubtedly satisfy the suitability test. Chen further emphasises that the suitability test has always been satisfied in practice.⁴⁵⁶ Therefore, "the suitability test" is said to fail to play an essential role in the application of proportionality.

A similar view is held by Iles, who asserts that suitability and necessity tests are satisfied or dissatisfied together by the implemented measures.⁴⁵⁷ This opinion, in the researcher's view, is partly wrong. As acknowledged by Iles, different factors are considered in these two tests, although both are linked with the measures in question.⁴⁵⁸ The nature and purpose of the impugned means are taken into account to examine a rational means-end connection.⁴⁵⁹ Other factors, such as several alternatives, are considered for testing as to whether the measures in question achieve "the less restrictive means test".⁴⁶⁰ Correspondingly, they have different thresholds. Based on the earlier analyses, the suitability test can be satisfied even if the examined measure merely makes a negligible contribution,⁴⁶¹ while the necessity test requires not only the same benefit but also less cost.⁴⁶² By comparing these considerations and

⁴⁴⁹ Cohen-Eliya & Porat, 'Proportionality' (n 189) 464. Chen (n 405) 283.

⁴⁵⁰ Kingsbury & Schill (n 18) 86. Bücheler (n 18) 2.

⁴⁵¹ Quan Liu (trans), 'Ou Zhou Ji Ben Quan Li Bao Hu De Li Lun Yu Fang Fa-Yi Bi Li Yuan Ze Wei Li' (Andreas von Arnould, 'The Theory and Methods of the Protection of Fundamental Rights in Europe: Taking the Principle of Proportionality for Example') (2014) *Journal of Comparative Law* 182, 183 [in Chinese].

⁴⁵² Chen (n 405) 283. Cohen-Eliya & Porat, 'Proportionality' (n 189) 464.

⁴⁵³ Chen (n 405) 283.

⁴⁵⁴ Chen (n 156).

⁴⁵⁵ *ibid.*

⁴⁵⁶ *ibid.*

⁴⁵⁷ Iles (n 408) 84.

⁴⁵⁸ *ibid* 83-4.

⁴⁵⁹ *ibid.*

⁴⁶⁰ *ibid.*

⁴⁶¹ Text to 2.4.2.

⁴⁶² Text to 2.4.3.

thresholds, it is evident that the scope of suitable measures is broader than that of necessary means. In this regard, as pointed out by Iles, the means necessary to achieve the purpose are undoubtedly suitable. However, no sufficient evidence proves that a suitable measure is necessary to achieve the purpose. Instead, such means may fail to meet the necessity test because of their lower benefit or higher cost. Therefore, the tests of suitability and necessity should not be viewed as interchangeable.⁴⁶³ Being a suitable measure is the prerequisite for fulfilling the necessity test.⁴⁶⁴

To conclude, the legitimacy of the pursued purpose, or in general, the nature of the desired purpose, the implemented measure and the affected interest should be investigated first.⁴⁶⁵ If the requirements stipulated in relevant laws or case-related treaties are unsatisfactory, the investigation ends here. Otherwise, if such a prerequisite is met, the process of proportionality analysis would be triggered. Then three consecutive tests, namely the suitability test, the necessity test, and the test of proportionality *stricto sensu*, would be applied to examine the impugned measure.

2.5.2 The Approach to Proportionality Analysis

The application of proportionality varies by circumstances. To a certain extent, each situation can affect the judgment of competing values. Similarly, although proportionality is not currently prescribed in different decisions, even though the factual backgrounds are similar.⁴⁶⁶ Demonstrated in practice, proportionality, as a valuable tool to balance competing values, has been adopted in two main ways: Horizontal and vertical approaches. These two methods will be examined and compared in this section to explore which one is more appropriate to the application of proportionality in international investment.

2.5.2.1 The Horizontal Approach to Proportionality Analysis

The horizontal approach to applying proportionality can be seen in the practice of South Africa. The word "horizontal" indicates that all tests included in proportionality analysis are placed on the same level: No sequence exists among its different assessments.

As expressed previously, Article 36 of the South African Constitution provides a list of relevant factors that should be considered in applying proportionality.⁴⁶⁷ Rautenbach notes that this list has no details on the order in which such factors should be considered.⁴⁶⁸ The lack of precise instruction, in his view,

⁴⁶³ Pan (n 206).

⁴⁶⁴ *ibid.*

⁴⁶⁵ Text to 2.4.1

⁴⁶⁶ See 7.5 in Chapter Seven.

⁴⁶⁷ The Constitution of the Republic of South Africa (n 373). Text to see 2.4.

⁴⁶⁸ Rautenbach (n 207) 2246.

leaves the decision-makers room to consider the relevant factors from their own perspectives.⁴⁶⁹ As added by Bücheler, the absence of a fixed sequence means no order should be followed when applying proportionality to review the means in question.⁴⁷⁰ Moreover, based on the ordinary meaning of the term "include", Petersen puts that the list provided in Article 36 is non-exhaustive.⁴⁷¹ In this respect, the flexible application of proportionality in South Africa can be expressed from two aspects. The decision-makers enjoy discretionary power to decide what factors should be considered in proportionality analysis while retaining the capability to utilise those tests to review the impugned measure.⁴⁷²

A different view is held by Iles, who argues that Article 36 of the South African Constitution contains two approaches to proportionality analysis: The rational means-end connection test and the less restrictive means test.⁴⁷³ The former is prescribed in Article 36 (1) (d),⁴⁷⁴ while the latter is stipulated in Article 36 (1) (e).⁴⁷⁵ Correspondingly, the relevant considerations are classified into two groups. The pursued purpose and the nature of the implemented means, which are required in Article (36) (1) (a) and (c),⁴⁷⁶ are considered in assessing the rational means-end connection.⁴⁷⁷ Other factors, such as the extent of the limitation, are considered in the less restrictive means test.⁴⁷⁸ However, one noteworthy point is that "the importance of the purpose of the limitation" factor, which is provided in Article 36 (1) (b) of the South African Constitution,⁴⁷⁹ has not been referred to in the classifications. Such a factor is considered in neither the rational means-end connect test nor the less restrictive means test.⁴⁸⁰ As Iles clarifies, benefits and costs should be considered when assessing the implemented measure.⁴⁸¹ The requirement of "the less restrictive means", in his view, should be understood as one of the relevant considerations rather than the only decisive factor in the test.⁴⁸²

Moreover, Iles asserts that a particular order should be followed when applying proportionality to review the questioned means.⁴⁸³ Before initiating proportionality analysis, whether the examined measure is justified or not should be reviewed by decision-makers based on the actual circumstances.⁴⁸⁴

⁴⁶⁹ *ibid.*

⁴⁷⁰ Bücheler (n 18) 45.

⁴⁷¹ Niels Petersen, 'Proportionality and the Incommensurability Challenge in the Jurisprudence of the South African Constitutional Court' (2014) 30 *South African Journal on Human Rights* 405, 407. Iles (n 408) 77.

⁴⁷² Rautenbach (n 207) 2246.

⁴⁷³ Iles (n 408) 83.

⁴⁷⁴ The Constitution of the Republic of South Africa (n 373) Article 36 (1) (d).

⁴⁷⁵ *ibid* Article 36 (1) (e).

⁴⁷⁶ *ibid* Article 36 (1) (a) and (c). Text to 2.4

⁴⁷⁷ Iles (n 408) 84.

⁴⁷⁸ *ibid.*

⁴⁷⁹ The Constitution of the Republic of South Africa (n 373). Text to see 2.4.

⁴⁸⁰ Iles (n 408) 83-4.

⁴⁸¹ *ibid* 84-5.

⁴⁸² *ibid.*

⁴⁸³ *ibid* 86.

⁴⁸⁴ *ibid* 85.

Within this process, the nature and significance of the pursued purpose should be investigated.⁴⁸⁵ The nature and the impairment of the infringed rights should also be ascertained.⁴⁸⁶ Based on such factual backgrounds, whether a rational means-end connection exists is examined at the first stage of proportionality analysis.⁴⁸⁷ The assessment ends if no rational relationship exists between the implemented measure and the pursued purpose. Other factors listed in Article 36 of the South African Constitution become irrelevant.⁴⁸⁸ If such a rational connection is established, other considerations, such as the alternative measures to achieve the same purpose, are considered to examine whether a real balance is struck between the conflicting values.⁴⁸⁹ This approach, as put by Iles, reflects the internal logic of proportionality. Reviewers benefit from this clear guidance on applying proportionality, avoiding jumping or repetition within the process of review.

2.5.2.2 The Vertical Approach to Proportionality Analysis

The structured approach suggested by Iles can be seen in practice from Germany. The application of proportionality in Germany reviews the first two assessments to examine the questioned measure itself from different perspectives and then a value-oriented test.⁴⁹⁰

Based on the vertical approach, the first stage of proportionality analysis investigates whether the means contribute to achieving the pursued purpose.⁴⁹¹ Han puts that this assessment aims to preclude the situations in which the measures taken by public authorities are wholly invalid or the purpose pursued by them is manifest illegitimate.⁴⁹² If there is no rational means-end connection, the authorities should bear the corresponding liabilities of their actions.

Once the requirements of suitability are fulfilled, the necessity of the means in question is assessed in the second stage.⁴⁹³ In this phase, various available measures are compared from both perspectives of benefit and cost. If the disputed measures achieve the same purpose with less limit on fundamental rights, they are deemed necessary to pursue the desired aim. In this circumstance, the values on both sides are optimised. Then, at the last stage, the optimisations of both values are weighed against each other to see which side prevails. A balance is struck if the benefits exceed. As Sweet and Mathews stress, all these three tests should be fulfilled by the measure in question; The failure of any test would lead to

⁴⁸⁵ *ibid.*

⁴⁸⁶ *ibid.*

⁴⁸⁷ *ibid* 86.

⁴⁸⁸ *ibid.*

⁴⁸⁹ *ibid.*

⁴⁹⁰ Ranjan (n 18) 856. Sweet & Mathews, *A Comparative and Global Approach* (n 415) 30. Han, 'On the Application' (n 141) 234. Jans (n 372) 240-1.

⁴⁹¹ Han, 'On the Application' (n 141), 234.

⁴⁹² *ibid.*

⁴⁹³ *ibid.*

its invalidation.⁴⁹⁴

Based on the comparison between the horizontal and vertical approaches, it is evident that the vertical one follows the internal logical order implied in proportionality, maintaining uniformity and avoiding repetition. If proportionality is applied in the horizontal approach, the importance of the pursued purpose, which is a vital factor in proportionality analysis, may be omitted.⁴⁹⁵ On the contrary, applying proportionality in the vertical approach refers to all considerations. Moreover, based on the earlier discussion on various tools to review the means taken by public authorities, one advantage of proportionality is its structured approach,⁴⁹⁶ which supports the legality of the measure with solid evidence. Otherwise, as reflected in the later examinations of the Argentinian cases, random application of proportionality led to different or even opposite decisions in similar disputes.⁴⁹⁷

2.6 Conclusion

With its prevalent application in various legal systems to review the impugned means and weigh competing values, proportionality has been noted by scholars as an appropriate tool to strike a balance between the conflicting legitimate expectations of foreign investors and the host state and settle ISDs in international investment. However, in the context of international investment, the function of proportionality is affected by much uncertainty. These issues refer to the nature of proportionality and its constituent elements, as well as the structure of proportionality analysis and its practical approach.

Assuming proportionality fulfils the requirements stipulated in Article 38 (1) of the ICJ Statute, it falls into the categories of international customs or general principles of law. If so, it then can be universally applied in the ISDS to establish a balanced investor-state relationship. However, the issue is that those scholars who recognise the universal application of proportionality mainly refer to the practice of certain countries. They omit the practice of other specially affected states, including China. As a specially affected and hugely influential state in the context of international investment, China's practice contributes to the legal status of proportionality at the international level. Nevertheless, based on the later analysis in Chapter Seven, no consensus has been reached on the legal status of proportionality in the Chinese domestic legal system.⁴⁹⁸ Therefore, it is too early to conclude that proportionality is a general principle of law. Consequently, its application in the ISDS depends on the wording of instrument applicable to the case: The host state's domestic law or the particular IIA.

The principle of proportionality generally contains a rational means-end connection and a real balance

⁴⁹⁴ Sweet & Mathews, *A Comparative and Global Approach* (n 415) 30. Sweet & Cananea (n 415) 917.

⁴⁹⁵ Iles (n 408) 84-5.

⁴⁹⁶ Text to 2.3.

⁴⁹⁷ See in Chapter Five. Argentinian cases (n 5).

⁴⁹⁸ See generally in Chapter Seven.

between competing values, but its precise scope raises debates. Correspondingly, proportionality analysis includes the tests that aim to assess relevant considerations, but its structure is questioned. One uncertainty is whether the legitimate pursued purpose and the suitability of the implemented means are included in proportionality analysis. Which approach, the horizontal or the vertical, should be adopted to apply proportionality to review the impugned means is also questioned. Concluded from the debates among scholars, the nature of the purpose, the measure, and the right should be examined before applying proportionality. These assessments are prerequisites for proportionality analysis. As a result, the extension of proportionality is limited, and the situation in which malfeasance in the guise of a legitimate purpose is also prevented.

If the pursued purpose is legitimate and the impaired right falls into protected values, proportionality analysis is pertinent to review the means in question. On the basis of its internal logic, the tests of suitability, necessity, and proportionality *stricto sensu* should be carried out successively within the process of proportionality analysis. The first step is to find out a rational means-end connection, precluding the measures that do not contribute to or even impede the achievement of the pursued purpose. This test is always satisfied, followed by the second phase, aiming to assess whether the chosen measure is necessary. The measure's necessity is proved by the exclusion of its alternatives that not only achieve the same purpose but also do not have a suboptimal effect on the impaired values. Also, they should be reasonably available when acting. The real balance between the conflicting values is examined at the last stage. A balance is struck if the infringement of rights does not exceed the benefit of the achieved purpose.

This chapter examined the general understanding of proportionality and the role of proportionality analysis in assessing conflicting values. All of these prepare for the later discussions and examinations on the application of proportionality, in the context of international investment, to strike a balance between the conflicting legitimate expectations of foreign investors and the host state. However, some questions, for example, considering proportionality is neither an international custom nor a general principle of law, in which approach it can be brought into the ISDS regime, particularly in light of ISDs in which China is involved, still remain. These issues are being analysed in-depth in the following chapters from the international and Chinese perspectives.

Chapter 3

The Interaction between Treaty Interpretation and Proportionality

3.1 Introduction

Based on the discussion in Chapter Two, proportionality cannot clearly be defined either as an international custom or as a general principle of law, and it cannot be applied universally in the context of international investment.⁴⁹⁹ Therefore, whether proportionality can be applied to balance the conflicting values between foreign investors and the host state depends on whether such a utility is expressed by the language of a treaty, indicating a real need for treaty interpretation. Meanwhile, proportionality *stricto sensu*, which mainly focuses on the real balance between conflicting values, is also needed to strike a balance in the investor-state relationship in terms of treaty interpretation. The contribution of proportionality to a balanced treaty interpretation can be seen in a balance between the interpretative power of different interpreters and a balanced interpretative approach.

In the context of international investment, both the contracting states to a treaty and the tribunals share the responsibility to make treaty interpretations in accordance with interpretative rules stipulated in the Vienna Convention.⁵⁰⁰ The former provides guidance on interpretation, while the latter interprets controversial provisions in particular cases.⁵⁰¹ However, although they should counterbalance each other, the current relationship between their interpretative power is imbalanced. As noted by Zhang, in practice, the tribunals have paid insufficient attention to or even ignored the state's interpretation.⁵⁰² For example, in *Sanum v. Laos*,⁵⁰³ a case in which one point of dispute was whether the China-Laos BIT (1993) applied to Macao, a special administrative region (SAR) of China. Although there was no modifier of "territory" stipulated in the treaty,⁵⁰⁴ China confirmed twice with Laos that this BIT did not apply to Macao SAR through diplomatic notes.⁵⁰⁵ However, this joint interpretation from the contracting parties was still ignored by the tribunal. Conflicts arise between the interpretations provided by treaty parties and tribunals.⁵⁰⁶ Correspondingly, the establishment of a balanced investor-state relationship may be affected by conflicting interpretations. In this situation, proportionality can be adopted to offset any conflicting interpretative powers, effectively to neutralise interpretations upon which the investor-state relationship can be re-balanced.

Similarly, the principle of proportionality is also emphasised when ambiguous treaty provisions are

⁴⁹⁹ See 2.3 in Chapter Two.

⁵⁰⁰ Vienna Convention (n 47). Kathryn Gordon & Joachim Pohl, 'Investment Treaties over Time-Treaty Practice and Interpretation in a Changing World' (2015) OECD Working Papers on International investment 2015/02, 12-3.

⁵⁰¹ *ibid* 12-3.

⁵⁰² Zhang (n 55) 35.

⁵⁰³ *Sanum v. Laos*, UNCITRAL, PCA Case No. 2013-13.

⁵⁰⁴ China-Laos BIT (signed 31 January 1993, entered into force 1 June 1993) Article 1.

⁵⁰⁵ *Sanum v. Laos*, UNCITRAL, PCA Case No. 2013-13, Statement of the Chinese Foreign Ministry on the Applicability of the China-Laos BIT to Macao SAR, 21 October 2016.

⁵⁰⁶ Zhang (n 55) 35.

interpreted based on the rules of treaty interpretation.⁵⁰⁷ Proportionality, especially proportionality *stricto sensu*,⁵⁰⁸ can be utilised to balance different interpretative factors that should be considered in the process of interpreting treaty provisions. The most well-known rules are the "interpretation of treaties" stipulated in Section 3 of the Vienna Convention, which includes Articles 31 to 33.⁵⁰⁹ These rules refer to the general rule of treaty interpretation,⁵¹⁰ the supplementary interpretative means,⁵¹¹ and the interpretation in multiple languages, respectively.⁵¹² As rules of customary international law, they can be universally applied to ascertain the clear meaning of ambiguous treaty provisions.⁵¹³ Fauchald points out that Article 31 (1) has been frequently applied to interpret treaty provisions.⁵¹⁴ This general rule expresses the essential elements of interpretation, including a term's ordinary meaning, its context, the object and purpose of the treaty, and the principle of good faith.⁵¹⁵ The significance of the contracting parties' common intention is also emphasised, which can be observed in Article 31 (4).⁵¹⁶ Apart from Article 31, the supplementary means provided in Article 32 contribute to treaty interpretation,⁵¹⁷ especially *travaux préparatoires*, which aid the ascertainment of the contracting parties' common intention.

Furthermore, as commented by Wälde, those interpretative rules under the Vienna Convention are tantamount to a garden in which various interpretative approaches can grow.⁵¹⁸ Klabbers asserts that the Vienna Convention includes three traditional interpretative methods, which are textual, historical, and teleological approaches.⁵¹⁹ They stress the significance of a word's plain meaning, the treaty parties' intention, and the treaty's object and purpose, respectively.⁵²⁰ As further pointed out by Klabbers, Article 31 of the Vienna Convention reflects a hybrid approach, a compromise between the textual and teleological methods.⁵²¹ In the view of Dörr and Schmalenbach, the systemic approach also applies to treaty interpretation.⁵²² By definition, "systemic" emphasises the whole of a system rather than any constituent part of it.⁵²³ As further stressed by McLachlan, a treaty is part of international law,⁵²⁴ Thus,

⁵⁰⁷ *ibid* 35.

⁵⁰⁸ Barak (n 20) 4, 72-5.

⁵⁰⁹ Vienna Convention (n 47) Section 3.

⁵¹⁰ *ibid* Article 31.

⁵¹¹ *ibid* Article 32.

⁵¹² *ibid* Article 33.

⁵¹³ Gardiner (n 49) 6-7. UNCTAD (n 59).

⁵¹⁴ Fauchald (n 59) 314.

⁵¹⁵ Vienna Convention (n 47) Article 31 (1).

⁵¹⁶ Gardiner (n 49) 334.

⁵¹⁷ Vienna Convention (n 47) Article 32.

⁵¹⁸ Thomas W. Wälde, 'Interpreting Investment Treaties: Experiences and Examples' in Christina Binder & others (eds), *International Investment Law for the 21st Century: Essays in Honour of Christoph Schreuer* (OUP 2009) 746. Zhang (n 55) 32.

⁵¹⁹ Jan Klabbers, *International Law* (2nd edn, CUP 2017) 56-7. UNCTAD (n 59).

⁵²⁰ *ibid*.

⁵²¹ Klabbers (n 519) 57.

⁵²² Dörr & Schmalenbach (n 51) 603.

⁵²³ Fowler & Fowler (n 187) 1085. 'Systemic' (*Cambridge Dictionary*)

<<https://dictionary.cambridge.org/dictionary/english/systemic>> last accessed 22 October 2021.

⁵²⁴ Campbell McLachlan, 'The Principle of Systemic Integration and Article 31 (3) (c) of the Vienna Convention' (2005) 54

its interpretation cannot be isolated from the environment in which it exists. Seen in this sense, a disputed treaty provision should be interpreted against two systems. The instant one is the treaty in which it appears, while the distant one is the entire international law.⁵²⁵

Nevertheless, issues arise due to the lack of definite guidance on the consideration of interpretative elements and the application of interpretative methods. As indicated by the single "rule" in the heading of Article 31, no hierarchy exists among those interpretative elements. However, as reflected in practice, the significance of each element is stressed by its corresponding methods, which may lead to different interpretations. Set the ordinary meaning of the word in question as an example. The word's plain meaning is regarded as the starting point of any treaty interpretation because the wording is the first thing from which the contracting parties' authentic expression can be directly discerned.⁵²⁶ This is questioned by Lauterpacht,⁵²⁷ who argues that without solid evidence, a term's ordinary meaning is doubtful.⁵²⁸ Otherwise, there is neither dispute as to the definition of any wording nor the need for treaty interpretation.⁵²⁹ Therefore, the precise meaning of a term should be regarded as the ending rather than the starting point of treaty interpretation.⁵³⁰ The absence of a defined order in which the application of various interpretative approaches should follow may also further obfuscate or even reverse interpretations of the same term,⁵³¹ further unbalancing the investor-state relationship.

A balanced treaty interpretation contributes to striking a balance in the investor-state relationship, but this is not what can be seen. Apart from the imbalance between the interpretations provided by treaty parties and tribunals,⁵³² the imbalance between different interpretive considerations can also be observed in practice. The tribunals who apply the teleological approach may merely stress the promotion and protection of foreign investment as a treaty's purpose and then interpret any controversial provisions in favour of foreign investors.⁵³³ By contrast, the interpretation provided in the subjective approach emphasises the achievement of a purpose intended by the contracting parties. Therefore, balancing different factors is needed in both situations to find a reliably structured approach to consider interpretative elements and treaty interpretation.

The International & Comparative Law Quarterly 279, 280.

⁵²⁵ This is the researcher's opinion that the word in question should be interpreted via the two-tier systemic approach.

⁵²⁶ Gardiner (n 49) 165.

⁵²⁷ M. H. Lauterpacht, 'De l'interprétation des traités (Douzième Commission)' (1950) 43 (I) *Annuaire DE l'Institut de Droit International* 366-434, see from Haopei Li, *The Law of Treaties* (Law Press 1988) 412-3 [in Chinese]. See the English translation as to Lauterpacht's opinion from the comments by Sir Eric Beckett, in (1950) 43 (I) *Annuaire DE l'Institut de Droit International* 435-44.

⁵²⁸ *ibid.*

⁵²⁹ *ibid.*

⁵³⁰ *ibid.*

⁵³¹ Zhang (n 55) 38.

⁵³² *ibid.* 35.

⁵³³ See an example *MTD v. Chile*, ICSID Case No. ARB/01/7, Award, 25 May 2004.

Based on its comparison with reasonableness and balancing in Chapter Two, proportionality, which can balance the considerations on different interpretative elements, is considered a suitable tool to achieve that purpose because it is structured and relatively flexible.⁵³⁴ In other words, proportionality is complementary to treaty interpretation in balancing the conflicting values of foreign investors and the host state. Meanwhile, the conflicts arising from the consideration of different interpretative factors, as asserted by Barak, can be settled by applying proportionality *stricto sensu*.⁵³⁵ That is to say, in the context of international investment, the application of proportionality contributes to finding a neutral interpretation of the term in question, while a balanced treaty interpretation contributes to applying proportionality in the ISDS.

To investigate how treaty interpretation and proportionality complement each other and identify the appropriate interpretative approach in the ISDS, this chapter will provide an overview of who can provide the authentic treaty interpretation in the ISDS in 3.2. Once this question is answered, the analysis will examine the interpretative elements and approaches stipulated in the Vienna Convention, explicitly or by implication. Article 31, as the "general rule of interpretation",⁵³⁶ will be mainly analysed in 3.3. Article 32, in particular *travaux préparatoires*, will be analysed to discuss the investigation of treaty parties' common intention.

Then, in 3.4, the appropriate one will be adduced by comparing different interpretative approaches. Based on the comparison, the two-tier systemic approach, which is hybrid and varies according to circumstances, in the researcher's view, is the proper way to interpret treaties. The principle of proportionality is applied to balance various interpretative considerations in cases, while it can also be brought into the ISDS regime through a hybrid interpretative approach. More detail as to proportionality analysis will be further discussed in Chapter Five.⁵³⁷

This chapter will conclude that, in practice, a fissure exists between the theoretical and practical effects of treaty interpretation. Consequently, issues such as the unpredictable interpretative power of interpreters and inconsistent interpretations of the same term can and do arise. These issues will be analysed in 3.5, followed by a discussion on the suggested resolution and the application of proportionality.

3.2 The Interpreters

In the context of international investment, as mentioned above, the contracting states to the case-related

⁵³⁴ See 2.2 in Chapter Two.

⁵³⁵ Barak (n 20) 4, 72-5.

⁵³⁶ Vienna Convention (n 47) Article 31.

⁵³⁷ See generally in Chapter Five.

treaty and the tribunals share the responsibility to interpret any controversial provisions.⁵³⁸ As expressed by the maxim, [*e]ius est interpretare legem cuius condere* (whoever is authorised to establish the law is authorised to interpret it),⁵³⁹ the state that concludes a treaty obviously can interpret it. Once a case is initiated, the tribunals are delegated by states to settle the ISD. Due to the ambiguous treaty provisions, the tribunals enjoy, to a certain extent, the power to ascertain the definitive meaning of the term in question to settle the dispute. As required by the principle of good faith emphasised in Article 31 of the Vienna Convention, a balance needs to be struck between the interpretative power of treaty parties and tribunals to interpret treaty provisions.⁵⁴⁰ Meanwhile, their cooperation in a particular case plays a role in balancing the conflicting values of foreign investors and the host state from the perspective of treaty interpretation, but issues remain in practice. This section will investigate the interpreter and how they can wield "proportionality" in international investment through treaty interpretation.

3.2.1 The Contracting States to a Treaty

In accordance with international law, the state has the power to sign IIAs and interpret treaty provisions. Setting the initiation of investment arbitration as the line, the states' roles can be classified into two stages leading to other participation in treaty interpretation.

Before the initiation of an ISA, both states that signed an IIA play the same role, viz., the contracting parties to the treaty. As set out by Li, these treaty parties have the power to express the meaning of a term, explicitly or implicitly.⁵⁴¹ Their understanding of an ambiguous word can be reflected by the concordant and consistent application of the questioned provision in practice.⁵⁴² Alternatively, they can discuss its meaning and then define it in treaty provisions, the protocol, or the exchange of notes.⁵⁴³ One prime example is the China-Turkey BIT (2015),⁵⁴⁴ stipulating that the FET standard requires that "investors of one contracting party shall not be rejected to fairly judicial proceedings by the other contracting party or be treated with obvious discriminatory or arbitrary measures".⁵⁴⁵ This provision explicitly reflects that China and Turkey's common intention on the host state's particular conduct, namely "obvious discriminatory or arbitrary measures",⁵⁴⁶ would violate its FET obligation *vis-à-vis* foreign investors. As expressed, FET in this BIT contains the prohibition of denial of justice and the

⁵³⁸ Gordon K & Pohl J (n 500) 12-3.

⁵³⁹ Aaron X. Fellmeth & Maurice Horwitz, *Guide to Latin in International Law* (OUP 2009) <<https://www.oxfordreference-com.ezproxy-s1.stir.ac.uk/view/10.1093/acref/9780195369380.001.0001/acref-9780195369380-e-600?rskey=97kmPL&result=583>> last accessed 24 June 2022.

⁵⁴⁰ Gardiner (n 49) 178-9.

⁵⁴¹ Li (n 527) 421. Zhang (n 55) 33.

⁵⁴² Li (n 527) 423. Dörr & Schmalenbach (n 51) 595-6. Gardiner (n 49) 274-8. Zhang (n 55) 35.

⁵⁴³ Li (n 527) 421-3. Zhang (n 55) 33.

⁵⁴⁴ China-Turkey BIT (n 15).

⁵⁴⁵ *ibid* Article 2 (3). A more detailed list of the FET standard can be seen in Comprehensive Economic and Trade Agreement between Canada, of the One Part, and the European Union and Its Member States, of the Other Part (CETA) (2017) Article 8.10. (2).

⁵⁴⁶ *ibid* Article 2 (3).

prohibition of discrimination and arbitrary measures.

The contracting states can also express their common intention on the meaning of a particular term in the treaty protocol. The protocol of the China-Germany BIT (2003),⁵⁴⁷ for instance, further clarifies the term "activities" stipulated in the treaty. As prescribed in the protocol, this term includes but is not limited to "the management, maintenance, use, enjoyment and disposal of an investment".⁵⁴⁸ Moreover, a special interpretative mechanism is provided in some treaties to express contracting parties' common understanding of a term. A unique example is the Free Trade Commission (FTC), which was established based on the NAFTA to interpret treaty provisions.⁵⁴⁹ Such consensus on particular terms expressed by the contracting states in the treaty provides clear guidance *ab initio* to the arbitral tribunals in the ISDS.

Once the arbitration is triggered, the role of a state in international investment will enter the second stage. Treaty parties will be automatically divided into the host state (disputing treaty party) and the home state of foreign investors (non-disputing treaty party). Correspondingly, their treaty interpretations have different effects on the arbitration. From the perspective of a disputing treaty party, the final award of the case is closely linked to its international responsibilities. In this regard, the host state's unilateral interpretation, to a large extent, may be regarded as its "self-serving" tool to influence the arbitral tribunals and eschew its responsibilities.⁵⁵⁰ This unilateral interpretation lacks credibility because it expresses no common intention of the contracting parties.

Meanwhile, a non-disputing treaty party can still participate in treaty interpretation to settle the ISD even though it is not a participant in the ISDS. This party's participation in the interpretation is referred to in Article 68 of the amended ICSID Arbitration Rules, which explicitly expresses that

The tribunal *shall* permit a party to a treaty that is not a party to the dispute ("non-disputing treaty party") to make a submission on the interpretation of the treaty at issue in the dispute and upon which consent to arbitration is based. The tribunal, may, after consulting with the parties, invite a non-disputing treaty party to make such a submission.⁵⁵¹ [italic added]

Based on the imperative "shall", the non-disputing treaty party has the absolute right to express its

⁵⁴⁷ China-Germany BIT (signed 1 December 2003, entered into force 11 November 2005).

⁵⁴⁸ Protocol to the Agreement between the People's Republic of China and the Federal Republic of Germany on the Encouragement and Reciprocal Protection of Investments 4.

⁵⁴⁹ NAFTA (entered into force 1 January 1994) Article 2001 (1) "[t]he Parties hereby establish the Free Trade Commission, comprising cabinet-level representatives of the Parties or their designees". Article 2001(2) (c) "[t]he Commission shall: resolve disputes that may arise regarding its interpretation or application".

⁵⁵⁰ Schreuer, 'Diversity' (n 76) 147. Anthea Roberts, 'Power and Persuasion in Investment Treaty Interpretation: The Dual Role of States' (2010) 104 *The American Journal of International Law* 179, 180. Zhang (n 55) 35.

⁵⁵¹ ICSID Arbitration Rules (2022) Article 68. A similar provision can be seen in the UNCITRAL Rules on Transparency in Treaty-based Investor-State Arbitration (2014) Article 5 with the heading 'Submission by a non-disputing Party to the treaty', which stipulates that "[t]he arbitral tribunal shall, subject to paragraph 4, allow, or, after consultation with the disputing parties, may invite, submissions on issues of treaty interpretation from a non-disputing party to the treaty".

understanding of the disputed term. As suggested by Argentina, special interpretative mechanisms should be applied if provided in the treaty.⁵⁵² Costa Rica evaluated that a unilateral interpretation provided by the non-disputing treaty party could contribute to ascertaining the contracting states' real intention when they concluded the treaty.⁵⁵³ If all non-disputing treaty parties in their unilateral statements confirm the disputing treaty party's unilateral assertion, the latter's interpretation can be deemed the authentic treaty interpretation;⁵⁵⁴ Otherwise, the tribunals should consider all treaty parties' understandings of the questioned term to make decisions.⁵⁵⁵

Although the contracting parties can express their interpretations of the same term in unilateral statements,⁵⁵⁶ the nature of the authentic interpretation is still their common intention or consensus on such a word. The participation of all treaty parties contributes to a neutral interpretation, establishing a balanced investor-state relationship at the stage of treaty interpretation. If only one party can express its understanding of the disputed term, it is questionable as to if such a state abuses this opportunity.

However, those issues can be prevented by an internal agreement of contracting states' interpretative power. If they achieve a consensus on a particular meaning of the term, the balance is struck. This interpretation has binding force on the tribunals in the ISDS. If there is no common intention amongst treaty parties, one party's interpretation, to a certain extent, is affected by another party's statement. This leaves a gap for the tribunals to do the real balancing based on the actual circumstances.

3.2.2 The Arbitral Tribunals

Legal reasoning cannot be separated from legal interpretation. When the tribunals have been delegated the power to settle disputes, they are also implicitly granted interpretative power.⁵⁵⁷ As stressed in *MTD v. Chile*,⁵⁵⁸ the duty of a tribunal is to "apply the provisions of the BIT and interpret them in accordance with the norms of interpretation established by the Vienna Convention on the Law of Treaties".⁵⁵⁹ However, the tribunal's such power is a non-exclusive interpretative power,⁵⁶⁰ which is reflected in Article 19 (2) of the China-Mexico BIT (2008).⁵⁶¹ This provision stipulates that "[a]ny interpretation *jointly* formulated and agreed upon by the contracting parties with regard to any provision of this agreement *shall be binding on any tribunal* established under this section".⁵⁶² As implied by the

⁵⁵² ICSID, Compendium of Comments for Working Paper #4, 54, comment from Argentina.

⁵⁵³ ICSID, Rule Amendment Project—Member State & Public Comments on Working Paper # 1 (August 3, 2018) Costa Rica, 320.

⁵⁵⁴ UNCTAD (n 59) 14.

⁵⁵⁵ Schreuer, 'Diversity' (n 76) 147.

⁵⁵⁶ *ibid.*

⁵⁵⁷ Zhang (n 55) 34-5. Roberts (n 550) 180.

⁵⁵⁸ *MTD v. Chile* (n 533).

⁵⁵⁹ *ibid* para 112.

⁵⁶⁰ Zhang (n 55) 34-5. Roberts (n 550) 180.

⁵⁶¹ China-Mexico BIT (signed 11 July 2008, entered into force 6 June 2009).

⁵⁶² *ibid* Article 19 (2) [*italic added*]. See also China-Tanzania BIT (n 261) Article 17.

imperative "shall" and the term "jointly", the tribunal is bound by treaty parties' common understanding of the questioned word.

The tribunals interact with the contracting parties in treaty interpretation.⁵⁶³ Roberts asserts that the tribunals settle the dispute on behalf of disputing parties and ascertain the meaning of controversial provisions within the process of the ISDS.⁵⁶⁴ A similar view is held by Liu,⁵⁶⁵ who points out that, in the ISDS, the tribunals enjoy the power to interpret treaty provisions relatively independent from the control of states.⁵⁶⁶ Tribunals' power should be restricted in a reasonable scope because their interpretations and decisions, more or less directly or indirectly, affect the host state's public interest.⁵⁶⁷ That expresses a process of weighing and balancing the interpretative power of treaty parties and tribunals.

Both contracting states and tribunals have the power to bring proportionality into the ISDS regime through treaty interpretation. As the master of their treaty, the contracting parties can stipulate the textual basis of proportionality implicitly or explicitly in the agreement. The prime example here is the China-Colombia BIT (2008),⁵⁶⁸ explicitly prescribing that the measures should be "proportional to the objective they seek to achieve" in the exception clause.⁵⁶⁹ More details on such textual bases will be discussed in Chapters Five and Six.⁵⁷⁰ Once an ISA is initiated, tribunals become the key players with the power to bring proportionality into the ISDS by interpreting treaty provisions through the systemic approach. Six Argentinian cases arising from its economic crisis of 2001/2, which will be analysed later, are excellent to present how the tribunals conveyed proportionality to balance the conflicting values of foreign investors and the host state.⁵⁷¹

3.3 Rules of Treaty Interpretation

Bianchi asserts that the rules on interpretation should be complied with in interpreting any controversial provisions.⁵⁷² In his view, the interpretative legitimacy does come from the Vienna Convention, in

⁵⁶³ Sheng Zhang, 'Guo Ji Tou Zi Fa Kuang Jia Xia De Di Yue Guo Jie Shi Yan Jiu' (A Study on the Interpretation by the Contracting States under the Framework of International Investment Law Regime) (2015) 37 *Modern Law Science* 163, 169 [in Chinese].

⁵⁶⁴ Roberts (n 550) 180.

⁵⁶⁵ Sun Liu, 'Zhong Cai Ting De Tiao Yue Jie Shi Quan Ji Wei Ye Na Tiao Yue Fa Gong Yue De Yin Dao Yu Zhi Yue' (Using the Treaty Law Convention to Guide and Restrict the Arbitral Tribunal's Power of Treaty Interpretation) (2021) *Journal of South China Normal University* 139, 140 [in Chinese].

⁵⁶⁶ *ibid* 140-1.

⁵⁶⁷ *ibid*. Zhang (n 55) 35.

⁵⁶⁸ China-Colombia BIT (n 124).

⁵⁶⁹ *ibid* Article 12 (d).

⁵⁷⁰ Seen in Chapters Five and Six.

⁵⁷¹ See generally in Chapter Five.

⁵⁷² Andrea Bianchi, 'The Game of Interpretation in International Law: The Players, the Cards, and Why the Game is worth the Candle' in Andrea Bianchi & others (eds), *Interpretation in International Law* (OUP 2015) 44, 46.

which the treaty interpretations should be firmly rooted.⁵⁷³ As asserted by Gardiner, such interpretative rules, as rules of customary international law, can even be applied by states-parties who are not members of the Vienna Convention to ascertain the meaning of ambiguous provisions.⁵⁷⁴ The significance of these rules is also emphasised in practice. The tribunal in *MTD* emphasised that treaty provisions should be interpreted in accordance with the interpretative rules as prescribed in the Vienna Convention.⁵⁷⁵

Unlike others, Article 31 provides the general rule of interpretation of a treaty. Article 31 (1), as noted by Fauchald, is the most frequently mentioned rule on treaty interpretation, which prescribes the essential interpretive elements.⁵⁷⁶ As stipulated, "[a] treaty shall be interpreted in *good faith* in accordance with the *ordinary meaning* to be given to the terms of the treaty in their *context* and in the light of its *object and purpose*".⁵⁷⁷ The interpretive factors refer to the plain meaning of the word in question, the context, the object and purpose of a treaty, and the principle of good faith.⁵⁷⁸ A similar but different view was held by the ILC, who pointed out that Article 31 (1) refers to three principles of interpretation.⁵⁷⁹ They are "interpretation in good faith", "interpretation in accordance with the ordinary meaning of the term", and "interpretation in the context of the treaty and in the light of its object and purpose".⁵⁸⁰ These separate principles were reemphasised by the tribunal in *Methanex v. America*.⁵⁸¹ In the researcher's view, the only difference in these opinions is that, compared with the former, the latter regards the context as well as the object and purpose of the treaty as one consideration in treaty interpretation. Both stress that the disputed word should not be interpreted in the abstract. Instead, it should be interpreted with consideration of the treaty in which it appears. Apart from those objective elements, the importance of the subjective factor, namely the contracting parties' common intention, is stressed in Article 31 (4), stipulating that "[a] special meaning shall be given to a term if it is established that the parties so intended".⁵⁸² The plural "parties" reflects that the special meaning should be both contracting parties' common intention.

Therefore, based on the entire Article 31, the factors that should be considered in treaty interpretation include: (a) the principle of good faith, (b) a word's ordinary meaning, (c) its context, (d) the object and purpose of the treaty, and (e) the contracting parties' common intention. As shall be discussed later, the difference between (d) and (e) is that the former mainly focuses on the objective aims pursued by the

⁵⁷³ *ibid* 44-5.

⁵⁷⁴ Gardiner (n 49) 6-7.

⁵⁷⁵ *MTD v. Chile* (n 533) para 112.

⁵⁷⁶ Fauchald (n 59) 314. Weeramantry (n 49) 42.

⁵⁷⁷ Vienna Convention (n 47) Article 31(1).

⁵⁷⁸ Weeramantry (n 49) 42.

⁵⁷⁹ UN (n 61) 221, para12.

⁵⁸⁰ UN, *Yearbook of the International Law Commission Volume II, A/CN.4/SER.A/1964/Add.1* (1965) 56, para 14.

⁵⁸¹ *Methanex v. America*, UNCITRAL, Final Award of the Tribunal on Jurisdiction and Merits, 3 August 2005, Part II-Chapter B para 16.

⁵⁸² Vienna Convention (n 47) Article 31(4). Dörr & Schmalenbach (n 51) 613. Gardiner (n 49) 334.

treaty, while the latter stresses the states' subjective intention.⁵⁸³ Without these primary materials expressed in Article 31 for treaty interpretation, other supplementary means provided in Article 32, in particular *travaux préparatoires*, also contribute to treaty interpretation.

As asserted by Koskenniemi, Article 31 of the Vienna Convention is the result of comprising various interpretative elements, which contain "all thinkable interpretative methods".⁵⁸⁴ According to different criteria, the interpretative methods referred to in Article 31 can be divided into several groups. Based on his view, they can be generally classified as objective and subjective approaches.⁵⁸⁵ In Fitzmaurice's view, they are textual, "seeking intention", and teleological methods, which emphasise the significance of the text's ordinary meaning, treaty parties' intentions, and the object and purpose of the treaty, respectively.⁵⁸⁶ The interpretative approach chiefly stressing the treaty parties' intention, in Klabbers' view, is the historical method.⁵⁸⁷ As asserted by Bos, interpretative methods are "grammatical (textual, literal)", "historical (subjective)", "systematic", "teleological", and "sociological" approaches.⁵⁸⁸ The systematic emphasises the context in which the disputed word appears, while the sociological approach stresses the interaction between interpretation and social development.⁵⁸⁹ In Orakhelashvili's view, contextual factors are also taken into account when interpreting the term in question via the textual approach, considering the contextual method is its variant.⁵⁹⁰

Concerning the appropriate interpretative method, Klabbers asserts a compromise of textual and teleological approaches.⁵⁹¹ In the view of Bos, that is a compound of systematic, teleological, and sociological approaches.⁵⁹² As highlighted by Koskenniemi, objective and subjective approaches are interwoven, and "neither can be maintained alone".⁵⁹³ The essential factors of treaty interpretation provided in the Vienna Convention, in particular Article 31, and their complementary interpretative approaches will be analysed below to present, in the researcher's view, the hybrid two-tier systemic method is proper for producing a balanced interpretation of treaties and applying proportionality in terms of treaty interpretation. To be clear, the systemic method in the current study interprets the questioned words against the treaty in which it appears and against the entire international law.⁵⁹⁴

⁵⁸³ Klabbers (n 519) 57.

⁵⁸⁴ Martti Koskenniemi, *From Apology to Utopia: The Structure of International Legal Argument* (CUP 2006) 334.

⁵⁸⁵ *ibid* 333-45.

⁵⁸⁶ G. G. Fitzmaurice, 'The Law and Procedure of the International Court of Justice: Treaty Interpretation and Certain Other Treaty Points' (1957) 33 *The British Yearbook of International Law* 203, 204-9. Text in 3.4. Gardiner (n 49) 460-7. UN, *Yearbook of the International Law Commission Volume II, A/CN.4/SER.A/1958/Add.1* (1958) 54. Klabbers (n 519) 56-8.

⁵⁸⁷ Klabbers (n 519) 57.

⁵⁸⁸ Bos (n 57) 136.

⁵⁸⁹ *ibid* 137-8.

⁵⁹⁰ Orakhelashvili (n 67) 339-40.

⁵⁹¹ Klabbers (n 519) 57.

⁵⁹² Bos (n 57) 151.

⁵⁹³ Koskenniemi (n 584) 337.

⁵⁹⁴ Zhang (n 55) 74. Zhang also mentions the systemic interpretation refers to the interpretation of treaties at two levels. McLachlan (n 524) 279-80.

3.3.1 Interpreting in Good Faith

As stipulated in Article 31 (1) of the Vienna Convention, a notable and important factor that should be considered in interpreting treaties is "good faith".⁵⁹⁵ This principle also appears as "*pacta sunt servanda*" in Article 26, prescribing that "[e]very treaty in force is binding upon the parties to it and must be performed by them in good faith".⁵⁹⁶ Based on these rules, treaty provisions should be interpreted in accordance with the interpretative rules provided in the Vienna Convention; Meanwhile, such an interpretation should be carried out in good faith.⁵⁹⁷

"Good faith" is evaluated as "the overarching principle of treaty interpretation" by Bjorge.⁵⁹⁸ As asserted by Villiger, "good faith" lies at the centre of treaty interpretation.⁵⁹⁹ Although no detail is provided in the Vienna Convention, Gardiner points out that good faith requires a balance between different elements, linking itself to the principle of reasonableness.⁶⁰⁰ The tribunal in *Istrokapital SE v. Hellenic*⁶⁰¹ stressed that

[A]n interpretation in good faith is not simply *interpretation bona fides*, as opposed to the absence of *mala fides*, or a principle providing for the rejection of an interpretation that is abusive or that may result in the abuse of rights. It also means *the interpretation requires elements of reasonableness that go beyond the mere verbal or purely literal analysis*.⁶⁰² [italic added]

As emphasised, the meaning of a term interpreted in good faith is not merely a formal reasonable based on the consideration of verbal or literal elements. Instead, a balance needs to be struck between the obligations and rights expressed by the questioned terms.⁶⁰³ Based on the earlier discussion in Chapter Two, proportionality, especially proportionality *stricto sensu*, can be applied to reach the real balance between conflicting values arising from treaty interpretation.⁶⁰⁴ Different purposes pursued by ambiguous treaty provisions are weighed and balanced against their own social importance.⁶⁰⁵

Additionally, Fauchald asserts that good faith is closely linked to principles of effectiveness and restrictiveness.⁶⁰⁶ As required by effectiveness, the interpretation of the disputed word must make it

⁵⁹⁵ Vienna Convention (n 47) Article 31.

⁵⁹⁶ *ibid* Article 26.

⁵⁹⁷ Bjorge (n 54).

⁵⁹⁸ *ibid*.

⁵⁹⁹ Villiger, 'The Rules on Interpretation' (n 66) 108.

⁶⁰⁰ Gardiner (n 49) 176-7.

⁶⁰¹ *Istrokapital SE v. Hellenic*, ICSID Case No. ARB/13/8, Award, 9 April 2015.

⁶⁰² *ibid* para 284.

⁶⁰³ Gardiner (n 49) 176-7.

⁶⁰⁴ See 2.4.4 in Chapter Two. Barak (n 20) 71-5.

⁶⁰⁵ Barak (n 20) 73.

⁶⁰⁶ Fauchald (n 59) 317.

meaningful.⁶⁰⁷ More specifically, its interpretation should not conflict with that of other provisions in the same treaty, aiming to maximally contribute to the realisation of the object and purpose of the treaty.⁶⁰⁸ In this respect, effectiveness is closely related to the teleological approach.⁶⁰⁹ However, considering the treaty's object and purpose mainly focusing on the promotion and protection of foreign investments, the ambiguous treaty provision may be interpreted in favour of foreign investors. By contrast, the principle of restrictiveness aims to protect the host state's sovereignty.⁶¹⁰ That is to say, the preference for a party's value is implied in the consideration of each interpretative factor.

3.3.2 The Ordinary Meaning of the Word in Question

In order to ascertain the value contained in the questioned term, the ordinary meaning of such a word should be considered. The plain meaning of the disputed term is regarded as the starting point of interpretation because the text itself is the first thing based on which the treaty parties' authentic intention can be ascertained.⁶¹¹ As emphasised by the ICJ, "the first duty of a tribunal which is called upon to interpret and apply the treaty provisions, is to endeavour to give effect to them in their *natural and ordinary meaning* in the context in which they occur".⁶¹² Its corresponding interpretive method is the textual approach.⁶¹³ However, there is an exception in Article 31 (4), stressing the significance of the contracting parties' common intention in treaty interpretation,⁶¹⁴ which will be discussed in 3.3.5.

The disputed term's plain meaning, as asserted by Villiger, is its "current and normal, regular and usual meaning".⁶¹⁵ Concluded from practice, the dictionary is the most common tool applied to find the plain meaning of controversial terms.⁶¹⁶ The importance of the dictionary can be seen in *Caratube v. Kazakhstan*,⁶¹⁷ a case in which one controversial issue is whether the term "commercial discovery" contains a requirement for finding new oil.⁶¹⁸ As defined in English language dictionaries, "discovery" emphasises the first time finding something that had never known its existence before.⁶¹⁹ This definition was also confirmed by the Respondent's expert, Dr Thapar, in the field of the oil industry.⁶²⁰ As he put, "discovery" in this particular industry refers to the new oil requirement.⁶²¹ In other words, the ordinary

⁶⁰⁷ *Asian Agricultural Products Ltd. v. Republic of Sri Lanka*, ICSID Case No. ARB/87/3, Final Award, 27 June 1990, para 40 Rule E.

⁶⁰⁸ Fauchald (n 59) 317.

⁶⁰⁹ *ibid.*

⁶¹⁰ *ibid.*

⁶¹¹ UN (n 61) 218 para 2, 220-1 para 11-2. Gardiner (n 49) 165. Villiger, 'The Rules on Interpretation' (n 66) 109.

⁶¹² 'Competence' (n 60) 582.

⁶¹³ Text to 3.4.1. UN (n 61) 220, para 11.

⁶¹⁴ Vienna Convention (n 47) Article 31 (4).

⁶¹⁵ Villiger, 'The Rules on Interpretation' (n 66) 109. Fitzmaurice (n 586) 211-2.

⁶¹⁶ Zhang (n 55) 92. Gardiner (n 49) 184.

⁶¹⁷ *Caratube v. Kazakhstan*, ICSID ARB/13/13, Award, 27 September 2017.

⁶¹⁸ *ibid* para 833.

⁶¹⁹ *ibid.*

⁶²⁰ *ibid.*

⁶²¹ *ibid.*

meaning of "discovery" makes sense in the context in which it occurs.⁶²²

However, a word's definition in the dictionary still raises uncertainties because the truth in practice is that diverse meanings of a term, from common to rare, can be seen in the dictionary.⁶²³ If the questioned word is merely interpreted based on the consideration of its ordinary meaning defined in the dictionary, a confusing situation can emerge: The more definitions in the dictionary, the more uncertainties in the meaning of the disputed word.⁶²⁴ This situation can be seen in *Saluka*.⁶²⁵ Saluka brought a case against the Czech Republic because its investment in IPB, one of the "Big Four Banks" in the Czech Republic, had been impaired by the host state's intervention and finally experienced forced administration. One controversial issue was whether the Czech Republic had breached its FET obligation *vis-à-vis* foreign investors as stipulated in the Czech Republic-Netherlands BIT (1991).⁶²⁶ Based on the treaty, the host state "shall ensure fair and equitable treatment" to foreign investors.⁶²⁷ To settle the dispute, the tribunal started with finding the ordinary meaning of FET. Based on the interpretative rules, the tribunal first ascertained the ordinary meaning of "fair" and "equitable".⁶²⁸ However, as it found, the meaning of these terms refers to "just", "even-handed", "unbiased", and "legitimate", which are still ambiguous and vague.⁶²⁹

Due to those uncertainties, the significance of the ordinary meaning of the text is doubted. As criticised by Sir Lauterpacht, the word's natural meaning as an interpretation has been over-estimated.⁶³⁰ Instead of the starting point, he regards the term's precise meaning as the ending of interpretation.⁶³¹ The plain meaning of the disputed word is doubtful because there is no need to interpret it if its definition is clear.⁶³² Such a need for interpretation implies that the credibility of the plain meaning is not solid.⁶³³

3.3.3 The Context

Then, other factors should be considered to investigate the meaning of the word in question. No word is drafted in isolation,⁶³⁴ and the context in which the disputed word appears plays a vital role that should

⁶²² 'Competence' (n 60) 584.

⁶²³ *United States-Measures Affecting the Cross-Border Supply of Gambling and Betting Services*, WT/DS285/AB/R, Report of the Appellate Body, 7 April 2005, para 164.

⁶²⁴ Hosseinejad (n 63).

⁶²⁵ *Saluka v. Czech Republic* (n 84).

⁶²⁶ Czech Republic-Netherlands BIT (n 101).

⁶²⁷ *ibid* Article 3 (1).

⁶²⁸ *Saluka v. Czech Republic* (n 84) para 297.

⁶²⁹ *ibid*.

⁶³⁰ Lauterpacht (n 527).

⁶³¹ *ibid*. Francis G. Jacobs, 'Varieties of Approach to Treaty Interpretation: With Special Reference to the Draft Convention on the Law of Treaties before the Vienna Diplomatic Conference' (1969) 18 *International & Comparative Law Quarterly* 318, 341.

⁶³² Lauterpacht (n 527).

⁶³³ *ibid*.

⁶³⁴ Villiger, 'The Rules on Interpretation' (n 66) 109.

be taken into account in treaty interpretation.⁶³⁵ As asserted by Dörr and Schmalenbach, such a context supports whether its ordinary meaning is reasonable⁶³⁶ and helps interpreters to ascertain the appropriate explanation from a range of definitions provided in the dictionary.⁶³⁷

Based on the wording of Article 31, the relation between the interpreted term and the context in which it appears refers to three layers, from the immediate to the distant. By definition, the restrictive "context" means "the parts in which *immediately* precede or follow any particular passage or 'text' and determine its meaning".⁶³⁸ The context in this sense means the rest of the provisions of the same treaty, the preamble and any annexes.⁶³⁹ Villiger opines that the meaning of an ambiguous term can only be determined based on "the entire treaty text".⁶⁴⁰ For example, the precise meaning and scope of FET can be further confirmed by the context in which it appears.⁶⁴¹ Different phrases or terms stipulated in IAs, such as "no more than",⁶⁴² "requires",⁶⁴³ and "includes",⁶⁴⁴ lead to various understandings of this standard. More detail as to the vital role of such an immediate "context" in determining the meaning of FET will be discussed in Chapter Four.⁶⁴⁵

Another two layers of the "context" can be seen in Article 31 (2) and (3) in the Vienna Convention,⁶⁴⁶ which refers to "agreements relating to the treaty" and "instruments related to the treaty"⁶⁴⁷ as well as "any subsequent agreement" and "any subsequent practice",⁶⁴⁸ respectively. In Li's view, the former expresses the internal factors of a treaty, whereas the latter represents the external factors.⁶⁴⁹ This is rejected by Dörr and Schmalenbach, who argue that none of them is an integral part of the treaty itself.⁶⁵⁰ Instead, they are closely linked to the treaty from different aspects.⁶⁵¹ Setting the conclusion of a treaty

⁶³⁵ Vienna Convention (n 47) Article 31 (1).

⁶³⁶ Dörr & Schmalenbach (n 51) 582-4.

⁶³⁷ *ibid* 590. *AES Corporation v. Kazakhstan*, ICSID ARB/10/16, Award, 1 November 2013, para 314.

⁶³⁸ 'Context' (*OED*) <https://www.oed-com.ezproxy-s1.stir.ac.uk/search?searchType=dictionary&q=context&_searchBtn=Search> last accessed 22 October 2021 [italic added].

⁶³⁹ Vienna Convention (n 47) Article 31 (2).

⁶⁴⁰ Villiger, 'The Rules on Interpretation' (n 66) 109. Dörr & Schmalenbach (n 51) 582.

⁶⁴¹ Text to 3.4.1. *Pope & Talbot v. Canada*, UNCITRAL, Award on the Merits of Phase 2, 10 April 2001.

⁶⁴² See an example China-Mexico BIT (n 561) Article 5 (2), which reads that "[t]he concept of "fair and equitable treatment" ...do *not* require treatment *in addition to or beyond* that which is required by the international law minimum standard of treatment of aliens as evidence of state practice and *opinion juris*'.

⁶⁴³ "Require" implies an exhaustive list of FET's constituent elements. See an example Agreement on Investment among the Government of the Hong Kong Special Administrative Region of the People's Republic of China and the Member States of the Association of Southeast Asian Nations (signed 12 November 2017, entered into force 17 June 2019) Article 5 (1) (a), which reads that "'[f]air and equitable treatment" *requires* each party not to deny justice in any legal or administrative proceedings in accordance with the principles of due process of law'.

⁶⁴⁴ "Include" means an exemplified list of FET. See an example China-Colombia BIT (n 124) Article 2 (4) (c), which reads that "'[f]air and equitable treatment" *includes* the prohibition against denial of justice in criminal, civil, or administrative proceedings in accordance with the general accepted principles of customary international law'.

⁶⁴⁵ See 4.2.3 in Chapter Four.

⁶⁴⁶ Li (n 527) 426.

⁶⁴⁷ Vienna Convention (n 47) Article 31 (2).

⁶⁴⁸ *ibid* Article 31 (3).

⁶⁴⁹ Li (n 427) 426.

⁶⁵⁰ Dörr & Schmalenbach (n 51) 561.

⁶⁵¹ *ibid* 588-92.

as the critical point, Article 31 (2) relates to the development of this treaty and contributes to its conclusion,⁶⁵² while Article 31 (3) refers to the materials that emerge after that process.⁶⁵³ As they assert, compared with the latter, the former has a closer connection with a treaty's conclusion.⁶⁵⁴

Dörr and Schmalenbach further highlight that the significance of a broader context, namely the entire international law, can be observed in Article 31 (3) (c).⁶⁵⁵ Unlike the context that appears in other subparagraphs of Article 31, that in Article 31 (3) (c) is stipulated in a more general sense, referring to "any *relevant* rules of international law applicable in the relations between the parties".⁶⁵⁶ As emphasised by "relevant", those rules should deal with the same or similar issues with the interpreted treaty, or treaty parties are also member states of the other treaty.⁶⁵⁷ In Koskenniemi's view, this provision expresses the concept of "systemic integration",⁶⁵⁸ requiring a treaty should be interpreted "in the context of the rules of interpretation law".⁶⁵⁹ He further evaluates that it governs all treaty interpretation.⁶⁶⁰ A similar view is held by McLachlan, who asserts that no treaty is produced isolated from international law.⁶⁶¹ Like a term should be interpreted in the context (treaty) it appears, a treaty should also be interpreted in the context (entire international law) it appears. Therefore, considering international law as a whole legal system, an ambiguous word should also be interpreted against the background of other rules and principles.⁶⁶² Interpreting ambiguous treaty provisions in this general background aids in eliminating the fragmentation of international law and balancing conflicts.⁶⁶³ In Zhang's view, a balanced approach is required in a broad context rather than one-sided protection provided to foreign investors or the host state.⁶⁶⁴

3.3.4 The Object and Purpose of the Treaty

Another essential interpretative factor in Article 31 (1) of the Vienna Convention is "the object and purpose of the treaty".⁶⁶⁵ Its corresponding interpretive method is the teleological approach.⁶⁶⁶

The importance of this factor in treaty interpretation is emphasised, but its application raises debates

⁶⁵² *ibid* 593.

⁶⁵³ *ibid*.

⁶⁵⁴ *ibid*.

⁶⁵⁵ Dörr & Schmalenbach (n 51) 592.

⁶⁵⁶ Vienna Convention (n 47) Article 31 (3) (c) [*italic added*]. Gardiner (n 49) 290.

⁶⁵⁷ Dörr & Schmalenbach (n 51) 604. Martti Koskenniemi, *Fragmentation of International Law: Difficulties Arising from the Diversification and Expansion of International Law*, Document A/NC.4/L.682, 160. Gardiner (n 49) 299.

⁶⁵⁸ Koskenniemi (n 657) 206.

⁶⁵⁹ *ibid* 216, para 430.

⁶⁶⁰ *ibid* 208.

⁶⁶¹ McLachlan (n 524) 279, 280

⁶⁶² UN, *Yearbook of the International Law Commission Volume II Part Two*, A/CN.4/SER.A/2006/Add.1 (2006) 177-8.

⁶⁶³ Dörr & Schmalenbach (n 51) 604.

⁶⁶⁴ Zhang (n 55) 74-8.

⁶⁶⁵ Vienna Convention (n 47) Article 31 (1).

⁶⁶⁶ Morse (n 72) 36, 41. Text to 3.4.2.

among scholars, such as its role in treaty interpretation. Article 19 of the Harvard Draft Convention on the Law of Treaties prescribes that "[a] treaty is to be interpreted in the light of the general purpose which it is intended to serve".⁶⁶⁷ As asserted by Morse, the purpose of treaty interpretation is to realise "the object and purpose of a treaty".⁶⁶⁸ This perspective is repudiated by Gardiner, who argues that the "object and purpose of a treaty", like the "context", is an interpretative factor that contributes to cognition or confirmation of the plain meaning of the terms of a treaty.⁶⁶⁹ In other words, the precondition for considering this element is the finding of the questioned term's ordinary meaning.⁶⁷⁰

Furthermore, identifying a treaty's purpose and object raises issues due to the ambiguousness of relevant wording.⁶⁷¹ In Gardiner's view, from the treaty preamble to its substantive provisions and even the treaty parties' practice, all of these materials can be applied to deduce a treaty's object and purpose.⁶⁷² He regards the treaty preamble as the starting point of identifying a treaty's intention.⁶⁷³ Dörr and Schmalenbach also note that the preamble is the place in which the contracting parties regularly contextualise why they intend to agree on such a treaty.⁶⁷⁴ However, ambiguous wording of a treaty preamble more or less affects the perceived validity of the purpose,⁶⁷⁵ and the contribution of such an interpretative element to treaty interpretation may be undermined.

3.3.5 The Common Intention of the Contracting States

Although the contracting states' common intention is not explicitly prescribed in Article 31 of the Vienna Convention, its significance can also be observed in Article 31 (1) and (4). The former implicitly mentions this subjective element of interpretation, while the latter explicitly expresses its importance in treaty interpretation.

As pointed out by Song, the phrase "to be given to" in Article 31 (1) implies that the contracting parties' common intention is a vital interpretative element.⁶⁷⁶ This phrase describes a process, implicitly emphasising the significance of contracting parties as to who can give such a term's meaning, which indirectly stresses states' intention.⁶⁷⁷ Differently, Article 31 (4) is regarded as the only provision in

⁶⁶⁷ See from Gardiner (n 49) 63.

⁶⁶⁸ Morse (n 72).

⁶⁶⁹ Gardiner (n 49) 211.

⁶⁷⁰ *ibid.*

⁶⁷¹ *ibid* 217.

⁶⁷² *ibid* 213

⁶⁷³ *ibid* 217.

⁶⁷⁴ Dörr & Schmalenbach (n 51) 585.

⁶⁷⁵ Gardiner (n 49) 217. For example, as he illustrated, the phrase "boundaries between territories" mentioned in a treaty preamble with no detail may raise a debate on whether the term "boundary" refers to land and maritime boundaries or only one of them.

⁶⁷⁶ Jie Song, 'Dui Wei Ye Na Tiao Yue Fa Gong Yue Guan Yu Tiao Yue Jie Shi Gui Ze De Zai Ren Shi' (Revisiting the Interpretative Rules under the Vienna Convention on the Law of Treaties) (2007) 27 *Journal of Xiaogan University* 76, 78 [in Chinese].

⁶⁷⁷ *ibid* 78.

which the significance of treaty parties' common intention is explicitly emphasised. As it stipulates, "[a] special meaning shall be given to a term if it is established that the parties so intended".⁶⁷⁸ Instead of objective factors mentioned in Article 31 (1), it stresses the significance of treaty parties' intention, which is subjective. Meanwhile, the plural word "parties" indicates that to be adopted as the authentic treaty interpretation, a term's "special meaning" must be the common intention of contracting parties rather than a state's unilateral aim,⁶⁷⁹ corresponding to the earlier discussion in 3.2.1.⁶⁸⁰

Different views are held by scholars on the role of "contracting parties' common intention" in treaty interpretation. As emphasised by Cicero, *semper in fide quid senseris, non quid dixeris cogitandum* (in a promise, the parties' intention must be noted, rather than the wording),⁶⁸¹ expressing the importance of this subjective interpretative element. Sir Lauterpacht also stresses the significance of treaty parties' common intention in interpreting treaties.⁶⁸² In his view, the main point of treaty interpretation is to ascertain treaty parties' intentions.⁶⁸³ As he further clarified, a term's ordinary meaning reflects a hypothesis as to their intention, which can subsequently be replaced by the real intention in actual circumstances.⁶⁸⁴

Even if the aim of treaty interpretation, as stressed by Sir Lauterpacht, is to find the contracting parties' actual common intention, one may question how to determine it. If an explicit provision contains a special meaning of the word, as stipulated in Article 31 (4) of the Vienna Convention, then that is the answer. If there is no clear consensus, other materials, such as *travaux préparatoires*, may be used to identify the disputed term's special meaning.⁶⁸⁵ How to access those materials, however, is, in practice, extremely difficult.

3.3.6 *Travaux Préparatoires*

Travaux préparatoires, namely preparatory work, is explicitly referred to in Article 32 of the Vienna Convention, stipulating that

Recourse may be had to *supplementary means* of interpretation, *including* the preparatory work of the treaty and the circumstances of its conclusion, in order to *confirm* the meaning resulting from the application of article 31, or to *determine* the meaning when the interpretation according to article 31:

(a) leaves the meaning *ambiguous or obscure*; or

⁶⁷⁸ Vienna Convention (n 47) Article 31(4).

⁶⁷⁹ Dörr & Schmalenbach (n 51) 614.

⁶⁸⁰ Text to 3.2.1

⁶⁸¹ See from Li (n 527) 406.

⁶⁸² Lauterpacht (n 527).

⁶⁸³ *ibid.* UN, *Yearbook of the International Law Commission* (n 580) 53.

⁶⁸⁴ *ibid.*

⁶⁸⁵ Dörr & Schmalenbach (n 51) 614.

(b) leads to a result which is *manifestly absurd or unreasonable*.⁶⁸⁶ [italic added]

As reflected in this wording, like the word "may", Article 32 is more flexible than Article 31.⁶⁸⁷ As indicated by the term "include", this is an exemplified rather than an exclusive list, reflecting that the supplementary means of interpretation are not limited to the listed materials.⁶⁸⁸ Meanwhile, the term "supplementary means" and their aim clearly express a hierarchy between Articles 31 and 32. The latter cannot be independently applied and contributes to the confirmation or determination of the meaning of the disputed word interpreted based on Article 31.⁶⁸⁹

However, that view is denied by Schwebel, who questions the role of *travaux préparatoires* in two special situations.⁶⁹⁰ If the meaning of a word interpreted based on Article 31 differs from that interpreted on the basis of Article 32, or if the supplementary means provided in Article 32 cannot confirm a word's clear interpretation, then the role of such supplementary means in the interpretation of treaties would raise doubts.⁶⁹¹ Instead of a hierarchy, both rules express different interpretative approaches, which need to be balanced.⁶⁹² Although the Vienna Convention chiefly stresses the significance of the textual method, other factors of teleological and subjective approaches can also be observed in the rules.⁶⁹³

Nevertheless, Linderfalk argues that a hierarchy as a fixed structure between Articles 31 and 32 is settled, which is reflected in the wording of the Vienna Convention.⁶⁹⁴ Therefore, within the process of treaty interpretation, the primary means stipulated in Article 31 should be applied first, followed by the application of supplementary means according to the circumstances. As to Schwebel's doubts, he further points out that the proponents of *travaux préparatoires* do not expect an answer, corresponding to Schwebel's opinion that the question is unanswerable.⁶⁹⁵ It is in the researcher's view that the hierarchical structure in the Vienna Convention has no conflicts with a balance in various interpretative approaches. Based on the earlier discussion on Article 31, this provision itself refers to different interpretative methods, and a balance is required by the principle of good faith.⁶⁹⁶

⁶⁸⁶ *ibid* 618. Vienna Convention (n 47) Article 32.

⁶⁸⁷ Dörr & Schmalenbach (n 51) 628. Gardiner (n 49) 347-8.

⁶⁸⁸ Dörr & Schmalenbach (n 51) 620, 626-7. Weeramantry (n 49) 99-100.

⁶⁸⁹ Ulf Linderfalk, 'Is the Hierarchical Structure of Articles 31 and 32 of the Vienna Convention Real or Not? Interpreting the Rules of Interpretation' (2007) 54 *Netherlands International Law Review* 135-36. Zhang (n 55) 115-6.

⁶⁹⁰ Stephen M. Schwebel, 'May Preparatory Work be Used to Correct Rather than Confirm the "Clear" Meaning of a Treaty Provision' [1997] *SvJT* 797, 799-803 <<https://svjt.se/svjt/1997/803>> last accessed 24 June 2022.

⁶⁹¹ *ibid*.

⁶⁹² *ibid*.

⁶⁹³ *ibid*.

⁶⁹⁴ Linderfalk (n 689) 136. Zhang (n 55) 119-20.

⁶⁹⁵ Linderfalk (n 689) 137. Schwebel (n 690).

⁶⁹⁶ Text to 3.3.1.

In fact, the main issue in applying *travaux préparatoires* is its accessibility.⁶⁹⁷ By analysing 98 cases, Fauchald found that *travaux préparatoires* were utilised to interpret treaty provisions in 25 cases and were discussed in detail in only a few cases.⁶⁹⁸ Zhang also asserts that its availability is decisive in applying *travaux préparatoires* in treaty interpretation.⁶⁹⁹ *Pope & Talbot*, a case mentioned before, is a prime example to prove the difficulties in accessing such materials.⁷⁰⁰

To recap, both contracting states of the treaty and tribunals should consider the interpretative elements when they ascertain the meaning of the term in question. Considering the sequence between Articles 31 and 32, the primary means should be adopted first to interpret ambiguous treaty provisions. As indicated by the single word "rule" in the heading of Article 31, no hierarchy exists among these factors.⁷⁰¹ Instead, the internal logic of interpreting treaty provisions is implied in this provision.⁷⁰² No ranking exists among the interpretive factors, but their intrinsic logical order should be followed.⁷⁰³ Villiger asserts that the interpretative elements should be considered from the immediate to the distant, from the intrinsic to the extraneous.⁷⁰⁴ Similarly, Gardiner points out that this process "starts from the terms to context, through any agreements at the time of conclusion of a treaty, to subsequent agreements and practice".⁷⁰⁵

That is to say, the interpretation of treaties starts from the queried word itself. If its ordinary meaning makes sense in the treaty, that interpretation holds. Otherwise, the remaining part of the same provision in which the term in question appears is firstly considered, followed by the enquiry of the rest clauses and the preamble in the same treaty.⁷⁰⁶ The external contexts, including other relevant international instruments, are finally studied to confirm that the interpretation of such an obligation is in accordance with states' duties in other international instruments.⁷⁰⁷ Meanwhile, following the principle of good faith, all elements should be considered and balanced on a case-by-case basis, contributing to a balanced treaty interpretation. In this respect, proportionality *stricto sensu*⁷⁰⁸ can be used to weigh and balance different interpretative factors based on the social importance of their different purposes.

However, it can be concluded from practice that whether the interpretation of treaties is balanced is also

⁶⁹⁷ Zhang (n 55) 120-2. Weeramantry (n 49) 101, 108. Schreuer, 'Diversity' (n 76) 137.

⁶⁹⁸ Fauchald (n 59) 349-50.

⁶⁹⁹ Zhang (n 55) 121.

⁷⁰⁰ *Pope & Talbot v. Canada* (n 641).

⁷⁰¹ Gazzini (n 52). Bjorge (n 54).

⁷⁰² Gardiner (n 49) 222.

⁷⁰³ Villiger, 'The Rules on Interpretation' (n 66) 114.

⁷⁰⁴ *ibid.*

⁷⁰⁵ Gardiner (n 49) 290.

⁷⁰⁶ *ibid.* 222. Villiger, 'The Rules on Interpretation' (n 66).

⁷⁰⁷ Villiger, 'The Rules on Interpretation' (n 66) 114.

⁷⁰⁸ As mentioned in Chapter Two, proportionality *stricto sensu* is the value-oriented factor contained in the principle of proportionality, aiming at the real balance between conflicting values.

affected by the applied interpretative method. As noted by Schreuer, considering the treaty's object and purpose, interpreters prefer to produce effective rather than restrictive interpretations.⁷⁰⁹ Also, the treaty interpretations produced in the restrictive approach have always been rejected by tribunals.⁷¹⁰ Such differences reemphasise the significance of a balance interpretative method. Based on the examinations and comparisons between different interpretative approaches below, it is the researcher's view that the two-tier systemic method is suitable to re-balance the investor-state relationship in terms of treaty interpretation.

3.4 Approaches to Treaty Interpretation

As stressed by Bos, "a choice of a rule of interpretation often includes a choice of one or more methods".⁷¹¹ Different interpretative approaches can be deduced from the wording of Article 31 of the Vienna Convention, including textual, teleological, and subjective ways.⁷¹² These approaches stress the significance of the term's ordinary meaning, the treaty's object and purpose, and the treaty parties' intention, respectively.⁷¹³ The UNCTAD emphasises that all elements should be comprehensively considered to interpret ambiguous treaty provisions.⁷¹⁴ Compared with these methods, in the researcher's view, the two-tier systemic approach, which is hybrid, is a proper way to treaty interpretation.

3.4.1 The Textual Approach

Derived from practice, Fauchald notes that the textual approach, which centres on the disputed terms, has been the most frequently applied to interpret treaties.⁷¹⁵ This method focuses on the disputed word and the context in which it appears. In Orakhelashvili's view, the contextual method is a variant of the textual method.⁷¹⁶ As discussed in 3.3.1, the meanings provided in the dictionary are considered to determine the ordinary meaning of the questioned term, but issues remain if there are various nuanced definitions. "Then", as stressed by the ICJ, "and only then, by resort to other methods of interpretation, seek to ascertain what the parties indicated when they used the word".⁷¹⁷

As demonstrated in *Pope & Talbot*,⁷¹⁸ the contextual elements should be considered to further clarify the questioned term. This case arose from the measure taken by Canada to control the export of softwood lumber products, and Pope & Talbot claimed that Canada had breached its FET obligation prescribed

⁷⁰⁹ Schreuer, 'Diversity' (n 76) 133.

⁷¹⁰ *ibid.*

⁷¹¹ Bos (n 57) 143.

⁷¹² Klabbbers (n 519) 56-8.

⁷¹³ *ibid.*

⁷¹⁴ UNCTAD (n 59). Fauchald (n 59).

⁷¹⁵ Fauchald (n 59) 316.

⁷¹⁶ Orakhelashvili (n 67) 339-40.

⁷¹⁷ 'Competence' (n 60) 582.

⁷¹⁸ *Pope & Talbot v. Canada* (n 641).

in the NAFTA. The disputing parties failed to reach a consensus on the relationship between FET provided in Article 1105 (1) of the NAFTA and the requirement of international law. Canada argued that it had not violated the FET obligation unless its conducts were "egregious".⁷¹⁹ This view was denied by the tribunal. Based on the consideration of the connection between Article 1105 and other clauses in the NAFTA, particularly the provisions of "national treatment" (NT, Article 1102⁷²⁰) and "most-favoured-nation treatment" (MFN, Article 1103⁷²¹), the tribunal pointed out that FET is not restricted by the rules of international law.⁷²² It further clarified that the provisions of the NAFTA should be interpreted in consistent with the language of other BITs signed by the contracting parties of the NAFTA with other countries.⁷²³ Otherwise, there would be a conflict between Articles 1105 and 1103,⁷²⁴ breaching the principle of effectiveness. Also, as required by NT, the protections and promotions enjoyed by foreign investors should not be any less favourable than those enjoyed by Canada's domestic investors.⁷²⁵ The latter's rights are not restricted by the rules of international law;⁷²⁶ Thus, the FET standard stipulated in the NAFTA is unrestricted. Otherwise, Article 1105 would conflict with Article 1102.⁷²⁷

A similar consideration of the context in which the disputed word appears can be observed in *Saluka v. Czech Republic*.⁷²⁸ In this case, one controversial point is whether the FET stipulated in the Czech Republic-Netherlands BIT (1991) is an autonomous standard. To answer this question, the tribunal compared the FET clause prescribed in the treaty with that in Article 1105 (1) of the NAFTA. Based on the comparison, the tribunal found the omission of the phrase "customary international law minimum standard of treatment of aliens" in the treaty.⁷²⁹ Therefore, it asserted that such an absence implied the lack of connection between FET and international standards.⁷³⁰ In other words, the FET standard provided in the Czech Republic-Netherlands BIT (1991) is autonomous.⁷³¹

3.4.2 The Teleological Approach

While interpreting a treaty, its preamble plays an essential role from different perspectives. As evaluated by Dörr and Schmalenbach, this factor is considered in both the textual and teleological approaches because it is the place in which the contracting parties express their purpose and reason for such a

⁷¹⁹ *ibid* para 108.

⁷²⁰ NAFTA (n 549) Article 1102.

⁷²¹ *ibid* Article 1103.

⁷²² *Pope & Talbot v. Canada* (n 641) para 117.

⁷²³ *ibid* para 115.

⁷²⁴ *ibid* para 117.

⁷²⁵ *ibid*.

⁷²⁶ *Pope & Talbot v. Canada* (n 641) para 9.

⁷²⁷ *ibid* 117.

⁷²⁸ *Saluka v. Czech Republic* (n 84).

⁷²⁹ *ibid*.

⁷³⁰ *ibid*.

⁷³¹ *ibid*.

concluded treaty.⁷³² Unlike the textual method, teleological is an approach in which the disputed terms are interpreted to achieve the treaty's aim. In Morse's view, this interpretative method stresses a particular intention, viz. "the intention of the treaty in question".⁷³³ Schreuer gauges that this approach is particularly popular and leads to interpretations favouring foreign investors.⁷³⁴

Nevertheless, issues, like inconsistent interpretations of the same term, may arise from applying the teleological approach. These conflicts can be seen by comparing the different meanings of FET interpreted in *Enron*⁷³⁵ and *Saluka*.⁷³⁶ The tribunal, in both cases, regarded the treaty preamble as a vital factor in ascertaining FET. The applicable treaty of *Enron* is the Argentina-US BIT (1991),⁷³⁷ while that of *Saluka* is the Czech Republic-Netherlands BIT (1991).⁷³⁸ In the treaty preamble, both BITs express the contracting parties' desire to "promote greater economic cooperation between them".⁷³⁹ Also, treaty parties' recognition of FET as an investment treatment that will "stimulate the flow of private capital and the economic development of the parties" is presented.⁷⁴⁰

However, tribunals arrived at different interpretations of FET even though they considered similar treaty preambles. In *Saluka*,⁷⁴¹ the Czech Republic-Netherlands BIT (1991)⁷⁴² expresses the promotion of foreign investments and the stimulation of economic cooperation between contracting states in the treaty preamble. In the tribunal's view, this wording is "more subtle and balanced", indicating a balanced approach to interpreting the provisions of substantive treatments provided to foreign investors.⁷⁴³ Instead of the sole aim, it regarded the protection of foreign investment as a necessary element to pursue the overall aim of the BIT, which aims to enhance and promote contracting parties' economic cooperation.⁷⁴⁴ It further stressed that the overprotection of foreign investment should be avoided; Otherwise, the host state's willingness to accept foreign capital would be impaired because of the restriction on its regulatory power for the public interest,⁷⁴⁵ leading to the failure to achieve the treaty's overall aim.⁷⁴⁶ In this respect, the tribunal emphasised the significance of "a balanced approach" in treaty interpretation,⁷⁴⁷ although it, in practice, still interpreted FET from the perspective of foreign

⁷³² Dörr & Schmalenbach (n 51) 583.

⁷³³ Morse (n 72) 36, 41.

⁷³⁴ Schreuer, 'Diversity' (n 76) 133.

⁷³⁵ *Enron v. Argentina* (n 5).

⁷³⁶ *Saluka v. Czech Republic* (n 84) para 300.

⁷³⁷ Argentina-US BIT (n 120) Preamble.

⁷³⁸ Czech Republic-Netherlands BIT (n 101) Preamble.

⁷³⁹ Argentina-US BIT (n 120) Preamble. Czech Republic-Netherlands BIT (n 101) Preamble.

⁷⁴⁰ *ibid.*

⁷⁴¹ *Saluka v. Czech Republic* (n 84).

⁷⁴² Czech Republic-Netherlands BIT (n 101) Preamble.

⁷⁴³ *Saluka v. Czech Republic* (n 84) para 300.

⁷⁴⁴ *ibid.*

⁷⁴⁵ *ibid.*

⁷⁴⁶ *ibid.*

⁷⁴⁷ *ibid.*

investors,⁷⁴⁸ which was not a balanced interpretation.

Conversely, the tribunal in *Enron*⁷⁴⁹ ignored the host state's values and solely focused on the promotion and protection of foreign investment. With consideration of the preamble of the Argentina-US BIT (1991),⁷⁵⁰ it stated that a stable legal framework is one of the treaty's aims. In its view, the FET standard is closely linked to that purpose.⁷⁵¹ Then, it decided that a stable framework is one element of FET.⁷⁵²

A similar interpretation of FET can be seen in *MTD*,⁷⁵³ a dispute arising from the state's refusal to approve the zoning changes necessary to carry out the claimants' project. MTD claimed that Chile had breached its FET obligation provided in Article 2(2) of the Chile-Malaysia BIT (1992),⁷⁵⁴ which stipulates that "[i]nvestments of investors of either contracting party shall at all times be accorded to fair and equitable treatment".⁷⁵⁵ In order to find the answer, the tribunal first ascertained the meaning of FET based on the interpretative rules.⁷⁵⁶ As expressed in the preamble, the contracting states desire to stimulate and enhance both parties' economic prosperity and stress the significance of promoting and protecting foreign investment.⁷⁵⁷ In the tribunal's view, the pro-active terms mentioned in the preamble, such as "promote", "stimulate", and "create", implied that the host state should take measures proactively rather than passively to achieve the treaty's aim.⁷⁵⁸ In this regard, it concluded that FET should be understood as the "treatment in an even-handed and just manner, conducive to fostering the promotion of foreign investment".⁷⁵⁹

As reflected in the above interpretations of FET, most tribunals who use the teleological approach interpret the disputed word in favour of foreign investors due to the protection and promotion of foreign investment explicitly stressed in the preamble. Only those who understand the object and purpose of a treaty from the perspectives of both foreign investors and treaty parties stress the importance of a balanced interpretative method. Such a gap reemphasises the need for applying proportionality in interpreting balanced treaty provisions.

3.4.3 The Subjective Approach

The above methods, mainly focusing on the wording of the treaty itself, are objective. In contrast, the

⁷⁴⁸ *ibid* 301.

⁷⁴⁹ *Enron v. Argentina* (n 5).

⁷⁵⁰ Argentina-US BIT (n 120) Preamble.

⁷⁵¹ *Enron v. Argentina* (n 5) para 259.

⁷⁵² *ibid* para 260.

⁷⁵³ *MTD v. Chile* (n 533).

⁷⁵⁴ Chile-Malaysia BIT (signed 11 November 1992, entered into force 4 August 1995).

⁷⁵⁵ *ibid* Article 2 (2).

⁷⁵⁶ *MTD v. Chile* (n 533) para 113.

⁷⁵⁷ Chile-Malaysia BIT (n 754) Preamble.

⁷⁵⁸ *MTD v. Chile* (n 533) para 113.

⁷⁵⁹ *ibid*.

interpretative approach, which focuses on the contracting parties' common intention, is subjective. The object and purpose of the treaty emphasised in the teleological method differ from the contracting parties' common intention stressed in the subjective approach, even though the former is regarded as the authentic expression of the latter. As pointed out by Li, the difference can be observed first in nature: The former is objective while the latter is subjective.⁷⁶⁰ Also, unlike a treaty's aim that can be seen directly from the treaty wording, such as the preamble, the contracting parties' common intention may not be articulated in the treaty.

One may, therefore, question which approach to investigate the contracting parties' common intention should be considered within the process of treaty interpretation raises issues. In Gardiner's view, *travaux préparatoires* of a treaty is the material that interpreters most commonly adopt to ascertain contracting parties' intention,⁷⁶¹ but no detail as to its scope and content has been provided in the rules. In Fauchald's view, such material refers to a broad range of events before the conclusion or enforcement of a treaty.⁷⁶² However, as analysed in 3.3.6, its availability is questioned, affecting the application of subjective approach in practice.

3.4.4 The Systemic Approach

By definition, the term "systemic" stresses the whole of a system rather than part of it.⁷⁶³ In the researcher's view, the systemic approach in the context of international investment law refers to the "system" at two levels, which are figuratively similar to a concentric circle. As presented in Graph 3.1, the inner circle mainly focuses on the IIA in which the disputed term appears. The outer circle refers to the broad circumstance, namely the entire international law. Correspondingly, on the one hand, via the systemic interpretive approach, any ambiguous term should be interpreted based on the consideration of the treaty as a whole. On the other hand, it should be interpreted against the entire international law rather than a particular field of the system, contributing to eliminating the fragmentation of international law.



Graph 3.1

⁷⁶⁰ Li (n 527) 426.

⁷⁶¹ Gardiner (n 49) 373.

⁷⁶² Fauchald (n 59) 349.

⁷⁶³ Fowler & Fowler (n 187) 1085. 'Systemic' (n 523).

As clarified by Fitzmaurice, there are six principles in treaty interpretation, including the principle of integration.⁷⁶⁴ This principle is linked with good faith and emphasises that the disputed term should be interpreted with the context in which it occurs.⁷⁶⁵ This context not only refers to the particular provision or section in which it appears but also stresses the treaty as a whole.⁷⁶⁶ Meanwhile, McLachlan asserts that Article 31 (3) (c) of the Vienna Convention expresses systemic integration, which stresses that the word in question should be interpreted against a broad system, namely the international legal system.⁷⁶⁷ In this respect, the two-tier systemic approach in the current research is a hybrid method.

Based on the earlier discussion in 3.3.3, Dörr and Schmalenbach point out that the systemic interpretation in the broad sense can be brought into treaty interpretation via Article 31 (3) (c) of the Vienna Convention, which emphasises the consideration of "any relevant rules of international law applicable in the relations between the parties".⁷⁶⁸ Due to the absence of qualifying language and the term "any" stipulated, they assert that the source of such applicable rules is implicit as Article 38 (1) of the ICJ Statute.⁷⁶⁹ That is to say, other treaties, international customs, and general principles of law should be taken into account within the process of treaty interpretation. This view is supported by McLachlan, who stresses that a term should be interpreted considering other relevant international instruments.⁷⁷⁰ As further clarified by Dörr and Schmalenbach, different from another two sources, other relevant treaties considered in interpretation should refer to the "similar object" or the "same legal issue" with the treaty in question.⁷⁷¹

Nevertheless, consideration of those sources, in practice, can also result in conflicts. As mentioned in Chapter One, conflicts exist in applying different applicable laws for the ISD. A set of Argentinian cases are the prime example to present the conflicting criteria for invoking necessity due to the consideration of different laws. As will be analysed in Chapter Five, the tribunals in some cases, including *Sempra*,⁷⁷² utilised the requirements of "necessity" stipulated in the Wrongful Act to assess whether Argentina could invoke the necessity based on Article XI of the Argentina-US BIT (1991).⁷⁷³ The *ad hoc* committee in *Sempra* pointed out the tribunal failed to apply the proper law and manifestly exceeded its powers.⁷⁷⁴ More detail as to the application of proportionality in the ISDS will be discussed in-depth

⁷⁶⁴ UN, *Yearbook of the International Law Commission Volume II* (n 580) 55-6, para 12. Other principles are "textuality", "the nature and ordinary meaning", "effectiveness", "subsequent practice", and "contemporaneity".

⁷⁶⁵ *ibid* 56, para 14.

⁷⁶⁶ *ibid*.

⁷⁶⁷ McLachlan (n 524) 279.

⁷⁶⁸ Dörr & Schmalenbach (n 51) 592, 604. Vienna Convention (n 47) Article 31 (3) (c).

⁷⁶⁹ Dörr & Schmalenbach (n 51) 605.

⁷⁷⁰ McLachlan (n 524) 280.

⁷⁷¹ Dörr & Schmalenbach (n 51) 605.

⁷⁷² *Sempra v. Argentina* (n 5).

⁷⁷³ See 5.4.2 in Chapter Five.

⁷⁷⁴ *Sempra v. Argentina*, ICSID Case No. ARB/02/16, Decision on the Argentine Republic's Application for Annulment of the Award, 29 June 2010, paras 160-5.

in Chapter Five.

The systemic approach was applied by the tribunal in *Philip v. Uruguay*⁷⁷⁵ to ascertain the scope and contour of FET. In this case, the ISA was initiated due to the measures taken by Uruguay regarding the packaging of tobacco products. Philip claimed that the host state's act had breached its FET obligation stipulated in the Switzerland-Uruguay BIT (1988),⁷⁷⁶ which prescribes that

Each contracting party shall ensure *fair and equitable treatment* within its territory of the investments of the investors of the other contracting party. This treatment shall not be less favourable than that granted by each contracting party to investments made within its territory by its own investors, or than that granted by each contracting party to the investments made within its territory by investors of the most favoured nation, if this latter treatment is more favourable.⁷⁷⁷ [italic added]

As reflected, the FET standard in this provision is stipulated without any qualifying language. The disputing parties in *Philip* held different views on its scope and content. The claimant regarded FET as an autonomous standard, while the respondent linked it to the minimum standard in customary international law (MST).⁷⁷⁸ Considering the significant interpretative factors emphasised in the Vienna Convention, including the ordinary meaning, the context, and object and purpose of the treaty, the claimants argued that the respondent's understanding of FET could not be deduced from the wording of Article 3 (2).⁷⁷⁹ The tribunal also noted the absence of qualifying language, but it neither supported the claimant's view nor that of the respondent.⁷⁸⁰ Instead, based on Article 31 (3) (c) of the Vienna Convention, which stipulates that "[a]ny relevant rules of international law applicable to the relations between the parties",⁷⁸¹ the tribunal stated that FET should be interpreted by reference to "rules of international law".⁷⁸² Therefore, considering the evolution of customary international law and interpretations of FET in persuasive cases, it concluded that the contour of FET referred to legitimate expectation and the stability of the host state's legal framework.⁷⁸³

To sum up, based on the emphasis on different interpretative elements, a variety of interpretative approaches, like textual and teleological methods, can be used to ascertain the meaning of the disputed word. None of them can be seen as the perfect method to interpret ambiguous treaty provisions. Each approach has its own advantages and disadvantages.⁷⁸⁴ For example, the interpretation provided via the

⁷⁷⁵ *Philip v. Uruguay*, ICSID Case No. ARB/10/7, Award, 8 July 2016.

⁷⁷⁶ Switzerland-Uruguay BIT (signed 07 October 1988, entered into force 22 April 1991).

⁷⁷⁷ *ibid* Article 3 (2).

⁷⁷⁸ *Philip v. Uruguay* (n 775) para 312.

⁷⁷⁹ *ibid* para 313.

⁷⁸⁰ *ibid* para 316.

⁷⁸¹ Vienna Convention (n 47) Article 31 (3) (c).

⁷⁸² *Philip v. Uruguay* (n 775) para 317.

⁷⁸³ *ibid* para 317-24.

⁷⁸⁴ Klabbers (n 519) 56-7.

teleological approach plays a role in achieving the object and purpose of a treaty, but it may be interpreted as one-sided protection in favour of foreign investors, skewing the investor-state relationship towards foreign investors. Similarly, these methods do have degrees of interactivity with each other. On the one hand, the considerations in different approaches overlap. For example, the treaty preamble is of both textual and teleological importance.⁷⁸⁵ On the other hand, as stressed by Waldock, no interpretative method is exclusively the correct approach to treaty interpretation.⁷⁸⁶

Therefore, it is the researcher's view that the interpretation of treaty provisions is a process of weighing and balancing different interpretative elements by proportionality *stricto sensu* based on the values of the purpose which each factor pursues to make a balanced interpretation on a case-by-case basis. Compared with other interpretative approaches, the systemic method is the appropriate one that can bring proportionality into the ISDS regime and balance the conflicting values of foreign investors and the host state at the stage of treaty interpretation. Through this approach, the disputed word is not interpreted merely based on the definitions provided by the dictionary. Instead, it is interpreted in the actual circumstance in which it appears, aiding its correct placement in the interpretation of each treaty. This is proved by the later analysis of FET in Chapter Four,⁷⁸⁷ which will present that the scope and components of FET vary from one treaty to another due to the differences in the context in which it appears.

Also, unlike teleological and subjective methods, which express the preference for one disputing party's value, the two-tier systemic approach results in a relatively balanced treaty interpretation. In this approach, the treaty, even the international law itself, is regarded as a whole, and both investment and non-investment values are considered to interpret an ambiguous treaty provision. In the "inner circle", IIA, if non-investment values are mentioned or stipulated in the treaty, then they should be considered when interpreting the questioned term, like FET. If not, according to the "outer circle", the entire international law and non-investment values emphasised in other relevant international instruments should be weighed within the process of treaty interpretation. Consequently, a balanced interpretation is made based on contemplating and evaluating investment and non-investment values, reflecting the application of proportionality in treaty interpretation. Based on this interpretation, proportionality can be brought into the ISDS regime to settle the ISD. Also, such a balanced interpretation guarantees the consistency of a state's international obligations in different fields.

3.5 Issues Arising from Treaty Interpretation

The above analyses present the role of the principles of interpretation stipulated in the Vienna

⁷⁸⁵ Dörr & Schmalenbach (n 51) 583.

⁷⁸⁶ UN, *Yearbook of the International Law Commission Volume II* (n 580) 54 para 7.

⁷⁸⁷ See generally in Chapter Four.

Convention in treaty interpretation. As evaluated by Wälde:

They are also open-ended and fluid enough to allow the various approaches practised to claim their spiritual home in Articles 31-3 of the Vienna Convention, thus using, as always, ambiguity to create the appearance of consensus, while allowing a variety of flowers to grow in the same garden.⁷⁸⁸

However, in Raz's view, the practical guide is absent.⁷⁸⁹ On the contrary, as reflected in practice, interpretative issues are always there: From the imbalanced interpretative power between contracting parties and tribunals to the inconsistent interpretations of the same word.

3.5.1 The Imbalanced Interpretative Power between States and Tribunals

As mentioned in 3.2, treaty parties and tribunals share the joint responsibility to interpret the disputed word in the ISDS.⁷⁹⁰ With regard to the ideal state of their cooperation, Zhang suggests that states express their consensus on the term during the negotiation and signature of a treaty, while tribunals interpret controversial provisions when they settle the dispute.⁷⁹¹

Nevertheless, doubts over a balance between both interpreters have been raised in practice.⁷⁹² One reason for that is the tribunal's qualms and ignorance of the state's interpretation, while another is their failure to follow interpretative rules strictly. Roberts puts that an imbalance would emerge "if either body dictates to, or ignores, the other".⁷⁹³ As noted by Zhang, treaty interpretations provided by contracting parties have always been ignored and even denied in practice.⁷⁹⁴ The host state's dual role in the ISDS leads to the question of the credibility of its interpretation.⁷⁹⁵ Moreover, based on the empirical analysis of a variety of cases, Fauchald discovered that instead of contracting parties' subsequent agreement or practice, the material most frequently considered by tribunals is the persuasive precedent.⁷⁹⁶ Such an imbalance, in the researcher's view, may be settled by explicit expression provided by the parties to the treaty: The more clarified provisions, the less discretion enjoyed by tribunals.

3.5.2 The Inconsistent Interpretations of the Same Term

Another issue in treaty interpretation is that interpreters fail to follow the interpretative rules consistently. As a result, various interpretations of the same generic term emerge even in cases with the same applicable treaty and factual background, which can be seen in practice. Based on the later discussion

⁷⁸⁸ Wälde (n 518).

⁷⁸⁹ Joseph Raz, *Between Authority and Interpretation: On the Theory of Law and Practical Reason* (OUP 2009) 322.

⁷⁹⁰ Text to 3.2. UNCTAD (n 59) 3.

⁷⁹¹ Zhang, 'Guo Ji Tou Zi' (n 563) 169.

⁷⁹² Zhang (n 55) 35.

⁷⁹³ Roberts (n 550) 225.

⁷⁹⁴ Zhang (n 55) 35.

⁷⁹⁵ Zhang, 'Guo Ji Tou Zi' (n 563) 170.

⁷⁹⁶ Fauchald (n 59) 333, 335, 356-7.

in Chapter Five, in which a set of cases arising from Argentina's economic crisis will be compared, tribunals' failure to follow the interpretative rules provided in the Vienna Convention led to different, even opposite, interpretations of the same term.⁷⁹⁷

Similarly, the tribunal in *Pope & Talbot*⁷⁹⁸ ignored the wording of Article 1105 of the NAFTA, which stipulates that "[e]ach party shall accord to investments of investors of another party treatment in accordance with international law, *including* fair and equitable treatment".⁷⁹⁹ The tribunal compared the provision of FET in the NAFTA with that in Model BIT (1987), which prescribes that "[i]nvestment shall at all times be accorded fair and equitable treatment, shall enjoy full protection and security and shall *in no case be accorded treatment less than* that required by international law".⁸⁰⁰ It is evident that two treaty provisions are different, one is "including", whereas another is "no less than". However, the tribunal reached the same conclusion on the relationship between FET and the requirement of international law without any consideration of the literal differences.⁸⁰¹ It interpreted FET as an additive element to the requirements of international law. In other words, in its view, the treatments enjoyed by foreign investors based on Article 1105 were international minimum standard "plus" FET. Consequently, the FET standard provided in the NAFTA was interpreted as additive treatment provided by international law,⁸⁰² inadvertently expanding the understanding of FET and unbalancing the investor-state relationship.

In Sornarajah's view, the broad interpretation of FET provided by the tribunal in *Pope & Talbot* was "a bold attempt" to expand its contour.⁸⁰³ As he emphasises, such a broad FET standard that allows tribunals to create new elements based on the particular situation may threaten to states' regulatory power in the public interest,⁸⁰⁴ worsening the imbalance between the values of foreign investors and the host state.

3.6 Conclusion

In the context of international investment, treaty parties and tribunals have the shared power to interpret treaty provisions. In a perfect state, their interpretative cooperation maintains a balanced investor-state relationship from the perspective of treaty interpretation and the ISDS. Moreover, according to the two-tier systemic approach, the treaty itself is regarded as a whole, and the disputed word is also interpreted against the entire international law. Consequently, proportionality can be brought into the ISDS to strike

⁷⁹⁷ See generally in Chapter Five. Argentinian cases (n 5).

⁷⁹⁸ *Pope & Talbot v. Canada* (n 641).

⁷⁹⁹ NAFTA (n 549) Article 1105 [italic added].

⁸⁰⁰ See from *Pope & Talbot v. Canada* (n 641) para 111 [italic added].

⁸⁰¹ *ibid* paras 110-5.

⁸⁰² *ibid*.

⁸⁰³ M Sornarajah, *The International Law on Foreign Investment* (5th edn, CUP 2021) 442.

⁸⁰⁴ *ibid*.

a balance between the conflicting values of foreign investors and the host state, including their legitimate expectations of the state's stable legal framework.

Nevertheless, in practice, various issues arise from treaty interpretation. One is the imbalanced interpretative power of treaty parties and tribunals. In practice, the former's interpretations may be ignored by the latter, who relies on persuasive precedents.⁸⁰⁵ They also fail to comply with the interpretative rules provided in the Vienna Convention when interpreting treaty provisions. From the aspect of interpretations, although there is no hierarchy between different interpretative factors, the lack of a balance between them may lead to an interpretation in favour of one party.⁸⁰⁶ Also, due to the absence of a clear relationship among various interpretation approaches, interpreters may apply them randomly to interpret treaty provisions, leading to inconsistent interpretation of the same term. Therefore, in order to strike a balance in the investor-state relationship at the stage of treaty interpretation, the application of proportionality is needed to settle these unbalanced issues.

Concerning the imbalanced interpretative power of states and tribunals, as shall be discussed in Chapter Five, treaty parties can explicitly stipulate the limitations in the treaty to restrict tribunals' discretionary power. For instance, by adding the term "it", contracting states clarify that only the host state is the decision-maker in relevant situations.⁸⁰⁷ Moreover, in practice, proportionality as a tool can be applied to balance both interpreters' power on a case-by-case basis. As a result, there is a neutral or balanced interpretation of the disputed term, contributing to a balanced investor-state relationship.

Meanwhile, during the process of interpreting treaties, interpreters should interpret treaty provisions in accordance with the rules of the Vienna Convention. All interpretative elements should be considered and balanced when interpreting treaty provisions. The social importance of each desired purpose pursued by the text should be balanced based on proportionality *stricto sensu*, contributing to a balanced interpretation. Also, the internal logical order of these interpretative factors cannot be disregarded. As emphasised by the ICJ, "[i]f the relevant words in their natural and ordinary meaning make sense in their context, that is an end of the matter".⁸⁰⁸ The ordinary meaning of the term in question is the starting point of treaty interpretations. Other factors, such as the context and the treaty's purpose, should be considered from the immediate to the distant and from the intrinsic to the extraneous to confirm or ascertain the clear meaning of the questioned word.

Based on the emphasis on different interpretive factors, complementary approaches can be used to

⁸⁰⁵ Zhang (n 55) 129-30.

⁸⁰⁶ *ibid* 43-5.

⁸⁰⁷ See 5.3.1 in Chapter Five.

⁸⁰⁸ 'Competence' (n 60) 582. Gardiner (n 49) 222.

interpret treaties. Like their textual basis, these interpretative methods, including textual, systemic, teleological, and subjective approaches, have the same value in treaty interpretation. Although considering the intrinsic logic of treaty interpretation, the first choice for interpreters to interpret the questioned term should be the textual approach;⁸⁰⁹ With the two-tier systemic approach assisting to maintain a balanced interpretation. In the systemic method, not only investment but also non-investment values are considered within the process of interpreting ambiguous provisions, indicating the application of proportionality. The fragmentation between different fields of international law can also be eliminated. In other words, as examined in this chapter, proportionality and treaty interpretation interact with each other to establish a balanced investor-state relationship. Such a relationship will also be tested in the following chapters, which will explore the conflicting legitimate expectations of foreign investors and the host state and the approach to balance such conflicts,⁸¹⁰ respectively.

⁸⁰⁹ Fauchald (n 59) 316-7.

⁸¹⁰ See in Chapters Four and Five.

Chapter 4

Fair and Equitable Treatment, Legitimate Expectations, and Proportionality

4.1 Introduction

Based on the aforementioned analysis, proportionality could be a valuable tool to balance conflicting values.⁸¹¹ Its contribution in the context of international investment can be seen from both treaty interpretation and application perspectives. As presented in Chapter Three, proportionality interconnects with treaty interpretation.⁸¹² The former can be brought into the ISDS regime via the two-tier systemic interpretative approach, while the application of proportionality can contribute to a balanced treaty interpretation. This chapter seeks to test proportionality analysis in interpreting ambiguous clauses.

Due to its frequent use in restricting the host state's right to regulate in the public interest,⁸¹³ FET is the proper standard applied to examine the application of proportionality in the ISDS. Meanwhile, finding a clear meaning of FET is the precondition for ascertaining whether the host state has breached such a treaty obligation *vis-à-vis* foreign investors. This segues to the discussion on proportionality analysis in balancing the conflicts between the legitimate expectations of foreign investors and the host state in the following chapters.

To build foreign investors' confidence in its investment environment and attract their capital, the host state provides various treatments in IIAs. FET is the most frequently invoked standard in IIAs and practice.⁸¹⁴ Also, it is the most popular standard used by tribunals to decide in favour of foreign investors.⁸¹⁵ According to the data from the UNCTAD, in 595 out of 697 ISDs, the host state was challenged by foreign investors as a violation of its FET obligation; Meanwhile, investors' claims that the host state had violated its FET obligation were supported by tribunals in 168 out of 256 cases.⁸¹⁶ However, such investment protections, to a certain extent, may restrict the host state's regulatory power and even threaten its sovereignty. One issue arising from FET's popularity, for instance, is "the potential for striking an inadequate balance between the private and public interests affected by the administrative or governmental decision under scrutiny".⁸¹⁷

As put by Sornarajah, "all treaties constrain sovereignty",⁸¹⁸ but states do not lose all power. Wälde also emphasised that IIAs can interfere in states' domestic regulatory and administrative sovereignty, but

⁸¹¹ See generally in Chapter Two.

⁸¹² See generally in Chapter Three.

⁸¹³ Wälde, 'Investment' (n 83) 206. UNCTAD, *Issues in International Investment Agreement II* (n 79) 10.

⁸¹⁴ UNCTAD, *Issues in International Investment Agreement II* (n 79) xiii, 1.

⁸¹⁵ *supra* note 83.

⁸¹⁶ *supra* note 81.

⁸¹⁷ UNCTAD, *Issues in International Investment Agreement II* (n 79) 10.

⁸¹⁸ Sornarajah, *The International Law on Foreign Investment* (n 88) 272-3.

such interventions should be appropriate.⁸¹⁹ However, the extent to which they are appropriate is questioned. In Sornarajah's view, the term "equity" indicates that both foreign investors' conduct and that of the host state should be taken into consideration in making the final decision.⁸²⁰ In other words, a balance needs to be struck between the conflicting values of both parties, including their legitimate expectations of the state's stable legal framework.⁸²¹ Within the process of decision-making, tribunals should consider whether foreign investors are at fault or whether the reactions of the host state are to blame.

Similar issues arise in practice. Most IIAs heavily regulate the host state's obligations and foreign investors' rights. The China-Kazakhstan BIT (1992),⁸²² for instance, provides treatments without duties to foreign investors. From the investors' perspective, they enjoy a degree of protection of their investments. By contrast, from the host state's perspective, those standards set a low threshold of its liability and restrict its ability to wield regulatory power in the public interest. Consequently, host states, especially developing countries, face a dilemma: Taking administrative or legislative measures to react to very fluid domestic circumstances may leave them open to allegations by foreign investors that they have violated treaty obligations.⁸²³ The prime example here is a set of Argentinian ISDs arising from its economic crisis of 2001/2.⁸²⁴ Different measures were taken by the Argentine Government in response to its economic crisis, but such means were claimed as violations of its treaty obligations by foreign investors, including FET.⁸²⁵

Meanwhile, due to tribunals' overly broad interpretation, there is the caption of unequal treatment: The protection of foreign investors' legitimate expectations often overrides the host state's legitimate regulatory power.⁸²⁶ Therefore, a clear boundary needs to be drawn between the state's misconduct and its actions and reactions, which do, in fact, pursue legitimate purposes.⁸²⁷ The latter cannot be regarded as breaches of treaty obligations even if they impair foreign investors' values.⁸²⁸ In such a situation, a balance between the private rights of foreign investors and the public interest in the host state has drawn attention. Applying proportionality, a principle rooted in domestic legal systems, in the context of international law to strike such a balance is a challenge.

To expand the examination of the application of proportionality in both treaty interpretation and

⁸¹⁹ Wälde (n 83) 210.

⁸²⁰ Sornarajah, *The International Law on Foreign Investment* (n 88) 555.

⁸²¹ UNCTAD, *Issues in International Investment Agreement II* (n 79) 77. Wälde (n 83) 210.

⁸²² China-Kazakhstan BIT (signed 10 August 1992, entered into force 13 August 1994).

⁸²³ UNCTAD, *Issues in International Investment Agreement II* (n 79) 2.

⁸²⁴ Argentinian cases (n 5).

⁸²⁵ See generally in Chapter Five. Argentinian cases (n 5).

⁸²⁶ UNCTAD, *Issues in International Investment Agreement II* (n 79) 11, 67.

⁸²⁷ *ibid* 3, 15.

⁸²⁸ *ibid*.

application, this chapter will first ascertain the nature and contour of FET, one of the most frequently invoked standards in IIAs and practice. In 4.2, this standard will be examined according to the interpretative rules and the systemic approach analysed in Chapter Three.⁸²⁹ Even if no provision of FET occurs in IIAs, in practice, foreign investors may still allege that the host state has violated such a treaty obligation. This is related to the nature of FET: If it is an international custom, it has a binding force on all states. 4.3 will investigate whether the FET standard fulfils the requirements stipulated in Article 38 (1) of the ICJ Statute, followed by a discussion on its constituent elements in 4.4.

Although there is no ironclad universal definition of FET, its generic scope can be depicted based on practice. As concluded by Gallagher and Shan, this standard refers to "transparency, good faith, fair, legitimate expectations, and stability and predictability of legal and business framework".⁸³⁰ Sornarajah puts that, unlike other elements,⁸³¹ the protection of legitimate expectations is new and essential.⁸³² Apart from that, the notion of proportionality, to a certain extent, falls within the scope of FET.⁸³³ Proportionality, in some cases, is also applied to ascertain whether the host state has failed to protect investors' legitimate expectations. The protection of legitimate expectations and proportionality will be analysed in-depth in 4.4. The legitimate expectations of foreign investors and those of the host state will also briefly be reflected in this chapter. How proportionality should be applied to balance each disputing party's conflicting values in the ISDS will be explored in the following chapters.

4.2 History and Meaning of Fair and Equitable Treatment

4.2.1 The History of Fair and Equitable Treatment

The wording "equitable treatment" first appeared in Article 23 (e) of the Covenant of the League of Nations, requiring the member states "to secure and maintain freedom of communications and of transit and *equitable treatment for the commerce* of all Members of the League".⁸³⁴ Almost 30 years later, a similar wording, "just and equitable treatment", was used in the Havana Charter for an International Trade Organisation (1948),⁸³⁵ acknowledged by scholars as the first trade document containing FET.⁸³⁶ As stipulated in Article 11.2,

⁸²⁹ See 3.4 in Chapter Three.

⁸³⁰ Shan & Gallagher (n 9) 143 [in Chinese].

⁸³¹ UNCTAD, *Issues in International Investment Agreement II* (n 79) 12, 53, 58, 80.

⁸³² Sornarajah, *The International Law on Foreign Investment* (n 88) 417.

⁸³³ Schill, 'Fair and Equitable Treatment' (n 115) 22-3.

⁸³⁴ The Covenant of the League of Nations (signed 28 June 1919, expired 31 July 1947) Article 23(e) [italic added]. Theodore Kill, 'Don't Cross the Streams: Past and Present Overstatement of Customary International Law in Connection with Conventional Fair and Equitable Treatment Obligations' (2008) 106 MLR 853.

⁸³⁵ Havana Charter for an International Trade Organisation (1948).

⁸³⁶ Patrick Dumberry, 'Fair and Equitable Treatment: Its Interaction with the Minimum Standard and Its Customary Status' (2017) 1 International Investment Law & Arbitration 1. Kill (n 834) 853. J. Roman Picherack, 'The Expanding Scope of the Fair and Equitable Treatment Standard: Have Recent Tribunals Gone Too Far?' (2008) 9 The Journal of World Investment & Trade 255.

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- (a) Make *recommendations* for and promote bilateral or multilateral agreements on measures designed.
- (i) To assure *just and equitable treatment* for the enterprises, skills, capital, arts and technology brought from one Member country to another;⁸³⁷ [italic added]

The soft treaty language, like "recommendations", indicates only a suggestion instead of a binding obligation on the host state *vis-à-vis* foreign investors.⁸³⁸ In the same year, the concept of "equitable treatment" was brought in Article 22 of the Economic Agreement of Bogota, prescribing that "[f]oreign capital shall receive *equitable treatment*".⁸³⁹ As it further explains, "[t]he states agree not to take *unjustified, unreasonable or discriminatory measures* that would impair the legally acquired rights or interests of nationals of other countries in the enterprises, capital, skills, arts or technology they have supplied".⁸⁴⁰ Compared with the Havana Charter, this does clarify the fundamental elements of FET as justifiability, reasonability, and non-discrimination. However, both agreements failed to enter into force due to the lack of support.⁸⁴¹

The significance of FET, particularly in the context of international investment, has been emphasised in two draft documents: the Draft Convention on Investments Abroad (also called Abs-Shawcross Draft Convention) and the Draft Convention on the Protection of Foreign Property (OECD Draft Convention).⁸⁴² Both favour the capital-exporting states and stress that "[e]ach Party shall at all times ensure *fair and equitable treatment* to the property of the nationals of other Parties".⁸⁴³ "At all times" is a vital phrase, as, unless otherwise specified, foreign investors can enjoy FET protection during the entire period of their investments in the host state.⁸⁴⁴ The OECD Draft has significantly influenced the development of subsequent BITs even though it was never opened for signature.⁸⁴⁵ The member states of the OECD regard it as a framework for their agreements on protecting foreign property.⁸⁴⁶

4.2.2 The Ordinary Meaning of Fair and Equitable Treatment

The popularity of FET can be proved by the data collected from the UNCTAD. Almost 95 per cent of the available IIAs (2574 in total) refer to the wording "fair and equitable treatment" or its equivalent

⁸³⁷ Havana Charter (n 835) Article 11.2 (a) (i).

⁸³⁸ UNCTAD, *Issues in International Investment Agreements* (n 95) 25.

⁸³⁹ Economic Agreement of Bogota Article 22 [italic added].

⁸⁴⁰ *ibid* [italic added].

⁸⁴¹ Dumberry, 'Fair and Equitable Treatment' (n 836) 1. UNCTAD, *Issues in International Investment Agreements* (n 95) 7. OECD, *International Investment Law-A Changing Landscape A Companion Volume to International Investment Perspectives* (2005) 76.

⁸⁴² UNCTAD, *Issues in International Investment Agreements* (n 95) 4.

⁸⁴³ Draft Convention on Investment Abroad (Abs-Shawcross Draft Convention) Article 1 [italic added]. See also Draft Convention on the Protection of Foreign Property Article 1 [italic added].

⁸⁴⁴ UNCTAD, *Issues in International Investment Agreements* (n 95) 45.

⁸⁴⁵ OECD, 'Fair and Equitable Treatment' (n 94) 5. UNCTAD, *Issues in International Investment Agreements* (n 95) 8.

⁸⁴⁶ Tudor (n 87) 19.

terms, such as "equitable treatment".⁸⁴⁷ As noted by Tudor, since 1961, many countries, including China, have gradually adopted the FET clause in their BITs to promote and protect international investment.⁸⁴⁸ For example, the China-Kuwait BIT (1985)⁸⁴⁹ prescribes FET in the rubric of "promotion and protection of investments" like that "[e]ach contracting state shall at all times ensure fair and equitable treatment to the investments and returns of investors of the other contracting states".⁸⁵⁰ In the China-Egypt BIT (1994),⁸⁵¹ FET is linked with MFN in Article 3, emphasising that FET "shall not be less favourable than that accorded to investments and activities associated with such investments of investors of a third state".⁸⁵²

Nevertheless, there are heated debates over the precise meaning of FET on account of its ambiguous wording. Various FET clauses are provided in IIAs with details neither on its scope nor components, implying the necessity and significance of treaty interpretation. As stressed by the OECD,

Because of the difference in its formulation, *the proper interpretation of the 'fair and equitable treatment' standard depends on the specific wording of the particular treaty, its context, the object and purposes of the treaty, as well as on negotiating history or other indications of the parties' intent.*⁸⁵³ [italic added]

Based on the research in Chapter Three, the ordinary meaning of the disputed term is the starting point of its interpretation.⁸⁵⁴ Thus, the ascertainment of FET starts from its plain meaning. By definition, the term "fair" means "just", "even-handed", "unbiased", "legitimate", and "in accordance with rules",⁸⁵⁵ while "equitable" means "fair" and "just".⁸⁵⁶ However, these meanings are subjective, failing to provide a universal definition of FET. Other interpretative elements, such as "the context", then should be considered to find FET's definite meaning.⁸⁵⁷

4.2.3 The Context of Fair and Equitable Treatment

As discussed in Chapter Three, treaty interpretations are affected by the particular treaty language.⁸⁵⁸ This view is confirmed by the UNCTAD, who clarified that even though the same FET standard is

⁸⁴⁷ *supra* note 80.

⁸⁴⁸ Tudor (n 87) 2.

⁸⁴⁹ China-Kuwait BIT (signed 23 November 1985, entered into force 24 December 1986).

⁸⁵⁰ *ibid* Article 2(2).

⁸⁵¹ China-Egypt BIT (signed 21 April 1994, entered into force 1 April 1996).

⁸⁵² *ibid* Article 3.

⁸⁵³ OECD, 'Fair and Equitable Treatment' (n 94) 40.

⁸⁵⁴ See 3.3.2 in Chapter Three.

⁸⁵⁵ J. B. Sykes (ed), *The Concise Oxford Dictionary of Current English* (7th edn, Oxford at the Clarendon Press 1982) 347. *MTD v. Chile* (n 533) para 113. UNCTAD, *Issues in International Investment Agreement II* (n 79) 7. *Azurix v. Argentina*, ICSID Case No. ARB/01/12, Award, 14 July 2006, para 329.

⁸⁵⁶ Sykes (n 855) 326. *MTD v. Chile* (n 533), para 113. *Azurix v. Argentina* (n 855) para 329.

⁸⁵⁷ See generally in Chapter Three.

⁸⁵⁸ See generally in Chapter Three.

prescribed in IIAs, its interpretations are different due to the differences in treaty provisions.⁸⁵⁹ As presented in Table 4.1, the context in which FET appears varies from one treaty to another. Correspondingly, the understandings of such a standard differ from the hortatory approach to the unqualified and qualified FET.⁸⁶⁰ The hortatory approach describes a situation in which FET is provided in the treaty preamble, implying it as a non-binding obligation on the host state *vis-à-vis* foreign investors. By contrast, both the unqualified and qualified FET do have binding force on the contracting parties to a treaty. The former prescribes the standard without limitations, while the latter qualified further details to define it.

Table 4.1 Different Formulations of FET

Formulations of FET	A Typical BIT
The Hortatory Approach	<u>The Finland-Slovenia BIT (1998) Preamble</u> Desiring to intensify economic cooperation to the mutual benefit of both countries and to maintain <i>fair and equitable conditions</i> for investments by investors of one Contracting Party in the territory of the other Contracting Party. ⁸⁶¹
The Unqualified FET	<u>The Australia-China BIT (1988) Article 3</u> A Contracting Party shall at all times ensure <i>fair and equitable treatment</i> in its own territory to investments and activities associated with such investments. ⁸⁶²
The Qualified FET	<u>The China-Colombia BIT (2008) Article 2</u> 3. Each Party shall accord <i>fair and equitable treatment</i> in accordance with <i>customary international law</i> ... 4. For greater certainty, a) The concept of " <i>fair and equitable treatment</i> "...do not require additional treatment to that required under <i>the minimum standard of treatment of aliens in accordance with the standard of customary international law</i> c) " <i>Fair and equitable treatment</i> " includes the prohibition against denial of justice in criminal, civil, or administrative proceedings in accordance with the general accepted principles of customary international law. ⁸⁶³

4.2.3.1 Fair and Equitable Treatment in the Hortatory Approach

Due to the treaty preamble falling short of imposing binding obligations on the signatories,⁸⁶⁴ FET

⁸⁵⁹ UNCTAD, *Issues in International Investment Agreement II* (n 79) 17.

⁸⁶⁰ UNCTAD, *Issues in International Investment Agreements* (n 95) 18. UNCTAD, *Key Issues Volume I* (n 96) 216. UNCTAD, *Issues in International Investment Agreement II* (n 79) 17-8.

⁸⁶¹ Finland-Slovenia BIT (signed on 01 June 1998, entered into force 03 June 2000, terminated 22 October 2021) Preamble [italic added].

⁸⁶² Australia-China BIT (signed on 11 July 1988, entered into force 11 July 1988) Article III [italic added].

⁸⁶³ China-Colombia BIT (n 124) Article 2 [italic added].

⁸⁶⁴ UNCTAD, *Issues in International Investment Agreement II* (n 79) 112. UNCTAD, *Issues in International Investment Agreements* (n 95) 59.

prescribed in the preamble is only a suggestion rather than an obligation on the host state.⁸⁶⁵ For instance, the Finland-Slovenia BIT (1998)⁸⁶⁶ mentioned this standard in the preamble, expressing the contracting parties' desire to maintain "*fair and equitable* conditions" for foreign investments.⁸⁶⁷ Both parties affirmed the importance of "fairness" and "equitability" in international investment⁸⁶⁸ but refrained from accepting it as a treaty duty.⁸⁶⁹

Conversely, as noted by Gallagher and Shan, if the FET standard is stipulated under the substantive provisions, such as "treatment of investment"⁸⁷⁰ or "promotion and protection of treatment",⁸⁷¹ it becomes a concrete obligation on the host state.⁸⁷² On the basis of the differences in specific treaty provisions, this standard can be divided into the unqualified and qualified FET.⁸⁷³

4.2.3.2 The Unqualified Fair and Equitable Treatment

The UNCTAD found that the FET clause stipulated in most IIAs, such as the Australia-China BIT (1988),⁸⁷⁴ solely requires the contracting parties to "ensure *fair and equitable treatment* in its own territory to investments and activities associated with such investments".⁸⁷⁵ The simple wording "fair and equitable treatment" reflect an unqualified standard.⁸⁷⁶ As a result, tribunals are left with the latitude to make an interpretive determination on whether the host state has breached its FET obligation on a case-by-case basis.⁸⁷⁷

Due to the lack of detail, the interpretations of unqualified FET provided by tribunals, compared with that of qualified FET, which will be discussed later in 4.2.3.3, are broad and favour foreign investors.⁸⁷⁸ Based on the comparison with qualified FET, foreign investors may enjoy the maximum protection provided by unqualified FET, whereas the host state may face a low threshold of liability, leading to high risks if found in breach of its FET obligation *vis-à-vis* foreign investors.⁸⁷⁹ As explained by the

⁸⁶⁵ UNCTAD, *Key Issues Volume I* (n 96) 216. See an example Havana Charter (n 835) Article 11.2 (a) (i), which reads that '[t]he Organisation may, in such collaboration with other inter-governmental organisations as may be appropriate: (a) make recommendations for and promote bilateral or multilateral agreements on measures designed (i) to assure just and equitable treatment for the enterprise, skills, capital, arts and technology brought from one Member country to another'.

⁸⁶⁶ Finland-Slovenia BIT (n 861)

⁸⁶⁷ *ibid* Preamble [italic added].

⁸⁶⁸ *ibid*.

⁸⁶⁹ UNCTAD, *Key Issues Volume I* (n 96) 216.

⁸⁷⁰ China-Netherlands BIT (signed 26 November 2001, entered into force 1 August 2004) Article 3.

⁸⁷¹ China-New Zealand BIT (signed 22 November 1988, entered into force 25 March 1989) Article 3.

⁸⁷² Norah Gallagher & Wenhua Shan, *Chinese Investment Treaties Policies and Practice* (OUP 2009) 127.

⁸⁷³ UNCTAD, *Issues in International Investment Agreements* (n 99) 18. UNCTAD, *Issues in International Investment Agreement II* (n 79) 17-8.

⁸⁷⁴ Australia-China BIT (n 862).

⁸⁷⁵ See an example Australia-China BIT (n 862) Article III [italic added]. UNCTAD, *Issues in International Investment Agreement II* (n 79) 17.

⁸⁷⁶ UNCTAD, *Issues in International Investment Agreement II* (n 79) 17.

⁸⁷⁷ UNCTAD, *Issues in International Investment Agreements* (n 95) 60.

⁸⁷⁸ UNCTAD, *Issues in International Investment Agreement II* (n 79) 22.

⁸⁷⁹ UNCTAD, *Investment Policy Framework for Sustainable Development* (2012) 51. UNCTAD, *Issues in International*

UNCTAD, the reasons for such differences include the lack of defined meaning of FET and the subjective characteristics referred to within the process of treaty interpretation.⁸⁸⁰ The previous analysis in 4.2.2 highlighted the ambiguous meaning of "fair" and "equitable".⁸⁸¹ Both concepts are also inherently subjective, which may lead to disputing parties' different, even opposite, understandings of the same FET clause.⁸⁸² Consequently, a problematic issue arises: Foreign investors may regard the host state's measures as a breach of FET, even though such protections have been provided from the state's perspective.⁸⁸³

Such different understandings of FET between the disputing parties can be seen in *Saluka v. Czech Republic*,⁸⁸⁴ in which the Czech Republic-Netherlands BIT (1991)⁸⁸⁵ required each contracting party to "ensure *fair and equitable treatment* to the investments of investors of the other contracting party".⁸⁸⁶ The disputing parties had divergences on whether FET is an autonomous treaty standard or a customary standard. As alleged by the claimant, FET is a treaty standard that should be interpreted broadly due to the lack of qualifying language.⁸⁸⁷ In this situation, the host state has a relatively lower threshold of its liability; Even minor inappropriate conduct might be perceived to violate the FET obligation. However, the respondent argued that such a standard was linked to the MST, which set a relatively higher threshold of its liability.⁸⁸⁸ As to these conflicting opinions on FET, the tribunal pronounced that it is an unqualified standard due to the absence of reference linked with it in Article 3 of the BIT.⁸⁸⁹

Moreover, some IIAs not only prescribe the unqualified FET but also adapt it by reference to other standards, such as NT and MFN. These conditions do not change the nature of FET as to unqualified or qualified. As expressed in Table 4.2, "NT" means that the host state treats the foreign investor, at least, as it treats nationals.⁸⁹⁰ Similarly, "MFN" requires the host state to treat one foreign investor at least as favourable as it treats others from a third country.⁸⁹¹ Lim notes that the notion of non-discrimination is inherently included in both treatments, especially MFN.⁸⁹²

Investment Agreement II (n 79) 22.

⁸⁸⁰ *ibid.*

⁸⁸¹ Text to 4.2.1.

⁸⁸² UNCTAD, *Issues in International Investment Agreements* (n 95) 10. UNCTAD, *Investment Policy* (n 879) 51.

⁸⁸³ UNCTAD, *Key Issues Volume I* (n 96) 212. UNCTAD, *Issues in International Investment Agreement II* (n 79) 22. Rudolf Dolzer & Vaughan Lowe, 'Fair and Equitable Treatment in International Law' (2006) 100 *Proceedings of the Annual Meeting (American Society of International Law)* 69. Rudolf Dolzer & Christoph Schreuer, *Principles of International Investment Law* (OUP 2008) 126.

⁸⁸⁴ *Saluka v. Czech Republic* (n 84).

⁸⁸⁵ Czech Republic-Netherlands BIT (n 101).

⁸⁸⁶ *ibid* Article 3 [*italic added*].

⁸⁸⁷ *Saluka v. Czech Republic* (n 84) paras 286-8.

⁸⁸⁸ *ibid* paras 289-90.

⁸⁸⁹ *ibid* para 294.

⁸⁹⁰ C. L. Lim, Jean Ho & Martins Paporinskis, *International Investment Law and Arbitration* (2nd edn, CUP 2021) 369.

⁸⁹¹ UNCTAD, *Most-Favoured-Nation Treatment UNCTAD Series on Issues in International Investment Agreements II* (2010) 13. Dolzer & Schreuer, *Principles* (n 113) 206, 211. Alejandro Faya Rodriguez, 'The Most-Favoured-Nation Clause in International Investment Agreements: A Tool for Treaty Shopping?' (2008) 25 *Journal of International Arbitration* 89.

⁸⁹² Lim, Ho & Paporinskis (n 890) 384. UNCTAD, *Most-Favoured-Nation Treatment* (n 891) 1, 14.

Table 4.2 The Modified Unqualified FET

The Modified Unqualified FET	A Typical BIT
National Treatment (NT)	<u>The China-Latvia BIT (2004) Article 3</u> 1. Investments of investors of each Contracting Party shall all the time be accorded <i>fair and equitable treatment</i> in the territory of the other Contracting Party. 2. Without prejudice to its laws and regulations, each Contracting Party shall accord to investments and activities with such investments by the investors of the other Contracting Party to treatment <i>not less favourable than</i> that accorded to the investments and associated activities by <i>its own investors</i> . ⁸⁹³
Most-Favoured-Nation Treatment (MFN)	<u>The China-Philippine BIT (1992) Article 3</u> 1. Investments and activities associated with such investments of investors of either Contracting Party shall be accorded <i>equitable treatment</i> ... 2. The treatment and protection referred to in paragraph 1 of this Article <i>shall not be less favourable than</i> that accorded to investments and activities associated with such investments of investors of <i>a third State</i> . ⁸⁹⁴

As put by Dolzer and Schreuer, "claimants have the right to benefit from substantive guarantees included in third treaties via the MFN clause in their basic BITs".⁸⁹⁵ As one of the substantive treatments provided in IIAs, FET can be imported by foreign investors from other treaties through the MFN clause in the basic treaty.

That approach was examined in practice in the case of *Rumeli & Telsim v. Kazakhstan*.⁸⁹⁶ In this case, due to the expulsive scheme carried out by the respondent, foreign investors alleged that it had violated the Kazakhstan-Turkey BIT (1992)⁸⁹⁷ and Kazakhstan's Foreign Investments Law. They argued that the respondent had failed to provide sufficient FET protection, even though no FET clause was included in the treaty.⁸⁹⁸ As they stressed, the "[r]espondent's obligation to provide "fair and equitable treatment" is imposed not only by customary international law but also by virtue of the MFN clause of the BIT".⁸⁹⁹ In other words, they were awarded the FET protection based on the provision of MFN in the same treaty.⁹⁰⁰ Such a statement was supported by the respondent, who agreed that "the duty of fair and equitable treatment was owed to claimants under the most favoured nation clause of the Turkey–Kazakhstan BIT in conjunction with the UK–Kazakhstan BIT".⁹⁰¹

⁸⁹³ China-Latvia BIT (signed 5 April 2004, entered into force 1 February 2006) Article 3 [italic added].

⁸⁹⁴ China-Philippine BIT (signed 20 July 1992, entered into force 8 September 1995) Article 3 [italic added].

⁸⁹⁵ Dolzer & Schreuer, *Principles* (n 883) 190-1.

⁸⁹⁶ *Rumeli & Telsim v. Kazakhstan*, ICSID Case No. ARB/05/16, Award, 29 July 2008.

⁸⁹⁷ Kazakhstan-Turkey BIT (signed 1 May 1992, entered into force 10 August 1995).

⁸⁹⁸ *ibid* Article II.

⁸⁹⁹ *Rumeli & Telsim v. Kazakhstan* (n 896) para 581.

⁹⁰⁰ Kazakhstan-Turkey BIT (n 897).

⁹⁰¹ *Rumeli & Telsim v. Kazakhstan* (n 896) para 591.

Furthermore, Vasciannie contends that the popularity of FET among states is a result of the growing network of BITs merged via the MFN standard.⁹⁰² However, one may question whether such a general application of FET accords with states' intention. A BIT is the result of negotiations between the contracting parties and reflects their common intention. The UNCTAD clarified that the absence of the FET clause from a treaty might indicate that both parties are reluctant to accept it as a treaty obligation or intend to avoid high risks of allegations of the breach of FET.⁹⁰³ Under both conditions, states hold negative attitudes toward providing FET protection. In this respect, if foreign investors can still enjoy such investment protection through the MFN clause, that would be contrary to what is intended by the contracting parties. Moreover, there may be another potential risk. Foreign investors may import a more favourable FET protection via the MFN clause if permitted, especially compared with the unqualified standard in the earlier IIAs, the qualified FET in current treaties is stipulated with limitations.⁹⁰⁴ Consequently, the imbalance between the conflicting values of foreign investors and the host state may deteriorate further.

4.2.3.3 The Qualified Fair and Equitable Treatment

Conversely, other IIAs describe FET with more detail, namely the qualified FET. As presented in Table 4.3, FET can be linked with international law, the MST under customary international law, and a list of substantive factors.

Table 4.3 The Qualified FET

The Qualified FET	A Typical BIT
Linked with Other Standards	<ul style="list-style-type: none"> ·International Law <u>The Kazakhstan-US BIT (1992) Article 2</u> (a) Investment shall at all times be accorded <i>fair and equitable treatment...shall in no case be accorded treatment less than that required by international law.</i>⁹⁰⁵ ·Minimum Standard Treatment <u>The Canada-China BIT (2012) Article 4</u> 2. The concepts of "fair and equitable "... <i>do not</i> require treatment <i>in addition to or beyond</i> that which is required by <i>the international law minimum standard of treatment of aliens as evidenced by general State practice accepted as law.</i>⁹⁰⁶
Listing Substantive Elements	<u>The China-Colombia BIT (2008) Article 2</u> 4. For greater certainty... "Fair and Equitable Treatment" <i>includes the prohibition against denial of justice in</i>

⁹⁰² Stephen Vasciannie, 'The Fair and Equitable Treatment Standard in International Investment Law and Practice' (1999) 70 British Yearbook of International Law 99.

⁹⁰³ UNCTAD, *Issues in International Investment Agreement II* (n 79) 20.

⁹⁰⁴ *ibid* 114.

⁹⁰⁵ Kazakhstan-US BIT (signed 19 May 1992, entered into force 12 January 1994) Article 2 (a) [italic added].

⁹⁰⁶ Canada-China BIT (n 421) [italic added].

	<i>criminal, civil, or administrative proceedings</i> in accordance with the general accepted principles of customary international law. ⁹⁰⁷
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Unlike the unqualified FET, the phrases from "no less" to "not beyond" and from "include" to "require", draw the boundaries of the qualified FET. As noted by Gallagher and Shan, these limitations contribute to the defined meaning of FET that appears in the same rule.⁹⁰⁸ For example, as reflected in the wording "no less favourable" under Article 2 (a) of the Kazakhstan-US BIT (1992),⁹⁰⁹ the requirement of international law was set as the "floor" of the FET standard. This requires that the protection of foreign investors provided by FET should go beyond, or at least equal to, that afforded by international law; Otherwise, the host state would violate its FET obligation to foreign investors.⁹¹⁰

The tribunal in *Azurix v. Argentina* had a similar perspective.⁹¹¹ In this case, Azurix participated in the privatisation of water service in Argentina and was granted a 30-year concession for the distribution of potable water and relevant service. Due to the Province's omissions or actions, such as the denial of the valuation methodology of tariffs, Azurix initiated a claim against Argentina and alleged that the state had breached its FET obligation stipulated in the Argentina-US BIT (1991).⁹¹² As provided in the treaty, "[i]nvestment shall at all times be accorded *fair and equitable treatment* ... shall in *no case* be accorded treatment *less than that required by international law*".⁹¹³

With consideration of the ordinary meaning of FET and the object and purpose of the BIT, especially the positive words mentioned in the preamble, like "promote" and "stimulate", the tribunal asserted that this standard should be understood as a treatment which was "conducive to fostering the promotion of foreign investment".⁹¹⁴ It also pointed out that the FET protection provided to foreign investors would not be less than that required by international law, regardless of its essential elements.⁹¹⁵ As it further clarified, the last sentence of Article II (2) (a) aimed to "*set a floor, not a ceiling*, in order to avoid a possible interpretation of these standards below what is required by international law".⁹¹⁶ Consequently, the protections enjoyed by foreign investors should be broader than those required by international law; Meanwhile, the liability threshold may also be higher compared with that of the unqualified FET. In order to establish the state's breach of FET, foreign investors must prove that the alleged measures have been lower than the requirements of international law.

⁹⁰⁷ China-Colombia BIT (n 124) Article 2 [italic added].

⁹⁰⁸ Gallagher & Shan (n 872) 133.

⁹⁰⁹ Kazakhstan-US BIT (n 905) Article 2 (a).

⁹¹⁰ UNCTAD, *Issues in International Investment Agreement II* (n 79) 23.

⁹¹¹ *Azurix v. Argentina* (n 855).

⁹¹² Argentina-US BIT (n 120).

⁹¹³ *ibid* Article 2(a) [italic added].

⁹¹⁴ *Azurix v. Argentina* (n 855) paras 360-1.

⁹¹⁵ *ibid* para 361.

⁹¹⁶ *ibid* [italic added].

Instead of a floor, a ceiling for FET is also provided in IIAs, such as the Canada-China BIT (2012).⁹¹⁷ Table 4.3 presents that FET is linked to the MST under customary international law through the wording "not beyond".⁹¹⁸ As indicated, the former falls into the latter's scope.⁹¹⁹ Such a relationship can also be implied by the term "include". A prime example here is the NAFTA,⁹²⁰ which stipulates that "[e]ach Party shall accord to investments of investors of another Party treatment in accordance with *international law, including fair and equitable treatment* and full protection and security" in Article 1105 (1).⁹²¹ A relationship is described by the word "include": FET is part of international law.

Those terms and phrases act as the boundaries for the scope of FET, but they fail to draw a definite picture of its components. Consequently, tribunals interpret its fundamental elements on a case-by-case basis, leading to inconsistent interpretations. However, to ensure certainty, some contracting parties explicitly express their consensus on the components of FET in relevant treaties.⁹²² A typical example is the Comprehensive Economic and Trade Agreement (CETA), which clarifies the FET standard by providing an explicit list.⁹²³ As stipulated:

2. A Party breaches the obligation of *fair and equitable treatment* referenced in paragraph 1 if a measure or series of measures constitutes:

(a) *denial of justice* in criminal, civil or administrative proceedings;

(b) *fundamental breach of due process*, including a fundamental breach of transparency, in judicial and administrative proceedings;

(c) *manifest arbitrariness*;

(d) *targeted discrimination on manifestly wrongful grounds*, such as gender, race or religious belief;

(e) *abusive treatment of investors*, such as coercion, duress and harassment; or

(f) a breach of any further elements of the fair and equitable treatment obligation adopted by the Parties in accordance with paragraph 3 of this Article.

3. The Parties shall regularly, or upon request of a Party, *review the content of the obligation to provide fair and equitable treatment*. The Committee on Service and Investment, established under Article 26.2.1(b) (Specialised Committee), may develop *recommendations* in this regard and submit them to the CETA Joint Committee for decision.

4. When applying the above fair and equitable treatment obligation, the tribunal may take into account whether a Party made a *specific representation* to an investor to induce a covered investment, that created a *legitimate expectation*, and upon which the investor *relied in deciding to make or maintain the covered investment*, but that the party subsequently *frustrated*.⁹²⁴ [italic added]

⁹¹⁷ Canada-China BIT (n 421).

⁹¹⁸ *ibid* Article 4.

⁹¹⁹ UNCTAD, *Issues in International Investment Agreement II* (n 79) 28.

⁹²⁰ NAFTA (n 549).

⁹²¹ *ibid* 1105 (1) [italic added].

⁹²² Ruman Islam, *The Fair and Equitable Treatment (FET) Standard in International Investment Arbitration* (Springer 2018) 65.

⁹²³ CETA (n 545).

⁹²⁴ *ibid* Article 8.10.

This provision explicitly expresses that the FET protection refers to the prohibition of denial of justice, due process, non-arbitrary conduct and non-abusive treatment.⁹²⁵ The adjectives used to describe the state's misconduct, such as "fundamental" and "manifest", convey that only very serious misconducts can be deemed violations of FET.⁹²⁶ Moreover, according to paragraph 3, a specialised committee, namely the Committee on Services and Investment, is authorised to review and make suggestions on the contour of FET. A certain amount of flexibility is left to that committee to add more elements to the list. Even though what it made are merely suggestions, the potential expansion of that list implies the iterative nature of FET. Furthermore, reading paragraph 2 in conjunction with paragraph 4 reveals a way that can be utilised by tribunals to assess whether the host state has breached the legitimate expectations of foreign investors. The clearer the FET clause, the more specific its constituent elements, and the less risk there is of finding a breach.⁹²⁷

Nevertheless, heated debates over the nature of the list provided in Article 8. 10 of the CETA has arisen from the absence of terms "include" and "require".⁹²⁸ Based on the UNCTAD's findings, these two words have different meanings and functions.⁹²⁹ By definition, "include" means "comprise or embrace as part of a whole".⁹³⁰ As implied by its ordinary meaning, FET includes but is not limited to the elements mentioned in the list. In contrast, "requires" reflects an exhaustive list of FET's elements.⁹³¹ However, the UNCTAD does not explain why the term "require" implies an exhaustive list.⁹³² Based on its plain meaning as "lay down as imperative",⁹³³ one may still question why such a term indicates an exhaustive list, even though that is a common understanding in practice. For example, the ASEAN Comprehensive Investment Agreement (2009) explicitly defines FET as the prohibition of denial of justice by prescribing that it "*requires* each member state not to deny justice in any legal or administrative proceedings in accordance with the principle of due process".⁹³⁴

Concerning the list provided in the CETA, although there are no terms to express its nature, various adjectives signal the degree of the inappropriateness of the host state's actions that could break FET. Meanwhile, the committee's potential recommendations reflect the room left to tribunals to exercise discretion. In this regard, it implicitly provides that FET does not merely contain the listed elements.

⁹²⁵ *ibid.*

⁹²⁶ UNCTAD, *Issues in International Investment Agreement II* (n 79) 110.

⁹²⁷ *ibid* xvii, 29.

⁹²⁸ Günes Ününvar, 'The Vague Meaning of Fair and Equitable Treatment Principle in Investment Arbitration and New Generation Clarifications' (2016) iCourts Working Paper Series No. 55, 19 <file:///Users/cc/Downloads/SSRN-id2774078.pdf> last accessed 27 June 2022.

⁹²⁹ UNCTAD, *Issues in International Investment Agreement II* (n 79) 30.

⁹³⁰ Sykes (n 855) 506.

⁹³¹ UNCTAD, *Issues in International Investment Agreement II* (n 79) 30.

⁹³² *ibid.*

⁹³³ Sykes (n 855) 884.

⁹³⁴ ASEAN Comprehensive Investment Agreement (done 26 February 2009) [italic added]. UNCTAD, *Issues in International Investment Agreement II* (n 79) 30.

However, compared with the unqualified FET, that list still restricts the host states' duty to adapt to the changing domestic needs.⁹³⁵ In the researcher's view, this formulation of FET is definite and flexible, implying a balance struck between the deference to the host state and tribunal's discretion, expressing the application of proportionality in weighing the conflicting interpretative powers.

4.2.4 The Object and Purpose of the Treaty

Like the context, the object and purpose of the treaty also contribute to the interpretation of FET. As discussed in Chapter Three, the starting point of ascertaining a treaty's purpose is the preamble,⁹³⁶ frequently mentioned when finding FET's fundamental elements.

In *Saluka*,⁹³⁷ the tribunal pointed out that the aims expressed in the treaty preamble refer to the promotion and protection of foreign investment and the enhancement of contracting parties' economic cooperation.⁹³⁸ In this respect, based on the disputing parties' values, the disputed treaty provision should be interpreted in a balanced approach to addressing the conflicts between their rights.⁹³⁹ However, the tribunal emphasised that the interpretation of FET should, at least, not deter foreign investors from investing.⁹⁴⁰ Its interpretation of FET was still viewed as protection favouring foreign investors because it interpreted this standard from the standpoint of foreign investors and considered it closely linked to their expectations.⁹⁴¹ This case re-emphasises that the interpretation of the questioned word in the teleological approach is always produced in favour of foreign investors.⁹⁴²

To recap, based on the previous discussions in Chapter Three, following the intrinsic logic of treaty interpretation, the first step is to ascertain the ordinary meaning of the term in question.⁹⁴³ However, the plain meanings of "fair" and "equitable" defined in the dictionary remain ambiguous and subjective, unhelpful in finding its precise definition. In this situation, other relevant elements, as stipulated in the Vienna Convention,⁹⁴⁴ including the rest of the wording in the same provision, other clauses in the same treaty, and the object and purpose of the treaty, should be considered from the immediate to the distant to ascertain the precise meaning of FET.

Nevertheless, the nature of FET is not straightforward, and its precise components remain unclear. Whether this standard falls into the category of international custom in the sense of Article 38 (1) (b) of

⁹³⁵ Ününvar (n 928) 22.

⁹³⁶ See 3.3.4 in Chapter Three. Gardiner (n 49) 217.

⁹³⁷ *Saluka v. Czech Republic* (n 84).

⁹³⁸ *ibid* para 300.

⁹³⁹ *ibid* 301.

⁹⁴⁰ *ibid*.

⁹⁴¹ *ibid* paras 301-2.

⁹⁴² Zhang (n 55) 44.

⁹⁴³ See 3.4 in Chapter Three.

⁹⁴⁴ Vienna Convention (n 47).

the ICJ Statute or is synonymous with the MST under customary international law is still in question.⁹⁴⁵ If the answer is positive, even with no FET clause stipulated in IIAs, foreign investors can obtain the protection provided by this standard because it is an international custom which can be universally applied. Additionally, the existing constituent elements of the MST can contribute to discerning FET's components.

4.3 The Nature of Fair and Equitable Treatment

The FET standard without limitations, in Mann's view, is an autonomous standard. As he further clarified,

The terms 'fair and equitable treatment' envisage conduct which goes far beyond the minimum standard and affords protection to a greater extent and according to a much more objective standard than any previously employed form of words. A tribunal would not be concerned with a minimum, maximum or average standard. *It will have to decide whether in all the circumstances the conduct in issue is fair and equitable or unfair and inequitable.* No standard defined by other words is likely to be material. *The terms are to be understood and applied independently and autonomously.*⁹⁴⁶ [italic added]

However, his view is rejected by others. Tudor points out that FET is an international custom due to its popularity in international investment.⁹⁴⁷ Sornarajah steps further and regards FET as a synonym of the MST under customary international law.⁹⁴⁸ As discussed in Chapter Two, based on Article 38 (1) (b) of the ICJ Statute, the rule in question must fulfil two requirements, being the "general practice" and "accepted as law", simultaneously, be an international custom.⁹⁴⁹ There should be broad and representative state practice of FET.⁹⁵⁰ Meanwhile, that protection should be provided by states out of a sense of legal obligation.⁹⁵¹

4.3.1 Inconsistent and Non-Uniform Application of Fair and Equitable Treatment

As evaluated by Tudor, "the FET standard became a customary norm of its time: quick in its formation and based the overwhelming number of states, which in the majority contains a FET clause".⁹⁵² This view is solidly confirmed by the data from the UNCTAD, which indicates that over 95 per cent of all IIAs contain a provision of FET.⁹⁵³ Meanwhile, among 697 available ISDs, 595 cases referred to the alleged breach of FET based on different applicable legal instruments.⁹⁵⁴ The tribunals in 168 out of

⁹⁴⁵ UNCTAD, *Issues in International Investment Agreements* (n 95) 10.

⁹⁴⁶ F. A. Mann, 'British Treaties for the Promotion and Protection of Investments' (1982) 52 *British Yearbook of International Law* 241.

⁹⁴⁷ Tudor (n 87) 85.

⁹⁴⁸ Sornarajah, *The International Law on Foreign Investment* (n 88). Cremades & Cairns (n 88). Mayeda (n 88).

⁹⁴⁹ ICJ Statute (n 19) Article 38 (1) (b). See 2.3.1 in Chapter Two.

⁹⁵⁰ UNCTAD, *Issues in International Investment Agreement II* (n 79) 105.

⁹⁵¹ *ibid.*

⁹⁵² Tudor (n 87) 85.

⁹⁵³ *supra* note 80.

⁹⁵⁴ *ibid.*

256 disputes found that the host state had violated its FET obligation *vis-à-vis* foreign investors.⁹⁵⁵ As proved, FET is an essential and common standard in IIAs and is widely applied in practice.

However, it should be noted that, in recent years, the provision of FET has been removed from certain states' IIAs.⁹⁵⁶ For example, instead of including a FET clause, the Indian Model BIT (2015),⁹⁵⁷ a pre-drafted boilerplate for India's future BITs, has explicitly clarified what measures taken by the host state can violate customary international law.⁹⁵⁸ Similarly, the Canada Model BIT (2021),⁹⁵⁹ a pre-drafted boilerplate for Canada's future BITs, stipulates various substantive treatments without FET.⁹⁶⁰ At the same time, as shall be discussed later, an increasing number of BITs, including the recent Chinese BITs, stipulate FET in more detail.⁹⁶¹ Such absences of or changes in FET clauses under IIAs, to a certain extent, raise doubts over its general application.

Being viewed as an international custom is not simply due to its frequent inclusion in IIAs. The consistency and uniformity of utilising the rule in question also play a significant role in transforming an international custom.⁹⁶² Dumberry emphasises that the prerequisite, namely the states' representative, uniform and consistent practice, should be fulfilled first.⁹⁶³ However, this does not appear to be the case. No consensus has been reached on the meaning of FET.⁹⁶⁴ Due to its inherent subjectivity, the understanding of this standard varies from one party to another. Consequently, the meaning of FET interpreted by the host state may be rejected by foreign investors and their home state.⁹⁶⁵ That divergence may be more evident if those countries have different cultural backgrounds and legal systems.⁹⁶⁶

The FET clause varies from one treaty to another, reflecting states' various intentions on this standard.⁹⁶⁷ In this respect, even the formal uniformity of FET fails to materialise. As argued by Tudor, such discrepancies merely reflect different levels of treatment provided by FET without differences in its

⁹⁵⁵ *ibid.*

⁹⁵⁶ Sornarajah, *The International Law* (n 803) 444.

⁹⁵⁷ The Indian Model BIT (2015)

⁹⁵⁸ *ibid* Article 3. Grant Hanessian & Kabir Duggal, 'The Final 2015 Indian Model BIT: Is This the Change the World Wishes to See?' *ICSID Review*, 32 (2017) 216, 220.

⁹⁵⁹ The Canada Model BIT (2021).

⁹⁶⁰ *ibid.* 'Canada Publishes 2021 Model Foreign Investment Promotion and Protection Agreement' (*IISD*, 24 June 2021) <<https://www.iisd.org/itn/en/2021/06/24/canada-publishes-2021-model-foreign-investment-promotion-and-protection-agreement/>> last accessed 27 June 2022.

⁹⁶¹ Sornarajah, *The International Law* (n 803) 444.

⁹⁶² See 2.3.1.1 in Chapter Two.

⁹⁶³ Dumberry, 'Has' (n 89).

⁹⁶⁴ UNCTAD, *Key Issues Volume I* (n 96) 212. Gallagher & Shan (n 872) 111.

⁹⁶⁵ Herman Walker Jr. 'Modern Treaties of Friendship, Commerce and Navigation' (1958) *Minnesota Law Review* 805, 812. UNCTAD, *Key Issues Volume I* (n 96) 212. Gallagher & Shan (n 872) 111.

⁹⁶⁶ *ibid.*

⁹⁶⁷ UNCTAD, *Issues in International Investment Agreement II* (n 79) 17-8. UNCTAD, *Issues in International Investment Agreements* (n 95) 22.

constituent elements.⁹⁶⁸ However, as mentioned in Chapter Three, the term itself is the initial basis for determining the contracting parties' common intention.⁹⁶⁹ To add to the confusion, the question of whether FET is an autonomous standard or synonymous with the MST under customary international law remains open-ended.⁹⁷⁰

Therefore, one may doubt whether FET in IIAs consists of the same elements. Such an issue can be observed in practice.⁹⁷¹ In light of the guidance on treaty interpretation and the absence of the doctrine of precedent in international investment, tribunals should interpret FET on a case-by-case basis.⁹⁷² Due to the differences in interpretative considerations, such as various formulations of FET and negotiating histories of signed treaties, it is almost impossible to prove a consensus on FET's scope and contour.⁹⁷³ In some BITs, FET merely refers to the prohibition of denial of justice.⁹⁷⁴ Conversely, others provide FET with a broad remit, including a stable business and legal framework,⁹⁷⁵ the legitimate expectations of foreign investors⁹⁷⁶ and transparency.⁹⁷⁷ Based on those differences, it cannot be concluded that the FET protection provided to foreign investors is consistent and uniform state practice. Thus, it fails to achieve the "general practice" required to be an international custom.

4.3.2 The Doubts on Fair and Equitable Treatment as a Legal Obligation

Apart from "state practice", the rule in question should also fulfil the "*opinio juris*" requirement, which expresses that such an obligation should be "accepted as law".⁹⁷⁸ The host state should treat foreign investors fairly and equitably out of "a sense of legal obligation".⁹⁷⁹ However, FET fails to meet this requirement.⁹⁸⁰ As noted by Vasciannie, most states provide no FET standard in their domestic legal systems.⁹⁸¹ Although the lack of the term "fair and equitable treatment" does not mean its absence in the domestic legal system,⁹⁸² that result, to a certain extent, implies the state's reluctance to accept it as a legal obligation.

⁹⁶⁸ Tudor (n 87) 77.

⁹⁶⁹ See 3.3.2 in Chapter Three.

⁹⁷⁰ UNCTAD, *Issues in International Investment Agreements* (n 95) 10-3.

⁹⁷¹ Dumberry, 'Has' (n 89).

⁹⁷² UNCTAD, *Issues in International Investment Agreement II* (n 89) 12.

⁹⁷³ *ibid.*

⁹⁷⁴ See an example ASEAN Comprehensive Investment Agreement (n 934).

⁹⁷⁵ Ecuador-US BIT (signed on 27 August 1993, entered into force 11 May 1997, terminated 18 May 2018) Preamble.

⁹⁷⁶ CETA (n 545) Article 8.10.

⁹⁷⁷ *ibid.*

⁹⁷⁸ ICJ Statute (n 19) 38 (1) (b). See 2.3.1.2 in Chapter Two.

⁹⁷⁹ UN (n 23) 138. ICJ Statute (n 19) Article 38 (1) (b). Dumberry, *The Formation* (n 23) 31, 128. ILC, 'Second Report on Identification of Customary International Law' (n 267) 8. Dumberry, 'Has' (n 89) 175.

⁹⁸⁰ Dumberry, 'Has' (n 89) 175-6. Spencer Zifcak, 'The Responsibility to Protect' in Malcolm D Evans (eds), *International Law* (4th edn, OUP 2014) 529.

⁹⁸¹ Vasciannie (n 902) 160.

⁹⁸² Dumberry, 'Has' (n 89) 176.

Moreover, based on the earlier discussion on the nature of proportionality,⁹⁸³ no necessary connection exists between the repeated treaty provisions and the formation of an international custom.⁹⁸⁴ This also works in the identification of the nature of FET. The repetition of FET clauses may reflect that such a standard is not an international custom that can be universally applied.⁹⁸⁵ Instead, its stipulation in IIAs is the result of contracting parties' negotiations.⁹⁸⁶ As demonstrated in practice, allegations of breached FET are always based on the investment protection expressly stipulated in IIAs. In other words, those states still regard FET as a treaty-based duty. Consequently, FET itself fails to transform into a rule of customary international law.

Alternatively, FET may indirectly become an international custom if it is synonymous with the MST under customary international law. Suppose FET equals the MST; In this situation, FET will become an obligation under customary international law because the MST is an international custom. However, problematic issues arise. From the perspective of treaty interpretation, based on the rules of interpretation, the term interpreted should contribute fully to the achievement of the treaty's object and purpose.⁹⁸⁷ If FET and the MST are the same treatments, it becomes redundant to stipulate both provisions, which is the opposite of the effective interpretation deriving from the principle of good faith.⁹⁸⁸ Dolzer and Schreuer argue that using different terms to express the same intention in IIAs is illogical.⁹⁸⁹ States should explicitly disclose their intentions in treaties if, in their view, FET and the MST are entirely one thing.⁹⁹⁰ A similar opinion is held by Gallagher and Wen, who state that the MST cannot be used to interpret FET unless there is an explicit expression.⁹⁹¹

Furthermore, whether the consensus on such an equivalent relationship has been reached among states is in doubt. As clarified by Dumberry, the emergency of FET is because of the continuous disagreements on the MST between developed and developing states.⁹⁹² If the former is interchangeable with the latter, then the stipulation of FET becomes meaningless. This lack of consensus is also supported by UNCTAD, which reveals that mainly the traditional capital-exporting states hold the view that FET equals the MST under customary international law.⁹⁹³

⁹⁸³ See generally in Chapter Two.

⁹⁸⁴ Todd Weiler, *The Interpretation of International Investment Law: Equality, Discrimination and Minimum Standards of Treatment in Historical Context* (Martinus Nijhoff 2013) 236. Dumberry, 'Has' (n 89) 157.

⁹⁸⁵ UN (n 23) 146.

⁹⁸⁶ *ibid.*

⁹⁸⁷ See 3.3.4 in Chapter Three.

⁹⁸⁸ The effective interpretation can see 3.3.1 in Chapter Three.

⁹⁸⁹ Dolzer & Schreuer, *Principles* (n 883) 124. UNCTAD, *Issues in International Investment Agreement II* (n 79) 13. Vasciannie (n 902) 99.

⁹⁹⁰ UNCTAD, *Key Issues Volume I* (n 96) 213.

⁹⁹¹ Gallagher & Shan (n 872) 111. UNCTAD, *Issues in International Investment Agreement II* (n 79) 13. *Saluka v. Czech Republic* (n 84) 294.

⁹⁹² Dumberry, 'Has' (n 89) 176.

⁹⁹³ UNCTAD, *Issues in International Investment Agreements* (n 95) 38-40.

Even though such an equivalent relationship does exist, it also raises problems. Based on this relationship, FET can be more easily interpreted by reference to the elements of the MST under customary international law.⁹⁹⁴ However, the latter's precise components are unclear, and it also requires interpretation. Sornarajah estimates that the MST is "highly indeterminate, lacks a clearly defined content and requires interpretation" and constantly developing.⁹⁹⁵ In this regard, one may doubt whether and to what extent the MST can assist in defining and interpreting FET.

Based on the above analyses, FET is not an international custom through direct or indirect transformation. Foreign investors can merely obtain the FET protection based on relevant treaty provisions. Therefore, proportionality is applied on a case-by-case basis to balance the conflicts between foreign investors' values provided by FET and the host state's right to regulate in the public interest. As discussed, the researcher will later suggest relevant recommendations for the changes in Chinese BITs, incorporating the nature of FET and applying proportionality to strike a balance in the investor-state relationship.⁹⁹⁶

4.4 Constituent Elements of Fair and Equitable Treatment

The provision of FET varies from one treaty to another, affecting its precise meaning and constituent elements.⁹⁹⁷ As pointed out by Sornarajah, no defined components of FET can be used to examine whether a host state has failed to fulfil such a treaty obligation.⁹⁹⁸ However, in Schefer's view, the generic shape of FET can be depicted based on the awards of available cases.⁹⁹⁹ Consistent with tribunals' interpretations, the host state would be in breach of FET where there is arbitrary conduct, denial of justice, failure to guarantee due process, lack of transparency, bad faith, and the violation of foreign investors' legitimate expectations.¹⁰⁰⁰ In addition, Dozler asserts that consistency, the prohibition of harassment or discriminatory measures and the stability of legal and business framework are also contained in the scope of FET.¹⁰⁰¹

Moreover, the UNCTAD published a document and clarified FET's essential elements, including

⁹⁹⁴ *ibid* 12.

⁹⁹⁵ UNCTAD, *Issues in International Investment Agreement II* (n 79) 28, 44. M. Sornarajah, 'The Fair and Equitable Standard of Treatment: Whose Fairness? Whose Equity?' in Federico Ortino and others (eds), *Investment Treaty Law: Current Issues II* (BIICL 2007) 167. M. Sornarajah, *The International Law on Foreign Investment* (2nd edn, CUP 2004) 328. *Waste v. Mexico (II)*, ICSID No. ARB(AF)/00/3, Award, 30 April 2004, para 92.

⁹⁹⁶ See generally in Chapters Six and Eight.

⁹⁹⁷ Cremades & Cairns (n 88) 340.

⁹⁹⁸ Sornarajah, *The International Law on Foreign Investment* (n 88) 412.

⁹⁹⁹ Krista Nadakavukaren Schefer, *International Investment Law Text, Cases and Materials* (2nd edn, EE 2016) 377, 379.

¹⁰⁰⁰ *ibid* 379.

¹⁰⁰¹ Rudolf Dolzer, 'Fair and Equitable Treatment: Today's Contours' (2014) 12 Santa Clara Journal of International Law 7. Schill, 'Fair and Equitable Treatment' (n 115) 11-23.

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- (a) *Prohibition of manifest arbitrariness in decision-making*, that is, measures taken purely on the basis of prejudice or bias without a legitimate purpose or rational explanation;
 - (b) *Prohibition of the denial of justice* and disregard of the fundamental principles of *due process*;
 - (c) *Prohibition of targeted discrimination on manifestly wrongful grounds*, such as gender, race or religious belief;
 - (d) *Prohibition of abusive treatment* of investors, including coercion, duress and harassment;
 - (e) *Protection of the legitimate expectations of investors* arising from a government's specific representations or investment-including measures, although *balanced with the host State's right to regulate in the public interest*.¹⁰⁰² [*italic added*]

That is to say, the host state will breach its FET obligation if its conduct amounts to the denial of justice, discrimination, abusive treatment, arbitrariness, and the violation of legitimate expectations.¹⁰⁰³ Schill points out that proportionality is also an element of FET.¹⁰⁰⁴ Although proportionality is still a new factor of FET, it contributes to re-balance the conflicting values between foreign investors and the host state.¹⁰⁰⁵ The prime example is the Argentinian cases, which will be discussed in Chapter Five.¹⁰⁰⁶ In Sornarajah's view, the notion of legitimate expectations has been deemed the "dominant element" of FET, even though it is relatively new,¹⁰⁰⁷ compared with other components of this standard. The significance of legitimate expectation has also been confirmed in practice. As evaluated, "[i]t has become clear that the basic touchstone of fair and equitable treatment is to be found in the legitimate and reasonable expectations of the parties, which derive from the obligation of good faith".¹⁰⁰⁸ These two essential elements, proportionality and legitimate expectations, are also interconnected with each other. Based on the earlier discussion in Chapter Two, proportionality, as a structured and flexible tool, can be applied to weigh and balance the conflicting legitimate expectations of foreign investors and the host state.

4.4.1 Proportionality

Apart from being a flexible tool to strike a balance in the investor-state relationship through three consecutive tests, proportionality is also regarded as an essential element of FET. As stressed by Yannaca-Small, when determining whether the host state has violated its FET obligation, tribunals should weigh its implemented measures against "other legally relevant interests", which include "the state's sovereign right to pass legislation and to adopt decisions for the protection of its public interest, especially if they do not provoke a *disproportionate* impact on foreign investors".¹⁰⁰⁹ This describes a

¹⁰⁰² UNCTAD, *Issues in International Investment Agreement II* (n 79) xvi.

¹⁰⁰³ *ibid* 12, 53, 58, 80.

¹⁰⁰⁴ Schill, 'Fair and Equitable Treatment' (n 115) 22-3.

¹⁰⁰⁵ *ibid* 23.

¹⁰⁰⁶ See generally in Chapter Five.

¹⁰⁰⁷ Sornarajah, *The International Law on Foreign Investment* (n 88) 417. Sornarajah, *The International Law* (n 803) 445. Trevor Zeyl, 'Charting the Wrong Course: The Doctrine of Legitimate Expectations in Investment Treaty Law' (2011) *Arbitration Law Review* 207.

¹⁰⁰⁸ *El Paso v. Argentina* (n 5) para 339.

¹⁰⁰⁹ Katia Yannaca-Small, 'Fair and Equitable Treatment Have Its Contours Fully Evolved?' in Katia Yannaca-Small (ed),

process of balancing different values, and the term "disproportionate" emphasises the requirement of proportionality.

Similarly, the tribunal in *Saluka*¹⁰¹⁰ asserted that one essential and necessary part of deciding whether the host state has violated its FET obligation is "a weighing of the claimant's legitimate and reasonable expectations on the one hand and the respondent's legitimate regulatory interests on the other".¹⁰¹¹ As reflected in this case, both parties' legitimate expectations should be considered, expressing the process of weighing and balancing different values, which corresponds to proportionality *stricto sensu*,¹⁰¹² one essential element of proportionality focusing on the real balance between conflicting values. In other words, proportionality is a vital element that should be considered to ascertain whether the host state has breached its FET obligation *vis-à-vis* foreign investors.

Proportionality, as an essential element of FET, can also be seen in practice.¹⁰¹³ The tribunal in *Occidental v. Ecuador* observed that proportionality as part of FET had been referred to in several cases,¹⁰¹⁴ including *MTD v. Chile*.¹⁰¹⁵ In *MTD*,¹⁰¹⁶ FET was defined as "a broad and widely-accepted standard" which includes a variety of essential elements, such as "good faith, due process, non-discrimination, and proportionality".¹⁰¹⁷ However, there was no further discussion on this definition.

Moreover, in *Total v. Argentina*,¹⁰¹⁸ a case arising from the Argentinian economic crisis of 2001/2, the tribunal emphasised that both the host state's duty in exercising regulatory power for the public interest and foreign investors' legitimate expectations should be considered.¹⁰¹⁹ It further stressed that the fairness of the disputed measure should be evaluated not only according to the result but also based on the reason for its adoption.¹⁰²⁰ Whether such actions are proportionate to the pursued purpose was found to be one of such considerations.¹⁰²¹ In this case, proportionality, as an essential element of FET, was also considered to ascertain whether foreign investors' legitimate expectations, another factor that falls into the category of FET, had been breached by the disputed measures.

Arbitration under International Investment Agreements a Guide to the Key Issues (2nd edn, OUP 2018) 510-1.

¹⁰¹⁰ *Saluka v. Czech Republic* (n 84).

¹⁰¹¹ *ibid* para 306. Stephen Fietta, 'Expropriation and the "Fair and Equitable" Standard the Developing Role of Investors' "Expectations" in International Investment Arbitration' (2006) 23 *Journal of International Arbitration* 375. *Glamis Gold v. USA*, UNCITRAL, Award, 8 June 2019, para 571.

¹⁰¹² See 2.4.4 in Chapter Two.

¹⁰¹³ See examples *MTD v. Chile* (n 533). *Tecmed v. Mexico* (n 112). *SD Myers v. Canada*, Partial Award, 13 November 2000.

¹⁰¹⁴ *Occidental v. Ecuador*, ICSID Case No. ARB/06/11, Award, 5 October 2012, para 404. As it observed, these cases refer to *MTD v. Chile* (n 533). *LG&E v. Argentina* (n 5). *Tecmed v Mexico* (n 112). *Azurix v. Argentina* Award (n 855).

¹⁰¹⁵ *MTD v. Chile* (n 533).

¹⁰¹⁶ *ibid*.

¹⁰¹⁷ See the Opinion of Judge Steven Schwebel cited in *MTD v. Chile* (n 533), para 109.

¹⁰¹⁸ *Total v. Argentina*, ICSID Case No. ARB/04/01, Decision on liability, 27 December 2010.

¹⁰¹⁹ *ibid* para 123.

¹⁰²⁰ *ibid* para 164.

¹⁰²¹ *ibid*.

4.4.2 The Protection of Legitimate Expectation and Proportionality

The notion of legitimate expectation is borrowed from domestic administrative law.¹⁰²² In the context of international investment, it is related to the host state's change in various aspects, including the legislation system, administrative conduct, and the business environment in general.¹⁰²³ As pointed out by Sornarajah, the protection of legitimate expectations, which is included in expansive FET that absorbs new element if it is needed,¹⁰²⁴ is created by the tribunal.¹⁰²⁵

The recognition of the protection of legitimate expectations as a core element of FET can be observed in practice.¹⁰²⁶ One typical case is *Tecmed*,¹⁰²⁷ which is related to the denial of a permit and the withdrawal of a license to operate a landfill. As required by Article 4 (1) of the Mexico-Spain BIT (1995), each contracting party "guarantees in its territory fair and equitable treatment, in accordance with international law, for the investments made by investors of the other Contracting Party".¹⁰²⁸ Starting with the ordinary meaning of "fair" and "equitable" and following the guidance on treaty interpretation, the tribunal interpreted FET as a standard that

[R]equires the Contracting Parties to provide to international investments treatment that *does not affect the basic expectations* that were taken into account by the foreign investor to make the investment. The foreign investor *expects the host State to act in a consistent manner, free from ambiguity and totally transparently*... The foreign investor also *expects the host State to act consistently*... The foreign investor also *expects the state to use the legal instruments* that govern the actions of the investor or the investment in conformity with the function usually assigned to such instruments, and not to deprive the investor of its investment without the required compensation.¹⁰²⁹ [italic added]

As noted by Dolzer and Schreuer, the above interpretation of FET has always been cited in different cases.¹⁰³⁰ The tribunal illustrated that the primary purpose of FET is to protect foreign investors' "basic expectations",¹⁰³¹ which refer to the host state's actions, from transparency and legality.¹⁰³² In *Yannaca-Small*, legitimate expectations refer to the regulatory experience.¹⁰³³

¹⁰²² Sornarajah, *The International Law on Foreign Investment* (n 88) 426.

¹⁰²³ UNCTAD, *Issues in International Investment Agreement II* (n 79) 63.

¹⁰²⁴ Sornarajah, *The International Law on Foreign Investment* (n 88) 412.

¹⁰²⁵ Sornarajah, *The International Law* (n 803) 444.

¹⁰²⁶ *Genin v. Estonia*, ICSID Case No. ARB/99/2, Award, 25 June 2001, para 371. UNCTAD, *Issues in International Investment Agreement II* (n 79) 77. Dolzer, 'Fair and Equitable Treatment' (n 1001) 17.

¹⁰²⁷ *Tecmed v. Mexico* (n 112). Michele Potesta, 'Legitimate Expectations in Investment Treaty Law: Understanding the Roots and the Limits of a Controversial Concept' (2013) 28 ICSID Review 88, 92.

¹⁰²⁸ Mexico-Spain BIT (signed 23 June 1995, entered into force 18 December 1996, terminated 3 April 2008) Article 4(1).

¹⁰²⁹ *Tecmed v. Mexico* (n 112) para 154.

¹⁰³⁰ Dolzer & Schreuer, *Principles* (n 113) 142.

¹⁰³¹ *Tecmed v. Mexico* (n 112) para 154.

¹⁰³² *ibid.*

¹⁰³³ *Yannaca-Small* (n 1009) 515.

Nevertheless, whether the host state's legitimate expectation is also protected by FET may be questionable. In Sweet's view, the protection of legitimate expectations is provided to both parties.¹⁰³⁴ As he puts, foreign investors have legitimate expectations of their investment in the host state, while the state has legitimate expectations of investors' conduct.¹⁰³⁵ The precondition for balancing the conflicts is to understand both parties' legitimate expectations, which is also the main object of this section. Once their legitimate expectations are clear, a balance can be struck between the conflicting values by applying proportionality based on the actual circumstances.

4.4.2.1 Foreign Investors' Legitimate Expectations

As required by FET, the host state should provide foreign investors treatments that do not frustrate their "basic expectations" when investing in the country.¹⁰³⁶ However, there is a gap between what is expected by foreign investors and which of those expectations are actually protected by the host state.

In international investment, foreign investors expect the host state to act consistently, transparently, free from ambiguity¹⁰³⁷ and abide by its treaty obligations in good faith. In addition, on the basis of the doctrine of estoppel, they can rely on the host state's representations to carry out investments.¹⁰³⁸ They also expect that the host state's legal stability should be maintained once it offers promises to investors. In Schønberg's view, the reason why investors have expectations of the stability of the host state's legal framework is that a stable legal framework allows them to plan their activities related to investments as well as predict the results of their behaviour.¹⁰³⁹

Nevertheless, this does not mean all foreign investors' expectations are protected by FET. As stressed by Muchlinski, all relevant circumstances should be considered to review whether the host state failed to protect investors' legitimate expectations,¹⁰⁴⁰ implying a process of weighing and balancing different values. The expectations and their relevant sources should first be defined.¹⁰⁴¹ The tribunal in *El Paso*¹⁰⁴² emphasised that foreign investors' legitimate expectations and relevant violation should be

¹⁰³⁴ Alec Stone Sweet, 'Investor-State Arbitration: Proportionality's New Frontier' (2010) 4 *Law & Ethics of Human Rights* 47, 62.

¹⁰³⁵ Sweet (n 1053) 62. See examples *CMS v. Argentina* (n 5). *AES v. Kazakhstan* (n 637). *Saluka v. Czech Republic* (n 84).

¹⁰³⁶ See an example *Tecmed v. Mexico* (n 112).

¹⁰³⁷ *Tecmed v. Mexico* (n 112) para 154.

¹⁰³⁸ See an example *Tecmed v. Mexico* (n 112) paras 153-66, 173-4.

¹⁰³⁹ Søren J. Schønberg, *Legitimate Expectations in Administrative Law* (OUP 2000) 12,23. Hector A. Mairal, 'Legitimate Expectations and Informal Administrative Representations' in Stephan W. Schill (ed), *International Investment Law and Comparative Public Law* (OUP 2010) 416. Anne-France Colla, 'Elements for a General Theory of Legitimate Expectations' (2017) 4 *Moral Philosophy & Politics*, 283. Kenneth J Vandeveld, 'A Unified Theory of Fair and Equitable Treatment' (2010) 43 *NYU Journal of International Law & Politics*, 43. Yannaca-Small (n 1009) 519.

¹⁰⁴⁰ Peter Muchlinski, 'Trends in International Investment Agreement: Balancing Investor Rights and the Right to Regulate: The Issue of National Security' in Karl P Sauvant (ed), *Yearbook on International Investment Law and Policy 2008-2009* (OUP 2009) 58.

¹⁰⁴¹ *ibid.*

¹⁰⁴² *El Paso v. Argentina* (n5).

examined objectively to ascertain whether a state has breached its FET obligations *vis-à-vis* investors.¹⁰⁴³ In one of its studies, the UNCTAD clarified that three requirements should be fulfilled to obtain the protection of legitimate expectations.¹⁰⁴⁴ As listed,

- (a) *Legitimate* expectations may arise only from a state's *specific representations or commitments* made to the investor, on which the latter has *relied*;
- (b) The investor must be aware of the *general regulatory environment* in the host country;
- (c) Investor's expectations must be *balanced* against *legitimate* regulatory activities of host countries.¹⁰⁴⁵ [*italic added*]

As reflected in the wording, the protection of foreign investors' legitimate expectations is provided based on the actual circumstances. Such protection is not unconditional. As stressed by Dolzer and Schreuer, instead of subjective desires of foreign investors, their legitimate expectations should be created based on objective facts,¹⁰⁴⁶ namely "specific representations or commitments" expressed by the host states,¹⁰⁴⁷ such as particular guarantees promised by it. Yannaca-Small further asserts that if the promises or guarantees provided to foreign investors are more precise, there are higher possibilities for them to have legitimate expectations on the basis of such commitments.¹⁰⁴⁸

Meanwhile, foreign investors' own behaviour also plays a vital role in protecting their legitimate expectations.¹⁰⁴⁹ Before investing, they should have comprehensive knowledge of the real circumstances in a particular state, including the relevant environment of investment and the need for the potential host state to exercise regulatory power reactively to protect the public interest. Therefore, they can have a reasonable prediction or expectation of the potential development of their investments in that state.

The emphasise on foreign investors' due diligence implies the notion of proportionality, in particular one of its constituent elements, proportionality *stricto sensu*, which is explicitly stressed by the UNCTAD in the last requirement. As required, "[t]he foreign investor's expectation must be *balanced* against legitimate regulatory activities of the host state".¹⁰⁵⁰ The word "balanced" indicates a process of weighing and balancing the conflicting values between foreign investors' legitimate expectations and the host state's right to regulate in the public interest, which is included in the application of

¹⁰⁴³ *ibid* para 356.

¹⁰⁴⁴ UNCTAD, *Issues in International Investment Agreement II* (n 79) 68.

¹⁰⁴⁵ *ibid*.

¹⁰⁴⁵ *ibid*.

¹⁰⁴⁶ Dolzer & Schreuer, *Principles* (n 113) 170. see also Rudolf Dolzer, 'Fair and Equitable Treatment' (n 1001) 16.

¹⁰⁴⁷ *ibid*.

¹⁰⁴⁷ UNCTAD, *Issues in International Investment Agreement II* (n 79) 68.

¹⁰⁴⁸ Yannaca-Small (n 1009) 521.

¹⁰⁴⁹ UNCTAD, *Issues in International Investment Agreement II* (n 79) 68, 71.

¹⁰⁵⁰ *ibid* 68 [*italic added*].

proportionality. In other words, the protection provided to foreign investors is not absolute. The values legitimately expected by foreign investors should be balanced against the public interest desired by the host state. As discussed in Chapter Three, such a balance can be achieved by applying proportionality through the systemic treaty interpretation.¹⁰⁵¹

The fulfilment of these requirements listed by the UNCTAD is also emphasised in practice. In *EDF v. Romania*,¹⁰⁵² the tribunal stressed that

Legitimate expectations *cannot be solely the subjective expectations of the investor*. They must be examined as the expectations *at the time the investment is made*, as they may be deduced from *all the circumstances of the case*, due regard being paid to *the host State's power to regulate its economic life in the public interest*.¹⁰⁵³ [italic added]

A similar view is held by the tribunal in *AES*,¹⁰⁵⁴ who stated that the claimants should perform due diligence when making investments. In this case, the tribunal reasoned that the claimant should have realised the possibility of Kazakhstan taking measures, such as amending legislation, to reform its electricity market according to its national conditions.¹⁰⁵⁵ Based on the actual circumstances at the time of their investment, Kazakhstan's expectation of reforming its competition law was accessible to foreign investors, and its planned changes should have been predictable. Furthermore, the tribunal noted that the protection of foreign investors' legitimate expectations provided by FET is not absolute.¹⁰⁵⁶

A key question raised by this case was whether the measures taken by Kazakhstan were reasonable and proportionate.¹⁰⁵⁷ Based on the earlier discussion in Chapter Two on proportionality, its components include suitability and necessity of the measures in question and proportionality *stricto sensu*.¹⁰⁵⁸ The tribunal in *AES*¹⁰⁵⁹ stressed that "the duration of the restriction and its *necessity* to achieve the pursued goal are important criteria" to determine the proportionality of such restriction.¹⁰⁶⁰ Due to the failure to prove the necessity of the measures implemented by the Kazakh Government and the unreasonable duration of its implementation, Kazakhstan was found to have violated its FET obligation because its means were beyond what was necessary.¹⁰⁶¹

¹⁰⁵¹ See generally in Chapter Three.

¹⁰⁵² *EDF v. Romania*, ICSID Case No. ARB/05/13, Award, 8 October 2009.

¹⁰⁵³ *Ibid* para 219. UNCTAD, *Issues in International Investment Agreement II* (n 79) 67.

¹⁰⁵⁴ *AES v. Kazakhstan* (n 637). *Saluka v. Czech Republic* (n 84).

¹⁰⁵⁵ *AES v. Kazakhstan* (n 637) para 279.

¹⁰⁵⁶ *Ibid* para 401.

¹⁰⁵⁷ *Ibid* para 402.

¹⁰⁵⁸ See 2.4 in Chapter Two.

¹⁰⁵⁹ *AES v. Kazakhstan* (n 637). *Saluka v. Czech Republic* (n 84).

¹⁰⁶⁰ *AES v. Kazakhstan* (n 637) para 403 [italic added].

¹⁰⁶¹ *Ibid* paras 404-9. See generally in Chapter Five.

4.4.2.2 The Host State's Legitimate Expectations

In the context of international investment, the state can be a host state to where capital is deployed or a home state in which foreign investors are domiciled. As a host state, it has expectations of foreign investors' conduct and investments. However, the host state is also a sovereign country in international law. In this regard, it has the power to regulate for its own national public interest. These expectations are related to the non-economic objectives of IIAs. As below, a state's expectations will be discussed from these two important perspectives.

In international investment, once foreign investors make investments in a particular country, they automatically become part of the latter's society. As one party to international investment, the host state expects its counterparty, namely foreign investors, to act in accordance with its local laws and regulations.¹⁰⁶² Based on the wording of IIAs, it has been explicitly expressed that the investments that satisfy the requirement for admission are eligible for protection under treaties and prescription of investors' general obligations.¹⁰⁶³ These requirements can be found in treaty provisions, such as the "definition" and "scope and application" clauses.¹⁰⁶⁴

A typical example is the Indian Model BIT (2015).¹⁰⁶⁵ Different from others, this BIT particularly stipulates "investor obligations" in an independent chapter, including two articles.¹⁰⁶⁶ Based on Article 11 (i), apart from specific obligations,¹⁰⁶⁷ such as anti-corruption, foreign investors are generally required to comply with the host state's domestic laws and regulations during the whole process of their investments, which refers to the "*establishment, acquisition, management, operation and disposition*".¹⁰⁶⁸

From the perspective of foreign investors, these requirements mean that they should abide by local laws when investing to secure admission and enjoy investment protection.¹⁰⁶⁹ Even after entry, they should continue complying with the host state's regulations; Otherwise, they and their investments will not be

¹⁰⁶² Bin Cheng, *General Principles of Law as Applied by International Courts and Tribunals* (CUP 1953) 119. Sweet (n 1034) 62.

¹⁰⁶³ Lars Markert, 'The Crucial Question of Future Investment Treaties: Balancing Investors' Rights and Regulatory Interests of Host States' in M. Bungenberg et al. (eds.), *International Investment Law and EU Law* (Springer 2011) 151.

¹⁰⁶⁴ See examples China-Tanzania BIT (n 261) Article 1.1. China-Uzbekistan BIT (signed 19 April 2011, entered into force 1 September 2011) Article 1.

¹⁰⁶⁵ The Indian Model BIT (n 957).

¹⁰⁶⁶ *ibid* Chapter III. This chapter includes "compliance with laws" and "corporate social responsibility". Jeongho Nam, 'Model BIT: an Ideal Prototype or a Tool for Efficient Breach?' (2017) 48 *Georgetown Journal of International Law* 1275, 1277.

¹⁰⁶⁷ The Indian Model BIT (n 957) Article 11 (i), (iii), (iv).

¹⁰⁶⁸ *ibid* Article 11 (i) [*italic added*].

¹⁰⁶⁹ See an example the Netherlands Model BIT (2019) Article 2.

protected by treaties.¹⁰⁷⁰ For instance, as explicitly mentioned in the CETA,¹⁰⁷¹ if investors make their investments through "fraudulent misrepresentation, concealment, corruption, or conduct amounting to an abuse of process",¹⁰⁷² they may not be allowed to be offered treaty protections by the arbitral tribunals. This is similar to the one prerequisite for applying proportionality. As analysed in Chapter Three, before initiating proportionality analysis to ascertain whether the disputed measure violates treaty obligations, the affected rights should fall into the category of protected values. Otherwise, the application of proportionality will not be triggered.

Meanwhile, as a sovereign country, the host state is also responsible for the development of its whole society and the welfare of its entire populace. The state's legitimate expectations of these non-investment values can be seen from two perspectives. From the state its own perspective, in order to develop and protect non-investment values, it can modify rules and regulations as it pleases to react to changing circumstances and protect its public interest.¹⁰⁷³ Such power can be usually found in the treaty preamble and the exception clauses.¹⁰⁷⁴ Based on a survey provided by Gordon, Pohl and Bouchard, 75.5% of IIAs signed between 2008 and 2013 refer to the terms like "sustainable development" or "responsible business conduct",¹⁰⁷⁵ emphasising the significance of non-investment values.

For example, the China-Tanzania BIT (2013)¹⁰⁷⁶ expresses that one of its purposes is to "promote healthy, stable and sustainable economic development, and *to improve the standard of living of nationals*" in the preamble.¹⁰⁷⁷ Other treaties, like the China-Turkey BIT (2015),¹⁰⁷⁸ stress the importance of non-economic values in the main text. As prescribed in Article 4, in general exceptional situations, the host state's necessary measures will not be regarded as violations of its treaty obligations.¹⁰⁷⁹ Such exceptions refer to various fields, including environmental protection and the conservation of natural resources.

However, the state's legitimate expectations are somewhat affected by the broad protection and

¹⁰⁷⁰ Stephan W. Schill, 'Illegal Investments in Investment Treaty Arbitration' (2012) 11 *The Law & Practice of International Courts and Tribunals* 281. Rahim Molloo & Alex Khachaturian, 'The Compliance with the Law Requirement in International Investment Law' (2011) 34 *Fordham International Law Journal* 1471. The Republic of South Africa, *Bilateral Investment Treaty Policy Framework Review Government Position Paper* (2009) 29. Sornarajah, *The International Law on Foreign Investment* (n 88) 275.

¹⁰⁷¹ CETA (n 545).

¹⁰⁷² *ibid* Article 8.18.3.

¹⁰⁷³ Yulia Levashova, *The Right of States to Regulate in International Investment Law: The Search for Balance between Public Interest and Fair and Equitable Treatment* (Wolters Kluwer 2019) 238.

¹⁰⁷⁴ Markert (n 1063) 151. Hanessian & Duggal (n 958) 225. See examples China-Tanzania BIT (n 261) Preamble and Article 10. The Indian Model BIT (n 957) Article 33.

¹⁰⁷⁵ Kathryn Gordon, Joachim Pohl & Marie Bouchard, 'Investment Treaty Law, Sustainable Development and Responsible Business Conduct: A Fact Finding Survey' (2014) *OECD Working Papers on International Investment* 2014/01, 11.

¹⁰⁷⁶ China-Tanzania BIT (n 261).

¹⁰⁷⁷ *ibid* Preamble [*italic added*].

¹⁰⁷⁸ China-Turkey BIT (n 15).

¹⁰⁷⁹ *ibid* Article 4.

treatment enjoyed by foreign investors. Based on the later analysis of the Argentinian cases arising from its economic crisis, even the measures taken by the host state to maintain its public order and guarantee non-investment values were challenged by foreign investors.¹⁰⁸⁰ This reflects the imbalance between the legitimate expectations of foreign investors and those of the host state, highlighting the need to apply the principle of proportionality to re-balance the investor-state relationship.

Concerning the protection of its public interests, the host state also has legitimate expectations of foreign investors' conduct, which is closely linked to non-investment values. As expected by the host state, foreign investors should act as good corporate citizens¹⁰⁸¹ endeavouring to fulfil corporate social responsibility (CSR) and be responsible for the social consequences of their investment activities.¹⁰⁸² For example, as specifically stipulated in Article 12 of the Indian Model BIT (2015)¹⁰⁸³ with the heading "corporate social responsibility",

Investors and their enterprises operating within the territory of each party *shall endeavour to voluntarily* incorporate internationally recognised standards of corporate social responsibility in their practices and internal policies, such as statements of principle that have been endorsed or are supported by the parties. These principles may address issues such as *labour, the environment, human rights, community relations and anti-corruption*.¹⁰⁸⁴ [italic added]

As indicated by the modal verb "shall", CSR is an absolute obligation on foreign investors *vis-à-vis* the host state. However, the language "endeavour to voluntarily incorporate", to a certain extent, dilutes its power. By definition, "voluntarily" describes a situation in which people do with neither compulsion nor other determining force.¹⁰⁸⁵ Foreign investors are encouraged rather than compelled to fulfil such an obligation. As highlighted by Hanessian and Duggal, that provision explicitly presents that India imposes CSR as investors' obligation to specifically settle the issues related to "labour, the environment, human rights, community relations and anti-corruption".¹⁰⁸⁶

A similar provision appears in the draft of the Chinese Model BIT, which has not been approved as a model as such.¹⁰⁸⁷ Article 13 stipulates that "[t]he Parties agree to *encourage* investors to conduct their investment activities in a socially responsible manner, by complying with the OECD Guideline for

¹⁰⁸⁰ See generally in Chapter Five. Argentinian cases (n 5).

¹⁰⁸¹ Sweet (n 1034) 62. Jeremy Moon, 'The Contribution of Corporate Social Responsibility to Sustainable Development' (2007) 15 Sustainable Development 296, 298-9. Paul Hohnen, 'Corporate Social Responsibility: An Implementation Guide for Business' 2007 International Institute for Sustainable Development 4, 4-5.

¹⁰⁸² *ibid.*

¹⁰⁸³ The Indian Model BIT (n 957) Chapter III.

¹⁰⁸⁴ *ibid* Article 12.

¹⁰⁸⁵ 'Voluntarily' (*OED*) < <https://www.oed-com.ezproxy-s1.stir.ac.uk/view/Entry/224553?redirectedFrom=voluntarily#eid>> last accessed 20 November 2021.

¹⁰⁸⁶ The Indian Model BIT (n 957) Article 12. Hanessian & Duggal (n 958) 225.

¹⁰⁸⁷ Draft of the Chinese Model BIT, see from Shan & Gallagher (n 9) 460-7.

Multinational Enterprises and participating in the United Nations Global Compact".¹⁰⁸⁸ Compared with the CSR clause in the Indian Model BIT (2015),¹⁰⁸⁹ this draft provides more detail on the basis of external instruments, such as the OECD Guidance. From this, investors should "contribute to economic, environmental and social progress with a view to achieving sustainable development"¹⁰⁹⁰ and undertake "risk-based due diligence".¹⁰⁹¹ They are also required to disclose relevant information on their investments timely and accurately,¹⁰⁹² and follow the in anti-corruption and anti-bribery law and policy.¹⁰⁹³ However, the term "encourage" used in the Chinese Model BIT (draft)¹⁰⁹⁴ indicates that the CSR obligation is non-compulsory, hence weaker,¹⁰⁹⁵ compared with the wording "*shall endeavour*" adopted in the Indian Model BIT (2015).¹⁰⁹⁶ In other words, the nature of CSR in the Chinese Model BIT (draft) is an encouragement for investors to regulate their behaviour and restrict the harmful effects of their investment activities on the host state's society,¹⁰⁹⁷ boosting their positive contributions to the host state.¹⁰⁹⁸

As reflected by the wording of recent IIAs, states' intentions have gradually become broader: From investment protection to sustainable development and from economic development to environmental protection.¹⁰⁹⁹ Nevertheless, considering that relevant investors' values can be hampered by the host state's measures to protect its public interest, conflicts appear between parties when the host state exercises its regulatory power to change laws and policies, re-emphasising the significance of applying proportionality to strike a balance in the investor-state relationship.

4.5 Conclusion

As an absolute treatment stipulated in treaties, FET plays an increasingly significant role in the context of international investment and its interaction with proportionality. Meanwhile, with the increasing number of ISD arising from the uncertainties of FET, the imbalance in the investor-state relationship is further skewed. Such issues refer to FET's nature and fundamental elements, which can be best revealed through systemic treaty interpretation and settled by the application of proportionality.

¹⁰⁸⁸ *ibid* Article 13 [italic added].

¹⁰⁸⁹ The Indian Model BIT (n 957) Article 12.

¹⁰⁹⁰ OECD, *Guidelines for Multinational Enterprises* (2011) 19.

¹⁰⁹¹ *ibid* 20.

¹⁰⁹² *ibid* 27.

¹⁰⁹³ *ibid* 47.

¹⁰⁹⁴ Gallagher & Shan (n 872) 445.

¹⁰⁹⁵ Laurence Dubin, 'Corporate Social Responsibility Clauses in Investment Treaties' (*Investment Treaty News*, 21st December 2018) <<https://www.iisd.org/itn/2018/12/21/corporate-social-responsibility-clauses-in-investment-treaties-laurence-dubin/>> last accessed on 24 June 2022.

¹⁰⁹⁶ The Indian Model BIT (n 957) Article 12.

¹⁰⁹⁷ Dubin (n 1095). Hanessian & Duggal (n 958) 225.

¹⁰⁹⁸ The Indian Model BIT (n 957) Article 12. Hanessian & Duggal (n 958) 225.

¹⁰⁹⁹ That trend can be proved by the changes in the Chinese BITs, which will be discussed in Chapter Six. See more examples The Netherlands Model BIT (n 1069) Preamble. China-Uzbekistan (n 1064) Preamble. China-Tanzania BIT (n 261) Preamble.

Based on the earlier discussion on treaty interpretation in Chapter Three, FET's various formulations and different contexts in which it appears in IIAs lead to its different interpretations. These interpretations of FET, on the one hand, present doubts on whether it is an international custom; On the other hand, they depict the generic scope of FET. As discussed previously, the rule in question should be a general practice and applied out of a sense of legal obligation to be an international custom.¹¹⁰⁰ Tudor regards the repeated FET clause in IIAs as a signal that this standard is a rule of customary international law.¹¹⁰¹ However, as analysed, FET satisfies neither "state practice" nor "*opinio juris*".¹¹⁰² Various expressions of FET, somewhat reflect states' different understandings of such a standard. In this regard, FET is not mature enough to be an international custom. Correspondingly, obtaining the FET protection depends on the relevant treaty provisions on a case-by-case basis.

Regarding the components of FET, although they are interpreted on a case-by-case basis, a general contour can be deduced from practice. Regardless of the differences in the FET clauses stipulated in IIAs, as concluded, its constituent elements include the principle of good faith, due process, a stable legal and business framework, transparency, non-discrimination, proportionality, and the protection of foreign investors' legitimate expectations. Proportionality as an element of FET can be seen in practice, stressing the significance of a balance between the conflicting values of foreign investors and the host state. Meanwhile, its importance is emphasised when balancing their legitimate expectations.

As the most important factor, the protection of legitimate expectations stands above other elements of FET. Other factors, such as the stability of the legal and business framework in the host state, may also be expected by foreign investors when investing.¹¹⁰³ In the context of international investment, both foreign investors and the host state have legitimate expectations as to the investment between them. From the perspective of foreign investors, they have expectations of the state's stable legal framework, based on which they can plan their investment and predict the relevant results. Their legitimate expectations are closely linked to the protection of investment values. With regard to the state, it has expectations from the perspective of the host state as well as expectations from the perspective of a sovereign country. Unlike investors, the host state also has legitimate expectations of the protection and development of its non-investment values, such as essential security interests and the public order.

Conflicts always exist between investment values and non-investment values. Once foreign investors' legitimate expectations conflict with the host state's regulatory power for its public interest, an ISA may be initiated. How to assuage such conflicting values is vital to establishing a balanced investor-state

¹¹⁰⁰ See 2.3.1 in Chapter Two.

¹¹⁰¹ Tudor (n 87) 85.

¹¹⁰² Dumberry, 'Has' (n 89) 175-6.

¹¹⁰³ UNCTAD, *Issues in International Investment Agreement II* (n 79) 67.

relationship. According to the previous discussion in Chapter Two, proportionality is the appropriate tool.¹¹⁰⁴ In this respect, one critical point in determining whether the host state has violated its FET obligation *vis-à-vis* foreign investors is to ascertain the proper proportion between disputing parties' values. In the next chapter, how such conflicting expectations should be and have been settled by applying proportionality in practice will be discussed and examined based on the analyses and comparisons of different awards of available cases.

¹¹⁰⁴ See generally in Chapter Two.

Chapter 5

The Application of the Principle of Proportionality in Balancing the Conflicting Legitimate Expectations of Foreign Investors and the Host State in the Argentinian Cases

5.1 Introduction

As shown by the researcher, the imbalance in the investor-state relationship¹¹⁰⁵ can stem from a lack of uniformity in interpreting FET.¹¹⁰⁶ Furthermore, based on the analysis in Chapter Four, one issue that appears as an element of FET is the protection of legitimate expectations.¹¹⁰⁷ Both the host state and foreign investors have legitimate expectations about international investments between them. However, what is expected by the host state in exercising its regulatory power to respond to its constantly changing circumstances may be at odds with investors' legitimate expectations, in particular on the stability of the host state's legal and business framework.¹¹⁰⁸

Concluded from practice seen amongst treaty parties, proportionality is a useful tool to review the measures implemented by the host state's public authorities.¹¹⁰⁹ Proportionality is a structured and flexible tool to balance such impasses in international investment.¹¹¹⁰ As stressed by Sweet, "[b]alancing pushes arbitrators toward [*sic*] proportionality",¹¹¹¹ which provides "a measure of analytic, or procedural, determinacy to the balancing exercise".¹¹¹² Based on the earlier discussions, although proportionality is neither an international custom nor a general principle of law,¹¹¹³ it may still be applied in the ISDS to strike a balance in the investor-state relationship if its textual basis exists in the case-related legal instrument.¹¹¹⁴

Nevertheless, most BITs contain no provision of proportionality,¹¹¹⁵ raising questions over the credibility of proportionality analysis. As reflected in the conclusions in Chapters Two and Three, if proportionality is expressed in the case-related treaty, explicitly or implicitly, it can strike a balance in the investor-state relationship by interpreting its treaty textual basis via the systemic interpretative approach.¹¹¹⁶ Alternatively, if such a principle matches the host state's domestic law, which is the

¹¹⁰⁵ Ursula Kriebaum, 'Regulatory Takings: Balancing the Interests of the Investor and the State' (2007) 8 *Journal of World Investment & Trade* 717.

¹¹⁰⁶ See generally in Chapter Four.

¹¹⁰⁷ See 4.4.2 in Chapter Four.

¹¹⁰⁸ See examples *CMS v. Argentina* (n 5). *AES v. Kazakhstan* (n 637). *Saluka v. Czech Republic* (n 84).

¹¹⁰⁹ See 2.2 in Chapter Two.

¹¹¹⁰ Bücheler (n 18) 194. Kingsbury & Schill (n 18) 79. Schill & Djanic (n 191) 46.

¹¹¹¹ Sweet (n 1034) 62 [*italic added*]. Kingsbury & Schill (n 18) 79. Schill & Djanic (n 191) 46. See in general Stephan W. Schill, 'International Investment Law and the Host State's Power to Handle Economic Crises Comment on the ICSID Decision in *LG&E v. Argentina*' (2007) 24 *Journal of International Arbitration* 265.

¹¹¹² Sweet (n 1034) 62.

¹¹¹³ See 2.3 in Chapter Two.

¹¹¹⁴ Based on the discussion in Chapter Two, there are two routes to the application of proportionality. One applicable approach depends on the interpretation of proportionality textual basis in treaties, which should be interpreted via the systemic method.

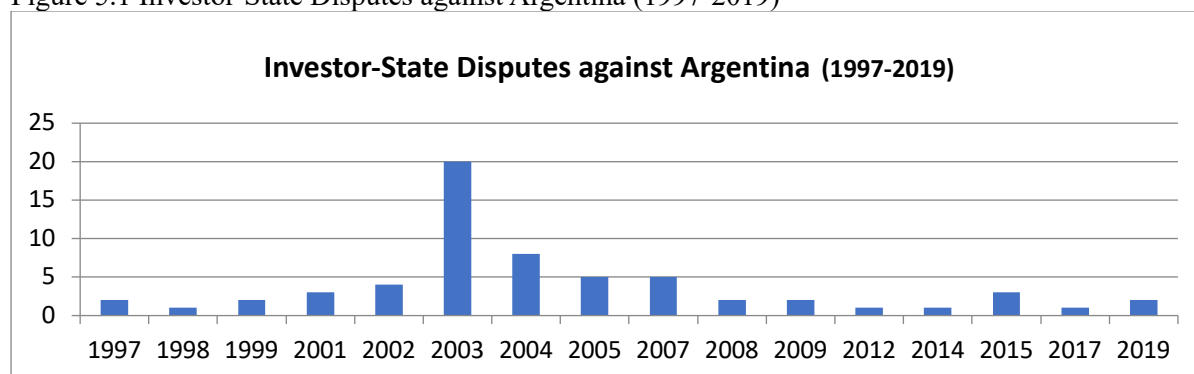
¹¹¹⁵ However, the Colombia Model BIT (2008) explicitly refers to the term "proportional". China-Colombia BIT (n 124) is the only Chinese BIT in which "proportionality" explicitly appears.

¹¹¹⁶ See generally in Chapters Two and Three.

applicable instrument of the case, it may also enable the balance of conflicting legitimate expectations of foreign investors and the host state.¹¹¹⁷

This chapter aims to investigate the possibility and feasibility of the first route to the application of proportionality, in which its utilisation depends on the particular treaty provision. This assessment will be carried out by analysing and discussing six cases arising from Argentina's economic crisis of 2001/2.¹¹¹⁸ According to the chronological order, they are *CMS*,¹¹¹⁹ *Enron*,¹¹²⁰ *LG&E*,¹¹²¹ *Sempra*,¹¹²² *Continental*,¹¹²³ and *El Paso*.¹¹²⁴ These cases are prime examples to express the application of proportionality in the ISDS regime because of their broad influences. Argentina has the largest number of ISDs in which it was involved as the respondent state.¹¹²⁵ As reflected in the data from the UNCTAD, 62 cases have been filed against Argentina from 1997 to 2019.¹¹²⁶ Figure 5.1 shows that the ISDs against Argentina peaked in 2003 with 20 cases.¹¹²⁷ As pointed out by Lavopa, the disputes brought against Argentina from 2003 to 2007 occupied a quarter of all cases arbitrated under ICSID rules within the same period.¹¹²⁸

Figure 5.1 Investor-State Disputes against Argentina (1997-2019)



Meanwhile, typical issues of applying proportionality are reflected in these cases from both treaty interpretation and application perspectives. Although all cases were brought by American investors in

¹¹¹⁷ ICSID Convention (n 7) Article 42.

¹¹¹⁸ Argentinian cases (n 5).

¹¹¹⁹ *CMS v. Argentina* (n 5).

¹¹²⁰ *Enron v. Argentina* (n 5).

¹¹²¹ *LG&E v. Argentina* (n 5).

¹¹²² *Sempra v. Argentina* (n 5).

¹¹²³ *Continental v. Argentina* (n 5).

¹¹²⁴ *El Paso v. Argentina* (n 5).

¹¹²⁵ Data collected from Investment Policy Hub. 'Investment Dispute Settlement Navigator-Argentina-Cases as Respondent State' (*Investment Policy Hub*) <<https://investmentpolicy.unctad.org/investment-dispute-settlement/country/8/argentina>> last accessed to 20 June 2022.

¹¹²⁶ 27 cases arose from Argentina's economic crisis of 2001/2. Federico Lavopa, 'Crisis, Emergency Measures and the Failure of the ISDS System: The Case of Argentina' (2015) South Centre Investment Policy Brief 1, 3.

¹¹²⁷ Investment Policy Hub (n 1125).

¹¹²⁸ Argentinian cases (n 5). Lavopa (n 1126) 1.

an ICSID arbitration relying on the same treaty, namely the Argentina-US BIT (1991),¹¹²⁹ the tribunals reached different conclusions on whether Argentina's reaction to its severe economic crisis met the requirements to invoke the necessity. More specifically, they had different views on the relationship between the necessity stipulated in Article XI, the exception clause of the BIT,¹¹³⁰ and the state of necessity provided in Article 25 of the Wrongful Act.¹¹³¹ For instance, the tribunal in *CMS* regarded Article XI as the same as Article 25.¹¹³² In contrast, the tribunal in *Continental* explicitly expressed that these provisions were different for invoking the necessity.¹¹³³

Furthermore, proportionality as a flexible tool has been utilised by those tribunals in various ways, leading to different outcomes. As discussed in Chapter Two, the all-encompassing proportionality analysis contains three consecutive tests, which aim to assess suitability, necessity, and proportionality *stricto sensu*, respectively.¹¹³⁴ Compared with the horizontal approach, this vertical method that expresses the internal logical order of proportionality is the appropriate mode for its application.¹¹³⁵ However, some tribunals in Argentinian cases merely adopted the necessity test, while others applied the all-encompassing proportionality analysis. Considering the influences of Argentinian cases, they are good subjects demonstrating the textual basis of applying proportionality in the ISDS and showing how this tool has been applied in practice to re-balance the investor-state relationship.

This chapter is composed of four sections. The factual background of six cases will be introduced in 5.2 from two perspectives to present the discord between the legitimate expectations of foreign investors and the host state. One is the period in which Argentina's State Reform Programme was initiated to attract foreign investors, while another is the duration in which a set of policy actions were taken by Argentina to manage its economic crisis of 2001/2. In this section, the circumstances will be depicted in which foreign investors' legitimate expectations were both created and infringed.

The application of proportionality in the ISDS will be discussed in 5.3 and 5.4. The former focuses on proportionality analysis from the perspective of treaty interpretation, while the latter examines its utilisation from the perspective of treaty application. The textual basis of proportionality will be ascertained first, followed by a discussion on the decision-maker, who has the power to decide critical decisions within applying proportionality. The decision-maker might deliberate on whether the state's

¹¹²⁹ Argentina-US BIT (n 120).

¹¹³⁰ *ibid.*

¹¹³¹ Wrongful Act (n 422) Article 25.

¹¹³² *CMS v. Argentina* (n 5),

¹¹³³ *Continental v. Argentina* (n 5).

¹¹³⁴ See 2.5.1 in Chapter Two. Sweet & Cananea (n 415) 917. Han, 'The Application of the Principle of Proportionality' (n 145) 642-3. Giovanni Zarra, 'Right to Regulate, Margin of Appreciation and Proportionality: Current Status in Investment Arbitration in Light of *Philip Morris v. Uruguay*' (2017) 14 *Brazilian Journal of International Law* 95, 106.

¹¹³⁵ See 2.5.2 in Chapter Two.

interests are at stake and need to be protected by specific measures. The actual application of proportionality in these cases was affected by the muddled relationship between the necessity test under the Argentina-US BIT (1991)¹¹³⁶ and the state of necessity in Article 25 of the Wrongful Act.¹¹³⁷ As shall be discussed in-depth later, although both provisions mention the necessary measures, they refer to the questioned means of different natures and provide different criteria for necessity.

Once proportionality is brought into the ISDS regime via the systemic treaty interpretation, how it can be used to strike a balance in the investor-state relationship will be explored in 5.4 by analysing the tribunals' legal reasoning in these cases. This assessment will be carried out based on the internal logical order of proportionality, starting from suitability and ending with proportionality *stricto sensu*.¹¹³⁸ By comparing their legal reasoning and decisions, the application of proportionality in practice and the corresponding uncertainties will be presented, reflecting the merits and drawbacks of applying proportionality in the ISDS.

As analysed and clarified in this chapter, proportionality can be applied based on the systemic interpretation of its textual basis, but it should be adopted via the vertical approach to balance the conflicting values of foreign investors and the host state. This investigation of proportionality's textual basis will also contribute to the future analysis of proportionality in Chinese BITs.

5.2 The Conflicting Legitimate Expectations of Foreign Investors and the Host State

This section will present the factual background of several cases arising from the Argentinian economic crisis of 2001/2, showing how foreign investors' legitimate expectations clashed with Argentina's regulation for its own public interest. Based on the different purposes pursued by the Argentine Government, the measures it implemented can be divided into two phases. Between the late 1980s and 1990s, the Government of Argentina launched the State Reform Programme, and foreign investors were attracted to participate in Argentina's privatisation. However, Argentina had to take various emergency policy measures to deal with a crippling economic crisis in 2001/2.

5.2.1 State Reform Programme-Creating Legitimate Expectations

Due to an economic crisis, Argentina experienced a deep recession and hyperinflation in the late 1980s. A set of policy developments were implemented by the Government of Argentina to carry out its State Reform Programme. Some restructuring, such as the promulgation of the State Reform Law, enabled the privatisation of state-owned enterprises.¹¹³⁹

¹¹³⁶ Argentina-US BIT (n 120) Article XI.

¹¹³⁷ Wrongful Act (n 422) Article 25.

¹¹³⁸ See 2.5.1 in Chapter Two.

¹¹³⁹ *Sempra v. Argentina* (n 5) para 82. *LG&E v. Argentina* (n 5) para 35. *CMS v. Argentina* (n 5) para 53. *Enron v. Argentina* (n

Specific instruments were also enacted in some particular industries to govern privatisation. For example, the Gas Law, its implementing regulations, and the Basic Rules of the License were adopted to provide comprehensive regulations and oversee the industry for the natural gas transport and distribution service.¹¹⁴⁰ More specifically, the tariffs were calculated in US dollars and expressed in Argentine pesos.¹¹⁴¹ The tariffs would be adjusted every six months based on "the United States Producer Price Index (US PPI)".¹¹⁴² Based on the Convertibility Law, a fixed exchange rate was settled between the Argentina peso and the US dollar.¹¹⁴³ Moreover, according to the regulations, the Government of Argentina could not unilaterally revoke or modify the licenses.¹¹⁴⁴

Additionally, other attractive measures were taken by Argentina to attract and encourage foreign investors to participate in its privatisation.¹¹⁴⁵ More than 50 BITs had been agreed by Argentina with another contracting state in the 1990s,¹¹⁴⁶ enhancing foreign investors' confidence in investing in Argentina. Consequently, foreign investors made various investments and actively participated in the State Reform Programme in Argentina. Their investments could be seen in the privatisation of Argentina's public services, from gas transportation to water distribution.¹¹⁴⁷ As a result, Argentina's economy grew dramatically.

5.2.2 Economic Crisis—Raising Conflicts

Nevertheless, an economic crisis was approaching, reaching its peak in late 2001. Deposits were withdrawn from banks due to the sharp rise in public debt and solvency issues in Argentina. This crisis severely affected the situation in Argentina. Over fifty per cent of the urban population experienced poverty.¹¹⁴⁸ Five presidents resigned successively in less than ten days,¹¹⁴⁹ reflecting instability across the whole of Argentina's society. In such circumstances, the United Nations General Assembly even reduced Argentina's membership dues; For the first time in its history.¹¹⁵⁰

5) para 41.

¹¹⁴⁰ *LG&E v. Argentina* (n 5) paras 37-43. *CMS v. Argentina* (n 5) para 54. *Enron v. Argentina* (n 5) para 42.

¹¹⁴¹ *CMS v. Argentina* (n 5) para 57. *Enron v. Argentina* (n 5) para 41.

¹¹⁴² *CMS v. Argentina* (n 5) para 57.

¹¹⁴³ *CMS v. Argentina* (n 5) para 53. *LG&E v. Argentina* (n 5) para 36. *Continental v. Argentina* (n 5) paras 104-5.

¹¹⁴⁴ *LG&E v. Argentina* (n 5) para 41.

¹¹⁴⁵ *ibid* paras 49-50. Paolo Di Rosa, 'The Recent Wave of Arbitrations against Argentina under Bilateral Investment Treaties: Background and Principal Legal Issues' (2004) 36 *The University of Miami Inter-American Law Review* 41, 47.

¹¹⁴⁶ Collected the data from Investment Policy Hub. 'International Investment Agreements Navigator-Argentina BITs' (Investment Policy Hub) <<https://investmentpolicy.unctad.org/international-investment-agreements/countries/8/argentina>> last accessed 24 June 2022.

¹¹⁴⁷ For example, *CMS v. Argentina* (n 5). *Enron v. Argentina* (n 5). *Suez v. Argentina*, ICSID Case No. ARB/03/17, Decision on Liability, 30 July 2010. *Suez & Vivendi v. Argentina*, ICSID Case No. ARB/03/19, Award, 9 April 2015.

¹¹⁴⁸ *Continental v. Argentina* (n 5) para 108.

¹¹⁴⁹ *LG&E v. Argentina* (n 5) paras 63, 216. *CMS v. Argentina* (n 5) para 64.

¹¹⁵⁰ *El Paso v. Argentina* (n 5) para 92.

In response to its economic crisis, a variety of measures were taken by the Government of Argentina. Bank savings were frozen, and the foreign exchanges were tightly controlled. The Emergency Law was enacted on 6 January 2002, abrogating the Convertibility Law.¹¹⁵¹ In this respect, the parity between the Argentina peso and the US dollar was abrogated. The foreign exchange system, which was so crucial to foreign investors, was also changed.¹¹⁵² Concerning the specific industries, the US PPI adjustment of gas tariffs was temporarily suspended and even terminated.¹¹⁵³ In order to guarantee the supply for domestic applications, exports of hydrocarbon were also restricted.¹¹⁵⁴ From foreign investors' perspective, those measures taken by Argentina infringed their rights. This led to them initiating ISA under the ICSID rules and claiming that Argentina had violated its obligations stipulated in the Argentina-US BIT (1991).¹¹⁵⁵

5.2.3 Conflicts between the Disputing Parties' Legitimate Expectations

Those measures, more or less, contributed to the resolution of Argentina's economic crisis but led to its conflicts with foreign investors. As claimed by investors, the government's reactions to the crisis adversely impaired their rights that they felt should have been protected and guaranteed by the state, such as the protection provided by FET. They pointed out that Argentina had almost thoroughly altered the stability and predictability of the investment environment based on which they made investments in Argentina.¹¹⁵⁶ In contrast, Argentina argued that all its responses aimed to settle the economic crisis and maintain public order. Particularly the "pesification" was a necessary measure to prevent a worse situation and poverty and return to a stable economy in entire Argentina.¹¹⁵⁷ In its view, such measures could be justified based on the invocation of the necessity under Article XI of the treaty and Article 25 of the Wrongful Act. It argued that the measures implemented "were reasonable and proportional" to the desired purpose.¹¹⁵⁸

As stipulated in Article II (2) (a) of the Argentina-US BIT (1991),¹¹⁵⁹ which is the applicable legal instrument in all six Argentinian cases, the investments made by foreign investors "shall at all times be accorded fair and equitable treatment" by the host state,¹¹⁶⁰ including the protection of their legitimate expectations.¹¹⁶¹ Schönberg points out that in the context of international investment, one of the foreign investors' expectations is the stability of the host state's legal and business framework.¹¹⁶² They would

¹¹⁵¹ *LG&E v. Argentina* (n 5) para 64.

¹¹⁵² *ibid.*

¹¹⁵³ For example, *CMS v. Argentina* (n 5) para 60.

¹¹⁵⁴ For example, *El Paso v. Argentina* (n 5) paras 95, 105.

¹¹⁵⁵ Argentina-US BIT (n 120).

¹¹⁵⁶ *CMS v. Argentina* (n 5) paras 267-9.

¹¹⁵⁷ *ibid.* *LG&E v. Argentina* (n 5) para 67.

¹¹⁵⁸ *CMS v. Argentina* (n 5) para 288.

¹¹⁵⁹ Argentina-US BIT (n 120) Article II (2) (a).

¹¹⁶⁰ *ibid.*

¹¹⁶¹ See 4.4.2 in Chapter Four. *Saluka v. Czech Republic* (n 84) para 302.

¹¹⁶² *supra* note 1039.

expect the host state's legal framework would stay the same as it was when they decided to make investments.¹¹⁶³ Therefore, they can rely on such a stable framework to plan their activities as to investments in advance and predict the corresponding results.¹¹⁶⁴

Underpinning the claims by foreign investors in these Argentinian cases, the legal and business framework they relied on to make investments had been dismantled.¹¹⁶⁵ In order to attract foreign investors and promote its privatisation, the Government of Argentina provided attractive conditions in the BIT and the domestic laws, such as the Gas Law. One of those treatments was the guarantee as to the tariffs. As stated by the Argentine Government, the tariffs "would be calculated in US dollars" and "would be subjected to semi-annual adjustments according to the US PPI".¹¹⁶⁶ The foreign investors who participated in the privatisation of public services in Argentina and made relevant investments, such as gas transport and distribution centre, clarified that those assurances were why they invested in relevant industries in Argentina.¹¹⁶⁷

With consideration of the treaty preamble, which emphasises "to maintain a stable framework for investments and maximum effective use of economic resources", the tribunal in *CMS*¹¹⁶⁸ pointed out that "a stable legal and business environment" is an essential element of FET.¹¹⁶⁹ As it stated, FET was closely linked to "stability and predictability".¹¹⁷⁰ In these cases, the guarantees provided by Argentina, like "the tariff regime and its relationship with a dollar standard and adjustment mechanisms", played a significant role in foreign investors' investment decisions.¹¹⁷¹

However, the measures taken by Argentina, in particular the promulgation of the Emergency Law, to react to the crisis broke those guarantees. This law not only revoked the PPI adjustments but also calculated the tariffs in Argentine pesos rather than US dollars.¹¹⁷² As claimed by foreign investors, their rights were impaired by such actions.¹¹⁷³ For example, the changes in the tariffs negatively affected their return from investments, which was the opposite of their expectations.¹¹⁷⁴ Consequently, they brought claims against Argentina under the ICSID rules and stated that the host state had violated its treaty obligations, including the protection of foreign investors' legitimate expectations provided by FET. Tribunals found that the guarantees, which were provided to foreign investors and vital for their

¹¹⁶³ *ibid.*

¹¹⁶⁴ *ibid.*

¹¹⁶⁵ See an example *CMS v. Argentina* (n 5) para 286.

¹¹⁶⁶ *LG&E v. Argentina* (n 5) para 119.

¹¹⁶⁷ *CMS v. Argentina* (n 5) paras 267-9. *LG&E v. Argentina* (n 5) para 52.

¹¹⁶⁸ *Argentina-US BIT* (n 120).

¹¹⁶⁹ *CMS v. Argentina* (n 5) para 274.

¹¹⁷⁰ *ibid* paras 276, 284.

¹¹⁷¹ *CMS v. Argentina* (n 5).

¹¹⁷² *LG&E v. Argentina* (n 5) paras 65, 108.

¹¹⁷³ *ibid* para 120.

¹¹⁷⁴ *ibid.*

investment decisions, had been altered.¹¹⁷⁵ Therefore, Argentina had breached its FET obligation, which was situated in Article II (2) (a) of the BIT.¹¹⁷⁶

As analysed previously, it is unreasonable to expect that a state's legal and business framework remains indefinitely unchanged. In order to be protected, instead of being subjectively decided by investors themselves,¹¹⁷⁷ the expectations should be reasonable and legitimate in light of the whole circumstances.¹¹⁷⁸ These considerations refer to investment protection and the host state's legitimate expectations, such as its power to react to the constantly changing circumstances and protect its public welfare.¹¹⁷⁹ In these cases, Argentina, as a host state, expected that foreign investors would exercise due diligence before making investments;¹¹⁸⁰ As a sovereign nation, it had expectations that it could exercise regulatory power for the public interest. Therefore, in Argentina's view, all measures it implemented were necessary to solve its economic crisis.¹¹⁸¹ It argued that the challenged means could be justified by invoking the necessity based on Article XI of the Argentina-US BIT (1991)¹¹⁸² and Article 25 of the Wrongful Act.¹¹⁸³

That is to say, one of the disputed issues in these cases is the discord between the legitimate expectations of foreign investors and the host state, or, more specifically, the conflicts between investors' expectations of the stability of the state's legal and business framework and the host state's right to change its laws and regulations to react to the changing circumstances. In such a situation, a balance needs to be struck to protect both parties' values, which can be achieved by using proportionality as a suitable tool if it can be brought into and applied in the ISDS.¹¹⁸⁴

5.3 The Interpretation of Proportionality in the Argentinian Cases

Based on the earlier discussion, proportionality can be adopted to balance competing values by interpreting its textual basis in the case-related treaty, either implicit or explicit. This route to its application can be seen in the Argentinian cases. Although the term "proportionality" was not in the Argentina-US BIT (1991),¹¹⁸⁵ its application was expressed by the systemic treaty interpretation. This section will analyse what wording or language can be the textual basis of proportionality. The uncertainties as to proportionality analysis from the perspective of treaty interpretation, such as the

¹¹⁷⁵ *CMS v. Argentina* (n 5) para 275.

¹¹⁷⁶ *ibid* para 281.

¹¹⁷⁷ *Saluka v. Czech Republic* (n 84) para 304.

¹¹⁷⁸ *ibid*.

¹¹⁷⁹ *Levashova* (n 1073) 238.

¹¹⁸⁰ *Sempra v. Argentina* (n 5) para 289.

¹¹⁸¹ *ibid* para 122.

¹¹⁸² Argentina-US BIT (n 120) Article XI.

¹¹⁸³ Wrongful Act (n 422) Article 25.

¹¹⁸⁴ See generally in Chapter Two.

¹¹⁸⁵ Argentina-US BIT (n 120).

undefined criteria for "necessity", will also be discussed to ascertain its application in striking a balance in the investor-state relationship.

5.3.1 The Textual Basis of Proportionality

The principle of proportionality can be reflected in the wording of the Argentina-US BIT (1991).¹¹⁸⁶ One textual basis is Article XI, namely the exception clause.¹¹⁸⁷ This provision explicitly mentions the term "necessary", corresponding to the necessity test, which is one essential element of proportionality.¹¹⁸⁸ Alternatively, through the systemic interpretative approach, interpreting substantive treatments provided to foreign investors in conjunction with Article XI expresses a balance between competing values, reflecting the notion of proportionality, in particular proportionality *stricto sensu*, a value-oriented factor contained in proportionality.¹¹⁸⁹

Professor Brontons asserts that Article XI of the treaty is a safeguard clause, excluding the application of substantive treaty provisions when the measures are implemented.¹¹⁹⁰ As stipulated,

This treaty shall not preclude the application by either party of measures *necessary for the maintenance of public order*, the fulfilment of its obligations with respect to *the maintenance or restoration of international peace or security*, or *the protection of its own essential security interests*.¹¹⁹¹ [italic added]

This provision lists three exceptional situations in which, even though the measures taken by the host state are against its obligations *vis-à-vis* foreign investors, they are not violations of the treaty.¹¹⁹² The wording, particularly the adjective "necessary", indicates the limits on the implemented measures. Based on the interpretative rules previously analysed, the plain meaning of the questioned term is the starting point of interpretation.¹¹⁹³ As defined in the dictionary, "necessary" describes an action that "needs to be done" or "is done in order to achieve the desired result or effect",¹¹⁹⁴ conveying a means-end connection. Based on the earlier discussion in Chapter Two, a reasonable and close relationship between the implemented measures and the pursued purpose is required by suitability and necessity, which are elements of proportionality.¹¹⁹⁵ In other words, the term "necessary" prescribed in the exception clause at least expresses the necessity test contained in proportionality analysis.

¹¹⁸⁶ *ibid.*

¹¹⁸⁷ *ibid* Article XI.

¹¹⁸⁸ See 2.4.3 in Chapter Two.

¹¹⁸⁹ See 2.4.4 in Chapter Two.

¹¹⁹⁰ *Mobil v. Argentina*, ICSID Case No. ARB/04/16, Separate Opinion of Professor Antonio Remiro Brontons, 27 March 2013, paras 7, 8, 12. *Continental v. Argentina* (n 5) para 164.

¹¹⁹¹ Argentine-US BIT (n 120) Article XI.

¹¹⁹² *Mobil v. Argentina* (n 1190).

¹¹⁹³ See 3.3.2 in Chapter Three

¹¹⁹⁴ 'Necessary' (*OED*) <<https://www.oed-com.ezproxy-s2.stir.ac.uk/view/Entry/125629?redirectedFrom=necessary#eid>> accessed on 11 January 2022.

¹¹⁹⁵ See 2.4 in Chapter Two.

A similar term, "necessity", presenting a means-end connection, can be seen in Article 25 of the Wrongful Act, which was another basis on which the tribunals in these cases considered whether Argentina could be exempted from liability. As stipulated,

1. Necessity may not be invoked by a state as a ground for precluding the wrongfulness of an act not in conformity with an international obligation of that state unless the act:
 - (a) is *the only way* for the state to safeguard *an essential interest against a grave and imminent peril*; and
 - (b) does not seriously impair an essential interest of the state or states towards which the obligation exists, or of the international community as a whole.
2. In any case, necessity may not be invoked by a State as a ground for precluding wrongfulness if:
 - (a) the international obligation in question excludes the possibility of invoking necessity, or
 - (b) the state *has contributed to the situation of necessity*.¹¹⁹⁶ [italic added]

Based on the interpretative rules, the wording of Article 25 differs from that of the exception clause of the BIT, explicitly expressing "the only way" criterion for invoking necessity.¹¹⁹⁷ However, as discussed in 5.3.3, the lack of defined criteria for "necessary" in Article XI of the BIT¹¹⁹⁸ leads to heated debates over its relationship with "the state of necessity" under Article 25. Their muddled relationship resulted in the tribunals' different decisions on the questioned measures taken by Argentina to react to the economic crisis.¹¹⁹⁹

Apart from the ordinary meaning, the context in which the term appears and the object and purpose of the treaty should also be considered at the time of treaty interpretation.¹²⁰⁰ The notion of proportionality can be expressed by interpreting the Argentina-US BIT (1991)¹²⁰¹ through the systemic approach. More specifically, proportionality can be expressed by interpreting the provision of substantive treatments, like FET, in conjunction with the exception clause. The importance of such a balanced interpretative approach was stressed by the tribunal in *El Paso*.¹²⁰² As it emphasised, "both state sovereignty and the state's responsibility to create an adapted and evolutionary framework for the development of economic activities, and the necessity to protect foreign investment and its contributing flow" should be considered when interpreting treaty provisions.¹²⁰³

Similarly, the tribunal in *CMS*¹²⁰⁴ determined that treaty provisions should be understood in a balanced

¹¹⁹⁶ Wrongful Act (n 422) Article 25.

¹¹⁹⁷ Text to 5.3.3.

¹¹⁹⁸ Argentina-US BIT (n 120).

¹¹⁹⁹ Text to 5.4.2.

¹²⁰⁰ See in Chapter Three. Vienna Convention (n 47) Article 31.

¹²⁰¹ Argentina-US BIT (n 120).

¹²⁰² *El Paso v. Argentina* (n 5).

¹²⁰³ *ibid* para 650.

¹²⁰⁴ *CMS v. Argentina* (n 5).

way, in which both parties' concerns should be considered.¹²⁰⁵ This interpretative process refers to weighing and balancing the conflicting values of foreign investors and the host state, corresponding to the requirement of proportionality *stricto sensu*.¹²⁰⁶ Based on the earlier discussion in Chapter Three, proportionality *stricto sensu* is also used in treaty interpretation to balance the different purposes of treaty provisions based on their social importance, contributing to the real balanced treaty interpretation.¹²⁰⁷

In these Argentinian cases, the conflicting values are, on the one hand, the protection of foreign investors' legitimate expectations of the stable legal framework in Argentina and, on the other hand, the legitimate right of the Argentine Government to exercise its regulatory power to react to the economic crisis and protect the public interest. From the perspective of foreign investors, their rights can be observed in the treaty preamble and the provisions of substantive treatments. For example, the protection of foreign investors' legitimate expectations, in particular of the stability of the host state's legal framework, can be seen in the preamble and Article II (2) (a) of the BIT.¹²⁰⁸ Based on the general conclusion on FET's constituent elements in Chapter Four, the protection of legitimate expectations is included in this standard.¹²⁰⁹ In *CMS*,¹²¹⁰ the tribunal pointed out that foreign investors have legitimate expectations, particularly of the stable legal and business framework.¹²¹¹ Considering the preamble, which explicitly stresses the significance of "a stable framework" for investment,¹²¹² the tribunal highlighted that a stable framework is an essential factor of FET.¹²¹³ In *LG&E*,¹²¹⁴ the tribunal also interpreted that stability of the legal and business framework is an essential element of FET by interpreting the treaty as a whole.¹²¹⁵ If what foreign investors legitimately expected from the host state was relied on by them when making investments, such legitimate expectations fall into the category of values protection by FET.¹²¹⁶ The guarantee provided to foreign investors, such as the tariffs, were vital for their investments. However, the commitments were altered, failing to protect their legitimate expectations.¹²¹⁷ In the view of foreign investors, Argentina failed to guarantee the stability of its legal framework and fulfil its treaty obligations to them. Consequently, they brought cases against Argentina according to the ICSID rules.

¹²⁰⁵ *ibid* para 360, the tribunal also stressed the significance of a balanced understanding of Article XI, in which both parties' concerns should be considered.

¹²⁰⁶ See 2.4.4 in Chapter Two.

¹²⁰⁷ See generally in Chapter Three.

¹²⁰⁸ Argentina-US BIT (n 120) Article II (2) (a).

¹²⁰⁹ See 4.4.2 in Chapter Four.

¹²¹⁰ *CMS v. Argentina* (n 5).

¹²¹¹ *ibid* paras 274-81.

¹²¹² Argentina-US BIT (n 120) Preamble.

¹²¹³ See examples *Enron v. Argentina* (n 5) para 259. *CMS v. Argentina* (n 5) para 274. *LG&E v. Argentina* (n 5) para 124.

¹²¹⁴ *LG&E v. Argentina* (n 5).

¹²¹⁵ *ibid* para 124.

¹²¹⁶ *ibid* para 127.

¹²¹⁷ *CMS v. Argentina* (n 5) paras 274-81.

Nevertheless, from the perspective of the host state, all measures it took attempted to manage the economic crisis as well as maintain public order and protect essential security interests,¹²¹⁸ as argued by Argentina, could be justified based on Articles IV (3) and XI of the BIT.¹²¹⁹ Article IV (3) prescribes that,

Nationals or companies of either party whose investments suffer losses in the territory of the other party *owing to war or other armed conflicts, revolution, state of national emergency, insurrection, civil disturbance or other similar events* shall be accorded treatment by such other party no less favourable than that accorded to its own nationals or companies or to nationals or companies of any third country, whichever is the more favourable treatment, as regards any measures it adopts in relation to such losses.¹²²⁰ [italic added]

In Argentina's view, this provision should be broadly interpreted and understood.¹²²¹ All essential interests mentioned should not only refer to the existence of a state but also include other emergencies.¹²²² In this respect, the Argentine economic crisis of 2001/2 fell into this category.¹²²³ Then, as defended by Argentina, it could be exempted from liability.

However, as criticised by Professor Alvarez, instead of an exemption, additional protections for foreign investors are provided in Article IV (3).¹²²⁴ The language expresses that the treatment shall be "no less favourable than that accorded to its own nationals or companies of any third country", indicating that the minimum treatments afforded to investors are still guaranteed even under the situations of the events listed.¹²²⁵ The tribunal in *CMS*¹²²⁶ also pointed out that such a clause provided "a floor treatment" to investors.¹²²⁷ As stated, Article IV (3) aimed to guarantee non-discrimination under the actions taken to offset or minimise the losses suffered by foreign investors. Therefore, this provision aims to provide investment protection rather than exceptional situations in which the state's measures can be justified, even if they do not accord with treaty obligations *vis-à-vis* foreign investors.

Unlike Article IV (3), Article XI of the treaty,¹²²⁸ another basis for Argentina's defence, focuses on protecting the state's public interest. As explicitly prescribed, the purposes pursued include "the maintenance of public order", "the maintenance or restoration of international peace or security", and "the protection of its own essential security interests".¹²²⁹ The means implemented should be

¹²¹⁸ *CMS v. Argentina* (n 5) para 272. *LG&E v. Argentina* (n 5) para 67.

¹²¹⁹ Argentina-US BIT (n 120) Preamble, Articles IV (3) and XI.

¹²²⁰ *ibid* Article IV (3).

¹²²¹ *Sempra v. Argentina* (n 5).

¹²²² *ibid* para 357.

¹²²³ *ibid*.

¹²²⁴ *Sempra v. Argentina* (n 5) para 364.

¹²²⁵ *ibid* paras 320-1.

¹²²⁶ *CMS v. Argentina* (n 5).

¹²²⁷ *ibid* para 375.

¹²²⁸ Argentina-US BIT (n 120) Article XI.

¹²²⁹ *ibid*.

"necessary" to achieve the aims listed. Once the measures in question fulfil these requirements provided in Article XI, there are no violations of the treaty, even if such means contravene the state's treaty obligations.¹²³⁰

According to the systemic interpretative approach,¹²³¹ both investment and non-investment values should be taken into account at the time of interpreting treaty provisions. That is to say, the provision of FET should be interpreted in conjunction with considering other provisions of the same BIT signed between Argentina and the US, including Article XI.¹²³² Based on the combined description of these provisions, the rights of foreign investors and the host state's power to regulate in the public interest counterbalance each other. Against this background, to investigate whether a measure implemented by the host state has violated its treaty obligation, the values of both sides should be considered: investment protection on the one side and the protection of the state's public interest on the other side.

Based on the interpretation of FET in conjunction with Article XI, the legitimate expectations of investors are protected based on FET, but such protections may be limited when the state's values are at stake. Meanwhile, these limits are restricted by the requirements as the legitimacy of the measures and the pursued purposes, which are required by the suitability test contained in proportionality analysis.¹²³³ As reflected by the adjective "necessary", the limits are also restricted by the necessity requirement.¹²³⁴ Although there is no explicit expression, as analysed later, the application of invoking necessity refers to the real balance against the conflicting values, corresponding to proportionality *stricto sensu*.¹²³⁵ In this respect, the joint interpretation of substantive treatments and exception clauses reflects a process of balancing any competing values, namely the application of proportionality.

However, issues arise within the process of applying proportionality because of ambiguous exception clauses. Due to the lack of qualifying language, the first uncertainty is the nature of the exception clause, namely Article XI of the treaty, leading to heated debates over who, the host state or the tribunal, has the power to make critical decisions on whether the state's value is at stake and needs to be protected by particular actions. At the same time, the lack of defined criteria which can be utilised to assess what measures are necessary emphasises the uncertain relationship between two criteria for "necessity": "the only way means" or "the less restrictive measure".¹²³⁶

5.3.2 Who Is the Decision-Maker?

¹²³⁰ *Mobil v. Argentina*, ICSID Case No. ARB/04/16, Decision on Jurisdiction and Liability, 10 April 2013.

¹²³¹ See generally in Chapter Three.

¹²³² Argentina-US BIT (n 120) Article XI.

¹²³³ See 2.4.1 and 2.4.2 in Chapter Two.

¹²³⁴ See 2.4.3 in Chapter Two.

¹²³⁵ See 2.4.4 in Chapter Two.

¹²³⁶ These two criteria for necessity were mentioned in Chapter Two. See 2.4.3 in Chapter Two.

Unlike its application in the domestic jurisdiction, in the context of international investment, who has the power to decide vital issues within the process of proportionality analysis raises debates. The answer is closely linked to the nature of the exception clause and more or less affects the actual application of proportionality in practice.

Based on the wording of Article XI of the Argentina-US BIT (1991),¹²³⁷ the lack of qualifying language is evident. As a result, one may question whether this provision is self-judging or not.¹²³⁸ If not, the tribunals have the power to decide whether there is an exceptional situation in which the state can invoke necessity and needs to be settled by certain measures.¹²³⁹ Otherwise, the state itself is the important decision-maker,¹²⁴⁰ while the tribunals can merely review whether it is acting in good faith.¹²⁴¹

As defended by Argentina in these cases, the consensus of the contracting parties to the Argentina-US BIT (1991) was that Article XI is a self-judging provision. It asserted that the ambiguity of this provision is a strategy purposely adopted by the US.¹²⁴² Concluded from other BITs signed by the US with another contracting party, it was Argentina's view that the exception clause was regarded by the US as a self-judging provision.¹²⁴³

Nevertheless, Argentina's viewpoint was supported by none of the tribunals in these cases. Instead, they asserted that Article XI was not self-judging.¹²⁴⁴ On the one hand, the plain meaning of the wording "measures necessary" provides no detail on the decision-maker.¹²⁴⁵ On the other hand, as required by Article 31 (4) of the Vienna Convention, "[a] special meaning shall be given to a term if it is established that the parties so intended".¹²⁴⁶ If Argentina and the US reached a consensus that Article XI is a self-judging provision, such an intention should be explicitly expressed in the treaty.¹²⁴⁷ The tribunal further clarified that based on the comparison between the Argentina-US BIT (1991) and the Russia-US BIT (1992).¹²⁴⁸ Unlike the former, the latter explicitly stipulated that "parties confirm their mutual understanding that whether a measure is undertaken by a party to protect its essential security interests

¹²³⁷ Argentina-US BIT (n 120) Article XI.

¹²³⁸ Andrea K. Bjorklund, 'Emergency Exceptions: State Necessity and Force Majeure' in Peter Muchlinski, Federico Ortino, & Christoph Schreuer (eds), *The Oxford Handbook for International Investment Law* (OUP 2008) 503-6.

¹²³⁹ Stephan Schill & Robyn Briese, "'If the State Considers': Self-Judging Clause in International Dispute Settlement' (2009) 13 Max Planck Yearbook of United Nations Law 61, 110-3. Bjorklund (n 1238) 503-6. *CMS Award* (n 5) paras 373-4.

¹²⁴⁰ Schill & Briese (n 1239) 67-9. Bjorklund (n 1238) 503-6.

¹²⁴¹ Schill & Briese (n 1239) 110-3. Bjorklund (n 1238) 503-6.

¹²⁴² *LG&E v. Argentina* (n 5) para 209.

¹²⁴³ *ibid.*

¹²⁴⁴ *LG&E v. Argentina* (n 5) paras 212-3. *CMS v. Argentina* (n 5) paras 366-73. *Continental v. Argentina* (n 5) paras 187-8. *Enron v. Argentina* (n 5) paras 335-9.

¹²⁴⁵ *LG&E v. Argentina* (n 5) paras 211-2. *Enron v. Argentina* (n 5) para 335.

¹²⁴⁶ Vienna Convention (n 47) Article 31 (4).

¹²⁴⁷ *CMS v. Argentina* (n 5) para 370.

¹²⁴⁸ Russia-US BIT (signed 17 June 1992, but still pending).

is *self-judging*" in the protocol.¹²⁴⁹ Based on the interpretative rules, protocol as part of the treaty should also be taken into account at the time of treaty interpretation. The term "self-judging" stipulated in the protocol explicitly expresses that both the US and Russia recognise the self-judging exception clause, but such a term does not appear in the Argentina-US BIT (1991).¹²⁵⁰

As mentioned by the tribunal in *Sempra*,¹²⁵¹ another type of qualifying language that indicates the self-judging nature of the exception clause can be seen in Article XXI of the GATT,¹²⁵² which provides that,

Nothing in this agreement shall be constructed

- (a) to require any contracting party to furnish any information the disclosure of which *it considers* contrary to its essential security interests; or
- (b) to prevent any contracting party from taking any action which *it considers* necessary for the protection of its essential security interests...¹²⁵³ [*italic added*]

As stressed by the tribunal, the wording of a provision should be precise if such a clause expresses a specific meaning.¹²⁵⁴ The phrase "it considers" in Article XXI explicitly reflects that the state has such power to examine the facts and decide what measures fulfil the requirements of necessity. However, neither the term "self-judging" nor the wording "it considers" appears in the Argentina-US BIT (1991),¹²⁵⁵ compared with the Russia-US BIT (1992),¹²⁵⁶ which was utilised by Argentina to support its defence. Both treaties contain the same exception clause, but the Argentina-US BIT (1991)¹²⁵⁷ differs in that it has no mention of "self-judging" which is prescribed in the protocol of the US BIT signed with Russia.¹²⁵⁸ Such a vital difference implies Article XI of the Argentina-US BIT (1991) as a not self-judging provision.

Moreover, based on analysing and comparing three different versions of the exception clause stipulated in the US BITs, Alvarez concluded that the US knew how to explicitly express its intention if it regarded such a clause as a self-judging provision.¹²⁵⁹ Every treaty only reflects the negotiations between particular contracting parties. Even if the US changed its attitude to the exception clause in the BIT signed with Russia, this could not prove that it had the same intention when it concluded a treaty with Argentina, which predated the former. Therefore, the absence of qualifying language in the Argentina-

¹²⁴⁹ *Sempra v. Argentina* (n 5) para 29 [*italic added*]. *CMS v. Argentina* (n 5) para 370.

¹²⁵⁰ *CMS v. Argentina* (n 5) paras 368-73.

¹²⁵¹ *Sempra v. Argentina* (n 5).

¹²⁵² General Agreement on Tariffs and Trade (1947).

¹²⁵³ *ibid* Article XXI "Security Exceptions".

¹²⁵⁴ *Sempra v. Argentina* (n 5) para 383.

¹²⁵⁵ Argentina-US BIT (n 120).

¹²⁵⁶ Russia-US BIT (n 1248).

¹²⁵⁷ Argentina-US BIT (n 120).

¹²⁵⁸ Russia-US BIT (n 1248).

¹²⁵⁹ *Sempra v. Argentina*, ICSID Case No. ARB/02/16, Opinion of José E. Alvarez, 12 September 2005, para 34.

US BIT (1991) indicates that the US regarded Article XI as a not self-judging provision.¹²⁶⁰ In other words, it should be the tribunals to make critical decisions within the process of applying proportionality to review the state's disputed measures.

Furthermore, as emphasised by the tribunal in *El Paso*,¹²⁶¹ even if Article XI is self-judging, this character is solely limited to "the essential security interests"¹²⁶² because only this type of value is modified by the language "its own".¹²⁶³ Without the modifier, other values, which refer to "the maintenance of public order" and "the maintenance or restoration of international peace or security",¹²⁶⁴ are still not self-judging. According to the comprehensive understanding of the circumstances in Argentina, the tribunal pointed out that the economic crisis in Argentina fell into the latter category, in which the tribunal should be the decision-maker.¹²⁶⁵ Consequently, the tribunals were the decision-maker and had the power to make critical decisions in the process of proportionality analysis.

Based on such examinations, it is the researcher's view that the decision-maker, who can decide whether the state's values are at stake and is forced to take actions to meet changing circumstances, all depends on the wording of a treaty. If the contracting parties intend to be the decision-maker, they should express this intention precisely and explicitly by utilising language such as "it considers necessary" or "self-judging". Otherwise, the lack of qualifying language may result in the conclusion that the tribunal is the decision-maker, as shown in these Argentinian cases.

Nevertheless, one may question the tribunal's capacity to carry out the substantive review of the disputed means.¹²⁶⁶ As held by Vadi, the tribunals' role as the decision-maker raises doubts over the application of proportionality in the ISDS.¹²⁶⁷ Compared with the host state, they have no comprehensive knowledge and information as to the state to make critical decisions, in particular in emergencies.¹²⁶⁸ Also, they may benefit from hindsight, based on which the means implemented may have been replaced by alternative measures that are more suitable in the tribunals' view.¹²⁶⁹ Such doubts can be seen in Argentinian cases. As analysed below, all tribunals regarded Article XI as not a self-judging provision, but they reached different conclusions on whether Argentina met the requirements of necessity to justify the measures implemented to react to the economic crisis due to their different capacities and understandings of the crisis and the invocation of necessity.

¹²⁶⁰ *Sempra v. Argentina* (n 774) para 204. *Mobil v. Argentina* (n 1230) paras 1037-56.

¹²⁶¹ *El Paso v. Argentina* (n 5).

¹²⁶² *ibid* para 588.

¹²⁶³ *Argentina-US BIT* (n 120) Article XI.

¹²⁶⁴ *ibid*.

¹²⁶⁵ *El Paso v. Argentina* (n 5) para 588.

¹²⁶⁶ Vadi, 'The Migration' (n 196) 337, 353.

¹²⁶⁷ *ibid*.

¹²⁶⁸ *ibid*.

¹²⁶⁹ *ibid*.

5.3.3 The Criterion for Necessity

Within the process of applying proportionality, issues arose from the lack of a defined criterion for "necessity" in the treaty. Based on the earlier discussion on proportionality, the criteria that can be utilised to assess whether the questioned actions fulfil the necessity test are "the only way" and "the less restrictive means".¹²⁷⁰

A prime example of the former criterion is Article 25 of the Wrongful Act.¹²⁷¹ Based on the wording, in particular the phrase "the only way", it is evident that the measures taken by the state should be the only measure that could be adopted to achieve the desired purpose. Otherwise, it fails to be necessary. Meanwhile, the adjectives "grave" and "imminent" reflect that the pursued purpose should be urgent and must be achieved immediately, which are not required by the necessity test included in the application of proportionality. In this respect, the necessity in Article 25 is more stringent and stricter, compared with that in Article XI. The latter, as the exception clause in the BIT, merely lists three types of pursued purposes without more detail.

Another criterion for necessity, as analysed in Chapter Two, is "the less restrictive means", proving the necessity of the implemented measures by excluding other alternative measures.¹²⁷² More specifically, this criterion requires that, compared with other measures that achieve the same purpose, the actions that were taken should make the same contribution with less cost, specifically limits on individual rights.¹²⁷³ The prerequisite for excluding the alternatives is the existence of its alternative measures. Therefore, in the researcher's view, "the less restrictive means" test, in fact, contains "the only way" test in particular circumstances. As a criterion for necessity, "the less restrictive means" is more reasonable than "the only way".¹²⁷⁴

However, based on the later discussion in 5.4.2, the differences in the wording of Article XI of the BIT and Article 25 of the Wrongful Act were omitted by some tribunals in the Argentinian cases.¹²⁷⁵ They utilised the criterion "the only way" provided in Article 25 to review whether the questioned measures were justified based on the necessity in Article XI,¹²⁷⁶ leading to issues of the actual application of proportionality.

¹²⁷⁰ See 2.4.3 in Chapter Two.

¹²⁷¹ Text to 5.3.1.

¹²⁷² See 2.4.3 in Chapter Two.

¹²⁷³ See 2.4.3 in Chapter Two.

¹²⁷⁴ See 2.4.3 in Chapter Two.

¹²⁷⁵ Text to 5.4.2.

¹²⁷⁶ Text to 5.4.2.

5.4 The Application of Proportionality in the Argentinian Cases

Based on the earlier discussion in Chapter Two, the whole process of proportionality analysis contains three consecutive tests, examining suitability, necessity, and proportionality *stricto sensu*, respectively.¹²⁷⁷ This section will analyse the tribunals' reasoning in the Argentinian cases following such an internal logic of proportionality. Consequently, the application of proportionality, as used in practice to balance the competing values of foreign investors and the host state, will be presented and examined. The differences between its application from theoretical and practical perspectives will also be highlighted, contributing to the further discussion on its application in the settlement of Chinese ISDs.

In *CMS*,¹²⁷⁸ *Sempra*,¹²⁷⁹ *Enron*,¹²⁸⁰ and *El Paso*,¹²⁸¹ the review of the disputed measures taken by Argentina terminated at the stage of the necessity test because, as pointed out by the tribunals, the means failed to meet the requirements of invoking necessity to be justified. Conversely, in *LG&E*¹²⁸² and *Continental*,¹²⁸³ the tribunal recognised the actions taken by Argentina and stressed that such measures were solely justifiable within a particular duration, namely the period of its economic crisis, based on weighing the competing values, emphasising the significance of proportionality *stricto sensu*.

5.4.1 The Suitability Test-A Rational Means-End Connection

As an essential element of proportionality, suitability requires the disputed means to contribute to achieving the pursued legitimate purpose, emphasising the significance of a reasonable means-end connection.¹²⁸⁴ Correspondingly, the suitability test examines whether the disputed actions do, in fact, achieve the desired purpose.¹²⁸⁵

Based on the analyses in Chapter Two, the impugned measures always fulfil the suitability test if the state acts in good faith.¹²⁸⁶ In these Argentinian cases, although the tribunals directly considered whether the disputed measures met the requirements of necessity stipulated in Article XI of the BIT or Article 25 of the Wrongful Act without a detailed review of the suitability, such a test was referred to. As Alvarez emphasised in *Sempra*,¹²⁸⁷ to invoke necessity, the existence of "a *nexus* between *the specific challenged actions* and *the maintaining public order or responding to a threat to its own essential*

¹²⁷⁷ See 2.5 in Chapter Two.

¹²⁷⁸ *CMS v. Argentina* (n 5).

¹²⁷⁹ *Sempra v. Argentina* (n 5).

¹²⁸⁰ *Enron v. Argentina* (n 5).

¹²⁸¹ *El Paso v. Argentina* (n 5).

¹²⁸² *LG&E v. Argentina* (n 5).

¹²⁸³ *Continental v. Argentina* (n 5).

¹²⁸⁴ See 2.4.1 and 2.4.2 in Chapter Two.

¹²⁸⁵ See 2.4.2 in Chapter Two.

¹²⁸⁶ See 2.4.2 in Chapter Two.

¹²⁸⁷ *Sempra v. Argentina* (n 5).

security interests or to international peace and security" should be proved.¹²⁸⁸ This not only expresses the requirement of a rational means-end connection corresponding to suitability but also stresses that the suitability test is a precondition for the test of necessity.

5.4.2 The Necessity Test—Confused with the State of Necessity

According to the internal sequence of proportionality, once the implemented measure is suitable to achieve the desired purpose, then whether it is necessary to pursue the legitimate purpose should be assessed.¹²⁸⁹ However, in the Argentinian cases, the tribunals' different understandings of "necessity" and its criterion created debates over whether Argentina's reactions were necessary to respond to its severe economic crisis. One issue is the muddled relationship between the necessity stipulated in Article XI of the BIT and the state of necessity prescribed in Article 25 of the Wrongful Act,¹²⁹⁰ while another is the lack of a defined criterion for "necessity" in the BIT. Due to such uncertainties, different awards were made by the tribunals on whether Argentina had violated its treaty obligations *vis-à-vis* foreign investors.

Compared with Article XI of the BIT, providing exceptional situations in which the host state's measures should not be precluded,¹²⁹¹ Article 25 is stricter and more stringent, requiring that the questioned means should be "the only way".¹²⁹² The importance and urgency of the desired purpose, which should be "grave" and "imminent", are also emphasised in Article 25.¹²⁹³ Article 25 (2) further prescribes that the invocation of necessity is restricted by two limits.¹²⁹⁴ As required, the questioned obligation should not preclude the possibility of invocation of necessity; Meanwhile, the state should not contribute to the state of necessity.¹²⁹⁵ Otherwise, the state of necessity cannot be invoked to justify the measures in question. However, these requirements are absent in Article XI.¹²⁹⁶ In this respect, the state of necessity in Article 25 of the Wrongful Act differs from the necessity in Article XI of the BIT. Compared with the latter, the former stipulates more detail, providing more stringent requirements for justifying the questioned measures based on the invocation of the state of necessity.

Moreover, Article XI of the BIT and Article 25 of the Wrongful Act should be applied to review the impugned measures with different natures, although both provisions refer to similar terms, namely "necessary" and "necessity". As pointed out by Kurtz, the preconditions and effects of applying these

¹²⁸⁸ *Sempra v. Argentina* (n 1259) para 47 [italic added].

¹²⁸⁹ See in Chapter Two.

¹²⁹⁰ *CMS v. Argentina* (n 5) para 374.

¹²⁹¹ *Argentina-US BIT* (n 124) Article XI.

¹²⁹² *Wrongful Act* (n 422) Article 25.

¹²⁹³ *ibid.*

¹²⁹⁴ *ibid* Article 25 (2).

¹²⁹⁵ *ibid.*

¹²⁹⁶ *Argentina-US BIT* (n 120) Article XI.

two clauses are different.¹²⁹⁷ Based on the wording of Article 25, the questioned measures should have violated the international obligation in question before invoking necessity.¹²⁹⁸ This can also be observed from the heading of the Wrongful Act as "internationally wrongful acts".¹²⁹⁹ In contrast, if the disputed measures meet the requirements of Article XI of the BIT, the state has not violated the treaty even if its actions contravene the obligation *vis-à-vis* foreign investors. So, the nature of the challenged means that are reviewed based on Article XI of the BIT and Article 25 of the Wrongful Act is different. The measures are still legal based on Article XI but not based on Article 25.

Nevertheless, the above differences between two provisions were omitted by some tribunals in the Argentinian cases, which confused Article XI of the BIT and Article 25 of the Wrongful Act in practice.¹³⁰⁰ According to their understanding of the relationship between these clauses, the tribunals can be divided into two groups. The tribunals in *CMS*,¹³⁰¹ *Sempra*,¹³⁰² and *Enron*,¹³⁰³ stated that no substantive differences existed between the provisions of necessity. However, this view was rejected by the tribunals in *El Paso*,¹³⁰⁴ *LG&E*,¹³⁰⁵ and *Continental*.¹³⁰⁶

In *CMS*,¹³⁰⁷ the tribunal firstly examined Argentina's measures in question based on the strict requirements in Article 25 of the Wrongful Act. As it pointed out, Argentina failed to meet the requirements from both affirmative and negative perspectives. Based on the earlier findings, in order to invoke necessity according to this provision, the emergence should be "a grave and imminent peril".¹³⁰⁸ The tribunal recognised that the economic crisis experienced by Argentina was severe, but it eschewed that such a crisis resulted in "a total economic and social collapse", which could trigger the state of necessity. Meanwhile, based on previous economic crises, the tribunal insisted that a variety of measures could have been applied to resolve the 2001/2 crisis.¹³⁰⁹ In this respect, the means taken by Argentina failed to be "the only way". Concerning the appropriate alternatives, the tribunal explained that its task was to decide whether the questioned measures were irreplaceable rather than find the appropriate one.¹³¹⁰ Therefore, in its view, Argentina failed to fulfil the requirements that should be met to invoke

¹²⁹⁷ Jürgen Kurtz, 'Adjudging the Exceptional at International Investment Law: Security, Public Order and Financial Crisis' (2010) 59 *International & Comparative Law Quarterly* 325, 337.

¹²⁹⁸ *ibid.*

¹²⁹⁹ Wrongful Act (n 422).

¹³⁰⁰ *CMS v. Argentina* (n 5) paras 308, 374. *CMS v. Argentina*, ICSID Case No. ARB/01/8, Decision of the *ad hoc* Committee on the Application for Annulment of the Argentine Republic, 25 September 2007, para 124. *Enron v. Argentina* (n 5). *Sempra v. Argentina* (n 5).

¹³⁰¹ *CMS v. Argentina* (n 5).

¹³⁰² *Sempra v. Argentina* (n 5).

¹³⁰³ *Enron v. Argentina* (n 5).

¹³⁰⁴ *El Paso v. Argentina* (n 5).

¹³⁰⁵ *LG&E v. Argentina* (n 5).

¹³⁰⁶ *Continental v. Argentina* (n 5).

¹³⁰⁷ *CMS v. Argentina* (n 5).

¹³⁰⁸ Wrongful Act (n 422) Article 25.

¹³⁰⁹ *CMS v. Argentina* (n 5) para 323.

¹³¹⁰ *ibid.*

necessity.

This tribunal further stated that Argentina also violated the limits that should be avoided to justify the impugned measures based on the state of necessity.¹³¹¹ As noted, the Government of Argentina had itself substantively contributed to the situation of necessity. More specifically, the tribunal pointed out that Argentina's economic crisis of 2001/2 was rooted in its earlier crises.¹³¹² The crisis was worsened due to the deficient policies and measures taken by the Argentine Government, reaching its peak in 2002.¹³¹³ Therefore, Argentina failed to meet the requirements in Article 25 of the Wrongful Act and so failed to be exempted from liability by invoking necessity based on this provision.

Furthermore, the tribunal stressed that Article XI of the BIT was the same as Article 25 of the Wrongful Act.¹³¹⁴ Consequently, Argentina's defence on the basis of the exception clause of the BIT was also rejected by the tribunal. Similar reasoning can be seen in *Sempra*¹³¹⁵ and *Enron*,¹³¹⁶ in which the tribunals concluded that Argentina failed to invoke necessity based on Article 25 of the Wrongful Act and Article XI of the BIT.¹³¹⁷

Nevertheless, the decisions made by those tribunals in Argentinian cases were criticised by their corresponding *ad hoc* committees,¹³¹⁸ who pointed out that the tribunals failed to distinguish Article XI of the Argentina-US BIT (1991) from Article 25 of the Wrongful Act.¹³¹⁹ Like the earlier discussion,¹³²⁰ the committees also emphasised the differences in the necessity stipulated in these two different provisions. It was the committees' view that Article XI of the treaty was a *lex specialis*, compared with Article 25 of the Wrongful Act, and should be adopted first to review the disputed measures.¹³²¹ Only when the exception clause is not applicable could Article 25 be applied to assess the means in question.¹³²²

That is to say, the tribunals in Argentinian cases should first examine whether Argentina had breached its treaty obligations. If the measures it took contravened its obligations *vis-à-vis* foreign investors, the tribunals then should consider whether they were justified by invoking necessity on the basis of Article XI of the BIT. If the answers are affirmative, such disputed means cannot be precluded because they

¹³¹¹ *ibid* paras 326-8.

¹³¹² *ibid* para 329.

¹³¹³ *ibid*.

¹³¹⁴ *CMS v. Argentina* (n 5).

¹³¹⁵ *Sempra v. Argentina* (n 5).

¹³¹⁶ *Enron v. Argentina* (n 5).

¹³¹⁷ *Sempra v. Argentina* (n 5) paras 349-50, 354, 388, 390. *Enron v. Argentina* (n 5) para 341.

¹³¹⁸ *CMS v. Argentina* (n 1300).

¹³¹⁹ *ibid* para 129-31.

¹³²⁰ Text to 5.3.1.

¹³²¹ *Sempra v. Argentina* (n 774) paras 115-6, 200, 203. Kurtz (n 1297) 344.

¹³²² *ibid*.

fall into the category of exceptional situations. Only if not should Article 25 of the Wrongful Act be adopted by the tribunals to review Argentina's challenged measures. This logical sequence between the application of Article XI of the BIT and Article 25 of the Wrongful Act, which should be followed, was ignored by the tribunals in *CMS*,¹³²³ *Sempra*,¹³²⁴ and *Enron*.¹³²⁵

Meanwhile, one noteworthy point in *Enron*,¹³²⁶ compared with *CMS*¹³²⁷ and *Sempra*,¹³²⁸ was that the *ad hoc* committee raised questions over the meaning of "the only way" required in Article 25 of the Wrongful Act.¹³²⁹ As it pointed out, this phrase could have two different meanings. The first one emphasised the irreplaceability of the implemented means.¹³³⁰ Based on this criterion, no other measures can be adopted to achieve the pursued purpose, which is "the only way" in the narrow sense. Another stressed that the questioned means, compared with its alternatives, can fulfil the same desired purpose with fewer limits, reflecting "the less restrictive means".¹³³¹ Such a view held by the *ad hoc* committee corresponds to the debates over the criteria for "necessity" discussed previously in Chapter Two,¹³³² reflecting the uncertainties of the defined criteria for "necessity".

Unlike the tribunals in those three cases, the tribunals in *LG&E*,¹³³³ *Continental*,¹³³⁴ and *El Paso*,¹³³⁵ explicitly emphasised the differences between Article XI of the Argentina-US BIT (1991) with Article 25 of the Wrongful Act. As stated, these two provisions provided different textual sources for Argentina to invoke necessity. In their view, the exception clause stipulated in the BIT should be applied first and be interpreted with the consideration of Article 25.¹³³⁶

For example, in *El Paso*,¹³³⁷ the tribunal clarified that Article 25 of the Wrongful Act contributed to the interpretation of Article XI of the BIT. More specifically, although no details of necessity were provided in the BIT, the tribunal in *El Paso* identified that "the state had not contributed to the situation of necessity",¹³³⁸ a requirement stipulated in Article 25 of the Wrongful Act, should be considered to

¹³²³ *CMS v. Argentina* (n 5).

¹³²⁴ *Sempra v. Argentina* (n 5).

¹³²⁵ *Enron v. Argentina* (n 5).

¹³²⁶ *ibid*.

¹³²⁷ *CMS v. Argentina* (n 5).

¹³²⁸ *Sempra v. Argentina* (n 5).

¹³²⁹ *Enron v. Argentina*, ICSID Case No. ARB/01/3, Decision on the Application for Annulment of the Argentine Republic, 30 July 2010, paras 369-72.

¹³³⁰ *ibid* 369.

¹³³¹ *ibid* 370.

¹³³² See 2.4.3 in Chapter Two.

¹³³³ *LG&E v. Argentina* (n 5).

¹³³⁴ *Continental v. Argentina* (n 5).

¹³³⁵ *El Paso v. Argentina* (n 5).

¹³³⁶ *Continental v. Argentina* (n 5) para 168. *El Paso v. Argentina* (n 5). *LG&E v. Argentina* (n 5).

¹³³⁷ *El Paso v. Argentina* (n 5).

¹³³⁸ *ibid* paras 649-65.

interpret "necessity" in the BIT.¹³³⁹ It regarded the non-substantial contributions of Argentina to its economic crisis of 2001/2 as a requirement of invoking necessity based on Article XI of the BIT. In arbitrator Stern's view, the claimant failed to provide solid evidence to prove that the economic crisis could be substantively attributed to the Argentine Government, which did not have strong effects on the economy, compared with the invisible hand of the market.¹³⁴⁰ However, by analysing and comparing different documents, the majority of the tribunal considered that the Argentine Government's failures to settle relevant issues, such as the fiscal deficit, were substantial contributions to its economic crisis of 2001/2.¹³⁴¹ Consequently, the tribunal decided that Argentina could not be exempted from liability based on Article XI of the Argentina-US BIT (1991).

Different from the tribunal in *El Paso*,¹³⁴² the tribunals in *LG&E*¹³⁴³ and *Continental*¹³⁴⁴ left a certain room for the host state.¹³⁴⁵ In *LG&E*,¹³⁴⁶ the tribunal explained that the exceptional situations stipulated in Article XI of the BIT¹³⁴⁷ caused conditions under which the state "has no choice but to act".¹³⁴⁸ As it pointed out, the whole situation in Argentina at the time of its economic crisis was "a total collapse of the Government and the Argentinian State".¹³⁴⁹ Social and economic development, even political survival, were threatened by such a crisis,¹³⁵⁰ which needed to be immediately and effectively handled.¹³⁵¹ Based on the tribunal's evaluation, the economic recovery package implemented by the Government of Argentina, as the means "across-the-board",¹³⁵² was the only way that could be applied during the period of economic crisis.¹³⁵³ In this respect, although the tribunal did not explicitly express its deference to Argentina, such reasoning at least reflected its recognition of Argentina's decision on the necessity of the challenged measures.

In *Continental*,¹³⁵⁴ the tribunal went further and explicitly stressed the significance of the margin of appreciation compared with *LG&E*.¹³⁵⁵ In its view, "a time of grave crisis is not the time for nice judgment", especially the arbitrators could benefit from hindsight if they made relevant decisions.¹³⁵⁶

¹³³⁹ *ibid* para 613. *Continental v. Argentina* (n 5) para 168.

¹³⁴⁰ *El Paso v. Argentina* (n 5) para 667.

¹³⁴¹ *ibid* para 656.

¹³⁴² *El Paso v. Argentina* (n 5).

¹³⁴³ *LG&E v. Argentina* (n 5).

¹³⁴⁴ *Continental v. Argentina* (n 5).

¹³⁴⁵ *ibid* para 181.

¹³⁴⁶ *LG&E v. Argentina* (n 5).

¹³⁴⁷ Argentina-US BIT (n 120) Article XI.

¹³⁴⁸ *LG&E v. Argentina* (n 5) para 239.

¹³⁴⁹ *ibid* para 231.

¹³⁵⁰ *ibid*.

¹³⁵¹ *ibid* paras 238, 257.

¹³⁵² *ibid* paras 238, 245, 257.

¹³⁵³ *ibid* para 257.

¹³⁵⁴ *Continental v. Argentina* (n 5).

¹³⁵⁵ *LG&E v. Argentina* (n 5).

¹³⁵⁶ *Continental v. Argentina* (n 5) para 181.

That is to say, compared with the tribunal, who has no comprehensive information and knowledge of the country, the state itself, namely Argentina in this case, should confirm that its reactions contributed to handling the crisis.¹³⁵⁷ It also emphasised that such measures were applied in "a reasonable and proportionate way" to solve the crisis,¹³⁵⁸ indicating a reasonable means-end connection and a proportionate relationship.

Based on the above analyses, the necessity test, as part of proportionality analysis, had been brought into the ISDS regime to settle the ISD by interpreting the term "necessary" stipulated in the exception clause in the BIT.¹³⁵⁹ However, due to the absence of qualifying language, its application raises various uncertainties, from its relationship with the state of necessity as an international custom to its undefined criterion. The tribunals' different understandings of these questions also result in different, even opposing, conclusions.

Among these cases, the tribunals in *CMS*,¹³⁶⁰ *Sempra*,¹³⁶¹ and *Enron*¹³⁶² regarded Article XI of the BIT as no different to Article 25 of the Wrongful Act. As they concluded, Argentina also failed to invoke the necessity based on Article XI due to its failure to meet the requirements provided in Article 25 of the Wrongful Act. Consequently, there was no need to weigh the investors' impaired values against the protected values in Argentina. By contrast, the tribunals in *LG&E* and *Continental* stated that the measures taken by Argentina were necessary to settle its economic crisis of 2001/2. However, they also emphasised that such invocation of necessity should be limited, implying the notion of proportionality *stricto sensu*.¹³⁶³

5.4.3 The Application of Proportionality *Stricto Sensu*

As the final step of proportionality analysis, proportionality *stricto sensu* is the real balance between competing values,¹³⁶⁴ seeking to ascertain whether the impairments of the affected right exceed the benefits of the achieved purpose. A measure has both positive and negative effects simultaneously once it is implemented. If its disadvantage outweighs its advantage, the whole situation would be worse, leading to doubts about the use of such means. Therefore, in order to strike the real balance between conflicting values, which is required by proportionality *stricto sensu*, the achievement, at least, should be equal to the cost.¹³⁶⁵

¹³⁵⁷ *ibid* para 197.

¹³⁵⁸ *Continental v. Argentina* (n 5).

¹³⁵⁹ *Argentina-US BIT* (n 120) Article XI.

¹³⁶⁰ *CMS v. Argentina* (n 5).

¹³⁶¹ *Sempra v. Argentina* (n 5).

¹³⁶² *Enron v. Argentina* (n 5).

¹³⁶³ *Kingsbury & Schill* (n 18) 87.

¹³⁶⁴ *ibid*.

¹³⁶⁵ *supra* note 441.

This requirement was referred to in *LG&E*¹³⁶⁶ and *Continental*,¹³⁶⁷ implicitly or explicitly. The tribunals in both cases recognised Argentina's defence as the invocation of necessity. They further stressed that such measures were solely justified within a particular duration. For example, as emphasised by the tribunal in *LG&E*,¹³⁶⁸ the necessity of Argentina's measures to maintain its essential security interests were merely limited to "the period of crisis".¹³⁶⁹ An exception in which Argentina failed to fulfil its obligations *vis-à-vis* foreign investors but did not violate treaty obligations is appropriate "only in emergency situations".¹³⁷⁰ The word "only" implies the strict time limit to invoke necessity. According to the real situation in Argentina, the tribunal explicitly pointed out the duration within which Argentina's means were necessary, and Argentina was exempted from 1 December 2001 to 16 April 2003.¹³⁷¹ The former is the time when Argentina's essential interests were threatened,¹³⁷² whereas the latter is the date on which President Kirchner was elected, initiating new stability in Argentina.¹³⁷³ As emphasised by the tribunal, Argentina should be responsible for its implemented reactions before and after the economic crisis,¹³⁷⁴ implying a balance between the reactions and their benefits and costs.

The application of proportionality *stricto sensu* can be seen more explicitly in *Continental*,¹³⁷⁵ compared with its application in *LG&E*.¹³⁷⁶ The tribunal in *Continental* pointed out that the Argentine Government had struck "an appropriate balance" between the protection of its essential security interest and the impairments of the rights of foreign investors.¹³⁷⁷ As examined by the tribunal based on the factual background in Argentina at the time of its economic crisis, all measures that were taken by the Government of Argentina, except the restructuring of the Treasury Bills, were applied in "a reasonable and proportionate" way to solve its economic crisis.¹³⁷⁸ It explained that, unlike other means, this measure was implemented after the settlement of Argentina's economic crisis. At that time, the situation in Argentina had gradually normalised, and the state of necessity ceased to exist.¹³⁷⁹ Therefore, such a measure exceeded what was necessary to protect Argentina's essential security interests, having been affected by the economic crisis of 2001/2. Consequently, Argentina should be responsible for the negative effects on foreign investors' rights.

¹³⁶⁶ *LG&E v. Argentina* (n 5).

¹³⁶⁷ *Continental v. Argentina* (n 5).

¹³⁶⁸ *LG&E v. Argentina* (n 5).

¹³⁶⁹ *ibid* paras 226, 261.

¹³⁷⁰ *ibid* para 261. See also *Mobil v. Argentina* (n 1230) para 1058.

¹³⁷¹ *LG&E v. Argentina* (n 5) para 266.

¹³⁷² *ibid* para 257.

¹³⁷³ *ibid* paras 70, 263.

¹³⁷⁴ *ibid* paras 265-6.

¹³⁷⁵ *Continental v. Argentina* (n 5) para 232.

¹³⁷⁶ *LG&E v. Argentina* (n 5).

¹³⁷⁷ *Continental v. Argentina* (n 5) para 227.

¹³⁷⁸ *ibid* para 232.

¹³⁷⁹ *ibid* para 222.

As evaluated by the *ad hoc* committee, although there was no clear expression in the decision, the application of proportionality *stricto sensu* can be seen in the tribunal's reasoning by reading its conclusion as a whole.¹³⁸⁰ The tribunal stressed that the basis for its decision that Argentina was exempted from liability was the necessity provided in Article XI of the BIT.¹³⁸¹ Meanwhile, it also highlighted that such exceptions were time-limited, which should be the duration of the state of necessity. Interpreting the exceptions stipulated in the BIT in conjunction with the time limit, Argentina's invocation of necessity as its defence was not acceptable once its economic crisis was assuaged. In other words, if Argentina still took the disputed measures after the crisis of 2001/2, it certainly violated the treaty obligations *vis-à-vis* foreign investors and should be responsible for the violations.¹³⁸²

Based on the above discussions, among six Argentinian cases, the tribunals in *LG&E*¹³⁸³ and *Continental*¹³⁸⁴ balanced the competing values to examine the disputed measures. In this respect, a balance had been struck between the protection of foreign investors' legitimate expectations and the host state's public interest. However, in other cases,¹³⁸⁵ the tribunals did not review Argentina's actions with further assessments included in proportionality analysis, mainly because they concluded that such measures failed to be necessary in the sense of Article XI of the Argentina-US BIT (1991) by incorrect consideration of the criterion for necessity provided in Article 25 of the Wrongful Act. Such differences reflect a gap between the theoretical and practical applications of proportionality in weighing conflicting values. In the researcher's view, this gap may be closed if the exceptional situation can be described in detail.

5.5 Conclusion

As two parties in international investment, the host state and foreign investors have their own expectations. Due to the differences in their roles, various conflicts may emerge from those expected by both parties, in particular, over the stability of the host state's legal and business framework. From the perspective of foreign investors, a stable framework can contribute to their plans for investments and help them manage the risk of their investment activities. From the perspective of the state, it has the regulatory power to reform laws and regulations to react to its constantly changing circumstances and meet the needs of social development. However, as proved by six Argentinian cases,¹³⁸⁶ once a state amends its laws and regulations, there would be hazards for it to be accused of breaching treaty

¹³⁸⁰ *Continental v Argentina*, ICSID Case No. ARB/03/9, Decision on the Application for Partial Annulment, and the Application for Partial Annulment, 23 October 2009, para 126.

¹³⁸¹ *ibid* para 126.

¹³⁸² *ibid*.

¹³⁸³ *LG&E v Argentina* (n 5) paras 226,229.

¹³⁸⁴ *Continental v Argentina* (n 5).

¹³⁸⁵ *Sempra v Argentina* (n 5). *Enron v Argentina* (n 5). *El Paso v Argentina* (n 5). *CMS v Argentina* (n 5).

¹³⁸⁶ Argentinian cases (n 5).

obligations *vis-à-vis* foreign investors. Under such conditions, a balance is needed to be struck between the conflicting values, which can be achieved by applying proportionality.

Although proportionality is neither an international custom nor a general principle of law, it can still be applied in the ISDS by interpreting the case-related treaty. Based on the consideration of the ordinary meaning, the wording of Article XI in the Argentina-US BIT (1991) depicts a means-end relationship.¹³⁸⁷ As stressed by the phrase "measures necessary", the necessity requirement, compared with other constituent elements of proportionality, is clearly expressed. Moreover, interpreting the treaty as a whole reflects the need to strike a balance between the competing values, indicating the notion of proportionality *stricto sensu*. On the one hand, such a balance can be seen from the wording of the treaty preamble, emphasising investment and non-investment values. On the other hand, it can be expressed according to the joint interpretation of the provisions of substantive treatments provided to investors and the exception clause.

This treaty language implies the application of proportionality in the ISDS, but issues still arise from ambiguous provisions, in particular, the absence of qualifying language. Although the necessity requirement is explicitly stipulated in Article XI of the treaty,¹³⁸⁸ no details are provided on the decision-maker who has the power to decide whether the state's interests are at stake and need to be guaranteed by particular measures. If the host state is such a critical decision-maker, it can decide based on its comprehensive information about the whole country and its expertise in each particular field. Considering its role in the ISDS as a respondent, one may query if the state utilises this chance as an excuse to be exempted from liability. The tribunal is the neutral third party compared with the host state, but its capacity may be doubtful.

In this respect, if the contracting parties regard themselves as the decision-makers that decide vital points within the process of proportionality analysis, they should explicitly express their special common intention in the treaty, which is also one interpretative requirement. In Argentinian cases, like other tribunals,¹³⁸⁹ the tribunals in *LG&E*¹³⁹⁰ and *Continental*¹³⁹¹ regarded Article XI of the BIT as not being a self-judging clause and deemed themselves to be the vital decision-maker. However, they still left the host state some room to make decisions on what measures were needed to protect its own interest.¹³⁹² The necessity of such means was confirmed by the tribunals, who judged that Argentina's reactions to its economic crisis were "reasonable and proportionate".¹³⁹³

¹³⁸⁷ Argentina-US BIT (n 120) Article XI.

¹³⁸⁸ *ibid.*

¹³⁸⁹ *Sempra v. Argentina* (n 5). *Enron v. Argentina* (n 5).

¹³⁹⁰ *LG&E v. Argentina* (n 5).

¹³⁹¹ *Continental v. Argentina* (n 5).

¹³⁹² *LG&E v. Argentina* (n 5) para 239. *Continental v. Argentina* (n 5) para 181.

¹³⁹³ *Continental v. Argentina* (n 5) para 227.

Nevertheless, the lack of defined criteria for "necessity" in the treaty raised a myriad of uncertainties. Due to such absence, the tribunals made decisions on whether the measures taken by Argentina to deal with its economic crisis were necessary based on their different understandings of "necessity", which require the disputed means to be "the only way" or "the less restrictive means". Some tribunals reviewed whether the measures taken by Argentina were justified based on Article XI of the BIT by reference to the criterion of "necessity" provided in Article 25 of the Wrongful Act, which is stricter and more stringent, compared with the exception clause.¹³⁹⁴

Based on the earlier discussion in Chapter Two, the criterion "the less restrictive measure" is more reasonable than "the only way".¹³⁹⁵ However, the tribunals in Argentinian cases did not clarify the differences between these two criteria for "necessity". Such a debate was touched upon by the *ad hoc* committee in *Enron* without further analysis.¹³⁹⁶ The requirement of "the only way" provided in Article 25, as stated by the *ad hoc* committee, also has two meanings. One is the absolute only way without consideration of the cost, and then this requirement has a high threshold. Alternatively, if it is a relative "only" way with consideration of the cost, this requirement is similar to "the less restrictive means".

Different from other Argentinian cases, once the tribunals in *LG&E*¹³⁹⁷ and *Continental*¹³⁹⁸ examined that the impugned measures fulfilled the necessity requirement, they truly balanced the conflicting values, reflecting the notion of proportionality *stricto sensu*. The tribunal, in both cases, emphasised that Argentina's questioned measures were only necessary for the duration of the economic crisis. In other words, foreign investors' rights could be restricted due to the protection of the state's own values, yet such restriction was also limited, reflecting a real balance between competing values.

Therefore, as examined in this chapter, the first route to applying proportionality by interpreting its textual basis through the systemic approach is applicable in practice. Based on the consideration of the plain meaning of the questioned word, a particular element of proportionality, such as "necessity", can be seen in the exception clause. According to the systemic interpretative approach, the treaty, which refers to investment protection as well as the guarantee of the public interest in the host state, is interpreted as a whole, implying the significance of balance.

However, suppose the contracting parties to a BIT explicitly express that they desire to apply proportionality to establish a balanced relationship with investors, the tribunal will get clear instructions

¹³⁹⁴ See an example *CMS v. Argentina* (n 5).

¹³⁹⁵ See in Chapter Two.

¹³⁹⁶ *Enron v. Argentina* (n 5).

¹³⁹⁷ *LG&E v. Argentina* (n 5).

¹³⁹⁸ *Continental v. Argentina* (n 5).

to consider both parties' values and strike a balance in the investor-state relationship.¹³⁹⁹ In other words, stipulating a proportionality clause in BITs seems to be an appropriate way to deal with the current imbalanced relationship seen in international investment. In the next section, different generations of Chinese BITs will be analysed, aiming to ascertain whether the textual basis of proportionality can be found in Chinese BITs and examine whether there is a tendency to apply proportionality in the ISDs in which China is involved as the host state.

¹³⁹⁹ See an example China-Colombia BIT (n 124).

Chapter 6

Can Proportionality Be Applied Based on Chinese Bilateral Investment Treaties?

6.1 Introduction

In recent decades, China has transitioned from a pure recipient country of foreign capital to both an investor and a recipient of FDI. The scope of its inbound and outbound FDI is further expanded by the unprecedented OBOR Initiative. Correspondingly, the paradigm of Chinese BITs has shifted: From one-sided investment protection to the dualistic protection of foreign investors' rights and the host state's right to regulate in the public interest.¹⁴⁰⁰

At the time of writing, China has concluded a large number of IIAs, including 145 BITs,¹⁴⁰¹ one trilateral investment treaty (TIT) signed with Japan and Korea,¹⁴⁰² and investment chapters included in free trade agreements (FTAs).¹⁴⁰³ The investment chapter provided in FTAs is similar to Chinese BITs from both the content and structural perspectives. BITs are the main components of Chinese IIAs and play a vital role in Chinese international investment. Although no official classification of Chinese BITs has been released, Chinese scholars consider these treaties can be roughly distinguished into three generations based on different features.¹⁴⁰⁴

In the late 1970s, the "Open Door" policy was implemented by China to restore its collapsed economy.¹⁴⁰⁵ The Chinese Government attempted to attract as much foreign capital as possible, and its BIT programme was launched in 1982.¹⁴⁰⁶ The first-generation Chinese BITs were mainly signed with developed countries from 1982 to 1989 (see Table 6.1), whereas the second-generation treaties mainly agreed with developing countries from 1990 to 1997 (see Table 6.2). Within these phases, China was a capital-importing country and held a conservative attitude towards its IIAs.¹⁴⁰⁷ Various substantive treatments are provided to foreign investors, but no provision or narrowly structured provision of ISDS is prescribed in these two generations of Chinese BITs.

With the development of its inbound FDI, China built up huge foreign exchange reserves and has begun to develop its outbound FDI since its "Going Abroad" strategy and accession to the World Trade Organisation (WTO).¹⁴⁰⁸ From 1998, the BITs signed by China with other countries became the third-generation category (see Table 6.3). Compared with the earlier BITs, these treaties provide higher

¹⁴⁰⁰ Wang & Wang (n 127) 2377.

¹⁴⁰¹ *supra* note 16.

¹⁴⁰² China-Japan-Korea, Republic of TIT (signed 13 May 2012, entered into force 17 May 2014).

¹⁴⁰³ YICAI, 'China Has Concluded 19 FTAs with 26 Countries or Districts' (*Ministry of Commerce*, 31 December 2020) <http://fta.mofcom.gov.cn/article/chinachile/chinachilegfguandian/202012/44120_1.html> [in Chinese] last accessed 26 June 2022.

¹⁴⁰⁴ *supra* note 127.

¹⁴⁰⁵ Shan & Gallagher (n 9) 6 [in Chinese].

¹⁴⁰⁶ *ibid.*

¹⁴⁰⁷ *ibid* 37.

¹⁴⁰⁸ *ibid* 13.

standards of treatment to foreign investors and grant them full access to ISA. As further pointed out by Wang and Wang, should China successfully sign the BITs with the US and the EU, respectively, which are still under negotiation, they would be the typical fourth-generation Chinese BITs with a more balanced paradigm.¹⁴⁰⁹

According to the World Investment Report, China was the world's second-largest recipient of FDI and the largest investor in 2020.¹⁴¹⁰ As a notable dual-role player in international investment, it is in China's interest to strike a fair balance between the conflicting values of foreign investors and the host state in a tailored approach. Concluded from Chinese practice, Berger observes a trend of a balanced paradigm of Chinese BITs.¹⁴¹¹ Moreover, considering China's special status in international investment, the approach it would adopt to establish a balanced investor-state relationship could benefit capital-importer and exporter.¹⁴¹²

As discussed in Chapters Two and Five, proportionality as a tool to balance competing values can be brought into the ISDS regime by interpreting particular treaty provisions.¹⁴¹³ According to the systemic interpretative approach, substantive treatments are interpreted in conjunction with exception clauses in which non-investment values are referred to, indicating a real balance between different values, corresponding to "proportionality *stricto sensu*".¹⁴¹⁴ In Chinese BIT practice, one may question whether such textual bases of applying proportionality appear in Chinese treaties, either implicitly or explicitly.

The Chinese Government has signed new treaties or replaced the old ones with new generation BITs, which provide more detailed substantive protections and refer to non-investment objectives.¹⁴¹⁵ These changes, to a certain extent, imply the application of proportionality from both interpretative and substantive perspectives. The former restricts the tribunals' discretionary power in interpreting treaty provisions,¹⁴¹⁶ while the latter stresses the significance of the host state's right to regulate in the public interest.¹⁴¹⁷ Some terms, such as "necessary" and "proportional", which refer to the notion of

¹⁴⁰⁹ Wang & Wang (n 127) 2382-4.

¹⁴¹⁰ UNCTAD, *World Investment Report 2021* (n 11) 5, 7.

¹⁴¹¹ Axel Berger, 'Investment Rules in Chinese Preferential Trade and Investment Agreements—Is China Following the Global Trend Towards Comprehensive Agreements?' (2013) Deutsches Institut für Entwicklungspolitik (DIE) Discussion Papers 7/2013, 10-1 <<https://www.files.ethz.ch/isn/163216/DP%207.2013.pdf>> last accessed 26 June 2022. Wang & Wang (n 127) 2384.

¹⁴¹² Wenhua Shan & Hongrui Chen, 'China-US BIT Negotiations and the Emerging Chinese BIT 4.0' in C. L. Lim (ed), *Alternative Visions of the International Law on Foreign Investment—Essays in Honour of Muthucumaraswamy Sornarajah* (CUP 2016) 228.

¹⁴¹³ See 2.3 in Chapter Two and Chapter Five. Because proportionality is neither an international custom nor a general principle of law, its application depends on the systemic interpretation of the case-related treaty.

¹⁴¹⁴ See generally in Chapter 5.

¹⁴¹⁵ See examples China-Uzbekistan BIT (n 1064), China-Tanzania BIT (n 261).

¹⁴¹⁶ *ibid.*

¹⁴¹⁷ *ibid.*

proportionality, also appear in Chinese BITs.¹⁴¹⁸ There are doubts over whether the term "necessary" in exception clauses implies one of three assessments included in proportionality analysis or merely the necessity test. As evaluated by Ranjan, at least, this word leaves a certain room to apply proportionality in the ISDS.¹⁴¹⁹ However, the application of proportionality is also questioned by him, arguing that the ambiguous treaty provisions fail to clarify what proportion should lie between the conflicting values of foreign investors and the host state.¹⁴²⁰

This chapter proceeds below to answer whether proportionality can be applied and how it should be applied in Chinese international investment practice via interpreting its textual basis from Chinese BITs. Its application at the different stages of Chinese international investment will also be ascertained. The developing trend of Chinese treaties will be presented in 6.2 by briefly introducing its BITs in three generations. Based on the earlier discussion in Chapter Two, proportionality's components include the implemented measures, the pursued purpose, and the infringed values.¹⁴²¹ Correspondingly, 6.3 will focus on the changes in the treaty preamble, the provision of FET, and the exception clause to find the textual basis of applying proportionality in Chinese ISA. On the basis that proportionality is found to be applicable in Chinese BIT practice, its application in balancing the values of investors and the host state will be analysed from both perspectives of treaty interpretation and application in 6.4.

Nevertheless, in the quest for answers, one difficulty, namely the lack of sufficient Chinese ISDs, cannot be ignored. By the end of February 2022, China had 28 cases (the home state of investors or the host state).¹⁴²² However, most cases are still pending.¹⁴²³ In other words, although proportionality is applicable based on the wording of Chinese BITs, its application cannot be currently verified in Chinese practice. Therefore, the example of Argentinian cases discussed in Chapter Five will be transposed to ascertain what problems may emerge within the process of the application of proportionality in Chinese ISA. However, the recent Chinese BIT practice, at least, expresses a trend to strike a fair balance between the conflicting values of foreign investors and the host state by applying proportionality.

6.2 Trends in Chinese BITs

Since the first BIT was signed by China with Sweden in 1982,¹⁴²⁴ the Chinese Government has promulgated three Chinese Model BITs, which were released in 1984, the late 1980s, and the late 1990s, respectively.¹⁴²⁵ A draft of the new Chinese Model BIT was released in 2010, but it has not been

¹⁴¹⁸ See examples Canada-China BIT (n 421), China-Colombia BIT (n 124).

¹⁴¹⁹ Ranjan (n 18) 876.

¹⁴²⁰ *ibid* 880.

¹⁴²¹ See 2.3 in Chapter Two.

¹⁴²² See Tables 1.2 and 1.3 in Chapter One.

¹⁴²³ See Tables 1.2 and 1.3 in Chapter One.

¹⁴²⁴ China-Sweden BIT (n 14).

¹⁴²⁵ *supra* note 127.

discussed further.¹⁴²⁶ Based on the different features of each model, Chinese BITs can be classified into three generations, which are presented in the tables below.

6.2.1 The First-Generation Chinese BITs: 1982-1989

As shown in Table 6.1, China signed 24 BITs and released its first Model BIT between 1982 and 1989.¹⁴²⁷ These treaties were mainly concluded by China with developed countries, like Germany.¹⁴²⁸ During this period, a complicated attitude was held by China regarding international investment.¹⁴²⁹ On the one hand, China provided various treatments, from FET to MFN, to attract foreign investors to target China for their investments. This was due to China's role in international investment at that time, which was a host state.¹⁴³⁰ On the other hand, it was conservative on the matters of NT and ISA.

It is evident from Table 6.1 that the provision of unqualified FET was stipulated in almost all first-generation Chinese BITs.¹⁴³¹ As discussed in Chapter Four, unqualified FET may provide the broadest protection to foreign investors than that afforded by qualified FET.¹⁴³² By contrast, the majority of these BITs had no provision of NT. This treatment, which was just provided to foreign investors in the China-UK BIT (1986)¹⁴³³ and the China-Japan BIT (1988),¹⁴³⁴ is highly qualified as "in accordance with the host state's laws and regulations".¹⁴³⁵ The reason for China's resistance to the stipulation of NT, on the one hand, was to protect its domestic industry from international investors; On the other hand, China's economic system at that time was a centrally planned economy. In such circumstances, as pointed out by Shan and Gallagher, NT was impossible to be provided.¹⁴³⁶

China was also disinclined to be involved in ISA as the respondent. Only a few foreign investors could enjoy the limited access to *ad hoc* arbitration.¹⁴³⁷ For example, as stipulated in Article 10 of the China-Pakistan BIT (1989),¹⁴³⁸ merely the ISDs as to "the amount of compensation for expropriation" could be submitted to an international arbitral tribunal.¹⁴³⁹ Prerequisites for bringing a claim before the tribunal were also stipulated, requiring that foreign investors should first file the complaint with the

¹⁴²⁶ Shan & Gallagher (n 9) 460-7.

¹⁴²⁷ *supra* note 16. Shan & Gallagher (n 9) 36-9.

¹⁴²⁸ Wang & Wang (n 127) 2380.

¹⁴²⁹ *ibid.*

¹⁴³⁰ Shan & Gallagher (n 9) 37. Shan & Chen (n 1412) 225.

¹⁴³¹ The provision of FET was not provided in the China-Japan BIT (signed 27 August 1988, entered into force 14 May 1989).

¹⁴³² See 4.2.3 in Chapter Four.

¹⁴³³ China-UK BIT (signed 15 May 1986, entered into force 15 May 1986).

¹⁴³⁴ China-Japan BIT (n 1431).

¹⁴³⁵ See examples China-Japan BIT (n 1431) Article 4. China-UK BIT (n 1433) Article 3.

¹⁴³⁶ Shan & Gallagher (n 9) 172-3.

¹⁴³⁷ See an example China-Switzerland BIT (signed 12 November 1986, entered into force 18 March, Terminated 13 April 2010) Article 12.

¹⁴³⁸ China-Pakistan BIT (signed 12 February 1989, entered into force 30 September 1990).

¹⁴³⁹ *ibid* Article 10.

host state's competent authority to review the disputed means.¹⁴⁴⁰ Only if this dispute cannot be settled "within one year after the complaint is filed" can the investor opt to submit the claim before "the competent court of the host state" or "an international arbitral tribunal".¹⁴⁴¹ This provision explicitly reflects China's disinclination to participate in ISA from 1982 to 1989. Shan and Gallagher explained that one reason for China's resistance might be its questions and doubts on the ICSID Convention and relevant regime.¹⁴⁴² In China's view, a state's sovereignty and regulatory power would be impaired by the ICSID,¹⁴⁴³ leading to its conservative attitude when signing BITs with another contracting country.¹⁴⁴⁴

Table 6.1 The First-Generation Chinese BITs*

Contracting States	Date of Signature	Treaty Preamble		FET Clause		Exception Clause
		IO	NO	U	Q	
Sweden	29/03/1982	√		√		
Germany	07/10/1983	√		√		
France	30/05/1984	√		√		
Belgian-Luxembourg	04/06/1984	√		√		
Finland	04/09/1984	√		√		
Norway	21/11/1984	√		√		
Italy	28/01/1985	√		√		
Thailand	12/03/1985	√		√		
Denmark	29/04/1985	√		√		
Netherlands	17/06/1985	√		√		
Austria	12/09/1985	√		√		
Singapore	21/11/1985	√		√		√
Kuwait	23/11/1985	√		√		
Sri Lanka	13/03/1986	√		√		√
United Kingdom	15/05/1986	√		√		
Switzerland	12/11/1986	√		√		
Poland	07/06/1988	√		√		
Australia	11/07/1988	√		√		
Japan	27/08/1988	√		None		
Malaysia	21/11/1988	√		√		
New Zealand	22/11/1988	√		√		√
Pakistan	12/02/1989	√		√		
Bulgaria	27/06/1989	√		√		
Ghana	12/10/1989	√		√		
"IO" means "investment objectives" "NO" means "non-investment objectives" "U" means "unqualified FET" "Q" means "qualified FET" *24 BITs in total **Modified by Additional Protocols: China-Sweden BIT (1982), Bulgaria-China BIT (1989)						

¹⁴⁴⁰ ibid Article 10.

¹⁴⁴¹ ibid.

¹⁴⁴² Shan & Gallagher (n 9) 39.

¹⁴⁴³ ibid.

¹⁴⁴⁴ ibid 37. Shan & Chen (n 1412) 225. Wang & Wang (n 127) 2380.

***Terminated: China-Germany BIT (1983), China-France BIT (1984), BLEU-China BIT (1984), China-Finland BIT (1984), China-Netherlands BIT (1985), China-Singapore BIT (1985), China-Switzerland BIT (1986)

6.2.2 The Second-Generation Chinese BITs: 1990-1997

China has agreed 67 BITs mainly with developing countries, from 1990 to 1997, which can be seen in Table 6.2.¹⁴⁴⁵ The second Chinese Model BIT was also promulgated at this phase.¹⁴⁴⁶ As pointed out by Wang and Lu, these treaties were primarily signed for diplomatic purposes, which aimed to enhance South-South cooperation, namely the cooperation between developing countries.¹⁴⁴⁷ Most clauses in these treaties are similar to those provided in the first-generation Chinese BITs, except the provisions of qualified NT and ISA.¹⁴⁴⁸

One reason for such differences was the change in China's attitude to the ICSID. The ICSID Convention was signed by China in 1990 and entered into force in 1993.¹⁴⁴⁹ Therefore, the second-generation Chinese BITs contain the ISDS provision, which allows a foreign investor to file complaints to the arbitral tribunals under the ICSID regime.¹⁴⁵⁰ As noted by Shan and Gallagher, the first Chinese treaty providing such an ISDS clause may be the China-Lithuania BIT (1993),¹⁴⁵¹ which stipulates that

[T]he dispute relating to *the amount of compensation and other disputes agreed upon by both parties* may be submitted to the International Centre for Settlement of Investment Disputes established under the Convention on the Settlement of Investment Dispute between States and Nationals of other States opened for signature at Washington DC on 18 March 1965.¹⁴⁵² [italic added]

This provision explicitly expresses that except for the complaint arising from "the amount of compensation", others may also be filed to the ICSID by investors only if both parties agree.¹⁴⁵³ This treaty language reflects that the scope of ISDs submitted to the ICSID is now expanded. Additionally, the prerequisites for arbitration mentioned in the first-generation Chinese BITs are no longer required.

However, Shan and Gallagher emphasised that these features can be seen in the second-generation Chinese BITs but are not referred to in all treaties concluded during this period.¹⁴⁵⁴ For example, as to

¹⁴⁴⁵ Shan & Gallagher (n 9) 454-6.

¹⁴⁴⁶ *ibid.*

¹⁴⁴⁷ Wang & Lu (n 127) 54. See Wang & Wang (n 127) 2380.

¹⁴⁴⁸ See an example China-Iceland BIT (signed 31 March 1994, entered into force 1 March 1997) Article 3.

¹⁴⁴⁹ 'Member States' (ICSID) <<https://icsid.worldbank.org/about/member-states/database-of-member-states>> last accessed 24 June 2022.

¹⁴⁵⁰ Shan & Gallagher (n 9) 39-40.

¹⁴⁵¹ *ibid.* 40. See an example China-Lithuania BIT (signed 8 November 1993, entered into force 1 June 1994) Article 8.

¹⁴⁵² *ibid.* Article 8 (2).

¹⁴⁵³ *ibid.* Shan & Gallagher (n 9) 40.

¹⁴⁵⁴ Shan & Gallagher (n 9) 40.

the prerequisites for submitting a case before the tribunal, the China-Lithuania BIT (1993)¹⁴⁵⁵ has no requirement on the qualification of both contracting parties, but the China-Greece BIT (1992)¹⁴⁵⁶ still requires that both contracting parties should "have become members" of the ICSID Convention for bringing a dispute before the ICSID.¹⁴⁵⁷

Table 6.2 The Second-Generation Chinese BITs*

Contracting States	Date of Signature	Treaty Preamble		FET Clause		Exception Clause
		I O	N O	U	Q	
Russia	21/07/1990	√		√		
Turkey	13/11/1990	√		√		
Papua New Guinea	12/04/1991	√		√		
Hungary	29/05/1991	√		√		
Mongolia	25/08/1991	√		√		
Slovakia	04/12/1991	√			None	
Czech Republic	04/12/1991	√			None	
Portugal	03/02/1992	√		√		
Spain	06/02/1992	√		√		
Uzbekistan	13/03/1992	√		√		
Bolivia	08/05/1992	√		√		
Kyrgyzstan	14/05/1992	√		√		
Greece	25/06/1992	√		√		
Armenia	04/07/1992	√		√		
Philippines	20/07/1992	√		√		
Kazakhstan	10/08/1992	√		√		
Korea, Republic of	30/09/1992	√			None	
Ukraine	31/10/1992	√		√		
Argentina	05/11/1992	√		√		
Moldova	06/11/1992	√		√		
Turkmenistan	21/11/1992	√		√		
Viet Nam	02/12/1992	√		√		
Belarus	11/01/1993	√			None	
Laos	31/01/1993	√		√		
Albania	13/02/1993	√		√		
Tajikistan	09/03/1993	√		√		
Georgia	03/06/1993	√		√		
Croatia	07/06/1993	√		√		
UAE	01/07/1993	√		√		
Estonia	02/09/1993	√		√		
Slovenia	13/09/1993	√		√		
Lithuania	08/11/1993	√		√		
Uruguay	02/12/1993	√		√		
Azerbaijan	08/03/1994	√		√		
Ecuador	21/03/1994	√		√		
Chile	23/03/1994	√		√		
Iceland	31/03/1994	√		√		

¹⁴⁵⁵ China-Lithuania BIT (n 1451).

¹⁴⁵⁶ China-Greece BIT (signed 25 June 1992, entered into force 21 December 1993)

¹⁴⁵⁷ ibid Article 10 (4).

Egypt	21/04/1994	√		√		
Peru	09/06/1994	√		√		
Romania	12/07/1994	√		√		
Jamaica	26/10/1994	√		√		
Indonesia	18/11/1994	√		√		
Oman	18/03/1995	√		√		
Morocco	27/03/1995	√		√		
Israel	10/04/1995	√		√		
Cuba	24/04/1995	√		√		
Serbia	18/12/1995	√		√		
Saudi Arabia	29/02/1996	√		√		
Mauritius	04/05/1996	√		√		√
Zimbabwe	21/05/1996	√		√		
Lebanon	13/06/1996	√		√		
Zambia	21/06/1996	√		√		
Cambodia	19/07/1996	√		√		
Bangladesh	12/09/1996	√		√		
Algeria	17/10/1996	√		√		
Syrian Arab Republic	09/12/1996	√		√		
Gabon	09/05/1997	√		√		
Nigeria	12/05/1997	√		√		
Sudan	30/05/1997	√		√		
Macedonia	09/06/1997	√		√		
Cameroon	10/09/1997	√		√		
Congo, Democratic Republic of	18/12/1997	√		√		
Yemen	16/02/1998	√		√		
Cape Verde	21/04/1998	√		√		
Ethiopia	11/05/1998	√		√		
Qatar	09/04/1999	√		√		
Bahrain	17/06/1999	√		√		
South Africa	30/12/1997	√		√		
"IO" means "investment objectives" "NO" means "non-investment objectives" "U" means "unqualified FET" "Q" means "qualified FET" *68 BITs in total **Modified by Additional Protocols: China-Slovakia BIT (1991), China-Romania BIT (1994), China-Cuba BIT (1995) ***Terminated: China-Russia BIT (1990), China-Turkey BIT (1990), China-Czech BIT (1991), China-Portugal BIT (1992), China-Spain BIT (1992), China-Uzbekistan BIT (1992), China-Korea, Republic of BIT (1992), China-Ecuador BIT (1994), China-Chile BIT (1994), China-Indonesia BIT (1994), China-Nigeria BIT (1997) ****Signed: China-Democratic Republic of Congo (1997)						

6.2.3 The Third-Generation Chinese BITs: from 1998 - Present

With the increasing successful development of its inward FDI, China built up huge foreign exchange reserves.¹⁴⁵⁸ Consequently, since 1998, China has developed a robust outbound FDI capability,¹⁴⁵⁹

¹⁴⁵⁸ Shan & Gallagher (n 9) 13.

¹⁴⁵⁹ Ranjan (n 18) 853, 863.

encouraged by its "Going Abroad" strategy and accession to the WTO.¹⁴⁶⁰ In this phase, China aims to promote and protect the inbound and outbound investments.¹⁴⁶¹

Some old Chinese BITs signed with developed countries were replaced by new treaties reflecting China's changing position in international investment.¹⁴⁶² Stronger investment protections are in China's interest to protect its own outbound investment.¹⁴⁶³ Improved commercial landscapes provided to foreign investors in the third-generation Chinese BITs, like substantial NT and full access to ISA, show higher standards than those afforded in the treaties signed in the first two generations.¹⁴⁶⁴ The China-Barbados BIT (1998),¹⁴⁶⁵ for instance, was the first treaty that allowed foreign investors to submit all disputes that could not be amicably settled within six months to the ICSID.¹⁴⁶⁶

Table 6.3 The Third-Generation Chinese BITs*

Contracting States	Date of Signature	Treaty Preamble		FET Clause		Exception Clause
		I O	N O	U	Q	
Barbados	20/07/1998	√		√		
Congo	20/03/2000	√		√		
Botswana	12/06/2000	√		√		
Iran	22/06/2000	√		√		
Brunei	17/11/2000	√		√		
Cyprus	17/01/2001	√		√		
Sierra Leone	16/05/2001	Not Available				
Mozambique	10/07/2001	√		√		
Kenya	16/07/2001	Not Available				
Nigeria	27/08/2001	√		√		
Jordan	15/11/2001	√	√		√	
Netherlands	26/11/2001	√		√		
Myanmar	12/12/2001	√		√		
Bosnia and Herzegovina	26/06/2002	√		√		
Trinidad and Tobago	22/07/2002	√	√	√		
Côte d'Ivoire	30/09/2002	√		√		
Guyana	27/03/2003	√	√	√		
Djibouti	18/08/2003	√		√		
Germany	01/12/2003	√		√		
Benin	18/02/2004	√		√		
Latvia	15/04/1004	√		√		
Uganda	27/05/2004	√		√		
Tunisia	21/06/2004	√		√		

¹⁴⁶⁰ Shan & Gallagher (n 9) 12-3

¹⁴⁶¹ Shan & Gallagher (n 9) 15. Wang & Wang (n 127) 2382.

¹⁴⁶² Wang & Wang (n 127) 2382.

¹⁴⁶³ *ibid* 2376.

¹⁴⁶⁴ Wang & Lu (n 127) 54. Congyan Cai, 'China-US BIT Negotiations and the Future of Investment Treaty Regime: A Grand Bilateral Bargain with Multilateral Implications' (2009) 12 *Journal of International Economic Law* 457, 462. Shan & Gallagher (n 9) 41. Ioannis Glinavos, 'Which Way Huawei? ISDS Options for Chinese Investors' in J. Chaisse et al. (eds.), *Handbook of International Investment Law and Policy* (Springer 2021) 2469.

¹⁴⁶⁵ Barbados-China BIT (signed 20 July 1998, entered into force 1 October 1999).

¹⁴⁶⁶ *ibid*. Shan & Gallagher (n 9) 41.

Finland	15/11/2004	√		√		√
Korea, Dem. People's Rep. of	22/03/2005	√		√		
Belgium-Luxembourg	06/06/2005	√		√		
Equatorial Guinea	20/10/2005	√		√		
Spain	14/11/2005	√		√		
Namibia	17/11/2005	√		√		
Guinea	18/11/2005	Not Available				
Madagascar	21/11/2005	√			√	√
Czech Republic	08/12/2005	√		√		
Portugal	09/12/2005	√		√		
Vanuatu	07/04/2006	√		√		
Russia	09/11/2006	√		√		
India	21/11/2006	√		√		√
Seychelles	10/02/2007	√			√	
Korea, Republic of	07/09/2007	√		√		
Costa Rica	24/10/2007	√			√	
France	26/11/2007	√			√	
Mexico	11/07/2008	√			√	
Colombia	22/11/2008	√			√	√
Switzerland	27/01/2009	√		√		
Mali	12/02/2009	√		√		
Malta	22/02/2009	√		√		
Bahamas	04/09/2009	Not Available				
Chad	26/04/2010					
Libya	04/08/2010					
Uzbekistan	19/04/2011	√	√		√	√
Congo, Democratic Republic of	11/08/2011	Not Available				
Canada	09/09/2012	√	√		√	√
Tanzania	24/03/2013	√	√		√	√
Turkey	29/07/2015	√			√	√
<p>"IO" means "investment objectives" "NO" means "non-investment objectives" "U" means "unqualified FET" "Q" means "qualified FET" *53 BITs in total ***Terminated: China-India BIT (2006) ****Signed: Botswana-China BIT (2000), Brunei-China BIT (2000), China-Sierra Leone BIT (2001), China-Kenya BIT (2001), China-Jordan BIT (2001), China-Cote d'Ivoire BIT (2002), China-Djibouti BIT (2003), Benin-China BIT (2004), China-Uganda BIT (2004), China-Namibia BIT (2005), China-Guinea BIT (2005), China-Vanuatu BIT (2006), China-Seychelles BIT (2007), Bahamas-China BIT (2009), Chad-China BIT (2010), China-Libya BIT (2010), China-Democratic Republic of Congo (2011)</p>						

China's role in international investment has transitioned from a passive pure recipient of foreign investment to an important capital-importer and energetic capital-exporter. In this respect, investment protection and the protection of public interest in the host state are equally as crucial for China. However, based on the earlier discussion on Argentinian cases arising from its economic crisis,¹⁴⁶⁷ which was

¹⁴⁶⁷ See generally in Chapter Five.

analysed in Chapter Five, broad protections for foreign investors may impair the host state's right to regulate in the public interest. Therefore, striking a balance between such conflicting values is vital for states, especially China considering its unique and powerful dual role in international investment.

In order to pursue such a fulcrum in the investor-state relationship, a balanced paradigm is needed. However, a gap may exist between the protections that could be provided by Chinese treaties and that need to be afforded in practice because the majority of Chinese BITs were concluded decades ago. Only 17 treaties have been resigned or replaced by the new version in the past four decades, including the BITs co-signed by Germany,¹⁴⁶⁸ France,¹⁴⁶⁹ BLEU,¹⁴⁷⁰ Finland,¹⁴⁷¹ Netherlands,¹⁴⁷² Singapore,¹⁴⁷³ Switzerland,¹⁴⁷⁴ Russia,¹⁴⁷⁵ Turkey,¹⁴⁷⁶ the Czech Republic,¹⁴⁷⁷ Portugal,¹⁴⁷⁸ Spain,¹⁴⁷⁹ Uzbekistan,¹⁴⁸⁰ the Republic of Korea,¹⁴⁸¹ Chile,¹⁴⁸² Mauritius,¹⁴⁸³ and Nigeria,¹⁴⁸⁴ respectively.

Nevertheless, specific changes can still be seen by comparing provisions stipulated in the old BITs with those in the new version. Compared with old BITs, these new treaties provide more details and clarifications on substantive treatments afforded to foreign investors. For example, compared with unqualified FET provided in the old China-France BIT (1984),¹⁴⁸⁵ qualified FET is stipulated in the new treaty.¹⁴⁸⁶ The significance of non-investment values is also emphasised. The new treaty signed between China and Finland describes exceptional situations in which the measures necessary for its essential security interests do not violate its obligations,¹⁴⁸⁷ which was not referred to in the China-Finland BIT (1984).¹⁴⁸⁸ These changes somewhat reflect how China has begun to seek a balanced paradigm of IIAs to re-balance the investor-state relationship under updated circumstances. A similar trend is also expressed in the wording of the third-generation Chinese BITs, particularly the treaties signed after 2008. Such changes in Chinese BITs will be analysed and discussed in-depth in 6.3 to ascertain whether

¹⁴⁶⁸ China-Germany BIT (n 547).

¹⁴⁶⁹ China-France BIT (signed 26 November 2007, entered into force 20 August 2010).

¹⁴⁷⁰ BLEU-China BIT (n 80).

¹⁴⁷¹ China-Finland BIT (signed 15 November 2004, entered into force 15 November 2006).

¹⁴⁷² China-Netherlands BIT (n 870).

¹⁴⁷³ China-Singapore FTA (signed 23 October 2008, entered into force 1 January 2009).

¹⁴⁷⁴ China-Switzerland BIT (signed 27 January 2009, entered into force 13 April 2010).

¹⁴⁷⁵ China-Russia BIT (signed 9 November 2006, entered into force 1 May 2009).

¹⁴⁷⁶ China-Turkey BIT (n 15).

¹⁴⁷⁷ China-Czech Republic BIT (signed 8 December 2005, entered into force 1 September 2006).

¹⁴⁷⁸ China-Portugal BIT (signed 9 December 2005, entered into force 26 July 2008).

¹⁴⁷⁹ China-Spain BIT (signed 14 November 2005, entered into force 1 July 2008).

¹⁴⁸⁰ China-Uzbekistan BIT (n 1064).

¹⁴⁸¹ China-Korea, Republic of BIT (signed 7 September 2007, entered into force 1 December 2007).

¹⁴⁸² Chile-China FTA (signed 18 November 2005, entered into force 1 October 2006).

¹⁴⁸³ China-Mauritius FTA (n 319).

¹⁴⁸⁴ China-Nigeria BIT (signed 27 August 2001, entered into force 18 February 2010).

¹⁴⁸⁵ China-France BIT (n 1469).

¹⁴⁸⁶ *ibid.*

¹⁴⁸⁷ China-Finland BIT (n 1471) Article 3 (5).

¹⁴⁸⁸ *ibid.*

proportionality can be applied by China to achieve its desired purpose, a balanced investor-state relationship, managing the conflicting values of foreign investors and the host state.

6.3 The Textual Basis of the Principle of Proportionality in Chinese BITs

A balance between investment protection and the protection of its public interest is being considered by every state participating in international investment. China is no exception. As previously discussed in Chapters Two and Five, proportionality, a useful tool to achieve the balanced investor-state relationship, can be included in the ISDS regime via treaty interpretation.¹⁴⁸⁹ On the one hand, particular terms, such as "necessity" or "proportional", imply the application of proportionality; On the other hand, the systemic interpretation of the whole treaty may also indicate proportionality analysis.¹⁴⁹⁰

The China-Colombia BIT (2008)¹⁴⁹¹ is a good example and the only Chinese BIT that explicitly expresses "proportionality". As stipulated in Article 12 (1) (d),¹⁴⁹² the measures that could be justified even though they are against the host state's treaty obligations *vis-à-vis* foreign investors should be "*proportional* to the objective they seek to achieve",¹⁴⁹³ reflecting a reasonable means-end connection embodied in the principle of proportionality. The term "proportional" indicates the application of proportionality in balancing the investor-state relationship between China and Colombia.

Also, the factors that should be taken into consideration when applying proportionality may be reflected in the interpretation of treaty provisions of Chinese BITs using the systemic approach.¹⁴⁹⁴ This can include interpreting clarified substantive protections in conjunction with exception clauses.

6.3.1 More Detailed FET Clauses—Clarifying Substantive Protections

Based on the earlier discussion in Chapter Four, ambiguous provisions may lead to broad treaty interpretations in favour of foreign investors,¹⁴⁹⁵ but as noted by Wang and Wang, the recent Chinese BITs provide detailed substantive treatments to foreign investors.¹⁴⁹⁶ A typical example here is FET, which is qualified with various requirements in the recent Chinese BITs, reflecting its scope and clarifying its components, compared with the unqualified FET provided in the early treaties.

6.3.1.1 The Unqualified Fair and Equitable Treatment

Tables 6.1 and 6.2 above present that the unqualified FET is provided in most Chinese BITs concluded

¹⁴⁸⁹ See 2.2 in Chapter Two and generally in Chapter Five.

¹⁴⁹⁰ See generally in Chapter Three.

¹⁴⁹¹ China-Colombia BIT (n 124).

¹⁴⁹² *ibid* Article 12 (1) (d).

¹⁴⁹³ *ibid* [italic added].

¹⁴⁹⁴ See 3.4.4 in Chapter Three.

¹⁴⁹⁵ See 4.2.3 in Chapter Four.

¹⁴⁹⁶ Wang & Wang (n 127) 2385.

in the first and second generations. Some treaties merely require the host state to "ensure fair and equitable treatment at all times to foreign investors" without any clarification on the meaning or scope of this treaty obligation.¹⁴⁹⁷ Although in other treaties, this standard is modified with different treatments provided to foreign investors, such as MFN and NT,¹⁴⁹⁸ its components remain undefined.

For example, Article 3 of the China-Laos BIT (1993)¹⁴⁹⁹ prescribes that FET provided to foreign investors "shall not be less favourable than that accorded to investments and activities associated with such investment of investors of a third state",¹⁵⁰⁰ linking it with MFN. Based on this clause, if a better FET standard is provided in other treaties signed by the host state with any third country, foreign investors can import such a better treatment via the MFN clause in the treaty.¹⁵⁰¹ As previously discussed in Chapter Four, both MFN and NT are regarded as the baseline of FET.¹⁵⁰² In Cai's view, the contribution of these treatments is to ascertain the level of FET enjoyed by foreign investors.¹⁵⁰³ However, they do not further clarify FET itself. It is the researcher's view, that linking FET with MFN, in fact, is a comparison between different FET standards provided in different treaties to find the better ones, but its constituent elements are still uncertain.

Due to the lack of details on FET, the tribunals have always interpreted the unqualified FET in favour of foreign investors with consideration of promoting and protecting foreign investment, which is the purpose and object of the treaty.¹⁵⁰⁴ Consequently, the broad protection of foreign investors is provided by the unqualified FET, but the host state is put at a disadvantage. This results in a high risk of being sued by investors, and the state could also see its regulatory power for the public interest diminished.¹⁵⁰⁵ In this respect, instead of contributing to a balanced investor-state relationship, the unqualified FET may worsen the conflicts between the values of foreign investors and the host state.

6.3.1.2 The Qualified Fair and Equitable Treatment

Since the China-New Zealand FTA was concluded in 2008,¹⁵⁰⁶ another scenario can be observed in Chinese BIT practice, in which substantive protections are clarified with detail. As stipulated in Article 143,

¹⁴⁹⁷ China-Sweden BIT (n 14) Article 2.

¹⁴⁹⁸ See an example Cape Verde-China BIT (21 April 1998, entered into force 1 January 2001) Article 3.

¹⁴⁹⁹ China-Laos (n 504).

¹⁵⁰⁰ *ibid* Article 3.

¹⁵⁰¹ *ibid*.

¹⁵⁰² See 4.2.3 in Chapter Four.

¹⁵⁰³ Congyan Cai, 'Outward Foreign Direct Investment Protection and the Effectiveness of Chinese BIT Practice' (2006) 7 *The Journal of World Investment & Trade* 621, 643.

¹⁵⁰⁴ See 3.4.2 in Chapter Three. As pointed out by Ranjan, the plain meaning of ambiguous provisions provided in most BITs expresses a preference investment protection. See in Ranjan (n 18) 883.

¹⁵⁰⁵ See generally in Chapter Five.

¹⁵⁰⁶ China-New Zealand FTA (signed 7 April 2008, entered into force 1 October 2008). Axel Berger, 'Hesitant Embrace: China's Recent Approach to International Investment Rule-Makin' (2015) 16 *Journal of World Investment & Trade* 843, 858.

Fair and equitable treatment *includes* the obligation to ensure that, having regard to general principles of law, investors are not denied justice or treated unfairly or inequitably in any legal and administrative proceeding affecting the investments of the investor.¹⁵⁰⁷ [italic added]

As reflected in the wording, this provision not only qualifies FET itself but also clarifies its components. The negative language explicitly describes the options available to the host state against its FET obligations *vis-à-vis* foreign investors, including the denial of justice. The term "includes" further presents an indicative list of FET's components provided in Article 143. Such a qualified FET, compared with the unqualified standard, clarifies the treatments afforded to foreign investors and refers to a higher threshold of the host state's liability.¹⁵⁰⁸

According to Table. 6.3, the qualified FET has gradually emerged into the recent Chinese BITs, implying a trend towards restricting the overly broad protection enjoyed by foreign investors. Concluded from these treaties, it is evident that FET has been qualified by reference to different factors, including the principles of international law, the MST under customary international law, and its particular components.¹⁵⁰⁹

The connection between FET and the principles of international law can be observed in BITs that China signed with Jordan,¹⁵¹⁰ Madagascar,¹⁵¹¹ Seychelles,¹⁵¹² Costa Rica,¹⁵¹³ France,¹⁵¹⁴ and Turkey,¹⁵¹⁵ respectively. However, the precise wording applied to describe their relationship varies from one treaty to another. For example, the China-Jordan BIT (2001)¹⁵¹⁶ links FET with "applicable principles of international law recognised by *both contracting parties*".¹⁵¹⁷ The phrase "recognised by both contracting parties" emphasises the significance of the contracting parties' common intention.

Conversely, the China-Mexico BIT (2008),¹⁵¹⁸ the China-Colombia BIT (2008),¹⁵¹⁹ and the Canada-China BIT (2012)¹⁵²⁰ stipulate FET by reference to the MST. Particularly the China-Mexico BIT

¹⁵⁰⁷ China-New Zealand FTA (n 1506) Article 143 [italic added].

¹⁵⁰⁸ See 4.2.3 in Chapter Four.

¹⁵⁰⁹ These Chinese BITs are China-Jordan BIT (signed 15 November 2001), China-Madagascar BIT (signed 21 November 2005, entered into force 1 July 2007), China-Seychelles BIT (signed 10 February 2007), China-Costa Rica BIT (signed 24 October 2007, entered into force 20 October 2016), China-France BIT (n 1469), China-Mexico BIT (n 561), China-Colombia BIT (n 124), China-Uzbekistan BIT (n 1064), Canada-China BIT (n 421), China-Tanzania BIT (n 261), China-Turkey BIT (n 15).

¹⁵¹⁰ China-Jordan BIT (n 1509).

¹⁵¹¹ China-Madagascar BIT (n 1509).

¹⁵¹² China-Seychelles BIT (n 1509).

¹⁵¹³ China-Costa Rica BIT (n 1509).

¹⁵¹⁴ China-France BIT (n 1469).

¹⁵¹⁵ China-Turkey BIT (n 15).

¹⁵¹⁶ China-Jordan BIT (n 1509).

¹⁵¹⁷ *ibid* Article 3 [italic added].

¹⁵¹⁸ China-Mexico BIT (n 561).

¹⁵¹⁹ China-Colombia BIT (n 124).

¹⁵²⁰ Canada-China BIT (n 421).

(2008),¹⁵²¹ as pointed out by Cai, was the first treaty that reflected China's acceptance of the concept of MST.¹⁵²² As stipulated in Article 5 of the China-Mexico BIT (2008)¹⁵²³ with the heading "minimum standard of treatment", the host state shall provide investors treatments "in accordance with international law, *including* fair and equitable treatment".¹⁵²⁴ Moreover, Article 5 (2) further clarifies that "the international law minimum standard of treatment of aliens" is the minimum standard of treatment provided to investors.¹⁵²⁵ Also, it stresses that FET has no more requirements than those required by "the interpretation law minimum standard of treatment of aliens as evidence of state practice and *opinio juris*".¹⁵²⁶ According to the principles of interpretation prescribed in the Vienna Convention,¹⁵²⁷ considering the context in which the questioned term appears, FET is contained in the MST. The heading of Article 5 and the term "including" are an example.

Similar provisions can be seen in the Canada-China BIT (2012),¹⁵²⁸ which links FET to the MST "as evidence by general state practice accepted as law".¹⁵²⁹ These wordings, from "state practice and *opinio juris*" to "general state practice accepted as law", as discussed previously in Chapter Two, express customary international law,¹⁵³⁰ reflecting China's indirect acceptance of such a concept. China's explicit acceptance can also be observed in its BIT signed with Colombia,¹⁵³¹ which unambiguously qualifies FET with "customary international law".¹⁵³²

Based on the language of these Chinese treaties, one may observe an interesting point as to China's hesitation to accept international customs. The China-Colombia BIT (2008)¹⁵³³ was signed between the conclusion of the China-Mexico BIT (2008)¹⁵³⁴ and the Canada-China BIT (2012),¹⁵³⁵ but the qualifications of FET fluctuate. As explained by Cai, one reason for China's fluid attitude to international customs is that, in China's view, the formation of customary international law is dominated by particular Western countries without the participation of developing countries, including China itself.¹⁵³⁶ As further pointed out by Levine, FET is not an international custom in China's historical instance.¹⁵³⁷

¹⁵²¹ China-Mexico BIT (n 561).

¹⁵²² *ibid.* Cai, 'China-US BIT' (n 1464) 469.

¹⁵²³ China-Mexico BIT (n 561).

¹⁵²⁴ *ibid.* Article 5 [*italic added*].

¹⁵²⁵ *ibid.*

¹⁵²⁶ *ibid.* Article 5(2).

¹⁵²⁷ Vienna Convention (n 47).

¹⁵²⁸ Canada-China BIT (n 421).

¹⁵²⁹ *ibid.* Article 4.

¹⁵³⁰ See in Chapter Two. ICJ Statute (n 19) Article 38 (1) (b).

¹⁵³¹ China-Colombia BIT (n 124) Article 2.

¹⁵³² *ibid.*

¹⁵³³ *ibid.*

¹⁵³⁴ China-Mexico BIT (n 561).

¹⁵³⁵ Canada-China BIT (n 421).

¹⁵³⁶ Cai, 'China-US BIT' (n 1464) 468.

¹⁵³⁷ Matthew Levine, 'Towards a Fourth Generation of Chinese Treaty Practice: Substantive Changes, Balancing Mechanisms,

Except for the above qualifications, FET may also be qualified by reference to its particular constituent elements. For example, Article 2 of the China-Colombia BIT (2008)¹⁵³⁸ clarifies that FET "includes the prohibition against denial of justice in criminal, civil, or administrative proceedings in accordance with the generally accepted principles of customary international law".¹⁵³⁹ A different but similar FET clause can be seen in the China-Turkey BIT (2015),¹⁵⁴⁰ which stipulates that FET "requires that investors of one contracting party shall not be rejected to fairly judicial proceedings by the other contracting party or be treated with obvious discriminatory or arbitrary measures" in Article 2.¹⁵⁴¹ Both treaties describe FET's components by listing its elements, which at least clarify that specific measures implemented by the host state would breach its FET obligation *vis-à-vis* foreign investors.¹⁵⁴² This can smooth the way to the settling of ISDs. However, with consideration of their plain meanings, the term "include" expresses an indicative list of FET's constituent elements provided in the China-Colombia BIT (2008),¹⁵⁴³ while the word "require" indicates an exhaustive list provided in the China-Turkey BIT (2015).¹⁵⁴⁴ Therefore, the description of FET provided in the treaty signed by China with Turkey is more specific than that in its treaty signed with Colombia.

By comparing the provision of FET stipulated in three generations of Chinese BITs, noting the transition from unqualified to qualified, the recent Chinese BIT practice tends to clarify substantive protections in detail. Consequently, the tribunals' discretionary power to interpret treaty provisions is diminished due to the unambiguous qualifications of FET provided in Chinese BITs. In Alvarez's view, such qualifications draw a clear boundary of FET.¹⁵⁴⁵ The rights of foreign investors provided by FET are clear, and then whether their case-related rights fall into such a category can be easily ascertained and avoid misinterpretations,¹⁵⁴⁶ thus enabling better interpretations.

6.3.2 The Pursued Purposes-Shifting to Non-Investment Values

Unlike the FET standard, which has been more narrowly defined, the object and purpose of the recent Chinese BITs have been expanded to encapsulate not only investment objectives but also non-investment objectives. Various values fall into the latter category, from essential security interests to public order, from public health to environmental protection. Such non-investment values can be

and Selective Adaption' in Julien Chaisse (ed), *China's International Investment Strategy: Bilateral, Regional, and Global Law and Policy* (OUP 2019) 216.

¹⁵³⁸ China-Colombia BIT (n 124).

¹⁵³⁹ *ibid* Article 2.

¹⁵⁴⁰ China-Turkey BIT (n 15).

¹⁵⁴¹ *ibid* Article 2. China-Uzbekistan BIT (n 1064) Article 5.

¹⁵⁴² Cai, 'China-US BIT' (n 1464) 468.

¹⁵⁴³ China-Colombia BIT (n 124).

¹⁵⁴⁴ As to the differences in terms "requires" and "includes" see in Chapter Four.

¹⁵⁴⁵ J. E Alvarez, 'The Evolving BIT' [2009] *Transnational Dispute Management* 1, 14.

¹⁵⁴⁶ Wang & Wang (n 127) 2385-6.

observed in the treaty preamble¹⁵⁴⁷ and provisions, in particular the exception clause.¹⁵⁴⁸

6.3.2.1 Non-Investment Objectives in the Treaty Preamble

Based on the earlier discussion in 6.2, the main reason for China to sign IIAs in the first two generations is to promote and protect inbound FDI, as China was a pure recipient of foreign investment at that time. Therefore, investment objectives were chiefly described in treaty preambles of Chinese BITs. These preambles mainly refer to the creation of favourable conditions for foreign investments,¹⁵⁴⁹ the stimulation of economic prosperity in both contracting states,¹⁵⁵⁰ and the enhancement of economic cooperation based on equality and mutual benefit.¹⁵⁵¹

With the transition of its role in international investment, China has gradually focused on quality rather than quantity of inbound FDI.¹⁵⁵² In the 11th Five-Year Plan on the Utilisation of Foreign Investment, the Chinese Government emphasised the significance of high-quality investment, like the environmental-friendly investment.¹⁵⁵³ Correspondingly, non-investment objectives, such as "improving living standards",¹⁵⁵⁴ have been mentioned in the preamble of Chinese BITs.¹⁵⁵⁵

According to the Vienna Convention,¹⁵⁵⁶ although the preamble does not give rise to enforceable rights and obligations, the object and purpose referred to should be taken into account in the overall interpretation of treaties.¹⁵⁵⁷ In this respect, based on the preamble of the recent Chinese BITs, the tribunals should consider the values of foreign investors and the host state, which may concurrently conflict with each other. More specifically, when interpreting FET, tribunals can no longer interpret in favour of foreign investors merely because of the investment protection emphasised in the preamble. Instead, both investment and non-investment values should be considered to ascertain FET's meaning and components, reflecting the need for a balanced interpretation approach, which is the two-tier systemic method in the researcher's review.¹⁵⁵⁸

¹⁵⁴⁷ See an example China-Uzbekistan BIT (n 1064) Preamble.

¹⁵⁴⁸ See an example Canada-China BIT (n 421) Article 33.

¹⁵⁴⁹ China-Finland BIT (n 1471) Preamble.

¹⁵⁵⁰ See an example China-New Zealand BIT (n 871) Preamble.

¹⁵⁵¹ See an example China-Finland BIT (n 1471) Preamble. Shan & Gallagher (n 9) 415. Leon E. Trakman, 'Geopolitics, China, and Investment-State Arbitration' in Lisa Toohey & others (eds.), *China in the International Economic Order: New Directions and Changing Paradigms* (CUP 2015) 272.

¹⁵⁵² '11th Five-Year Plan on the Utilisation of Foreign Investment' (MOFCOM, 13 November 2006)

<<http://www.mofcom.gov.cn/article/zhengcejd/bj/200612/20061204079662.shtml>> [in Chinese] last accessed 24 June 2022.

¹⁵⁵³ *ibid.*

¹⁵⁵⁴ China-Jordan BIT (n 1509) Preamble. China-Tanzania BIT (n 261). Wang & Wang (n 127) 2389.

¹⁵⁵⁵ See examples China-Trinidad and Tobago BIT (signed 22 July 2002, entered into force 7 December 2004), China-Guyana BIT (signed 27 March 2003, entered into force 26 October 2004), China-Uzbekistan BIT (n 1064), Canada-China BIT (n 421).

¹⁵⁵⁶ Vienna Convention (n 47). See generally in Chapter Three.

¹⁵⁵⁷ See 3.3.1.4 in Chapter Three.

¹⁵⁵⁸ See in Chapter Three. *El Paso v. Argentina* (n 5) paras 68, 70.

6.3.2.2 More Non-Investment Values in the Exception Clause

The non-investment purpose pursued by the host state can also be seen in the main text of a treaty, from the provision of prohibitions and restrictions to the exception clause. Both provisions clarify particular situations in which the implemented measures would not be in breach of the treaty even if they renege on the state's obligations *vis-à-vis* foreign investors.¹⁵⁵⁹ As pointed out by Vandeveldel, some treaties provide general exceptions that apply to all treaty obligations, while others prescribe exceptions that only apply to particular obligations,¹⁵⁶⁰ such as FET.

The protection of public interest first appeared in the provision of "prohibitions and restrictions" in the China-Singapore BIT (1985),¹⁵⁶¹ which stipulates that

The provisions of this Agreement *shall not* in any way limit the right of either contracting party to apply *prohibitions or restrictions* of any kind or take any other action which is *directed to* the protection of *its essential security interests*, or to the protection of *public health* or the prevention of *diseases and pests in animals or plants*.¹⁵⁶² [italic added]

This treaty provides a list of non-investment objectives,¹⁵⁶³ including "essential security interests", "public health", and "prevention of disease and pests".¹⁵⁶⁴ The language in this provision, particularly the phrase "directed to", denotes a means-end connection. Interpreting such a clause as a whole expresses that the measures taken by the host state to achieve the listed purposes are justified even if they impair the values of foreign investors, corresponding to the notion of proportionality.

Also, this provision emphasised the significance of "social rights", even though such a term was not explicitly stipulated in the BIT. No defined meaning of "social rights" is provided in the dictionary, but as observed by scholars, this type of right is generally provided to individuals based on their citizenship.¹⁵⁶⁵ As a citizen of a state, the individual has the right to enjoy social insurance, medical and health service, and other material assistance.¹⁵⁶⁶ In this respect, the word "public health" in Article 11 of the China-Singapore BIT (1985)¹⁵⁶⁷ implies the importance of "social rights", emphasising the significance of a state's right to regulate in the public interest. Similar provisions can be seen in Chinese

¹⁵⁵⁹ Dilini Pathirana & Mark McLaughlin, 'Non-Precluded Measures Clauses: Regime, Trends, and Practice' in Julian Chaisse et al. (eds.), *Handbook of International Investment Law and Policy* (Springer 2020) 1, 5.

¹⁵⁶⁰ Kenneth J. Vandeveldel, 'Rebalancing through Exceptions' (2013) 17 *Lewis and Clark Law Review* 449. Pathirana & McLaughlin (n 1559) 1, 5.

¹⁵⁶¹ China-Singapore BIT (signed 21 November 1985, entered into force 7 February 1986, terminated 16 October 2019).

¹⁵⁶² *ibid* Article 11.

¹⁵⁶³ *ibid*.

¹⁵⁶⁴ *ibid*.

¹⁵⁶⁵ See generally in Yuhong Hu, 'Lun She Hui Quan De Xing Zhi' (On the Nature of "Social Rights") (*CALAW*) <<http://www.calaw.cn/article/default.asp?id=14135>> [in Chinese] last accessed 27 June 2022.

¹⁵⁶⁶ See an example the Chinese Constitutional Law (n 45).

¹⁵⁶⁷ China-Singapore BIT (n 1561).

BITs signed with Sri Lanka,¹⁵⁶⁸ New Zealand,¹⁵⁶⁹ and Mauritius,¹⁵⁷⁰ respectively. Instead of "essential security interests", China and Sri Lanka reached a consensus on protecting "national interests".¹⁵⁷¹ The term "national interests", in Pathirana and McLaughlin's view, has a broader interpretation, compared with that of "essential security interests".¹⁵⁷² As they pointed out, national interests refer to various public policy concerns which are not limited to essential security interests.¹⁵⁷³ Additionally, the significance of environmental protection is emphasised in the China-Mauritius BIT (1996).¹⁵⁷⁴

Via the two-tier systemic interpretative approach discussed in Chapter Two, the substantive protections are interpreted in conjunction with the exceptional situations, and the balance of competing values is outlined, linked to the application of proportionality. The rights of foreign investors are protected, but such protection may be limited due to the protection of public interest in the host state. The languages of these two provisions are similar to Articles 33 and 51 of the Chinese Constitutional Law,¹⁵⁷⁵ whose joint interpretation emphasises the significance of the restrictions on the limitations on fundamental rights.¹⁵⁷⁶ More detail on the Constitution will be discussed in Chapter Seven to investigate the legal status of proportionality in the Chinese domestic legal system.¹⁵⁷⁷

The trend towards a balanced investor-state relationship can be seen more clearly in the exception clause, which is clarified even further in the third-generation Chinese BITs. Different exception clauses can be observed in the China-Madagascar BIT (2005),¹⁵⁷⁸ the China-Colombia (2008),¹⁵⁷⁹ and the Canada-China BIT (2012).¹⁵⁸⁰ The Chinese BIT signed with Madagascar stipulates exceptions in the FET clause,¹⁵⁸¹ while another two treaties provide the general exception clause.¹⁵⁸²

The China-Madagascar BIT (2005)¹⁵⁸³ stipulates qualified FET with some exceptional situations in which the measures taken by the host state do not violate its FET obligation. As prescribed in Article 3,

Legal or de facto obstacles to the fair and equitable treatment mainly mean, but not limited

¹⁵⁶⁸ China-Sri Lanka BIT (signed 13 March 1986, entered into force 25 March 1987) Article 11.

¹⁵⁶⁹ China-New Zealand BIT (n 871) Article 11.

¹⁵⁷⁰ China- Mauritius BIT (n 319) Article 11.

¹⁵⁷¹ China-Sri Lanka BIT (n 1568) Article 11.

¹⁵⁷² Pathirana & McLaughlin (n 1559) 1, 10. Amit Kumar Sinha, 'Non-Precluded Measures Provisions in Bilateral Investment Treaties of South Asian Countries' (2017) 7 Asian Journal of International Law 227, 249.

¹⁵⁷³ *ibid.*

¹⁵⁷⁴ China-Mauritius BIT (n 319) Article 11.

¹⁵⁷⁵ The Chinese Constitutional Law (n 45).

¹⁵⁷⁶ See 7.2 in Chapter Seven.

¹⁵⁷⁷ See 7.2 in Chapter seven.

¹⁵⁷⁸ China-Madagascar BIT (n 1509) Article 3.

¹⁵⁷⁹ China-Colombia BIT (n 124) Article 12.

¹⁵⁸⁰ Canada-China BIT (n 421) Article 33.

¹⁵⁸¹ China-Madagascar BIT (n 1509).

¹⁵⁸² China-Colombia BIT (n 124). Canada-China BIT (n 421).

¹⁵⁸³ China-Madagascar BIT (n 1509).

*to: non-equitable treatment of all kinds of restrictions on the means of production and management, non-equitable treatment of all kinds of restrictions on the sale of products at home and abroad, as well as other measures with similar effects. However, the measures for reasons of security, public order, health, ethical and environmental protection and other reasons shall not be regarded as obstacles.*¹⁵⁸⁴ [italic added]

The phrase "not limited to" suggests that an open-ended list of exceptions is provided in this provision. As stressed in the last sentence, the measures in question would not be a breach of FET, even if they are prohibited, only if such means aim to protect "security, public order, health, ethical and the environment".¹⁵⁸⁵ The exception clause aims to justify the measures taken by the host state to pursue the desired purpose, although they are against the FET obligation. However, as questioned by Chi, only the wording "not as obstacles" could not be interpreted as the exemption of the host state's liability.¹⁵⁸⁶ No explanation is provided by him, but it is the researcher's view that, compared with the wording "shall not be precluded" stipulated in the exception clause, the last sentence is weaker.

Unlike the China-Madagascar BIT (2005),¹⁵⁸⁷ both the Canada-China BIT (2012)¹⁵⁸⁸ and the China-Colombia BIT (2008)¹⁵⁸⁹ contains the wording "nothing in this agreement" in the exception clause, indicating that the exceptional situations should apply to the entire treaty.¹⁵⁹⁰ The prime example here is Article 33 (5) of the Canada-China BIT (2012),¹⁵⁹¹ which stipulates that

Nothing in this Agreement shall be construed:

- (a) to require a contracting party to furnish or allow access to any information if *the contracting party determines* that the disclosure of that information is contrary to *its essential security interests*;
- (b) to prevent a contracting party from taking any actions that *it considers necessary* for the protection of *its essential security interests*;
 - (i) relating to the traffic in arms, ammunition and implements of war and to such traffic and transactions in other goods, materials, services and technology undertaken directly or indirectly for the purpose of supplying a military or other security establishment,
 - (ii) in time of war or other emergencies in international relations, or
 - (iii) relating to the implementation of national policies or international agreements respecting the non-proliferation of nuclear weapons or other nuclear explosive devices; or
- (c) to prevent a contracting party from taking action *in pursuance of* its obligations under *the United Nations Charter for the maintenance of international peace and security.*¹⁵⁹² [italic added]

¹⁵⁸⁴ *ibid* Article 3.

¹⁵⁸⁵ *ibid*.

¹⁵⁸⁶ Manjiao Chi, 'The "Greenisation" of Chinese BITs: An Empirical Study of the Environmental Provisions in Chinese BITs and Its Implications for China's Future BIT-Making' (2015) 18 *Journal of International Economic Law* 511, 517.

¹⁵⁸⁷ China-Madagascar BIT (n 1509).

¹⁵⁸⁸ Canada-China BIT (n 421).

¹⁵⁸⁹ China-Colombia BIT (n 124).

¹⁵⁹⁰ Chi (n 1586) 528.

¹⁵⁹¹ Canada-China BIT (n 421).

¹⁵⁹² Canada-China BIT (n 421) Article 33 (5).

Learning from the Argentinian cases discussed in Chapter Five,¹⁵⁹³ the term "necessary" mentioned in the exception clause could be a textual basis of applying proportionality in the ISDS. One noteworthy point is that, compared with other sub-paragraphs in Article 33, Article 33 (5) contains the phrases "the contracting party determines", "its essential security interests", and "it considers necessary". Based on the earlier discussion, these wordings explicitly reflect the self-judging nature of this sub-paragraph.¹⁵⁹⁴ This conveys that the host state, rather than the tribunal, is the decision-maker who has the power to decide whether the state's interest is at stake and needs to be guaranteed by any particular measures.¹⁵⁹⁵ In this situation, the tribunal can merely review whether the state has acted in good faith.

Compared with its treaty signed with Canada,¹⁵⁹⁶ the Chinese BIT signed with Colombia prescribes a more detailed exception clause.¹⁵⁹⁷ Interestingly, almost all relevant factors that should be taken into consideration within the process of proportionality analysis are listed in Article 12, which stipulates that

Nothing contained in this Agreement shall be construed so as to prevent a Party from adopting or maintaining measures intended to preserve public order, including measures to protect the essential security interests of the state, provided that such measures:

- (a) are only applied where *a genuine and sufficiently serious threat* is posed to one of the *fundamental interests of society*;
- (b) are not applied in a manner constituting *arbitrary discrimination*;
- (c) do not constitute *a disguised restriction on investment*;
- (d) are *proportional to the objective they seek to achieve*;
- (e) are *necessary* and are applied and maintained only while necessary; and
- (f) are applied in a *transparent manner* and *in accordance with the respective national legislation*.

For greater clarity, nothing under this paragraph shall be construed to limit the review by an arbitral tribunal of a matter when such an exception is invoked.¹⁵⁹⁸[*italic added*]

Similar to Article 36 of the South African Constitution, which was discussed in Chapter Two,¹⁵⁹⁹ Article 12 of the China-Colombia BIT (2008)¹⁶⁰⁰ provides a list of constituent elements of proportionality: Article 12 (a) introduces the purposes pursued by the host state, Article 12 (b) (c) and (f) refer to the nature of the implemented means, and Article 12 (d) and (e) describe the means-end connection. More specifically, this provision stipulates that the purposes pursued by the host state are generally related to the conservation of public order.¹⁶⁰¹ As indicated by the word "including", the desired aims are not only

¹⁵⁹³ See in Chapter Five.

¹⁵⁹⁴ See 5.3.2 in Chapter Five.

¹⁵⁹⁵ See 5.3.2 in Chapter Five.

¹⁵⁹⁶ Canada-China BIT (n 421).

¹⁵⁹⁷ China-Colombia BIT (n 124).

¹⁵⁹⁸ *ibid* Article 12.

¹⁵⁹⁹ See 2.4 in Chapter Two.

¹⁶⁰⁰ China-Colombia BIT (n 124) Article 12.

¹⁶⁰¹ *ibid*.

limited to protecting essential security interests.¹⁶⁰² Article 12 (a) further stresses the importance of the value pursued by the host state, which should not only be "fundamental" but also be at stake.¹⁶⁰³ Such requirements reflect a high threshold for a state to invoke the necessity from the perspective of the desired purpose. However, due to the lack of defined criteria, one may doubt what threats are "genuine and sufficiently serious". As a result of the absence of qualifying language, such as "it considers", questions remain as to whether it is the host state or the tribunal that can decide what the fundamental interests are and whether they are at stake. These doubts may raise some issues in the application of proportionality in practice, as seen in the Argentinian cases.¹⁶⁰⁴

Concerning the limits on fundamental rights, its nature is uncovered from both positive and negative perspectives, emphasising the legitimacy of the means in question to avoid misapplication.¹⁶⁰⁵ On the one hand, its implementation should be transparent and follow the rules and regulations.¹⁶⁰⁶ On the other hand, the exception cannot be misused as an excuse to infringe on the rights of foreign investors.¹⁶⁰⁷

A reasonable connection between the implemented means and the achieved purpose is suggested in Article 12 (d) and (e), particularly the terms "necessary" and "proportional".¹⁶⁰⁸ Although the impairment of foreign investors' values is not referred to in this provision, it is one of those factors that should be considered in balancing conflicting values to answer whether the means are proportionate to the desired purpose. One notable point in the China-Colombia BIT (2008)¹⁶⁰⁹ is that this treaty is the only Chinese BIT in which the term "proportional" explicitly appears. By comparing the Chinese Model BIT (draft) and that of Colombia, such a feature of the China-Colombia BIT (2008) may result from the consideration of the Colombia Model BIT (2008),¹⁶¹⁰ which explicitly emphasises that in order to be justified, the measures implemented in contradiction of the state's obligations *vis-à-vis* foreign investors should be "proportional to the objectives sought".¹⁶¹¹

Moreover, the emphasis on a fair balance between the values of foreign investors and the host state's rights to regulate in the public interest, which corresponds to the notion of proportionality *stricto sensu*, can also be observed in the adverb "only" that appears twice in Article 12 of the China-Colombia BIT

¹⁶⁰² *supra* note 644, the word "includes" implies an exemplified list.

¹⁶⁰³ China-Colombia BIT (n 124).

¹⁶⁰⁴ See generally in Chapter Five.

¹⁶⁰⁵ Chi (n 1586) 521. Pathirana & McLaughlin (n 1559) 1, 15.

¹⁶⁰⁶ See examples China-Colombia BIT (n 124) Article 12. China-India BIT (signed 21 November 2006, entered into force 1 August 2007, terminated 3 October 2018) Article 14.

¹⁶⁰⁷ Pathirana & McLaughlin (n 1559) 1, 15. Chi (n 1586) 521.

¹⁶⁰⁸ China-Colombia BIT (n 124).

¹⁶⁰⁹ *ibid.*

¹⁶¹⁰ The Colombia Model BIT (n 1115).

¹⁶¹¹ *ibid* Article 8, stipulating that '[n]othing in this Agreement shall be construed to prevent a contracting party from adopting, maintaining, or enforcing any measure that it considers appropriate to ensure that an investment activity in its territory is undertaken in accordance with environmental law of the contracting party, provided that such measures are proportional to the objectives sought'.

(2008).¹⁶¹² The plain meaning of "only" stresses the exclusivity of exceptional situations in which foreign investors' interest is impaired for the public interest.¹⁶¹³ Such limits are restricted by the requirements of grave peril in which the state might find itself and the necessity of equally grave reactions. As suggested by the joint interpretation of Article 12 (a) and (e), once the threats subside, the host state should stop its action; Otherwise, it would breach treaty obligations *vis-à-vis* foreign investors and cannot be exempted from liability. This systemic interpretation further emphasises a balance between the conflicting values of foreign investors and the host state, which can be achieved by the test of proportionality *stricto sensu*, the last assessment included in proportionality analysis.

The above analyses and comparisons between the provision of prohibition and restrictions in earlier Chinese BITs and the exception clause in later ones reflect the evident expansion of non-investment values referred to in Chinese BITs. This dovetails with China's growing concerns about non-economic values.¹⁶¹⁴

6.3.3 Other Considerations-Increasing Obligations of Foreign Investors

Like many other countries, China mainly provided attractive investment environments rather than obligations to foreign investors in its decades-old, legacy IIAs.¹⁶¹⁵ However, the recent Chinese BITs have increasingly expanded foreign investors' positive obligations, thereby rebalancing the investor-state relationship.

There is no doubt that the protection of non-economic values in a state cannot be separated from the behaviours of individuals, including foreign investors.¹⁶¹⁶ As pointed out by Chi, the performance of investors' duties contributes somewhat to the protection of the host state's own public interest.¹⁶¹⁷ In Nathalie's view, those obligations, chief among them, CSR regulates and improves foreign investors' conduct.¹⁶¹⁸ This can ameliorate domestic issues in the host state, such as environmental protection and human rights.¹⁶¹⁹ Apart from compliance with the host state's domestic laws and regulations, which are required in the provision of definition,¹⁶²⁰ the CSR term is also mentioned in Chinese treaties. For example, the China-Tanzania BIT (2013)¹⁶²¹ encourages foreign investors to "respect corporate social

¹⁶¹² China-Colombia BIT (n 124).

¹⁶¹³ 'Only' (OED) <https://www-oed-com.ezproxy-s1.stir.ac.uk/search?searchType=dictionary&q=ONLY&_searchBtn=Search> last accessed 24 June 2022.

¹⁶¹⁴ Trakman (n 1551) 277.

¹⁶¹⁵ Eric De Brabandere & Paula Baldini Miranda da Cruz, 'The Role of Proportionality in International Investment Law and Arbitration: A System-Specific Perspective' (2020) 89 *Nordic Journal of International Law* 471, 473.

¹⁶¹⁶ Cai, 'China-US BIT' (n 1464) 503.

¹⁶¹⁷ Chi (n 1586) 538.

¹⁶¹⁸ Nathalie Bernasconi-Osterwalder, 'Inclusion of Investor Obligations and Corporate Accountability Provisions in Investment Agreements' in J.Chaisse et al. (eds.), *Handbook of International Law and Policy* (Springer 2021) 465.

¹⁶¹⁹ *ibid.*

¹⁶²⁰ *ibid* 472-3.

¹⁶²¹ China-Tanzania BIT (n 261).

responsibilities",¹⁶²² and the China-Japan-Korea TIT (2012)¹⁶²³ expresses investors' contribution to "the economic, social and environmental progress".¹⁶²⁴ However, these treaty provisions reflect encouragement rather than obligation because they do not have binding force due to appearing in the preamble.

Compared with the above treaties, the China-Namibia BIT (2005)¹⁶²⁵ goes further and stipulates a particular "corporate responsibility" clause, mandating foreign investors' obligations in a mandatory manner.¹⁶²⁶ As required in Article 10, "[i]nvestors shall abide by the host country's laws, regulations, administrative guidelines and policies in the same manner as any domestic investor".¹⁶²⁷ Unfortunately, this BIT has not entered into force partly because of Namibia's own negative attitude to BITs.¹⁶²⁸ As explained by Lindeque in the World Investment Forum 2014, due to the shortcomings of BITs, such as the threats to developing countries, the BIT regime was re-evaluated by the Government of Namibia.¹⁶²⁹

Foreign investors' positive obligations can also be seen in the new draft of the Chinese Model BIT.¹⁶³⁰ As expressed in Article 13, investors are encouraged "to conduct their investment activities in a socially responsible manner, by complying with the OECD Guideline for Multinational Enterprises and participating in the United Nations Global Compact".¹⁶³¹ Based on the Guideline, investors should "contribute to economic, environmental and social progress with a view to achieving sustainable development"¹⁶³² and undertake "risk-based due diligence".¹⁶³³ Meanwhile, they should also disclose relevant information on their investments timely and accurately¹⁶³⁴ and participate in anti-corruption and anti-bribery.¹⁶³⁵ Prescribing investors' obligations by reference to other international instruments, as ascertained by Bernasconi-Osterwalder, stresses the purpose pursued by states in international investment and other fields of international law,¹⁶³⁶ contributing to the coherence between a state's various duties stipulated in different international instruments. Article 13 reflects China's intention to regulate investors' conduct to protect non-investment values, but unfortunately, the draft has not been approved as a new Chinese Model BIT.

¹⁶²² *ibid* Preamble.

¹⁶²³ China-Japan-Korea, Republic of TIT (n 1402).

¹⁶²⁴ *ibid* Preamble.

¹⁶²⁵ China-Namibia BIT (signed 17 November 2005).

¹⁶²⁶ *ibid*

¹⁶²⁷ *ibid* Article 10.

¹⁶²⁸ Xiuli Han, 'Zhong Fei Shuang Bian Tou Zi Tiao Yue Xian Zhuang Yu Qian Jing' (China-Africa BITs: Current Condition and Future Prospects) [2015] *Journal of Xiamen University (Arts & Social Science)* 48, 50 [in Chinese].

¹⁶²⁹ Malan Lindeque, *The Statement of Namibia, World Investment Forum 2014: Investing in Sustainable Development* 1.

¹⁶³⁰ Shan & Gallagher (n 9) 460-7.

¹⁶³¹ *ibid* 463 [italic added].

¹⁶³² OECD, *Guidelines for Multinational Enterprises* (n 1090) 19.

¹⁶³³ *ibid* 20.

¹⁶³⁴ *ibid* 27.

¹⁶³⁵ *ibid* 47.

¹⁶³⁶ Bernasconi-Osterwalder (n 1618) 467.

Because of the above changes in the treaty preamble, the provision of FET and the exception clause in Chinese BITs, China has tangibly attempted to find a balanced paradigm of its IIAs to strike a balance between the conflicting values of foreign investors and the host state. Compared with the earlier treaties, more recent Chinese BITs clarify and specify substantive protections provided to foreign investors, restricting the discretion granted to tribunals and preserving the host state's regulatory power.

Meanwhile, the scope of protected non-investment values has been expanded, stressing the significance of the host state's right to regulate in the public interest. Additional emphasis is placed upon the importance of foreign investors' obligations. In the systemic interpretative approach, a treaty is interpreted as a whole.¹⁶³⁷ In this respect, all such factors in Chinese BITs should be considered when interpreting treaties. Like the two sides of a scale, the clarified protection of investment values counterbalances the expanded protection of non-investment values. At least from the perspective of treaty interpretation, this provides a fulcrum in the investor-state relationship.

6.4 Can Proportionality Be Applied in China's Investor-State Disputes?

Considering the uncertainties arising from applying the principle of proportionality in the ISDS, as seen in Chapters Two and Five, one may question how this structured and flexible tool could be applied in Chinese international investment practice.¹⁶³⁸ One difficulty that arises before answering this question is the insufficient number of cases in which China has been involved. So far, China has only participated in 28 ISDs: 19 cases as the claimant's home state¹⁶³⁹ and nine as the respondent.¹⁶⁴⁰ The most applicable instruments in these cases were Chinese BITs signed in the first two generations, which chiefly emphasised investment protection and provided unqualified FET.¹⁶⁴¹ Half of such cases are still pending (nine cases as the home state, five as the respondent state),¹⁶⁴² and none of the settled ISDs mentioned proportionality.

Due to the lack of Chinese cases upon which the application of proportionality could be analysed, this section mainly focuses on whether the principle of proportionality can be applied to settle Chinese ISDs in general, from both perspectives of treaty interpretation and application. This is especially considering Ranjan's disagreement with its application. In his view, no treaty provisions define how investment protection is balanced with the host state's regulatory power for the public interest.¹⁶⁴³ The earlier discussion on the application of proportionality in the Argentinian cases, which were analysed in

¹⁶³⁷ See 3.4.4 in Chapter Three.

¹⁶³⁸ See generally in Chapters Two and Five.

¹⁶³⁹ See Table 1.2 in Chapter One, including the investors who come from special administrative regions of China.

¹⁶⁴⁰ See Table 1.3 in Chapter One.

¹⁶⁴¹ See Tables 1.2 and 1.3 in Chapter One.

¹⁶⁴² See Tables 1.2 and 1.3 in Chapter One.

¹⁶⁴³ Ranjan (n 18) 881.

Chapter Five,¹⁶⁴⁴ will also be reflected on how such a tool might be applied in Chinese international investment practice.

6.4.1 Can Proportionality Be Applied in Treaty Interpretation?

Based on the earlier discussion in Chapter Four, the systemic approach is an appropriate interpretative method, which stresses that a treaty should best be interpreted as a whole.¹⁶⁴⁵ Articles 31 and 32 of the Vienna Convention explicitly stipulate that the critical interpretative elements are the ordinary meaning of the term in question, the context in which it appears, and the object and purpose of the treaty.¹⁶⁴⁶ All of these factors are vital in treaty interpretation. As emphasised by Gardiner, these interpretative elements should be considered to deduce treaty provisions on a case-by-case basis.¹⁶⁴⁷

Applying the principle of proportionality in treaty interpretation, as evaluated by Calamita, contributes to a balanced comprehension.¹⁶⁴⁸ "Proportionality" implies a balance,¹⁶⁴⁹ and its application, in his view, partly protects a state from its broad treaty obligations *vis-à-vis* foreign investors.¹⁶⁵⁰ However, Spiermann pointed out that proportionality is nothing but merely a scale without weights without the identified values.¹⁶⁵¹ Fortunately, as discussed above,¹⁶⁵² unlike its treaties signed decades ago, the recent Chinese BITs not only clarify substantive protections provided to foreign investors, but also stress the significance of the host state's power to regulate for the public interest. In the researcher's view, these changes provide details as to the weights on both sides of the scale, offering a balanced interpretation.

A prominent example here is the China-Tanzania BIT (2013),¹⁶⁵³ which mentions both investment and non-investment values and foreign investors' positive obligations in the preamble.¹⁶⁵⁴ Eschewing unqualified FET, this BIT provides qualified protection in Article 5 and clarifies certain exceptional situations in which the host state's measures are justified, even if they are against the treaty obligations in Article 10.¹⁶⁵⁵ Based on the rules of interpretation provided in the Vienna Convention, the FET standard enjoyed by foreign investors is considered first. As discussed previously, the FET clause with qualifying language limits the tribunals' discretion and avoids broad interpretations that unfairly favour

¹⁶⁴⁴ See in Chapter Five.

¹⁶⁴⁵ See 4.4.5 in Chapter Four.

¹⁶⁴⁶ See in Chapter Four.

¹⁶⁴⁷ Gardiner (n 49) 464.

¹⁶⁴⁸ N. Jansen Calamita, 'International Human Rights and the Interpretation of International Investment Treaties: Constitutional Considerations' in Freya Baetens (ed), *Investment Law within International Law* (CUP 2013) 174.

¹⁶⁴⁹ *ibid* 175.

¹⁶⁵⁰ *ibid* 174.

¹⁶⁵¹ Ole Spiermann, 'Twentieth Century Internationalism in Law' (2008) 18 *The European Journal of International Law* 785, 802.

¹⁶⁵² Text to 6.3.

¹⁶⁵³ China-Tanzania BIT (n 261).

¹⁶⁵⁴ *ibid*.

¹⁶⁵⁵ *ibid* Articles 5 and 10.

investors.¹⁶⁵⁶ Relevant contexts in which "FET" appears and the object and purpose of a treaty are then taken into account. In this respect, non-investment objectives referred to in the preamble and exception clause act as a counterbalance to FET and are considered to limit investors' rights. Similarly, these limits are also restricted by the requirements prescribed in the exception clause, such as the necessity of the implemented means. As an outcome of the systemic interpretation, the qualified substantive treatments are interpreted in conjunction with the protected non-investment values, illustrating a process of weighing and balancing competing values, which directly relates to the application of proportionality.

Nevertheless, as argued by Ranjan, applying proportionality in treaty interpretation may lead to issues.¹⁶⁵⁷ The application of proportionality may conflict with the principles of interpretation provided by the Vienna Convention.¹⁶⁵⁸ As discussed in Chapter Three, the interpretative rules require that treaty provisions be interpreted with consideration to the plain meaning of the questioned term, the context in which it appears, and the object and purpose of the treaty.¹⁶⁵⁹ However, as illustrated by Ranjan, the provision of expropriation explicitly expresses that foreign investors' investments should not be expropriated unless the purpose pursued is for the public and the appropriate compensation is provided.¹⁶⁶⁰ Conversely, according to the principle of proportionality, such measures would be justified if they are proportional to the achievement of the desired purpose, even if they oppose the treaty obligations to foreign investors.¹⁶⁶¹ From the perspective of this result, it seems like the latter interpretation is reasonable because of a rational means-end connection. However, it fails to follow the interpretative rules, revealing a tangible drawback of applying proportionality in treaty interpretation.

Ranjan also doubts that the application of proportionality may expand the scope of exceptions in which the host state does not breach its treaty obligations, even if its actions impair foreign investors' rights.¹⁶⁶² Not all IIAs contain the exception clause, and therefore not all tribunals have the power to apply proportionality in treaty interpretation. They should follow the treaty text itself when interpreting ambiguous provisions. However, as proved by Ranjan, any questionable measure may be justified due to its proportional connection to the pursued purpose without consideration of the requirement stipulated in the treaty.

Nevertheless, such a nature of proportionality is not agreed upon by the researcher, who found in Chapter Two that proportionality is neither an international custom nor a general principle of law.¹⁶⁶³

¹⁶⁵⁶ Wang & Wang (n 127) 2385.

¹⁶⁵⁷ Ranjan (n 18) 873-4.

¹⁶⁵⁸ *ibid* 873-4, 882.

¹⁶⁵⁹ Vienna Convention (n 47).

¹⁶⁶⁰ Ranjan (n 18) 869-70.

¹⁶⁶¹ *ibid*.

¹⁶⁶² *ibid* 873-4.

¹⁶⁶³ See 2.3 in Chapter Two.

As a flexible tool to balance competing values, the principle of proportionality could be applied in the ISDS based on its textual basis in case-related treaties, which can also be observed in Chinese treaties, especially the third-generation Chinese BITs. Although some values may need to be further clarified on the basis of other relevant international instruments, at least a scale is provided, implicitly or explicitly, to strike a balance. Instead of conflicting interpretations, interpreting the treaty as a whole by applying proportionality leads to a balanced interpretation.

6.4.2 Can Proportionality Be Applied in Treaty Application?

As a tool, proportionality can also be applied in treaty application if it is implicitly or explicitly expressed in treaties, such as the China-Colombia BIT (2008).¹⁶⁶⁴ However, due to China's limited ISDS in which it was involved and the absence of proportionality in these cases, it is difficult to ascertain the role of this tool in Chinese ISA practice.

Nevertheless, based on the earlier discussion on the Argentinian cases,¹⁶⁶⁵ at least, it is evident which approach to proportionality can be adopted in the ISDS to settle ISDs.¹⁶⁶⁶ By comparing the language of the applicable instrument of those Argentina's cases, namely the Argentina-US BIT (1991),¹⁶⁶⁷ with that of Chinese BITs, a potential trend can be seen where the principle of proportionality could be applied in Chinese ISDs.

The issues arising from applying proportionality in the Argentinian cases might also emerge in Chinese ISA practice. As analysed in Chapter Five, the term "necessary" appears in Article XI of the Argentina-US BIT (1991)¹⁶⁶⁸ as the basis of applying proportionality to balance the contradictory values of foreign investors and Argentina.¹⁶⁶⁹ Issues arose from the absence of qualifying language and the lack of defined criteria for "necessity". No detail was provided in the Argentina-US BIT (1991) to clarify who had the power to decide whether the state interest was at stake and needed to be protected by particular means. Without a defined criterion for "necessity", the necessity test included in proportionality analysis would be muddled with the state of necessity stipulated in Article 25 of the ILC's Articles.¹⁶⁷⁰ This could lead to different, even opposing, judgments on the same measures.

Similar to Article XI of the Argentina-US BIT (1991),¹⁶⁷¹ the exception clause contained in most Chinese BITs refers to "measures necessary for" the desired purpose but provides no word on the

¹⁶⁶⁴ China-Colombia BIT (n 124).

¹⁶⁶⁵ See generally in Chapter Five.

¹⁶⁶⁶ See generally in Chapter Five.

¹⁶⁶⁷ Argentina-US BIT (n 120).

¹⁶⁶⁸ *ibid* Article XI.

¹⁶⁶⁹ See 5.3.1 in Chapter Five.

¹⁶⁷⁰ Wrongful Acts (n 422).

¹⁶⁷¹ Argentina-US BIT (n 120).

decision-maker.¹⁶⁷² However, some changes can still be observed in the recent Chinese BITs. Instead of merely the term "necessary", the implemented measures are qualified with the phrase "it considers necessary".¹⁶⁷³ As expressed in this language, such an exception clause is a self-judging provision.¹⁶⁷⁴ Consequently, the host state is left with some leverage to make decisions on what means should be taken to protect its essential security interest.¹⁶⁷⁵ The tribunals solely carry out a good-faith review of the impugned measures.¹⁶⁷⁶

A notable point in Article 33 of the Canada-China BIT (2012)¹⁶⁷⁷ may be noted. The qualifying language "it considers" is merely referred to in the exceptional situation as a state's "essential security interests".¹⁶⁷⁸ The measures taken to protect other non-investment objectives, such as environmental protection, are only required to be "necessary" or "reasonable" without more detail.¹⁶⁷⁹ Such differences in the wording, which is applied to describe the implemented measures that contribute to the achievement of various non-investment values, may support the view of Henckels. She points out that based on the text of the applicable legal instrument, proportionality, as a tool, could be strict or deferential.¹⁶⁸⁰ The deference is left to the host state when making decisions on vital non-investment values. At the same time, the tribunals enjoy discretionary power to make decisions on other values. In the researcher's view, such flexible language balances the doubts on the host state's abuse of exception clauses and the arbitral tribunals' hindsight.

The terms "necessary" and "proportional"¹⁶⁸¹ also suggest the textual basis in Chinese BITs for the application of proportionality in the ISDS, somewhat balancing the conflicts between the values of foreign investors and the host state. Although there are no existing Chinese ISDs in which proportionality was overtly applied, this can be gleaned from the comparison between Article XI of the Argentina-US BIT (1991)¹⁶⁸² and the exception clause in Chinese BITs.

Some Chinese treaties even go a step further and explicitly identify the decision-maker within the process of proportionality analysis based on particular non-investment values pursued by the host state. These clarifications go some way to balancing the avoidance of the tribunals' second-guessing and the prevention of the host state's abuse of invoking the necessity based on exception clauses.

¹⁶⁷² *ibid* Article XI.

¹⁶⁷³ See examples China-Colombia BIT (n 124), Canada-China BIT (n 421).

¹⁶⁷⁴ See 5.3.2 in Chapter Five.

¹⁶⁷⁵ Sinha (n 1572) 249.

¹⁶⁷⁶ Pathirana & McLaughlin (n 1559) 1, 16-7.

¹⁶⁷⁷ Canada-China BIT (n 421).

¹⁶⁷⁸ *ibid*.

¹⁶⁷⁹ *ibid* Article 33 (2).

¹⁶⁸⁰ Caroline Henckels, 'Balancing Investment Protection and the Public Interest: The Role of the Standard of Review and the Importance of Deference in Investor-State Arbitration' (2013) 4 *Journal of International Dispute Settlement* 197, 203-4.

¹⁶⁸¹ China-Colombia BIT (n 124).

¹⁶⁸² Argentina-US BIT (n 120).

6.5 Conclusion

With the changes in China's role in international investment, it has placed more emphasis on equally protecting foreign investors' rights and guaranteeing the host state's right to regulate in the public interest. Meanwhile, with the increasing attention to non-economic values, the promotion and protection of investments are not the only object and purpose of a treaty, and non-investment objectives are also a significant aim. In this respect, striking a fair balance between the conflicting values of foreign investors and the host state and assuaging the resulting discord is entirely in China's fundamental interest.

However, the issue is that most Chinese BITs, which predominantly contain broad investment protections, were signed decades ago without any amendments. One may question which approach in Chinese ISA practice weighs the conflicting values between foreign investors and the host state. Based on the previous discussion, the application of proportionality in the ISDS depends on its textual basis in case-related treaties because it is neither an international custom nor a general principle of law.

The problem, then, is whether Chinese BITs refer to such a textual basis of the application of proportionality. By analysing the language of Chinese treaties, in particular its recent BITs, the substantive treatments provided to foreign investors are defined in detail, yet the scope of protected objectives is expanded, refers to investment but also contains non-investment values. These revisions show that China has sought to strike a balance between the rights of foreign investors and those of the host state, which can be achieved by applying proportionality. Some specific terms, such as "necessary" and "proportional", also directly imply the application of proportionality in practice.

Moreover, as suggested by the comparison between the wording of the exception clause in the Argentina-US BIT (1991)¹⁶⁸³ and that in Chinese BITs, proportionality is applicable to settle ISDs in which China is involved only if such a notion is referred to in the case-related treaty. Compared with the former,¹⁶⁸⁴ some recent Chinese treaties clarify exceptional situations with qualifying language, such as the phrase "it considers necessary", explicitly stressing that the host state has the critical power to decide whether the public interest is at stake and needs to be guaranteed by the particular measures. Moreover, as reflected in different wording applied in Article 33 of the Canada-China BIT (2012),¹⁶⁸⁵ the precise decision-maker in proportionality analysis varies from one specific desired purpose to another. It is the researcher's view that this language implies a balance between deference to the host state and the tribunals' discretion. Then, based on the application of proportionality, if the questioned measures taken by the host state can fulfil the requirements, they are justified even if they contravene

¹⁶⁸³ *ibid.*

¹⁶⁸⁴ *ibid.*

¹⁶⁸⁵ Canada-China BIT (n 421).

obligations *vis-à-vis* foreign investors. Consequently, the state is exempted from liability.

However, the issue arising from the application of proportionality in the Argentinian cases stemming from Argentina's economic crisis of 2001/2 may also appear when applying proportionality in Chinese ISA practice. As discussed in Chapter Five, the confused utilisation of two sources for invoking necessity led to different, even contradictory, results. One is the necessity test included in proportionality analysis, while another is the state of necessity stipulated in Article 25 of the Wrongful Act.¹⁶⁸⁶ Although different requirements should be fulfilled to invoke these two types of "necessity", the arbitral tribunals may omit their differences in practice. In addition, based on the earlier discussion in Chapter Two, the term "necessary" itself may contain two criteria, which are "the less restrictive means" test and "the only measure" test.¹⁶⁸⁷ The wording of Chinese BITs has no detail on which criterion should be adopted. Therefore, the issue arising from the uncertain application of two criteria for "necessity" may also affect the application of proportionality in Chinese ISA practice. However, "the less restrictive means" is more reasonable from both practical and analytical perspectives, as the researcher concluded in Chapter Two.¹⁶⁸⁸

China currently has no ISDs in which proportionality has been overtly applied, but as examined in this chapter, the textual basis of the application of proportionality in its ISA can be observed in its treaties, in particular the recent BITs. China has concluded new treaties or replaced old treaties with the new generation BITs that provide clarified substantive protections afforded to foreign investors and emphasise the importance of non-investment objectives. Such changes imply a trend in applying proportionality as a tool to balance opposing foreign investors' rights and the host state's power to regulate in the public interest. Although these BITs only occupy a small part of existing Chinese treaties, and some of them are affected by the model BIT of another contracting party, China has, slowly but steadily, applied a balanced paradigm of IIAs to weigh the conflicting values of foreign investors and the host states. This will be tested in future practice in China.

¹⁶⁸⁶ See 5.4.2 in Chapter Five

¹⁶⁸⁷ See 2.4.3 in Chapter Two.

¹⁶⁸⁸ See 2.4.3 in Chapter Two.

Chapter 7

Can Proportionality Be Applied Based on the Chinese Domestic Law?

7.1 Introduction

As established in Chapter Two, proportionality is neither an international custom nor a general principle of law, but it is a highly flexible tool which can be applied to weigh and balance competing values, if it is included in the applicable law for the dispute, including the case-related treaty or the domestic law of the host state.¹⁶⁸⁹ The first route was examined in Chapter Six, expressing that China has slowly but steadily adopted a balanced paradigm of IIAs to weigh discord between the values of foreign investors and the host state.¹⁶⁹⁰ This chapter focuses on another route, which is related to the legal status of proportionality in the Chinese domestic legal system.

According to the ISDS clause stipulated in IIAs, the tribunals shall "adjudicate in accordance with the law of the contracting party to the dispute accepting the investment including its rules on the conflict of laws, the provisions of the IIA".¹⁶⁹¹ Meanwhile, as one of the specially affected states in the context of international investment, the practice of proportionality in China, to a certain extent, affects the answer to the question of whether it is an international custom or a general principle of international law.¹⁶⁹² However, China has only been involved in 28 ISDs;¹⁶⁹³ Highlighting inherent difficulties in finding a workable Chinese consideration of applying proportionality from the arbitral awards.

Based on the earlier discussion in Chapter Three, the non-disputing treaty party can still participate in treaty interpretation during the arbitral proceedings.¹⁶⁹⁴ The interpretation of proportionality provided by China can be deduced from its courts' decisions. In this regard, applying proportionality in settling the cases in which China is involved could significantly depend on proportionality's legal status in the Chinese domestic legal system, especially considering China's current leviathan status in international investment.

Nevertheless, as Vadi pointed out, the legal status of proportionality in China remains uncertain.¹⁶⁹⁵ Unlike most other countries, debates on the principle of proportionality amongst Chinese scholars are relatively recent. In 1988, the concept of "proportionality" drew attention after the publication of Koichi's article *The Infringement of Basic Civil Rights and Grundsatz Der Verhältnismässigkeit*.¹⁶⁹⁶

¹⁶⁸⁹ See 2.3 in Chapter Two.

¹⁶⁹⁰ See generally in Chapter Six.

¹⁶⁹¹ See an example China-Turkey BIT (n 15) Article 9.

¹⁶⁹² See 2.3.1.1 and 2.3.2.1 in Chapter Two.

¹⁶⁹³ *supra* note 17.

¹⁶⁹⁴ See 3.2.1 in Chapter Three.

¹⁶⁹⁵ Vadi, *Proportionality* (n 22).

¹⁶⁹⁶ Yang (n 161). Xia Hua (trans), Aoyagi Koichi, 'Ji Ben Ren Quan De Qin Fan Yu Bi Li Yuan Ze' (The Infringement of Basic Civil Rights and Grundsatz Der Verhältnismässigkeit) (1988) *Journal of Comparative Law* 34 [in Chinese].

Until then, the word "proportionality" or its equivalent terms had made no appearance in Chinese laws and regulations. Debates over whether such a principle was included in the Chinese domestic legal system arose.

Following the ideology of positive law, Han¹⁶⁹⁷ and Hu¹⁶⁹⁸ state that the principle of proportionality does not exist due to the absence of an explicit provision. By contrast, others argue that this principle has been implied by the language of Chinese laws and regulations.¹⁶⁹⁹ In Lin and Ji's views, the principle of proportionality is derived from the notions of "the rule of law" and "human rights", which are contained in the Chinese Constitutional Law.¹⁷⁰⁰ Conversely, Huang and Yang regard it as a principle in Chinese administrative law.¹⁷⁰¹ The differences in these positions of proportionality are highlighted by Chen.¹⁷⁰² In his view, if proportionality is a constitutional principle, it requires the legislature to restrict the limits on citizens' rights within the necessary rubric for the public interest.¹⁷⁰³ In this respect, such a tool can be used to examine whether a law contravenes the Chinese Constitutional Law. Alternatively, if proportionality is a principle in administrative law, it merely requires the administrative authorities to balance differing values when exercising their power,¹⁷⁰⁴ emphasising the significance of a proportionate means-end relationship.

Those scholars who hold similar views on the legal status of proportionality also have divergencies on its nature and textual basis.¹⁷⁰⁵ For example, Men, Rao, and Chen regard proportionality as a constitutional principle based on different constitutional rules.¹⁷⁰⁶ As opined by Rao and Chen, the combination of Articles 33 and 51 of the Constitution implies proportionality,¹⁷⁰⁷ which is refused by Men.¹⁷⁰⁸ Instead, he points out that a hierarchy of interests is included in Article 51, indicating the lack of necessity and the possibility of balancing different values.¹⁷⁰⁹ To add to the confusion, applying proportionality as a constitutional principle in practice is in doubt because the Chinese Constitutional Law cannot be directly cited by the courts in their judgments.¹⁷¹⁰ Consequently, even if the notion of

¹⁶⁹⁷ Han, 'The Application of the Principle of Proportionality' (n 145) 650.

¹⁶⁹⁸ Hu, *Zhong Guo* (n 145) 130.

¹⁶⁹⁹ Men, 'Bi Li Yuan Ze' (n 148) 94. Yi Zhai, 'Bi Li Yuan Ze De Zhong Guo Xian Fa Gui Fan Ji Chu Xin Lun-Yi Xian Fa Di 33 Tiao Wei Zhong Xin' (The New Theory of the Chinese Constitutional Normative Basis of the Principle of Proportionality-Centred on Article 33 of the Chinese Constitution) (2012) *Social Sciences in Xinjiang* 88 [in Chinese].

¹⁷⁰⁰ Laifan Lin & Yanmin Ji, 'Ren Quan Bao Zhang: Zuo Wei Yuan Ze De Yi Yi' (The Protection of Human Rights: The Meaning as a Principle) (2005) 5 *Studies in Law and Business* 64, 65-7 (2005) [in Chinese].

¹⁷⁰¹ Huang & Yang (n 155) 15.

¹⁷⁰² Chen (n 156).

¹⁷⁰³ *ibid.*

¹⁷⁰⁴ *ibid.*

¹⁷⁰⁵ Men, 'Bi Li Yuan Ze' (n 148) 94. Rao & Chen (n 146) 38.

¹⁷⁰⁶ *ibid.*

¹⁷⁰⁷ Rao & Chen (n 146) 40.

¹⁷⁰⁸ Men, 'Bi Li Yuan Ze' (n 148) 94, 100-1.

¹⁷⁰⁹ *ibid.*

¹⁷¹⁰ Jinguang Hu, 'Lun Wo Guo Fa Yuan Shi Yong Xian Fa De Yuan Ze' (On the Principles of Applying the Constitution in the Chinese Courts) (2020) *Administrative Management Reform* 11 [in Chinese].

proportionality can be seen in the Constitution as a constitutional principle, it cannot be applied in practice. As emphasised by Chen, there is no room left for applying proportionality in the Chinese current domestic legal system.¹⁷¹¹

At the same time, the scholars who regard proportionality as a principle in administrative law also hold various opinions on its relationship with the principle of reasonableness,¹⁷¹² leading to the lack of consensus on whether proportionality is an independent principle in Chinese administrative law. Most scholars express different views on the relationship between proportionality and reasonableness without further explanation.¹⁷¹³ According to their different opinions, these scholars can be divided into three groups. The mainstream view is that proportionality is a sub-element of reasonableness, which is supported by Luo and Zhan.¹⁷¹⁴ In Chen's view, proportionality is synonymous with the principle of reasonableness, and their only difference is that the reasonableness principle has been more frequently applied than that of proportionality.¹⁷¹⁵ Others, like Ying, point out that reasonableness could be replaced by proportionality.¹⁷¹⁶ Conversely, Jiang and Yu highlight that the current principles of Chinese administrative law need to be further clarified, and proportionality should be regarded as an independent principle.¹⁷¹⁷ The opaque relationship between these principles can be seen in Chinese laws, policy documents, and judgments.

Nevertheless, even if proportionality were to be a principle in Chinese administrative law, its application would be restricted because Chinese courts mainly review the legality of a specific administrative act rather than its reasonableness.¹⁷¹⁸ Distinct from its position in theory, in practice proportionality has been cited by Chinese courts as a critical basis for their decisions. As observed by Chen, some Chinese courts in administrative cases referred to the principle of proportionality merely as a shortcut, while other courts applied it in different ways, leading to different decisions on a similar specific administrative act.¹⁷¹⁹

¹⁷¹¹ Chen (n 163) 82.

¹⁷¹² Huang & Yang (n 155) 8-9. Luo & Zhan (n 156) 33. Chen (n 156).

¹⁷¹³ These scholars express their own views on the relationship between proportionality and reasonableness in their works, but they do not provide further clarification. For example, Luo and Zhan assert that the principle of reasonableness contains five sub-principles, including the principle of proportionality. Luo & Zhan (n 156) 31-5. However, as criticised, when the Chinese scholars' discussion the legal status of reasonableness and proportionality in Chinese administrative law, they failed to consider the particular circumstances in which these principles originated.

¹⁷¹⁴ Luo & Zhan (n 156) 33.

¹⁷¹⁵ Chen (n 156).

¹⁷¹⁶ Songnian Ying, *Xing Zheng Fa Yu Xing Zheng Su Song Fa (Administrative Law and Administrative Litigation Law)* (2nd edn, China University of Political Science and Law Press 2011) 47-8 [in Chinese]. As clarified by Ying, these principles of administrative law are concluded from practice and may not have corresponding textual basis in Chinese laws and regulations

¹⁷¹⁷ Mingan Jiang & Linyun Yu, *Xing Zheng Fa (The Administrative Law)* (China Science Publishing and Media 2010) 65-6, 88-90 [in Chinese]

¹⁷¹⁸ The Chinese Administrative Litigation Law (2015) Articles 12 and 13.

¹⁷¹⁹ Chen (n 163) 80. Hongzhen Jiang, 'Bi Li Yuan Ze Wei Jie Zhi Xu De Si Fa Shi Yong' (Judicial Application of the Hierarchical Order in the Principle of Proportionality) (2020) 42 Chinese Journal of Law 41, 49 [in Chinese].

Such inconsistent application of proportionality somewhat affects its actual function in balancing conflicting values. Concluded from Chinese administrative law cases in which proportionality was applied, Jiang pointed out that each method used to apply proportionality, even the sole use of the necessity test or the application of all-encompassing proportionality, evidence its application and attributes.¹⁷²⁰ Most Chinese courts supported the administrative decisions made by the authority, if they reviewed the impugned measures solely based on the test of proportionality *stricto sensu*.¹⁷²¹ By contrast, the majority of courts always found the violation of proportionality if they reviewed the means under scrutiny on the basis of the necessity test or all three consecutive tests included in proportionality analysis.¹⁷²²

With the uncertainties and issues raised above, there are important unresolved questions about the legal status of proportionality in the Chinese domestic legal system. This chapter will investigate the complexity of proportionality in the Chinese Constitutional Law firstly from theoretical and practical perspectives. In 7.2, different versions of the Constitution will be examined and compared to investigate whether the principle of proportionality is included in the Chinese Constitutional Law. The provisions of the concepts "the rule of law" and "human rights", which are regarded as the basis of proportionality as a constitutional principle, will be the main focus of the analysis. Whether this principle has been adopted by the Chinese courts in practice will be examined in 7.3.

The discussion in 7.4 will examine the question of whether proportionality is a principle within Chinese administrative law. The wording of Chinese laws, regulations, and policy documents will be examined, followed by a discussion on its ambiguous relationship with the principle of reasonableness. The application of proportionality in administrative law cases will be analysed in 7.5. This chapter will conclude with the finding that although the principle of proportionality currently is not stipulated in the Chinese domestic law, there is a visible trend in its application. Proportionality is, at least, as a principle in Chinese administrative law, to balance the conflicts between individuals' rights, including their property rights, and the public authorities' power to act for the public interest.

7.2 The Textual Basis of Proportionality as a Chinese Constitutional Principle

China has promulgated four versions of its Constitution since 1954.¹⁷²³ The latest version, promulgated in 1982,¹⁷²⁴ has been amended five times since its enactment.¹⁷²⁵ The iteration currently enforced is the

¹⁷²⁰ Jiang (n 1719) 49.

¹⁷²¹ *ibid*.

¹⁷²² *ibid* 50.

¹⁷²³ 'The Chinese Constitutional Law' (*PKULAW.COM*) <<http://www.pkulaw.cn/>> [in Chinese] last accessed 26 November 2021.

¹⁷²⁴ *ibid*.

¹⁷²⁵ *ibid*.

Chinese Constitutional Law (2018).¹⁷²⁶ Although the word "proportionality" and its equivalent terms have not been found in the text of the Constitution, scholars opine that such a principle could be derived from "the rule of law" and "human rights", the concepts that can be seen from the changes in the Chinese constitutional rules.¹⁷²⁷

7.2.1 Proportionality Derived from the Rule of Law

As mentioned in Chapter Two, the stipulation of "the substantive rule of law" in the German Basic Law indicates the importance of the legitimacy of the pursued purpose, which is required by the principle of proportionality.¹⁷²⁸ A similar view is held by Jiang, who points out that proportionality is a requirement of the substantive rule of law and an integral component of *Rechtsstaat*, which means a state is governed by the law.¹⁷²⁹ As she explains, the rule of law restricts the state's regulatory power and substantially protects individual rights.¹⁷³⁰ The principle of proportionality can be applied to review whether the exercise of state's regulatory power satisfies the substantial justice and fairness to achieve a balanced means-end relationship.¹⁷³¹ Hao and Xi also opine that the purpose pursued by the substantive rule of law, such as freedom, can be achieved to the maximum extent by applying proportionality.¹⁷³²

Such a transition from "the formal rule of law" to "the substantive rule of law" can be reflected on the basis of the changes in relevant wordings under the Chinese Constitutional Law, in particular the preamble and Article 5. As presented in Table 7.1, the term *Fa Zhi* (法制, legal system) first appeared in the Chinese Constitutional Law (1982), emphasising the significance of improving "the *socialist legal system*" in the preamble.¹⁷³³ Article 5 further stressed that "[t]he state shall safeguard the unity and sanctity of the *socialist legal system*".¹⁷³⁴ It is evident that, at that time, merely the term "legal system" was prescribed in the Chinese Constitutional Law.

Table 7.1 Term "Legal System" / "Rule of Law" in the Chinese Constitutional Law

Year	Contents	The Preamble	Article 5

¹⁷²⁶ *ibid.*

¹⁷²⁷ Lin & Ji (n 1700) 64. Yang (n 161). Yang Mei, 'Bi Li Yuan Ze De Shi Yong Fan Wei Yu Xian Du' (The Scope and Limits of the Principle of Proportionality) (2020) 42 Chinese Journal of Law 57, 59 [in Chinese]. Xin Jiang, 'Bi Li Yuan Shi Yi Xue Jie Gou Gou Jian Ji Fan Si' (The Construction and Reflection of the Hermeneutics Structure of the Principle of Proportionality) (2008) Science of Law 45 [in Chinese]. Huiming Gao, 'Ji Ben Quan Li Xian Zhi Zhi Xian Zhi' (The Restrictions on the Limitation of Basic Rights) (2012) 45 Journal of Zhengzhou University 49, 51 [in Chinese].

¹⁷²⁸ See 2.4.1 in Chapter Two.

¹⁷²⁹ Jiang, 'Bi Li Yuan Ze' (n 146) 78-9. Cohen-Eliya & Porat, 'Proportionality' (n 189) 463.

¹⁷³⁰ Jiang, 'Bi Li Yuan Ze' (n 146) 80.

¹⁷³¹ *ibid* 77-80.

¹⁷³² Yinzhong Hao & Zuoli Xi, 'Xian Zheng Shi Jiao Xia De Bi Li Yuan Ze' (The Principle of Proportionality from the Perspective of Constitutionalism) (2004) Legal Business Research 69, 72 [in Chinese].

¹⁷³³ The Chinese Constitutional Law (1982) Preamble [italic added].

¹⁷³⁴ *ibid* Article 5 [italic added].

1954 (Expired)	N/A	N/A
1975 (Expired)	N/A	N/A
1978 (Expired)	N/A	N/A
1982 (Amended)	...improve the <i>socialist legal system</i> ...	1. The state upholds the uniformity and dignity of the <i>socialist legal system</i> .
1988 (Amendment)	...improve the <i>socialist legal system</i> ...	1. The state upholds the uniformity and dignity of the <i>socialist legal system</i> .
1993 (Amendment)	...improve the <i>socialist legal system</i> ...	1. The state upholds the uniformity and dignity of the <i>socialist legal system</i> .
1999 (Amendment)	...improve the <i>socialist legal system</i> ...	1. The People's Republic of China governs the country <i>according to law</i> and makes it a socialist country <i>under the rule of law</i> . 2. The state upholds the uniformity and dignity of the <i>socialist legal system</i> .
2004 (Amendment)	...improve the <i>socialist legal system</i> ...	1. The People's Republic of China governs the country <i>according to law</i> and makes it a socialist country <i>under the rule of law</i> . 2. The state upholds the uniformity and dignity of the <i>socialist legal system</i> .
2018 (Amendment)	...improve the <i>socialist rule of law</i> ...	1. The People's Republic of China shall practice <i>law-based governance</i> and build a socialist state <i>under the rule of law</i> . 2. The state shall safeguard the unity and sanctity of the <i>socialist legal system</i> . ¹⁷³⁵

The term *Fa Zhi* (法治, the rule of law) has been gradually incorporated into the Constitution until the 1999 Amendment. As emphasised, "[t]he People's Republic of China shall practice *law-based governance* and build a socialist state *under the rule of law*".¹⁷³⁶ Furthermore, the phrase "improve the socialist *legal system*" is replaced by "improve the socialist *rule of law*" in the current enforced Constitution.¹⁷³⁷ This change is regarded as a new development in the construction of the rule of law in China.¹⁷³⁸

As discussed previously, the ordinary meaning of the word in question is the starting point of interpreting such a term.¹⁷³⁹ According to the Chinese dictionary, the terms *Fa Zhi* (法制, legal system) and *Fa Zhi* (法治, the rule of law) have different definitions. The former is a combination of *Fa Lv* (法

¹⁷³⁵ 'Constitution of the People's Republic of China' (ENGLISH.GOV.CN) <http://english.www.gov.cn/archive/lawsregulations/201911/20/content_WS5ed8856ec6d0b3f0e9499913.html> last accessed 27 November 2021.

¹⁷³⁶ The Chinese Constitutional Law (amended 1999) Article 5 [italic added].

¹⁷³⁷ The Chinese Constitutional Law (n 45) [italic added].

¹⁷³⁸ Qinhuo He & Kaiyue Qi, 'Fa Zhi Cheng Wei Fa Zhi: Xian Fa Xiu Gai Tui Jin She Hui Zhu Yi Fa Zhi Jian She' (When Legal System Becomes Rule of Law: Propulsion by Constitutional Amendment to the Construction of Socialist Rule of Law) (2018) Shandong Social Science 5, 6 [in Chinese].

¹⁷³⁹ See 3.3.2 in Chapter Three.

律, law) and *Zhi Du* (制度, system), referring to the static legal system and the dynamic legal order.¹⁷⁴⁰ However, the latter is the antonym of *Ren Zhi* (人治, rule of man), stressing that a state is governed by law.¹⁷⁴¹

Moreover, as clarified by the National People's Congress (NPC), *Fa Zhi* (法制, legal system) is a common name of all Chinese laws and regulations,¹⁷⁴² focusing on the law in a formal sense.¹⁷⁴³ In this legal system, the spirit of the Chinese Constitutional Law might still be violated.¹⁷⁴⁴ By contrast, *Fa Zhi* (法治, the rule of law) emphasises the significance of the substantive rule of law and accords with the spirit of the Constitution.¹⁷⁴⁵ Such a transition, from "the formal rule of law" to "the substantive rule of law", in the Chinese Constitutional Law, corresponds with the discovery of Cohen-Eliya and Porat who pointed out that the notion of "proportionality" was initially deduced from *Rechtsstaat* before making its appearance in the German Basic Law in 1949.¹⁷⁴⁶ In this regard, proportionality is implied in the Chinese Constitutional Law.

7.2.2 Proportionality Derived from Human Rights

In addition to "the rule of law", it is Gao's view that "basic rights" can also be the logical starting point of proportionality.¹⁷⁴⁷ Consensus has been reached among certain scholars that proportionality aims to restrict the state's regulatory power, in order to protect human rights, but they disagree on the particular rules which could be the source that reflects the notion of proportionality.¹⁷⁴⁸

Generally, the existence of proportionality in the Chinese Constitutional Law is supported by the changes in the Constitution's structure and the provision of human rights. The structural change can be seen in the sequence between the chapters of "[t]he structure of the state" and "[t]he fundamental rights and duties of citizens".¹⁷⁴⁹ In the first three versions of the Chinese Constitutional Law, Chapter Two

¹⁷⁴⁰ He & Qi (n 1738) 7.

¹⁷⁴¹ *ibid* 8.

¹⁷⁴² 'General Principles' (NPC, 14 April 2010)

<<http://www.npc.gov.cn/npc/c13475/201004/0e53b6b04d1b4401b18404d93889a9a4.shtml>> [in Chinese] last accessed 27 November 2021.

¹⁷⁴³ *ibid*. Chunping Liu, 'Fa Zhi Yuan Ze Zai Zhong Guo Xian Fa Wen Ben De Shan Bian' (On the Rule of Law in the Textual Evolvement of the Constitution of PRC) (2009) 3 Northern Legal Science 30, 34 [in Chinese].

¹⁷⁴⁴ *ibid*.

¹⁷⁴⁵ 'General Principles' (n 1742).

¹⁷⁴⁶ See 2.4.1 in Chapter Two. Cohen-Eliya & Porat, 'Proportionality' (n 189) 475-6.

¹⁷⁴⁷ Gao (n 1727) 51. Mei (n 1727) 57.

¹⁷⁴⁸ Qianhong Qin & Gaoyang Di, 'He Xian Xing Shen Cha Zai Zhong Guo De Si Shi Nian' (Forty Years of Constitutional Review in China) (2019) Academics 47, 49 [in Chinese]. Xiuyan Shi, Ji Ben Ren Quan Zai Zhong Guo Xian Fa Zhong De Mo Shi Shan Bian' (The Mode Evolution of Basic Human Rights Principle at Chinese Constitution) (2011) Value Engineering 314 [in Chinese]. Lin & Ji (n 1700) 64-9.

¹⁷⁴⁹ Before the Chinese Constitutional Law (n 1733), the structure of the Constitution was 'General Principles-The Structure of the State-The Fundamental Rights and the Duties of Citizens-The National Flag, the National Emblem, the National Capital'. From the Chinese Constitutional Law (n 1733), the sequence became 'General Principles-The Fundamental Rights and Duties of Citizens-The Structure of the State-The National Flag, the National Emblem, the National Capital'. From the Chinese Constitutional Law (n 151), 'The National Anthem' was added into Chapter Four of the Constitution.

refers to the structure of the state, followed by Chapter Three in which the citizens' fundamental rights and duties are prescribed. This sequence raised heated debates during the process of drafting the constitution. During the discussion, as clarified by Tian, the reason for such a structure was that "citizens' rights are created in the political system".¹⁷⁵⁰ This explanation, in Han's view, reflects that the framers of the Constitution realised the existence of the interconnection between the state's power and the citizens' rights, but they might overestimate the contribution of the wielding of power to fulfil the rights.¹⁷⁵¹

However, that order has been changed, and these two chapters have been interchanged since the Chinese Constitutional Law (1982).¹⁷⁵² As asserted by Shen, this change in the Constitution's structure highlighted the importance of protecting citizens' rights and freedom.¹⁷⁵³ In Qin and Di's view, the current structure of the Chinese Constitutional Law reflects that China has recognised the significance of human rights and the protection of individual rights, at least from the formal perspective, compared with that of the Constitution (1954).¹⁷⁵⁴

Before a link can be made between human rights and the source of proportionality, a clarification has to be made that, foreign investors and foreign investments are also protected by the Chinese Constitutional Law and other domestic laws according to the NPC Committee; Despite no provision for the protection of foreigners appearing in the chapter of "citizens' fundamental rights" in the Constitution. Regarding foreigners' protection, the NPC clarified that foreigners could not be classified as citizens of China, yet their protections are closely linked to political and economic development.¹⁷⁵⁵ Consequently, the protections provided to such non-native parties have been stipulated in the general principle of the Chinese Constitutional Law as well as provided in the Constitution since 1954.¹⁷⁵⁶

Not only foreigners but also foreign investments have been protected under the Chinese Constitutional Law (1982).¹⁷⁵⁷ As stipulated in Article 18 of the Constitution (1982),

The People's Republic of China permits foreign enterprises, other foreign economic organisations and individual foreigners to invest in China and to enter into various forms of

¹⁷⁵⁰ At the meeting on draft of the Constitution, which was held by the National Committee of the Chinese People's Political Consultative Conference (CPPCC), Jiaying Tian clarified the structure of the Chinese Constitutional Law. See from Dayuan Han, *1954 Nian Xian Fa Yu Xin Zhong Guo Xian Zheng (The Chinese Constitutional Law 1954 and New Chinese Constitutionalism)* (Hunan People's Publishing House 2004) 437 [in Chinese].

¹⁷⁵¹ *ibid.*

¹⁷⁵² The Chinese Constitutional Law (n 1733).

¹⁷⁵³ Chunyao Shen, 'Zhong Guo Xian Fa Zhi Du De Ruo Gan Wen Ti' (The Issues in the Chinese Constitutional System) (npc.gov.cn, 29 June 2018) <<http://www.npc.gov.cn/npc/c541/201806/61f2a47be3014237b43a7958b32d0fd3.shtml>> [in Chinese] last accessed 19 June 2022.

¹⁷⁵⁴ Qin & Di (n 1748) 49. Shi (n 1748) 314.

¹⁷⁵⁵ 'General Principles' (n 1742).

¹⁷⁵⁶ *ibid.*

¹⁷⁵⁷ The Chinese Constitutional Law (n 1733).

economic cooperation with Chinese enterprises and other Chinese economic organisations in accordance with the law of the People's Republic of China.

All foreign enterprises, other foreign economic organisations, and Chinese-foreign joint ventures *within Chinese territory* must abide by the laws of the People's Republic of China. *Their lawful rights and interests are protected by the laws of the People's Republic of China.*¹⁷⁵⁸ [italic added]

In addition, Article 32 (1) of the Constitution prescribes that "[t]he People's Republic of China protects the lawful rights and interests of foreigners within Chinese territory; Foreigners on Chinese territory must abide by the law of the People's Republic of China".¹⁷⁵⁹ As expressed by the phrase "must abide by the laws of the People's Republic of China" in these provisions, foreign investors and their investments shall comply with Chinese laws and regulations. At the same time, their "lawful rights and interests" will be protected. The adjective "lawful" stresses the legitimacy of foreign investors' values. Similar details on the promotion and protection of foreign investments are stipulated in other specific laws, including the Chinese Foreign Investment Law.¹⁷⁶⁰

In addition to those rights that are closely linked to their particular roles as foreign investors in the context of international investment, foreigners can also enjoy the general protection of human rights. The term "human rights" first explicitly appeared in the Chinese Constitutional Law (2004), which emphasises "[t]he state respects and protects *human rights*" in Article 33.¹⁷⁶¹ The appearance of this term is regarded as a crucial development which expresses that the principle of "the protection of human rights" is set in the Chinese Constitutional Law.¹⁷⁶²

However, there is a difference between the wording of the state's duties in relation to human rights stipulated in the International Bills on Human Rights¹⁷⁶³ and that prescribed in the Chinese Constitutional Law.¹⁷⁶⁴ As required by the former, a state should "respect", "protect", and "fulfil" human rights.¹⁷⁶⁵ More specifically, in order to express the respect to human rights, a state shall not directly or indirectly impair individuals fundamental rights;¹⁷⁶⁶ It should also prevent individual rights from third parties or other peoples' infringement to protect such rights;¹⁷⁶⁷ Apart from negative obligations, a state

¹⁷⁵⁸ *ibid* Article 18. Wenhua Shan & Norah Gallagher, 'China' in Chester Brown (ed.), *Commentaries on Selected Model Investment Treaties* (OUP 2013) 134-5.

¹⁷⁵⁹ The Chinese Constitutional Law (n 1733) Article 32.

¹⁷⁶⁰ Foreign Investment Law of the People's Republic of China (2019) [in Chinese]. This law provides 'Investment Promotion' in Chapter Two and 'Investment Protection' in Chapter Three.

¹⁷⁶¹ The Chinese Constitutional Law (n 151) Article 33 (3) [italic added].

¹⁷⁶² Lin & Ji (n 1700) 64-9. Shi (n 1748) 314.

¹⁷⁶³ 'International Bill of Human Rights' (UN) <<https://www.ohchr.org/en/what-are-human-rights/international-bill-human-rights>> last accessed 26 June 2022. Including the Universal Declaration of Human Rights (UDHR), the International Covenant on Civil and Political Rights (ICCPR), and the International Covenant on Economic Social and Culture Rights (ICESCR)

¹⁷⁶⁴ The Chinese Constitutional Law (n 151).

¹⁷⁶⁵ 'International Bill of Human Rights' (n 1763).

¹⁷⁶⁶ *ibid*.

¹⁷⁶⁷ *ibid*.

should also pro-actively act to realise individual rights.¹⁷⁶⁸

Differently, the Chinese Constitutional Law merely stipulates the state's duties from both passive and pro-active approaches:¹⁷⁶⁹ "Respect" and "protect" human rights.¹⁷⁷⁰ A state shall refrain from impairing individual rights to respect human rights.¹⁷⁷¹ This requirement corresponds to that in the International Covenants.¹⁷⁷² As required by "protect", Jiao points out that a state shall not only prevent individual rights from impairment by others but also take actions to contribute to the realisation of such rights.¹⁷⁷³ In this respect, although only "respect" and "protect" are prescribed in the Constitution, the protection of human rights, which refers to the protection and realisation of human rights, is broader than that provided in the Covenants. Therefore, no substantial differences exist between the state's duties on human rights at national and international levels.

In Jiao's view, those obligations of the state in relation to human rights provided in Article 33 of the Constitution, indicate the importance of restricting the state's regulatory power that limits individual rights.¹⁷⁷⁴ However, his view is criticised by Rao and Chen, who argue that the principle of proportionality cannot be interpreted from Article 33 (3) solely based on the ordinary meaning of "respect" and "protect".¹⁷⁷⁵ As they highlight, the prerequisite for applying proportionality is that fundamental rights can be infringed to pursue the desired public interests.¹⁷⁷⁶ Jiao merely presented individual rights and the state's duties but failed to evidence such a connection between the pursued purpose and affected rights.

Unlike Jiao, Lin and Ji regard Article 33 (3) as the basis of proportionality from a different perspective.¹⁷⁷⁷ They determine the concept of proportionality from two subsets contained in the protection of human rights.¹⁷⁷⁸ In their views, Article 33 (3) not only requires the standard protection but also refers to the special protection.¹⁷⁷⁹ More specifically, the former stresses that individual rights shall be realised by the state's contributions and they shall be prevented from others' impairments as well as the state's infringement.¹⁷⁸⁰ Unlike the former, the latter depicts an exceptional situation in which even in the case that individual rights conflict with other values, they are still afforded protection.¹⁷⁸¹

¹⁷⁶⁸ *ibid.*

¹⁷⁶⁹ Jiao (n 148) 46. Rao & Chen (n 146).

¹⁷⁷⁰ The Chinese Constitutional Law (n 151) Article 33 (3).

¹⁷⁷¹ *ibid.*

¹⁷⁷² 'International Bill of Human Rights' (n 1763).

¹⁷⁷³ Jiao (n 148) 46. Lin & Ji (n 1700) 65-6.

¹⁷⁷⁴ Jiao (n 148).

¹⁷⁷⁵ Rao & Chen (n 146).

¹⁷⁷⁶ *ibid.*

¹⁷⁷⁷ Lin & Ji (n 1700) 65-6. Rao & Chen (n 146).

¹⁷⁷⁸ Lin & Ji (n 1700) 65-6.

¹⁷⁷⁹ *ibid.*

¹⁷⁸⁰ *ibid.*

¹⁷⁸¹ *ibid.* 66.

There is no doubt that divergences exist between different values. The cost of the realisation of one value may be the infringement on others.¹⁷⁸² As they emphasise, even in the conflicting values, the negatively affected fundamental rights should still be protected.¹⁷⁸³ In other words, the limits on individual rights should be restricted in a reasonable scope; Otherwise, it could be applied as an excuse to infringe fundamental rights.¹⁷⁸⁴ Such restrictions, especially that on the limits on individual rights should accord with proportionality.¹⁷⁸⁵

Rao and Chen have a different opinion on the textual basis of proportionality. As opined by them, instead of only Article 33 of the Constitution, its combination with Article 51 expresses the concept of proportionality.¹⁷⁸⁶ Article 51 can be interpreted as a limitation clause, which stipulates that each citizen "must not infringe upon the interests of the state, of society, or of the collective, or upon the lawful freedoms and rights of other citizens" when enjoying freedom and rights.¹⁷⁸⁷ Even when such rights are limited, according to Article 33 (3), they are still provided with fundamental protection, which in the researcher's view can be understood as the restriction on the limit on individual rights. In other words, interpreting Article 33 (3) in conjunction with Article 51 explicitly describes a process of weighing and balancing different values, which corresponds to proportionality, in particular proportionality *stricto sensu*.

More specifically, according to Article 33 (3), citizens have rights to enjoy the protection of their various fundamental rights provided by the Constitution, but part of those rights could be limited if the circumstances listed in Article 51 emerge. If the desired purposes of the public authorities fall into the category in the sense of Article 51, certain rights of citizens might be lawfully limited; Meanwhile, even if such fundamental rights are limited, the implemented measures shall still "respect and protect human rights", as stipulated in Article 33 (3) of the Constitution. The public authority has the power to limit the relative rights of individuals to pursue a legitimate purpose, but such limits should be restricted by the requirements of protecting and respecting human rights, corresponding to the requirement of proportionality.

Nevertheless, this view is rejected by Men, who argues that such a combination erodes the space for applying proportionality.¹⁷⁸⁸ In his view, Article 51 leaves no room to balance conflicting values because it has pre-set a hierarchy.¹⁷⁸⁹ As he points out, the ranking of "the interests of the State, of society, or of

¹⁷⁸² *ibid.* Rao & Chen (n 146).

¹⁷⁸³ Lin & Ji (n 1700) 66.

¹⁷⁸⁴ *ibid.*

¹⁷⁸⁵ Rao & Chen (n 146).

¹⁷⁸⁶ *ibid.*

¹⁷⁸⁷ The Chinese Constitutional Law (n 45) Article 51..

¹⁷⁸⁸ Men, 'Bi Li Yuan Ze' (n 148) 102.

¹⁷⁸⁹ *ibid* 100-1.

the collective" is higher than that of individual rights.¹⁷⁹⁰ Following this logic, if a particular individual right conflicts with the public interest, the former will undoubtedly be limited to pursuing the latter. However, in the researcher's view, this opinion held by Men is incorrect because he fails to interpret Article 51 with consideration of the entire context in which the questioned term appears. The importance of "other citizens' lawful freedom and rights" is also emphasised in this provision, which is ignored by Men.¹⁷⁹¹ As clarified by the NPC, instead of setting a hierarchy of values, Article 51 stresses that individual rights and freedoms cannot be abused.¹⁷⁹²

In Men's view, Articles 10 (3) and 13 (3) of the Constitution are the textual basis of proportionality, at least, in the protection of property rights.¹⁷⁹³ Both provisions prescribe that "[t]he state may, in the public interest and in accordance with law, expropriate or requisition land or private property for its use and make corresponding compensation".¹⁷⁹⁴ The phrases "in the public interest" and "in accordance with law" express the requirements on the desired purpose and the nature of limits on individual rights. As asserted by Men, such wordings confirm that the limits themselves should be legitimate.¹⁷⁹⁵ The measures taken by the public authorities, namely "expropriation and requisition", should also enhance, or maintain public interest, reflecting a rational means-end relationship.¹⁷⁹⁶ Men further points out that the word "may" implicitly expresses a comparison between different available measures that can achieve the same purpose to find the less restrictive means, reinforcing the necessity of the applied limits.¹⁷⁹⁷ Once the public authorities take expropriation or requisition, they should also "make corresponding compensation" to mitigate damage to individual rights affected, balancing competing values, which is required by proportionality *stricto sensu*.

As demonstrated in the above discussions, whether proportionality is a constitutional principle in the Chinese domestic legal system depends on the interpretation of relevant constitutional rules. However, no consensus has been reached on which specific constitutional rule is the textual basis of proportionality among Chinese scholars. Moreover, via different interpretative approaches, those scholars who regard the same rule as proportionality's textual basis provide different, even opposite, interpretations.¹⁷⁹⁸

¹⁷⁹⁰ *ibid.*

¹⁷⁹¹ The Chinese Constitutional Law (n 45) Article 51.

¹⁷⁹² 'The Fundamental Rights and Duties of Citizens' (NPC, 14 April 2010) <<http://www.npc.gov.cn/npc/c13475/201004/f6f0fa308715410b8e963fdbc7ac7e9d.shtml>> [in Chinese] last accessed 27 November 2021.

¹⁷⁹³ Men, 'Bi Li Yuan Ze' (n 148). Men, 'Han Yi Yu Yi Yi' (n 148).

¹⁷⁹⁴ The Chinese Constitutional Law (n 45) Article 10 (3) and Article 13(3)

¹⁷⁹⁵ Men, 'Bi Li Yuan Ze' (n 148).

¹⁷⁹⁶ *ibid.*

¹⁷⁹⁷ Men, 'Han Yi Yu Yi Yi' (n 148).

¹⁷⁹⁸ The misinterpretation of Article 51 provided by Men is a prime example here.

7.3 The Lack of Mandates in the Chinese Courts

The application of proportionality as a constitutional principle in China is based on the interpretation of the Chinese Constitutional Law. However, in practice, the Chinese courts have no power to make an authentic interpretation, as such power is reserved for the SCNPC on the basis of Article 67,¹⁷⁹⁹ which explicitly expresses that

The Standing Committee of the National People's Congress exercises the following functions and powers:

- (1) *to interpret the Constitution and oversee its implementation;*
- (2) to enact and amend laws other than those that shall be enacted by the National People's Congress;
- (3) to partially supplement and amend, when the National People's Congress is not in session, laws enacted by the National People's Congress, provided that the basic principles of these laws are not contravened;
- (4) to interpret laws...¹⁸⁰⁰ [italic added]

As reflected in Article 67 (1), the SCNPC has the power to interpret the Chinese Constitutional Law. More specifically, as further clarified in Article 70, that is the Constitution and Law Committee, a particular committee under the SCNPC, who has the power to interpret the constitutional rules.¹⁸⁰¹ However, the SCNPC's unwillingness to exercise its power granted by Article 67 exacerbated the problem of the interpretation of constitutional rules, including proportionality. As noted by Chen, the SCNPC has never released any materials with the title of "constitutional interpretation".¹⁸⁰² Based on Zou's investigation, the constitutional rules have never been (re)interpreted since the Chinese Constitutional Law 1982.¹⁸⁰³

Fan further illustrates the lack of guidance on the interpretative procedure of the SCNPC.¹⁸⁰⁴ In other words, even if the SCNPC plans to interpret a constitutional rule, no procedural rules can be followed to carry out any such interpretation. In Fan's view, the establishment of the Constitution and Law

¹⁷⁹⁹ The Chinese Constitutional Law (n 45) Article 67. Jinguang Hu, 'Lun She Li Xian Fa He Fa Lv Wei Yuan Hui De Yi Yi' (On the Significance of Establishing the "Constitution and Law Committee") (2018) 3 Journal of Political Science & Law 3, 8 [in Chinese]. Haopeng Yin & Zili Lin, 'Zhong Guo De Zhun Xian Fa Jie Shi Ji Zhi Yuan Li Yu Shi Jian' (The Quasi-Constitutional Interpretation Mechanism in China: Theories and Practice) (2002) 3 Cross-Strait Legal Science 62, 64 [in Chinese].

¹⁸⁰⁰ The Chinese Constitutional Law (n 45) Article 67.

¹⁸⁰¹ *ibid* Article 70, which clarifies that various special committees, including Constitution and Law Committee, were established by the National People's Congress to research, deliberate, and draft relevant bills under the discretion of the National People's Congress and its Standing Committee. Xinhua News Agency, Decision of the Standing Committee of the National People's Congress on Matters Concerning the Duties of the Constitution and Law Committee of the National People's Congress (www.gov.cn, 23 June 2018) <http://www.gov.cn/xinwen/2018-06/23/content_5300653.htm> [in Chinese] last accessed 17 November 2020.

¹⁸⁰² Chen (n 163) 81.

¹⁸⁰³ Pingxue Zou, 'Xian Fa He Fa Lv Wei Yuan Hui De Mu Biao Ding Wei Yu Ji Zhi Chuang Xin' (The Object Localisation and Mechanism Innovation of the Constitutional and Law Committee) (2018) China Law Review 43, 49 [in Chinese]. Jinxue Fan, 'Quan Guo Ren Da Xian Fa He Fa Lv Wei Yuan Hui De Gong Neng Yu Shi Ming' (The Function and Mission of the Constitutional and Law Committee of the National People's Congress) (2018) Journal of East China University of Political Science & Law 13, 17 [in Chinese]. Yin & Lin (n 1799) 66, 69.

¹⁸⁰⁴ Fan (n 1803) 21.

Committee provides the platform and mechanism for interpreting constitutional rules.¹⁸⁰⁵ However, the problem is that although this Committee has been established and replaced the previous Law Committee during the first session of the 13th NPC,¹⁸⁰⁶ which approach it should take to interpret the constitutional rules remains uncertain.¹⁸⁰⁷ Consequently, whether proportionality is a constitutional principle has not been tested by the SCNPC or the Constitution and Law Committee.

Moreover, under the current domestic legal system, the Chinese courts neither accept suits brought against unconstitutional acts, nor review the constitutionality of the applicable law in other cases.¹⁸⁰⁸ As stipulated in *The Specifications for Preparing Civil Judgments by the People's Courts*,¹⁸⁰⁹ the Chinese Constitutional Law shall not be directly referred to as the basis for judgments. Instead, the principles and spirit embodied in the Constitution can be mentioned in the reasoning,¹⁸¹⁰ but the question is that proportionality has not been formally recognised as a constitutional principle. Therefore, proportionality, as a principle, has not yet been tested by the SCNPC and the Chinese courts. Even if it is, proportionality is merely a theoretical concept, which is not available to be applied in practice.

7.4 The Textual Basis of Proportionality as a Principle in Chinese Administration Law

Unlike the Chinese Constitutional Law, Chinese administrative laws and regulations express the notion of proportionality in a straightforward way. This section intends to highlight the view that proportionality as a principle in administrative law is signified in Chinese laws, regulations, and policy documents.¹⁸¹¹ The word "proportionality" is also mentioned by the Chinese courts in their decisions. Nevertheless, at the same time, some effort will be made to point out that there is no definitive answer to the question of whether it is an independent principle or part of the principle of reasonableness.¹⁸¹² The researcher contends in this section that although the principle of proportionality has been applied in administrative law cases, its application is limited. Therefore, one may doubt the legal status of proportionality as a principle in Chinese administrative law even if it appears in relevant rules and practice.

¹⁸⁰⁵ *ibid* 17.

¹⁸⁰⁶ Xinhua News Agency (n 1801).

¹⁸⁰⁷ *ibid*.

¹⁸⁰⁸ Fuhui Zhu, 'Fa Lv He Xian Xing Jie Shi De Zhong Guo Yu Jing Yu Zhi Du Luo Ji-Jian Lun Wo Guo Fa Yuan Shi Yong Xian Fa De Xing Shi' (The Chinese Context and the Institutional Logic of Constitutionality of Legal Interpretation: The Forms of the Application of the Constitution by Courts in China) (2017) 39 *Modern Law Science* 3, 9 [in Chinese].

¹⁸⁰⁹ *ibid*. Notice of the Supreme People's Court on Issuing the Specifications for Preparing Civil Judgments by the People's Courts and the Style of Civil Litigation Documents (2016). Chen (n 163) 82.

¹⁸¹⁰ Notice of the Supreme People's Court (n 1809).

¹⁸¹¹ Rao & Chen (n 146) 41-2. Huang & Yang (n 155) 12-4.

¹⁸¹² Ying (n 1716) 47-8. Jiang & Yu (n 1717) 88-91. Luo & Zhan (n 156) 33. Huang & Yang (n 155) 12.

7.4.1 The Textual Basis of Proportionality in Chinese Administrative Law

The concept of proportionality can be investigated from the Chinese Administrative Compulsion Law, particularly Articles 5, 23, and 43.¹⁸¹³ Rao and Chen put their emphasis on Article 5, which stipulates that "[t]he setting and implementation of administrative compulsion shall be *appropriate*. If the purposes of administration *may be achieved by non-compulsory means, no administrative compulsion shall be set or implemented*".¹⁸¹⁴ Based on the definition of the adjective "appropriate", which means "suitable or proper",¹⁸¹⁵ the measures taken by the administrative authorities shall be suitable to the pursued purpose.¹⁸¹⁶ This requirement corresponds to the legitimacy of the measure itself and a rational means-end connection, which are essential elements of proportionality, as discussed in Chapter Two.¹⁸¹⁷ The second sentence further stresses that if different measures are available to achieve the same purpose, the implemented means shall have less restriction on the relative party's rights,¹⁸¹⁸ indicating the necessity of the implemented means. In other words, Article 5 requires that the means taken by the administrative authority shall be suitable and necessary to achieve its desired legitimate purpose, corresponding to the requirements of proportionality.¹⁸¹⁹

In Huang and Yang's views, Articles 23 and 43 of the Chinese Administrative Compulsion Law can also form the basis of proportionality.¹⁸²⁰ Article 23 reads that,

Seizure and impoundment *shall be limited to the case-related* premises, facilities or properties, and no premises, facilities or properties irrelevant to the illegal acts shall be seized or impounded. *The daily necessities* of citizens and their dependents *shall not be seized or impounded*.¹⁸²¹ [italic added]

While Article 43 stipulates that

Administrative organs *shall not conduct administrative enforcement at night or on a statutory public holiday*, except for an emergency.
Administrative organs *shall not force* the parties concerned to perform the relevant administrative decisions *by such means as cutting off the supply of water, electricity, heating or gas for the living of residents*.¹⁸²² [italic added]

As reflected in the wording "shall be limited to the case-related" and the phrase that the implemented measures "shall not" impair the citizens' daily necessities and supply, both provisions stress the

¹⁸¹³ Huang & Yang (n 155).

¹⁸¹⁴ The Chinese Administrative Compulsion Law (n 154) Article 5 [italic added].

¹⁸¹⁵ Fowler & Fowler (n 187) 42.

¹⁸¹⁶ See 2.4.2 in Chapter Two.

¹⁸¹⁷ See 2.4 in Chapter Two.

¹⁸¹⁸ Huang & Yang (n 155) 14.

¹⁸¹⁹ See 2.4 in Chapter Two.

¹⁸²⁰ Huang & Yang (n 155).

¹⁸²¹ The Chinese Administrative Compulsion Law (n 154) Article 23.

¹⁸²² *ibid* Article 43.

necessary scope of the limits on citizens' various fundamental rights. These rules stress that the purpose pursued by the administrative authority should be achieved without resorting to the unnecessary infringement of individual rights. Even for achieving the legitimate purpose, the case-related individual fundamental rights shall still be guaranteed by the authority, expressing the restriction on the limits on individual rights. In this respect, proportionality's components, including the necessity and proportionality *stricto sensu*, can be observed in these administrative rules.

Moreover, Article 43 is a prime example here to further clarify that conflicting values should be balanced according to the actual circumstances.¹⁸²³ Both paragraphs of this provision explicitly emphasise that individual fundamental rights should still be protected when specific measures are taken by the administrative authorities to pursue their desired purposes. The significance of balance is also emphasised by the differences in Articles 43 (1) and (2). The phrase "except for an emergency" referred to in the former implies that the protection of an individual's right to rest is relative rather than absolute. However, such wording disappears in the latter, which refers to the fundamental right to life. Based on the comparison, it is evident that the balance between conflicting values varies according to each particular circumstance. Consequently, striking a balance in different values is a dynamic process rather than a fixed order.

In addition to administrative laws and regulations, the basis of proportionality as a principle in Chinese administrative law can also be ascertained from policy documents.¹⁸²⁴ As pointed out by Yang, *The Program for Comprehensively Promoting "Administration by Law"* is a crucial basis of proportionality.¹⁸²⁵ This *Program* was set up by the State Council of the People's Republic of China (PRC) in 2004,¹⁸²⁶ aiming to provide clarification on "reasonable administration". As clarified, one of the essential requirements of administration by law is "reasonable administration", which requires that

The administrative organ shall follow the principle of fairness and justice when exercising administrative management. The administrative counterparts should be treated equally without partiality and discrimination. The exercise of discretion shall be in accord with the purpose of the law and eliminate the interference of irrelevant elements; *the implemented measures and means shall be necessary and appropriate; if there are various measures to achieve the purpose pursued by it, the administrative organ shall avoid the measures that impair the rights and interests of the relative party.*¹⁸²⁷ [italic added]

¹⁸²³ Huang & Yang (n 155) 14.

¹⁸²⁴ *ibid* 12-4. Yang (n 161). Rao & Chen (n 146) 41-2.

¹⁸²⁵ *ibid*.

¹⁸²⁶ The Notice of the State Council on Issuing the Program for Comprehensively Promoting "Administrative by Law" <http://www.gov.cn/gongbao/content/2004/content_70309.htm?gs_ws=tsina_636451536152493584> [in Chinese] last accessed 17 November 2020.

¹⁸²⁷ *ibid*.

All the constituent elements of proportionality discussed in Chapter Two can be seen in the last sentence, which consists of three phrases. The first requires the legitimacy of the purpose pursued by the measure in question; Meanwhile, the phrase "eliminate the interference of irrelevant elements" indicates a balance between different values. As stressed in the second phrase, the measure taken by the administrative authority shall be "necessary and appropriate", implying the requirements of suitability and necessity, which were discussed in Chapter Two.¹⁸²⁸ In the last phrase, the significance of the requirement of necessity is reemphasised. If various actions can be taken by the authorities to achieve the same purpose, the action taken should have the least infringement on the relative party's rights and values. Consequently, these requirements can be said to reflect the notion of proportionality and describe it as part of reasonable administration.¹⁸²⁹

7.4.2 The Muddled Relationship between Proportionality and Reasonableness

Chinese administrative laws and documents discussed above express the concept of proportionality and reflect its muddled relationship with the principle of reasonableness.¹⁸³⁰ The lack of a defined relationship between proportionality and reasonableness raises doubts on whether proportionality is an independent principle in Chinese administrative law.

As demonstrated in the development of Chinese administrative laws, regulations, and documents, the principle of reasonableness has been recognised by Chinese scholars since the 1980s,¹⁸³¹ earlier than proportionality which has not been realised by scholars until 1988.¹⁸³² Based on the earlier discussion in Chapter Two, the reasonableness principle consists of the legitimate purpose, the consideration of relevant factors, and the equal application of the law,¹⁸³³ which can be seen in Article 23 of the Chinese Administrative Compulsion Law and the Program mentioned above. As stressed in Article 23, only the case-related premises, facilities, or properties could be limited, and other irrelevant assets shall not be affected, implying the importance of relevant consideration, which is a factor that should be considered in the reasonableness test. Unlike the Law, the *Program* explicitly emphasises the importance of the reasonableness principle as part of reasonable administration. The phrases "without partiality and discrimination" and "irrelevant elements" mentioned in the *Program* also express the components of the principle of reasonableness.

Differing opinions are held by Chinese scholars on the relationship between proportionality and reasonableness. In the current mainstream view among Chinese scholars, proportionality is regarded as

¹⁸²⁸ See 2.4 in Chapter Two

¹⁸²⁹ Huang & Yang (n 155) 13.

¹⁸³⁰ Yang (n 161). Rao & Chen (n 146) 41-2. Huang & Yang (n 155). Wang (n 157) 22.

¹⁸³¹ Yang (n 161).

¹⁸³² Xia Hua (n 1696) 34.

¹⁸³³ See 2.2.1 in Chapter Two.

a sub-principle of the reasonableness principle.¹⁸³⁴ This is supported by Luo and Zhan,¹⁸³⁵ but they do not give a reason for such classification in their work. Conversely, Chen regards proportionality as being synonymous with reasonableness.¹⁸³⁶ In his view, these principles have the same meaning, and the only difference is that reasonableness, compared with proportionality, has been mentioned more frequently.¹⁸³⁷ As argued by He, although proportionality and reasonableness have some similarities, including the legitimate purpose pursued,¹⁸³⁸ they are still two different principles.¹⁸³⁹

As He asserts, the nature of proportionality is a quantitative issue while the reasonableness principle is qualitative.¹⁸⁴⁰ The former is objective, which can be expressed by a particular number, while the latter has subjective features and may vary from one individual to another.¹⁸⁴¹ Moreover, the application of proportionality involves additional considerations, which not only include the pursued purpose, but also refer to the counterpart's rights, compared with the test of reasonableness.¹⁸⁴² Consequently, as concluded by He, the principle of reasonableness emphasises the protection of the public interest,¹⁸⁴³ but both the public interest and individual rights are taken into account in the process of applying proportionality,¹⁸⁴⁴ stressing the balance between different values.

However, although proportionality differs from the principle of reasonableness, they are currently referred to without differentiation in Chinese administrative laws, regulations, and policy documents.¹⁸⁴⁵ Such a disorderly relationship can also be seen in practice, to a certain extent, affects the legal status of proportionality as an independent principle in Chinese administrative law.

7.5 Limited and Inconsistent Applications of Proportionality in Practice

At the time of writing, the term "proportionality" has been mentioned in 3960 administrative law cases (in total).¹⁸⁴⁶ Considering a case may experience several stages, the actual number would be lower. One explanation could be that the Chinese courts, according to the Chinese Administrative Litigation Law, mainly review the legality of a specific administrative act rather than its reasonableness.¹⁸⁴⁷ As shown

¹⁸³⁴ Wang (n 157).

¹⁸³⁵ Luo & Zhan (n 156).

¹⁸³⁶ Chen (n 156).

¹⁸³⁷ *ibid.*

¹⁸³⁸ He (n 156). Yang (n 161). Huang (n 222) 78.

¹⁸³⁹ He (n 156). Liu (n 235) 17. Yang (n 235) 46. Li (n 230) 41.

¹⁸⁴⁰ See 2.3 in Chapter Two. He (n 160). Liu (n 235) 17. Yang (n 235) 46.

¹⁸⁴¹ Li (n 230) 41.

¹⁸⁴² See generally in Chapter Two. He (n 156) 36.

¹⁸⁴³ He (n 156) 36-7.

¹⁸⁴⁴ He (n 156) 35.

¹⁸⁴⁵ See an example The Program for Comprehensively Promoting "Administrative by Law" (n 1826).

¹⁸⁴⁶ 'The Principle of Proportionality' and 'Administrative Cases' (*China Judgments Online*) <<https://wenshu.court.gov.cn/website/wenshu/181217BMTKHNT2W0/index.html?pageId=06940aa4b756b34eeffc37382b99c015&s21=%E6%AF%94%E4%BE%8B%E5%8E%9F%E5%88%99>> [in Chinese] last accessed 19 June 2022.

¹⁸⁴⁷ The Chinese Administrative Litigation Law (n 1718) Articles 12 and 13.

in relevant administrative provisions and cases, the courts solely refer to the reasonableness of the administrative act when it is an "abuse of power" or "manifestly inadequate".¹⁸⁴⁸ However, no consensus has been reached on the extent to which the inadequacy is manifest.¹⁸⁴⁹

Unlike its lack of practice in the Chinese Constitutional Law, in administrative law cases, the principle of proportionality has been applied by the courts in their decisions either implicitly or explicitly. As investigated by Liu, the notion of proportionality was first implied in *Hui Feng Industry Development Co., Ltd. v. Harbin City Planning Bureau (Hui Feng)*,¹⁸⁵⁰ and was first explicitly mentioned *Guo Jianjun v. Zhuji City Land and Resources Bureau (Guo Jianjun)*.¹⁸⁵¹

In *Guo Jianjun*, the court emphasised that the administrative authority should consider a balance between the cost and benefit when they exercise the discretionary power to act.¹⁸⁵² In other words, the implemented measures should comply with the principle of proportionality. As further clarified by the court, the authority should first take means with consideration of protecting the relative party's fundamental rights; Unless such means could not achieve the desired purpose, other more stringent measures could be taken by the authority. Otherwise, the authority was said to fail to abide by the principle of proportionality.¹⁸⁵³ In this respect, the significance of proportionality, at least, the necessity test and the test of proportionality *stricto sensu*, was reflected in *Guo Jianjun*.¹⁸⁵⁴

Furthermore, the notion of proportionality can also be observed in some guiding administrative law cases, such as *Chen Ning v. Zhuanghe Public Security Bureau (Chen Ning)*.¹⁸⁵⁵ As stipulated in *The Provisions of the Supreme People's Court (SPC) on Case Guidance*, "[t]he People's court at all levels shall refer to the guiding cases issued by the Supreme People's Court when adjudicating similar cases",¹⁸⁵⁶ stressing that although no doctrine of precedent exists in the Chinese domestic legal system, the Chinese courts shall still consider the guidance judgments when adjudicating similar cases.

Therefore, proportionality could be applied in similar cases due to its appearance in the guiding cases. However, this flexible tool has merely been applied in limited cases, and not applied consistently. As

¹⁸⁴⁸ For instance, in *Wang Liping v. The Communication Bureau of Zhongmou County*, the court decided that the administrative actions were abuse of the power and violated the principle of proportionality.

¹⁸⁴⁹ Liu, 'Xing Zheng Pan Jue' (n 433) 103.

¹⁸⁵⁰ Administrative Judgment No.20 of Supreme People's Court of the PRC (1999) [in Chinese]. Liu, (n 235) 24. Ying (n 1716) 48.

¹⁸⁵¹ *Guo Jianjun v. Zhuji City Land and Resources Bureau*, Administrative Judgment No 37 of Shaoxing Intermediate People's Court (2008) [in Chinese].

¹⁸⁵² *ibid.*

¹⁸⁵³ *ibid.*

¹⁸⁵⁴ *ibid.*

¹⁸⁵⁵ *Chen Ning v. The Public Security Bureau of Zhuanghe Municipality* [in Chinese].

¹⁸⁵⁶ The Provisions of the Supreme People's Court on Case Guidance (adopted 15 November 2010) Article 7 [in Chinese] [italic added]. Luo & Zhan (n 156) 12.

discussed below, some Chinese courts solely refer to proportionality in their decisions as a shortcut to reach their conclusions without any further analysis.¹⁸⁵⁷ Others apply it in different approaches, from the mere application of the necessity test or the sole application of proportionality *stricto sensu* to the strict application of all-encompassing proportionality.¹⁸⁵⁸ Due to its limited and inconsistent application in Chinese practice, the doubts on the legal status of proportionality in the Chinese domestic legal system still remain.

7.5.1 The Sole Application of the Necessity Test

The concept of proportionality, in particular the necessity requirement, was first mentioned implicitly in *Hui Feng*.¹⁸⁵⁹ In this case, two buildings had been expanded without planning permission and had impaired the view of a historical building.¹⁸⁶⁰ As a result of Hui Feng's conduct, the Planning Bureau imposed a fine and required it to dismantle several levels of the unapproved constructions. This administrative decision was appealed by Hui Feng. The Heilongjiang High People's Court held that the measures taken by the Bureau exceeded what was necessary to eliminate the negative effects of the unapproved buildings and impaired relative party's property rights, which was affirmed by the SPC.¹⁸⁶¹

As ruled by the SPC, "[t]he Bureau should decide the administrative punishment based on the real effects of the unapproved constructions and require Hui Feng to take the corresponding corrective actions".¹⁸⁶² In terms of "the real effects", the SPC stressed that the administrative authority should simultaneously weigh the achievement of its purpose with the protection of relative parties' rights when making decisions.¹⁸⁶³ As indicated by the adjective "corresponding", the scope of penalty should not go beyond what was necessary to achieve the desired purpose, which is also required by the necessity test contained in the application of proportionality.

However, in *Hui Feng*, both courts at two different levels stated that the administrative punishment imposed by the authority exceeded that which was necessary for achieving the pursued purpose. This purpose was reversing the negative effects of unapproved buildings, leading to unnecessary damage and excessive impairments of the relative party's property rights.¹⁸⁶⁴ As pointed out by the courts, such administrative acts were "manifestly unfair".¹⁸⁶⁵ Consequently, the Heilongjiang People's Court reduced

¹⁸⁵⁷ Chen (n 163) 79-81.

¹⁸⁵⁸ *Chen Ning v. The Public Security Bureau of Zhuanghe Municipality* (n 1855). *Qi Mingxi v. Shanghai Songjiang District People's Government*, The SPC (2017) SPC Xingshen No. 306 Administrative Ruling [in Chinese].

¹⁸⁵⁹ *Hui Feng Industry Development Co., Ltd. v. Harbin City Planning Bureau*, Administrative Judgment No.20 of Supreme People's Court of the PRC (1999) [in Chinese].

¹⁸⁶⁰ *ibid.*

¹⁸⁶¹ *ibid.*

¹⁸⁶² *ibid.*

¹⁸⁶³ *ibid.*

¹⁸⁶⁴ *ibid.*

¹⁸⁶⁵ *ibid.*

the fine and the dismantled area.¹⁸⁶⁶ In the SPC's view, these mitigated penalties could also contribute to achieving the purpose pursued by the Planning Bureau. Such an opinion reemphasises the significance of achieving the same purpose with less restrictive means, which is required by necessity.

Although the term "proportionality" was not mentioned in the court's legal reasoning in *Hui Feng*, the process of balancing the achievement of the desired purpose pursued by the Planning Bureau and the protection of the relative parties' property rights reflects its application.¹⁸⁶⁷ Instead of the three consecutive tests, namely the assessment of suitability, necessity, and proportionality *stricto sensu*, which should be followed when applying proportionality in a structured approach, as concluded in Chapters Two and Five,¹⁸⁶⁸ the Heilongjiang High People's Court and the SPC, in this case, merely adopted the necessity test. Reviewing the disputed measures based solely on the assessment of necessity, the courts always find the administrative authority's violation of the law.¹⁸⁶⁹

7.5.2 The Sole Application of Proportionality *Stricto Sensu*

Differently, the court in *Qi Mingxi v. Shanghai Songjiang District People's Government (Qi Mingxi)* balanced the conflicting values directly without referring to other assessments in the process of applying proportionality.¹⁸⁷⁰ In this case, Qi filed a request for obtaining government information as to the decision of forced demolition, which affected his property rights, as he said. In the Government Information Disclosure Application Notice, the Songjiang District People's Government only provided the relevant parties' family names and the abstract address of the unpermitted construction without any other detail. Qi felt dissatisfied with such a result. However, the administrative reconsideration and the judgments of both courts upheld the decision. Consequently, Qi applied for a retrial.

The SPC pointed out that the nature of this case was a conflict between a citizen's right to know and the protection of privacy. If the disclosure of the requested government information infringes the third party's lawful rights, the administrative authority shall act in accordance with the principle of proportionality to balance the conflicting values.¹⁸⁷¹ With regard to the disclosure of government information, Article 22 of the Chinese Regulations of Open Government Information prescribes that "[i]f the request for government information contains the content that shall not be disclosed but can be handled via differentiation, the administrative organ shall provide the requester with the information that can be disclosed".¹⁸⁷² As further clarified in Article 23,

¹⁸⁶⁶ *ibid.*

¹⁸⁶⁷ Huang & Yang (n 155) 15.

¹⁸⁶⁸ See 2.5 in Chapter Two and generally in Chapter Five.

¹⁸⁶⁹ Jiang (n 1719) 50.

¹⁸⁷⁰ *Qi Mingxi v. Shanghai Songjiang District People's Government* (n 1858).

¹⁸⁷¹ *ibid.*

¹⁸⁷² The Chinese Regulations of Open Government Information (2007) Article 22.

If, *in the administrative authority's view*, the requested government information refers to commercial secrets or individual privacy, and its disclosure might infringe the lawful rights and interests of the third party, the administrative organ shall write to the third party to seek its opinion.¹⁸⁷³ [italic added]

The phrase "in the administrative authority's view" reflects that the administrative authorities have the discretion to decide whether the requested government information refers to the details that should not be disclosed. They also have the power to decide the appropriate ways to disclose relevant information by differentiating the information or asking the third party's view based on different conditions. These provisions express a balance between one party's right to know and the third party's privacy, reflecting the application of proportionality, at least the test of proportionality *stricto sensu*, a value-oriented assessment focusing on the real balance between conflicting values.

In *Qi Mingxi*,¹⁸⁷⁴ the Songjiang District People's Government explained that some requested information, such as the full name of the third parties, was related to individuals' privacy that could not be disclosed.¹⁸⁷⁵ Meanwhile, based on investigations, it found that the decision of forced demolition was not related to Qi. In other words, Qi's rights were neither impaired by the forced demolition adjudicated upon by the administrative authority nor infringed by the concealed information. By contrast, if the requested information was provided to Qi, the authority would interfere with the third party's lawful rights and interests. Therefore, the Government selected differentiation as an appropriate way, in its opinion, to balance conflicting values.¹⁸⁷⁶ Its decision was supported by the SPC, who emphasised that the courts shall defer to the administrative authorities unless their measures are "manifestly unfair".¹⁸⁷⁷

Based on the earlier discussion in Chapters Two and Five, the impugned means should fulfil the requirements of suitability and necessity before assessing whether a fair balance exists between the conflicting values.¹⁸⁷⁸ However, it is evident that, instead of the all-encompassing proportionality, the courts in *Qi Mingxi*¹⁸⁷⁹ merely focus on the last test of proportionality, namely proportionality *stricto sensu*.¹⁸⁸⁰ This case also evidences Jiang's opinion, who notes that the courts always support the public authorities' measures if they review such means merely on the assessment of proportionality *stricto sensu*.¹⁸⁸¹

¹⁸⁷³ *ibid.*

¹⁸⁷⁴ *Qi Mingxi v. Shanghai Songjiang District People's Government* (n 1858).

¹⁸⁷⁵ *ibid.*

¹⁸⁷⁶ *ibid.*

¹⁸⁷⁷ *ibid.*

¹⁸⁷⁸ See in Chapters Two and Five.

¹⁸⁷⁹ *ibid.*

¹⁸⁸⁰ See 2.4.4 in Chapter Two.

¹⁸⁸¹ Jiang (n 1719) 50.

7.5.3 The Application of All-Encompassing Proportionality

Unlike the above cases, *Chen Ning* is the case in which all three consecutive tests contained in proportionality were used by the court to review the disputed measures.¹⁸⁸² In this case, Chen Ning's husband, Han Yong, had an accident when driving a cab. He was trapped in the driver's seat and his life was at stake. In order to rescue him, the traffic police and fire brigade of the Zhuanghe Public Security Bureau (PSB) utilised various techniques. Despite the use of gas welding for secure operation, Han died, and the cab caught on fire. Chen Ning, as Han's wife, claimed that the authorities' improper conduct impaired her property rights, including the damage to the cab because of the fire.¹⁸⁸³ Her request for compensation was rejected by the PSB. Consequently, Chen filed an administrative action with the Zhuanghe People's Court and then appealed to the Dalian Intermediate People's Court.

Concerning the compensation, Article 2 (1) of the Chinese State Compensation Law stipulates that,

Where State organs or State functionaries, *in violation of the law, abuse their functions and powers infringing upon the lawful rights and interests* of the citizens, legal persons, and other organisations, thereby causing damage to them, the victims shall have the right to State compensation in accordance with this law.¹⁸⁸⁴ [italic added]

As set out, the precondition of state compensation is the administrative authorities' improper conduct. The courts in *Chen Ning* investigated that the measures taken by the public officials to save her husband's life were not improper. In this case, the value of the life was more important than that of the cab. At the same time, they took as many safety precautions as much as possible to eliminate the infringements of her property rights. The implemented measures should not be reviewed in hindsight.¹⁸⁸⁵ In its in-depth analysis, the Liaoning High People's Court explained that the injured person's life or property rights might be further infringed in the rescue, involving a balance between conflicting values.¹⁸⁸⁶ It then reviewed the questioned measures by three consecutive assessments included in proportionality, which are the tests of suitability, necessity, and proportionality *stricto sensu*.¹⁸⁸⁷

In the first stage, the implemented means should achieve or, at least, contribute to achieving the purpose pursued by the administrative authority.¹⁸⁸⁸ In this case, the court stated that according to Article 8 of the Measures for Handling Road Traffic Accident, the injured person and property shall be rescued

¹⁸⁸² *Chen Ning v. The Public Security Bureau of Zhuanghe Municipality* (n 1855). Jiang (n 1719) 43.

¹⁸⁸³ According to Article 6 of the Chinese State Compensation Law (1994), which stipulates that "[i]n case of death of a victim, heirs or other relatives in maintenance relationship with him shall have the right to demand compensation", Chen Ning then had the right to claim compensation.

¹⁸⁸⁴ The Chinese State Compensation Law (n 1883) Article 2 (1).

¹⁸⁸⁵ See 5.3.2 and 5.4.2 in Chapter Five and 6.4.2 in Chapter Six.

¹⁸⁸⁶ *Chen Ning v. The Public Security Bureau of Zhuanghe Municipality* (n 1855).

¹⁸⁸⁷ *ibid*.

¹⁸⁸⁸ See 2.4.2 in Chapter Two.

immediately.¹⁸⁸⁹ It further clarified that the term "rescue" implied general obligations of the administrative authority, leaving some discretion to the functionaries in practice.¹⁸⁹⁰ As pointed out by Jiang, the suitability of the implemented measure not only means its direct contribution to the pursued purpose but also refers to its indirect contribution.¹⁸⁹¹ In this respect, the disputed actions directly opened the door and indirectly rescued Han, satisfying the suitability requirement of proportionality.

In the second stage, in order to pass the test of necessity, the disputed measures should achieve the pursued purpose with less restriction on individual rights.¹⁸⁹² Based on its investigation, the court noted that different measures had been utilised by the functionaries, proving their consideration of various options available to them. The failures of other means proved the necessity of cutting the cab by gas welding to rescue Han in emergency, although it resulted in the infringement of Chen Ning's property rights.

The final stage aims to ascertain whether there is a balance between the achievement of the desired purposes and the impairment of the infringed rights.¹⁸⁹³ As emphasised by the court, the conflicts between different values should be weighed against the actual circumstance in which the measures were taken rather than the final results led by the questioned means.¹⁸⁹⁴ In this case, the purpose pursued was Han's right to life, and the infringed value was Chen's property rights. The right to life falls into the category of the rights that shall not be lawfully limited, and property rights can be lawfully limited in a reasonable scope to pursue a legitimate purpose.¹⁸⁹⁵ In this respect, the right to life is higher or more significant than property rights. Based on the above analysis, the measure taken to rescue Han satisfied the successive tests of suitability, necessity, and proportionality *stricto sensu*, all requirements of proportionality. Consequently, such a measure was proportionate to the desired purpose.

As reflected in those three typical cases, it is evident that the principle of proportionality, to a certain extent, has been adopted in some Chinese administrative law cases, but it has not been consistently applied. They reflect the sole application of the necessity test, the sole utilisation of proportionality *stricto sensu*, and the application of all-encompassing proportionality. Due to applying proportionality in different ways, the results of the review of similar actions taken in comparable circumstances are different. As noted by Jiang, most courts that directly balance the conflicting values would support the

¹⁸⁸⁹ Measures for Handling Road Traffic Accident (2003) Article 8, which stipulates that "[a]fter receiving the report, the Public Security Bureau shall send functionaries to the spot of an accident immediately to rescue the injured person and property, survey the scene, collect evidence, and taken measures to restore the traffic as soon as possible."

¹⁸⁹⁰ *Chen Ning v. The Public Security Bureau of Zhuanghe Municipality* (n 1855).

¹⁸⁹¹ Hongzhen Jiang, 'Bi Li Yuan Ze Zai "Chen Ning" An Zhong De Shi Yong' (The Application of Proportionality in Chen Ning) (2014) *SJTU Law Review* 162, 167 [in Chinese].

¹⁸⁹² See 2.4.3 in Chapter Two.

¹⁸⁹³ See 2.4.4 in Chapter Two.

¹⁸⁹⁴ *Chen Ning v. The Public Security Bureau of Zhuanghe Municipality* (n 1855).

¹⁸⁹⁵ *Chen* (n 405) 295.

administrative decision,¹⁸⁹⁶ and they express deference to the administrative authority. However, the majority of courts that review the administrative action solely based on the test of necessity, or the whole process of proportionality analysis, would find the violation of proportionality.¹⁸⁹⁷

Demonstrated in Chinese administrative laws and regulations and the relevant administrative law cases, proportionality as a principle in Chinese administrative law could be ascertained from theoretical and practical perspectives, compared with its position in the Chinese Constitutional Law. Nevertheless, one may still question its legal status, at least, whether proportionality is an independent principle in China is unclear due to its uncertainties regarding the textual basis and confused relationship with the reasonableness principle.

7.6 Conclusion

As analysed in Chapter Two, whether proportionality is an international custom or a general principle of law is closely affected by the practice of China, one of the specially affected states in the context of international investment.¹⁸⁹⁸ Meanwhile, its nature also affects how proportionality can strike a balance between the conflicting values of foreign investors and the host state and settle ISDs in which China is involved. Therefore, the legal status of proportionality in the Chinese domestic legal system is vital in answering such questions.

From the perspective of positive law, neither term "proportionality" nor its equivalents appear in the Chinese laws and regulations; Therefore, the Chinese scholars who support the ideology of positive law deny its existence in the Chinese domestic legal system. However, others regard it as a constitutional principle or a principle in Chinese administrative law by interpreting certain constitutional rules or administrative laws and regulations. Based on the above analysis, the researcher's view is that although proportionality currently is not a principle in the Chinese domestic legal system, a trend in its application as a principle in China, at least, in Chinese administrative law, is identifiable.

The Chinese Constitutional Law refers to the essential concepts of "the rule of law" and "human rights", which could be the textual basis of proportionality as a constitutional principle in China. However, the Chinese courts have no power to interpret the constitutional rules. Instead, the SCNPC, or more specifically its special committee, the Constitution and Law Committee, is the body who has the power to interpret the Chinese Constitutional Law, but it has never issued any "constitutional interpretation". As a result, even the concept of proportionality can be deduced from the interpretation of relevant constitutional rules, its legal status as a constitutional principle has not been authentically tested.

¹⁸⁹⁶ Jiang (n 1719) 49.

¹⁸⁹⁷ *ibid* 50.

¹⁸⁹⁸ See 2.3 in Chapter Two.

Besides, the Constitution cannot be referred to directly by the courts as the basis for their decisions. Consequently, even proportionality is a constitutional principle in China, it could merely be a theoretical concept and cannot be adopted to balance the conflicting values in practice.

The status of proportionality in Chinese administrative laws and regulations, which contain certain essential components of proportionality, such as the necessity requirement, is different from that in the Chinese Constitutional Law. Yet there is no consensus among Chinese scholars on proportionality's legal status as an independent principle in administrative law. In Chinese administrative law, the notion of proportionality can be observed directly both in theory and in practice. However, proportionality's obfuscated relationship with the principle of reasonableness raises doubts about its precise legal status and a clear boundary exists between them. The current mainstream view among Chinese scholars is that proportionality is subsumed within the scope of reasonableness. Even though proportionality is a principle in Chinese Administrative Law, it differs from that discussed in Chapter Two.

Issues also arise from the limited and inconsistent application of proportionality as a principle in administrative law in China. Unlike its omission in practice as a constitutional principle, proportionality has been applied in some administrative law cases to balance the purpose pursued by the authority and the infringements of individuals' rights, such as property rights. However, the number of cases in which it was applied reflects its limited application. Moreover, its application varies from one case to another, leading to different, even opposite, decisions on similar measures in analogous factual backgrounds. Based on Jiang's discovery, each approach to applying proportionality expresses a preference for a particular value.¹⁸⁹⁹ Such inconsistent and limited application in practice, also implies the lack of unified recognition of proportionality's legal status in the Chinese domestic legal system.

As demonstrated in Chinese laws and domestic cases, the current legal status of proportionality in China remains uncertain, but the detectable momentum of proportionality becoming a stipulated principle in the Chinese domestic legal system cannot be denied. Such a result corresponds to the conclusion of Chapter Two: Proportionality is neither an international custom nor a general principle of international law due to its uncertain application in the domestic legal system of certain specially affected states in international investment.¹⁹⁰⁰ It is premature to conclude the nature of proportionality as an international custom or a general principle of law. More research is needed. Consequently, in the ISDs in which China is involved, whether proportionality can be applied to settle disputes and balance the conflicting values of foreign investors and the host state merely relies on the wording of the case-related treaty, as analysed in Chapter Six.

¹⁸⁹⁹ Jiang (n 1719) 49.

¹⁹⁰⁰ See 2.3 in Chapter Two.

Chapter 8

Conclusion and Recommendations

8.1 Summary

The introduction of this thesis posited the research theme "the challenges of applying the principle of proportionality in striking a balance in the investor-state relationship" in international investment, in particular in Chinese international investment, from the international and Chinese perspectives. To address this topic, the researcher examined the structured approach to proportionality analysis, the systemic approach to treaty interpretation, the FET standard and the conflicts between the legitimate expectations of foreign investors and the host state, proportionality's textual basis in Chinese BITs and its legal status in the Chinese domestic legal system.

As concluded by the researcher based on analyses and discussions in this study, the principle of proportionality, from the international perspective, can be applied to strike a balance in the investor-state relationship. However, due to its failure to fulfil the requirements to be an international custom or a general principle of law in the sense of Article 38 (1) of the ICJ Statute, its application is on a case-by-case basis if it can be brought into the ISDS by interpreting the applicable law for the dispute, like the case-related treaty, through the systemic interpretative approach.

Moreover, regarding Chinese international investment, the researcher noted two alternative routes to proportionality analysis. If proportionality is implicitly or explicitly mentioned in Chinese BITs, it can be used through systemic treaty interpretation. Alternatively, if it is included in the Chinese domestic legal system, which is the applicable legal instrument of the case, proportionality is applicable to settle ISDs in which China is involved as the host state.

As ascertained by the researcher, China's path to proportionality is cautious. Only the recent Chinese BITs refer to proportionality's textual basis. However, more recently Chinese international investment policy has sought a more balanced paradigm as evidenced in its more recent BITs. The alternative route to proportionality is currently unavailable to China, considering its absence in the Chinese domestic legal system, but a trend of applying proportionality in practice to balance competing values in China is becoming more prevalent. In other words, although it is premature to confirm that proportionality is applicable in the settlement of Chinese ISDs, China has slowly but steadily made it possible to apply proportionality to balance the conflicting values of foreign investors and the host state.

The reason for such research is the currently imbalanced investor-state relationship in international investment. This imbalance is not an anomaly. Clearly IIAs concluded by various states aim to enhance foreign investors' confidence to deploy investment capital, and each promotes their state as a low-risk destination for commercial ventures. However, with the development of international investment, some

states have gradually realised that no close causal link exists between the conclusion of IIAs and the attraction of foreign investment.¹⁹⁰¹ Instead, they have realised the significance of non-investment values and noticed that broad investment protection, to a certain extent, impedes their right and capability to regulate in their own public interest.¹⁹⁰² Such conflicts between the values of foreign investors and the host state should be addressed. Therefore, a proper approach to achieving a fair balance in the investor-state relationship has become a more pressing issue to states.

Derived from states' practices, various tools, not least proportionality, reasonableness, and balancing, have been utilised in different jurisdictions to review actions taken by public authorities to achieve both its desired purposes and assuage any conflicts between its public interest and individual rights.¹⁹⁰³ Compared with reasonableness and balancing, proportionality is positioned in the middle of the two ends of the spectrum, providing a structured and flexible approach to mediating competing values, such as the conflicts between the legitimate expectations of foreign investors and the host state.

This study examined the nature, interpretation, acceptance, and application of proportionality in the context of international investment. This was to investigate whether proportionality can address the conflicting legitimate expectations of foreign investors and the host state, thereby rebalancing the investor-state relationship in international investment. The researcher first ascertained the nature of proportionality in light of Article 38 (1) of the ICJ Statute and enquired into the possible universal application of proportionality as an international custom or a general principle of law. If so, it could be adopted by the tribunals to resolve ISDs, even if the term "proportionality" is absent from the case-related applicable legal instrument. Based on the analyses in this research, the researcher argued that the nature of proportionality is neither an international custom nor a general principle of law in Article 38 (1) because it fails to fulfil the corresponding requirements.

As a result of its general application in many domestic legal systems, some scholars do regard proportionality as a general principle of law.¹⁹⁰⁴ However, this practice was probed by the researcher and the doubts arising from the conclusion were also addressed in this research. Those scholars, like Barak,¹⁹⁰⁵ mainly focus on the practice of certain countries, such as Germany and South Africa, which clearly include the principle of proportionality in their domestic legal systems.¹⁹⁰⁶ As they allege, the considerable number of states in which proportionality has been implemented implies its general application. However, as highlighted by the researcher, instead of quantity, quality is a more critical

¹⁹⁰¹ UNCTAD (n 2) xiii, 6.

¹⁹⁰² *ibid* xiv. A typical example here is Namibia.

¹⁹⁰³ See 2. 2 in Chapter Two.

¹⁹⁰⁴ *supra* note 18.

¹⁹⁰⁵ Barak (n 20).

¹⁹⁰⁶ See 2.3 in Chapter Two.

factor in forming general practice, stressing the significance of the representativeness of the state whose practice contributes to the formation.¹⁹⁰⁷

The lack of investigation into proportionality's legal status in the specially affected states in international investment, not least in China, supported the researcher's contention that it is premature to recognise the universal application of proportionality in the sense of Article 38 (1) of the ICJ Statute.¹⁹⁰⁸ The researcher's view accords with that of Vadi, who also asserted that further studies would be needed to identify the nature of proportionality.¹⁹⁰⁹ Consequently, as confirmed in the research, the application of proportionality currently depends on the wording of the case-related applicable legal instrument. The situations in which proportionality can be applied in the ISDS regime include but are not limited to these two approaches: Ascertaining proportionality on the basis of interpreting treaty provisions in the systemic approach or recognising proportionality within the domestic legal system of the host state, in particular China.

The initial route to applying proportionality depends on whether it is implicitly or explicitly stipulated in the case-related treaty, stressing the significance of the proper interpretative approach. The factors that should be considered in interpretation and the corresponding interpretative approaches adopted to decipher ambiguous provisions can be seen in the rules of interpretation provided in the Vienna Convention, in particular Articles 31 and 32.¹⁹¹⁰ As prescribed, the ordinary meaning of the questioned term, the context in which it appears, the object and purpose of the treaty, and the contracting parties' common intention are essential elements of treaty interpretation. Correspondingly, textual, teleological, and subjective approaches are the methods that can be used to interpret treaties. Although there is no hierarchy between these interpretative approaches, each one reflects that one specific interpretative factor is preeminent over the others. For example, tribunals have always interpreted the FET clause in favour of foreign investors because, in their view, the aim of the treaty is to protect and promote foreign investments.¹⁹¹¹

As analysed in Chapter Three, it is the researcher's view that the systemic method is the appropriate approach to treaty interpretation. To be clear, the systemic interpretative approach referred to in the current study contains two systems, like a concentric circle: They are the treaty itself in which the words in question appear and the whole international legal system.¹⁹¹² Such a systemic approach differs from which solely emphasises the significance of the context or merely stresses the integration of

¹⁹⁰⁷ See 2.3 in Chapter Two.

¹⁹⁰⁸ See 2.3 in Chapter Two.

¹⁹⁰⁹ Vadi, *Proportionality* (n 22).

¹⁹¹⁰ Vienna Convention (n 47).

¹⁹¹¹ Zhang (n 55) 44.

¹⁹¹² See 3.4.4 in Chapter Three.

international law.¹⁹¹³ This systemic approach is a hybrid method, which is broader compared with other approaches. Its application contributes to the most balanced investor-state relationship from the perspective of treaty interpretation.

Unlike other approaches to the interpretation of treaties, this systemic method stresses integration at two different levels. As highlighted by Villiger, within the process of treaty interpretation, the sequence of relevant considerations is from the immediate to the distant.¹⁹¹⁴ Therefore, tribunals should first interpret the questioned term against the entire applicable treaty. Instead of one or several particular elements, all interpretative factors mentioned in Article 31 of the Vienna Convention should be considered in treaty interpretation. Both the protection and promotion provided to foreign investors and the protection of non-investment values stressed in the exception clause should be considered when interpreting treaty provisions.

If no exception clause is specified in the treaty, based on Article 31 (3) (c) of the Vienna Convention,¹⁹¹⁵ the protection of non-investment values stipulated in other relevant international instruments can be brought into the process of treaty interpretation and considered by the arbitral tribunals to produce the interpretation of treaties.¹⁹¹⁶ Consequently, not only investment values but also non-investment values should be taken into account by the tribunals in the process of treaty interpretation, contributing to a balanced and unbiased understanding of the words in question. Furthermore, the situation in which a state's treaty obligations to foreign investors would be at odds with its other international obligations can also be avoided by considering other relevant international instruments which are applicable in the relations between the treaty parties.¹⁹¹⁷

FET is one of the most significant and prevalent standards provided to foreign investors from both perspectives of the concluded IIAs and the ISDs.¹⁹¹⁸ It is a central research theme in the thesis based on which the application of proportionality and the systemic interpretative approach in the ISDS could be assessed. Although FET appears in almost all IIAs, its precise formulation and construct vary from one treaty to another, raising questions about its nature and components. It is the researcher's view that although FET is regarded as an international custom by some scholars, such as Tudor,¹⁹¹⁹ its scope and contour should be interpreted on a case-by-case basis through the systemic approach. In other words, tribunals should consider the whole treaty, including investment protections and non-investment protections if applicable, to discern FET in each case. Consequently, tribunals discretionary power can

¹⁹¹³ See 3.4 in Chapter Three.

¹⁹¹⁴ Villiger (n 66) 114. See 3.3 in Chapter Three.

¹⁹¹⁵ Vienna Convention (n 47).

¹⁹¹⁶ See 3.4.2 in Chapter Three.

¹⁹¹⁷ See 3.4.2 in Chapter Three.

¹⁹¹⁸ UNCTAD, *Issues in International Investment Agreement II* (n 79) xiii, 1.

¹⁹¹⁹ Tudor (n 87) 85.

be somewhat limited, and the situation in which the FET clause is interpreted skewed in favour of foreign investors can be prevented.

The rough contour of the FET standard can be deduced from practice.¹⁹²⁰ Compared with other elements of FET, the protection of legitimate expectations is a typical example depicting the discord between the values of foreign investors and the host state, especially in the current development of global cooperation. Therefore, such a component of FET was assessed by the researcher to demonstrate the utility of proportionality in balancing the investor-state relationship. Moreover, this research also drew out that the text basis of proportionality is mainly found within the exception clause, articulating some special situations in which the measures taken by the host state are still justified even though they are against its treaty obligations *vis-à-vis* foreign investors. These exceptions leave some room for the host state to exercise its regulatory power for public interest matters. However, an absence of qualifying language in treaties leads to heated debates over whether the host state or the tribunal is the critical decision-maker in the process of applying proportionality. As was shown, this led to different awards on the same or similar measures taken by the host state with the same or similar factual backgrounds. In the researcher's view, such divergent, even opposite, results of the decision on similar actions stressed the need for a proper approach to using proportionality in rebalancing the investor-state relationship. Without this, using proportionality, a structured and flexible tool, in an inconsistent manner fails to meet the desired outcome.

Now that China has transitioned to the dual role of large FDI recipient and major overseas investor, a balanced investor-state relationship is vital for its international investment policy. As noted by the researcher, this evidence for China's changing requirements can be found in the wording of different generations of Chinese BITs. The exception clause now appears in an increasing number of Chinese BITs with more detail. The expanded non-investment values referred to in the exception clause not only include essential security interests but also stress the protection of the environment and cultural industries.¹⁹²¹ Meanwhile, internationally, the increasing details on the protection of investment values act as a limit to the tribunals' discretionary power to produce broad treaty interpretation in favour of foreign investors. Such clarified provisions of investment protection can also be seen in the more recent Chinese BITs.

From the perspective of treaty interpretation, proportionality can be brought into the ISDS based on the interpretation of its contextual basis. According to the systemic approach, which is the most appropriate interpretative method in the researcher's view,¹⁹²² the provisions of detailed investment protection

¹⁹²⁰ See 4.4 in Chapter Four.

¹⁹²¹ See an example Canada-China BIT (n 421).

¹⁹²² See 3.4.4 in Chapter Three.

should be considered and interpreted in conjunction with the provisions of expanded non-investment values, utilising proportionality and creating a balanced treaty interpretation. As the researcher demonstrated, the application of proportionality based on the interpretation of the case-related treaty, so useful in balancing opposing yet legitimate expectations of foreign investors and the host state, can be applied to China.

The alternative route to the application of proportionality in the ISDS depends on whether it is included in the host state's domestic law which is the applicable legal instrument of the case. Nevertheless, this is currently unavailable to China. As the term "proportionality" and its equivalents do not feature in the Chinese Constitutional law, no consensus has been reached among scholars on its legal status in the Chinese domestic legal system. Although there is scholarly support that the notion of proportionality can be deduced from the interpretation of constitutional rules, such as "human rights" in Article 33 of the Constitution,¹⁹²³ they have different views on the specific textual basis of proportionality. Even if such a principle is explicitly articulated in the Constitution, as mentioned in Chapter Seven, this assumption has not been examined by the only competent authority, SPC or, more specifically, the Constitution and Law Committee.¹⁹²⁴ The ambiguity is further exacerbated by the inability to cite the Constitution in legal decision,¹⁹²⁵ making it difficult to ascertain whether proportionality should be viewed as a constitutional principle in China.

As noted by the researcher, the legal status of proportionality in the Chinese domestic legal system is even more complex because of its muddled relationship with the principle of reasonableness in Chinese administrative law. This is despite its constituent elements appearing in administrative laws and regulations and policy documents and having been implicitly or explicitly mentioned by the Chinese courts in their decisions on specific administrative actions.¹⁹²⁶ Some courts merely referred to proportionality as a basis for their decisions, whereas others applied this flexible tool variably, expressing the lack of consistent application of proportionality in Chinese practice.

Concluded from Chinese administrative law cases, the courts have applied proportionality in different ways, including the sole application of the necessity test, the plain application of proportionality *stricto sensu*, and the utilisation of all-encompassing proportionality including three successive tests.¹⁹²⁷ However, concluded from practice, each approach to proportionality analysis, to a certain extent, expresses an inclination.¹⁹²⁸ More specifically, the courts that reviewed the means in question by apply

¹⁹²³ See 7.2 in Chapter Seven.

¹⁹²⁴ See 7.2 in Chapter Seven.

¹⁹²⁵ See 7.3 in Chapter Seven.

¹⁹²⁶ See 7.5 in Chapter Seven.

¹⁹²⁷ See 7.5 in Chapter Seven.

¹⁹²⁸ See 7.5 in Chapter Seven.

only the necessity test or all-encompassing proportionality would uncover the violation of proportionality and decide in favour of the relative party. By contrast, those who reviewed the disputed actions merely by weighing the conflicting values, the last assessment included in the application of proportionality,¹⁹²⁹ would express their deference to the public authority and support its administrative decisions.¹⁹³⁰ As evaluated by Barak, the structured approach is one of the proportionality's advantages.¹⁹³¹ Therefore, proportionality should be applied based on the internal logical order of its constituent elements to investigate the measures in question sequentially.

The question of "the challenges of applying the principle of proportionality in striking a balance in the investor-state relationship" was answered from both the international and Chinese perspectives. From the international perspective, proportionality as a flexible tool can be applied to strike a fair balance between the conflicting legitimate expectations of foreign investors and the host state based on each particular circumstance. Its application depends on the interpretation of each case-related treaty because it is neither an international custom nor a general principle of law.¹⁹³²

From the Chinese perspective, among the existing Chinese ISDs, there are no specific cases in which the application of proportionality could be unambiguously examined. However, proportionality could be applied, based on the recent Chinese BITs, which refer to the clarified substantive treatments provided to foreign investors and the emphasised protection of non-investment values. This indicates a balancing process between conflicting values. The researcher also ascertained that the direct interpretative route in which proportionality is a principle of the host state's domestic legal system is currently unworkable for China, but it is entirely realistic and highly possible for proportionality to become a principle in the Chinese domestic legal system, which may be proven in China's future practice.

With consideration of the above issues in applying proportionality to balance the conflicts in international investment particularly involving China, there is a need for a clearer understanding of proportionality. This refers to the two-tier systemic interpretative approach, a clearer map of Chinese BITs, and the interplay between proportionality and the Chinese domestic law. Therefore, the researcher has a range of suggestions and recommendations to eliminate uncertainties in applying proportionality and contribute to establishing a balanced investor-state relationship in Chinese inbound and outbound FDI. These suggestions contain the structure of proportionality and the approach to its application, and the systemic interpretative approach. Finally, comments will be offered on Chinese BITs in which

¹⁹²⁹ See 2.4.4 in Chapter Two.

¹⁹³⁰ See 7.5 in Chapter Seven.

¹⁹³¹ Barak (n 20).

¹⁹³² See 2.3 in Chapter Two.

proportionality can be applied as a proper tool to balance the conflicts between the values of foreign investors and the host state, and on the legal status of proportionality in the Chinese domestic legal system.

8.2 Recommendations and Their Rationales

8.2.1 A Clearer Account of Proportionality

As reflected in the earlier discussion on proportionality at national and international levels, particularly, in the context of international investment, a more clearly defined and precise account of this principle is needed to further clarify its application. As conflicts will continue to arise between foreign investors and the host state, a clearer understanding of proportionality was promoted by the researcher, delving into aspects of its nature, components, and the approach to its application. This recommendation of clarity can assist parties and tribunals in balancing the legitimate expectations of foreign investors and the host state, especially of the state's stable legal framework.

While identifying whether proportionality is an international custom or a general principle of law under Article 38 (1) of the ICJ Statute, both quality and quantity of the state whose practice contributes to the formation are important factors. Unlike those scholars who mainly stress the number of states that contain proportionality in their domestic legal systems,¹⁹³³ the researcher highlights that the nature and practice of proportionality among different states need to be further investigated from an international perspective, which this thesis sought to do.

From the perspective of quantity, there is no doubt about the prevalence of proportionality, which is reflected in the sheer number of states in which this principle has been adopted.¹⁹³⁴ However, quantity does not necessarily equate to quality. Although proportionality is prevalent in many states' practices, it may not be a general practice due to the lack of sufficient support from representative states.

From the perspective of quality, the representativeness of the states in which proportionality is included is limited, and only a small number of specially affected states has been considered. Therefore, the paucity of studies of proportionality in the preeminent, specially affected states in the context of international investment, including China, raises doubts on whether proportionality is indeed a general principle of law, or even an international custom.

The current research confirmed a high potential for proportionality to become a principle in China. Nevertheless, it also highlighted the need to avoid a premature conclusion endorsing the arguments that

¹⁹³³ *supra* note 18.

¹⁹³⁴ See 2.3 in Chapter Two.

proportionality is a principle in the Chinese domestic law. This risks a potentially incorrect interpretation of its nature as a general principle of law in the sense of Article 38 (1) of the ICJ Statute further being brought into the ISDS. Consequently, further research is needed on the practice of the leading specially affected states in the context of international investment. These are the countries who have pro-actively participated in international investment as reflected in the number of their successfully concluded IIAs and their ISDs. Global stakeholders in international investment will be benefited from a more comprehensive understanding of proportionality analysis, especially the routes to its application.

Instead of including all considerations referred to in the process of applying proportionality, this study provided more evidence to describe the different stages included in proportionality analysis. As demonstrated by the researcher, the scope of proportionality should be neither expanded nor restricted. The consideration of the nature of conflicting values is the prerequisite for applying proportionality. Compared with the four- or two-element view, proportionality in this study is regarded as a principle consisting of three factors, including suitability, necessity, and proportionality *stricto sensu*.¹⁹³⁵ The significance of the legitimacy of both the pursued purpose and the infringed interest is recognised by the researcher, but such a consideration is the prerequisite for applying proportionality. Otherwise, there will be an unusual situation in which the disputed action violates the principle of proportionality due to the illegitimacy of the desired purpose, even though it may not be implemented.

Based on this prerequisite, only when both values fall into the category protected by the law can the application of proportionality be triggered. Although the assessments of suitability and necessity have some similarities, they reflect the means-end connection at different levels. Unlike the suitability test, which mainly articulates how the implemented means achieves the desired purpose, the necessity test also implies the comparison between the different implications of all potential measures that can achieve the same goal. In this respect, the former emphasises the positive effect of the implemented means, whereas the latter stresses its negative effect, expressing the means-end connection from different aspects. Once a measure that achieves the same purpose with less restriction on the infringed rights is confirmed, the value-oriented assessment can be undertaken to ascertain whether a balance is struck between the conflicts arising from different values. It is the researcher's view that proportionality as a flexible tool can fairly balance the conflicts between the values of foreign investors and the host state, such as their conflicting legitimate expectations of the stable legal framework. Proportionality should be applied following the internal sequence of its components, namely starting with the suitability test, followed by the necessity test and a real balancing between conflicting values.¹⁹³⁶

¹⁹³⁵ See 2.4 in Chapter Two.

¹⁹³⁶ See 2.5 in Chapter Two.

This view is also supported by cases at both international and national levels. Several ISDs arising from Argentina's economic crisis are typical cases here underlining the significance of a proper approach to applying proportionality. As discussed in Chapter Five, the reviews of similar measures taken by the Argentinian Government to react to its severe economic crisis were variable due to the inconsistent criteria and tests applied by the tribunals. One variance between those awards is that if the host state, to a certain extent, was provided with deference, its reactions would be supported by the tribunals only if such measures did not go beyond that which was necessary to achieve the desired purpose. The tribunals who carried out a real balancing between the conflicting values ascertained that Argentina's disputed reactions were justified only for a certain duration to settle the economic crisis and guarantee essential security interests.¹⁹³⁷

At the Chinese national level, in administrative law cases, some Chinese courts strictly applied proportionality based on its internal logical order, while others selectively utilised the necessity test or the assessment of proportionality *stricto sensu*. Underlying inclinations can be seen in their applications, leading to different reviews of similar measures against similar factual backgrounds. More deference could be provided if the proportionality *stricto sensu* test is the sole criterion to assess the questioned means. By contrast, if the necessity test or all three consecutive tests are applied to review the disputed measures, a violation would surely be found.¹⁹³⁸ Such different decisions or awards on similar measures reemphasise the importance of a proper approach to the application of proportionality in practice.

Therefore, the researcher contends that proportionality should be applied on the basis of the internal logical sequence of its constituent elements, namely the successive assessments of suitability, necessity, and proportionality *stricto sensu*, to review the means in question. Otherwise, even if such a flexible tool is adopted, a fair balance still fails to be struck between competing values. Both structure and flexibility indicated in this structured approach are the characteristics of proportionality. These are also its advantages, compared with reasonableness and balancing.

8.2.2 The Two-Tier Systemic Interpretative Approach-"A Concentric Circle"

The current study sought to outline a clearer definition of proportionality and answer general questions over its application in balancing the conflicts between disputing parties. The study then focused on its special application in striking a balance in the investor-state relationship in international investment, particularly in Chinese international investment. Due to the nature of proportionality, its application in the ISDS regime depends on the wording of the case-related applicable legal instrument.

¹⁹³⁷ *Continental v. Argentina* (n 5). *LG&E v. Argentina* (n 5).

¹⁹³⁸ Jiang (1719).

The first route to proportionality is the interpretation of treaty provisions which implicitly or explicitly express it. As recommended by the researcher, the two-tier systemic approach plays a vital role in bringing proportionality into the ISDS. Unlike other interpretative approaches, this method, as demonstrated, is hybrid and applied on a case-by-case basis. This approach is generally akin to a "concentric circle", which refers to two systems based on which the questioned words should be interpreted. Based on the in-depth analyses in Chapter Three, the "inner circle" means the treaty in which the disputed term appears, while the "outer circle" indicates the entire international law.¹⁹³⁹ This concentric circle should be considered from inside to outside, which is in accordance with the principles of interpretation stipulated in the Vienna Convention.¹⁹⁴⁰

The researcher noted that issues can and do arise from the gap between the principles of interpretation mentioned in theory and their actual applications in practice. The Vienna Convention emphasises that no hierarchy exists between different interpretative factors. The ordinary meaning of the questioned term as the starting point of a treaty interpretation is out of the logical order. Instead of a hierarchy, all factors, including the plain meaning of the term in question, its context, object and purpose of the treaty, and contracting parties' common intention, should be considered within the interpretation of treaties. Nevertheless, in practice, their corresponding interpretative approaches somewhat emphasise the significance of each individual interpretative element. Such an imbalance can be seen in the broad interpretation of FET. The tribunals who interpret FET in favour of foreign investors always emphasise the significance of the promotion and protection of foreign investment, which is mentioned as the object and purpose of the treaty in the preamble. It is worth noting that the application of these interpretative methods still finds in favour of one of the disputing parties and fails to make a fair treaty interpretation based on which a balance can be applied to conflicting values.¹⁹⁴¹

This issue could and should be settled by the two-tier systemic approach advocated by the researcher, contributing to striking a balance in the investor-state relationship at the stage of treaty interpretation. First the inner circle is applied. The entire case-related treaty is regarded as a system. In this respect, if the protection of non-investment values is mentioned, implicitly or explicitly, it should be considered by the tribunals in treaty interpretation. This can prevent tribunals interpreting overly broad interpretation in favour of foreign investors in considering the object and purpose of a treaty, as only investment values are outlined in the preamble. Instead, their discretionary power is slightly reigned in, due to the explicit provisions of non-investment values, such as the exception clause. A typical example

¹⁹³⁹ See 3.4.4 in Chapter Three.

¹⁹⁴⁰ Vienna Convention (n 47) Articles 31 and 32.

¹⁹⁴¹ For example, the tribunal who interpret ambiguous treaty provisions in teleological approach expresses a preference to investment protection. See in Zhang (n 55) 44.

of the application of inner circle is interpreting the provision of FET in conjunction with the exception clause. As stressed in these provisions, both investment and non-investment values are the dual purposes pursued by the contracting parties, indicating a clear requirement for balance between conflicting values. A balanced treaty interpretation also benefits a balance struck in the investor-state relationship.

Nevertheless, some IIAs signed several decades ago, such as the first two generations of Chinese BITs concluded between 1982 and 1997,¹⁹⁴² may not contain the exception clause. Instead of the protection of non-investment values, these older treaties mainly outline the contracting parties' intention to attract foreign investors and their investments. In this situation, the outer circle of the systemic interpretative approach, which refers to the whole of international law, plays a vital role in the balance of treaty interpretation.

In addition to international investment law, international law also refers to other legal fields. As a party in international law, a state is a participant in different fields and has various obligations at the international level. Its consistent obligations contribute to settling the fragmentation of various international instruments. The integration of different international instruments conveys a balanced treaty interpretation. More specifically, if the case-related treaty does not refer to non-investment values, such values mentioned in other relevant international instruments should be considered by the tribunals, but not all international instruments are relevant. As required by Article 31 (3) (c) of the Vienna Convention, such relevant international instruments should have a "similar object" or refer to a "same legal issue" with the treaty.¹⁹⁴³ In order to guarantee the consistency of a state's international obligations, both the language of IIAs and the wording of other relevant international instruments should be considered to decipher and clarify any ambiguous treaty provisions. Consequently, the protection of non-investment issues could be taken into account in treaty interpretation.

As described by the researcher, such a systemic interpretative approach is like a concentric circle, which, in fact, does not change the rules of interpretation provided in the Vienna Convention. Instead, this study consolidated all current approaches to interpreting treaty provisions. The application of such a hybrid interpretation approach varies based on the particular circumstances, striking a balance in the investor-state relationship in treaty interpretation, and contributing to a balanced investor-state relationship in international investment and the integration of different fields in international law.

8.2.3 A Clearer Map of Chinese Bilateral Investment Treaties

To further the understanding of the application of proportionality in Chinese international investment,

¹⁹⁴² See 6.2 in Chapter Six.

¹⁹⁴³ Vienna Convention (n 47) Article 31 (3) (c).

the current study presented a clearer map of Chinese BITs, reflecting the high potential for applying this tool to rebalance the investor-state relationship in Chinese inbound and outbound FDI.

As seen in Chapter Six, compared with older treaties signed decades ago, more recent Chinese BITs have various changes described in both investment and non-investment values, expressing the textual basis, at least of applying proportionality.¹⁹⁴⁴ One evident change is the clarified provisions of substantive treatments, such as the transition from unqualified FET to qualified FET.¹⁹⁴⁵ These important clarifications restrict the tribunals' discretion to avoid overly broad treaty interpretation that solely refers to investment values.¹⁹⁴⁶

Another change is the increasing number of Chinese BITs in which the exception clause refers to non-investment values. This amendment expresses that not only investment values, but also non-investment values have the attention of states. Based on the systemic interpretative approach mentioned above, interpreting the detailed substantive treatments in conjunction with the expanded protection of non-investment values reflects that a balanced paradigm of BIT has been pursued by China to strike a balance between the conflicting values of foreign investors and the host state.

Currently, China is not participating in any ISDs in which proportionality is being applied to review the measures taken by the host state in pursuit of the desired purpose. In this respect, the actual application of proportionality in Chinese international investment cannot be deeply examined. However, by comparing Chinese BITs to an applicable treaty where proportionality was applied, such as the Argentina-US BIT (1991),¹⁹⁴⁷ the textual basis of its application can also be observed in more recent Chinese BITs.¹⁹⁴⁸ Based on the earlier discussion in Chapter Five, one textual basis of applying proportionality in the Argentinian cases was the exceptional situations in which the host state's implemented measures would be justified even when they contravened treaty obligations *vis-à-vis* foreign investors.¹⁹⁴⁹ According to Table 6.3 in Chapter Six, a similar exception clause appears in eight third-generation Chinese BITs.¹⁹⁵⁰ One noteworthy point is that the China-Colombia BIT (2008)¹⁹⁵¹ explicitly stipulates that the measures "are *proportional* to the objective they seek to achieve",¹⁹⁵² expressing the application of proportionality. Based on the textual source provided in these treaties, it is possible for China to apply proportionality on a case-by-case basis to balance the conflicting

¹⁹⁴⁴ See in Chapter Six.

¹⁹⁴⁵ See Tables in Chapter Six.

¹⁹⁴⁶ UNCTAD (n 59).

¹⁹⁴⁷ Argentina-US BIT (n 120).

¹⁹⁴⁸ See 6.3 in Chapter Six.

¹⁹⁴⁹ See 5.3 in Chapter Five.

¹⁹⁵⁰ See Table 6.3 in Chapter Six. These Chinese BITs are the treaty signed by China with Finland, Madagascar, India, Colombia, Uzbekistan, Canada, Tanzania, and Turkey, respectively.

¹⁹⁵¹ China-Colombia BIT (n 124).

¹⁹⁵² *ibid* [italic added].

legitimate expectations of foreign investors and the host state in its international investment.

8.2.4 Recognising the Chinese Alternative Routes to Proportionality Analysis

When Chinese BITs are in question, the researcher further recommends the awareness of international and domestic routes to applying proportionality in Chinese international investment and how the Chinese court responds to the need for clarification. These recommendations for Chinese international investment can be seen in two parts, mirroring the two possible routes to applying proportionality in the ISDS. One is related to the legal status of proportionality in the Chinese domestic legal system, while the other is a balanced paradigm of Chinese international investment.

Regarding the first route, some time is needed to confirm that proportionality is a principle in the Chinese domestic legal system. There is undeniably a growing trend to stipulate proportionality in Chinese laws and regulations, despite the term "proportionality" being absent in the Chinese domestic law. The researcher recommends the relevant competent authority in China recognises this tangible trend towards the application of proportionality in China. It should exercise its power or discretion, where applicable, to confirm the principle of proportionality or endorse the authentic interpretation in order to react swiftly to the fast-changing needs of balancing conflicting rights.

As to the second route, less direct route, the above recommendation on recognising proportionality chiefly addresses the newer generation of Chinese BITs. However, as highlighted by the researcher, one important issue that affects the potential application of proportionality in Chinese international investment is that most Chinese BITs fall into the category of its first, or second-generation treaty, which provide ambiguous provisions of substantive treatments afforded to foreign investors without any reference to non-investment values.¹⁹⁵³ Furthermore, most of these treaties have never been amended.¹⁹⁵⁴

With regards to these old treaties, the researcher recommends the renegotiation between China and another contracting party on the inclusion, definition, scope, and interpretation of proportionality. The substantive treatment should be amended to restrict the tribunals' discretionary power to make overly broad treaty interpretation. Furthermore, non-investment values should also be accentuated in the treaty, to enable a more balanced interpretation. Both investment and non-investment values should be clearly articulated in the preamble; Otherwise, there are potential risks that the tribunals consider the promotion and protection of foreign investments as the default purpose of the treaty. In order to further protect and promote China's inbound and outbound FDI, the in-depth suggestions recommended by the researcher

¹⁹⁵³ See Tables in Chapter Six.

¹⁹⁵⁴ Only 17 Chinese BITs were amended or replaced by new treaties. *supra* note 168.

in 8.3 could be considered by China when it negotiates with another contracting state for a new treaty.

8.3 Suggestions on Chinese BITs

Concluded from the recent Chinese BITs and its resigned BITs, the recommendations on certain sections of Chinese BITs are put by the researcher. These suggestions refer to the wording of treaty preamble, the provision of FET, and the exception clause.

8.3.1 The Balanced Treaty Preamble

As presented below, the researcher suggests a balanced treaty preamble, which not only mentions investment values but also refers to non-investment values.

The Government of the People's Republic of China and the Government of _ (hereinafter referred to as the Contracting Parties).
Desiring to enhance the cooperation of both states;
Intending to create favourable conditions for investment by investors of one contracting party in the territory of the State of other contracting party;
Recognising that the reciprocal encouragement, promotion and protection of such investment on the basis of equality and mutual benefits will be conducive to stimulating business initiative of the investors and will increase economic prosperity in both states;
Respect for economic sovereignty of the contracting parties;
*Desiring to achieve the above goals by measures to promote a healthy, stable and sustainable development of economy, and to improve welfare of the peoples of the contracting parties.*¹⁹⁵⁵
[italic added]

This recommended treaty preamble explicitly emphasises the significance of both investment protection and the protection of non-investment interest. Consequently, even the tribunals mainly focus on the treaty's object and purpose when interpreting treaty provisions, they can no longer merely consider the protection of investment values. Such a balanced wording of the preamble contributes to a balanced investors-state relationship in the sense of treaty interpretation.

8.3.2 The Clarified Fair and Equitable Treatment

Based the research, a clarified provision of substantive treatments provided to foreign investors can avoid the tribunals overly broad interpretation in favour of investors. Therefore, the researcher suggests a detailed FET, namely the qualified FET with modifiers, should be stipulated to replace the unqualified standard.

Fair and Equitable Treatment

1. Each contracting party shall ensure to accord to investors of the other contracting party and associated investment in its territory fair and equitable treatment.
2. To clarify, "fair and equitable treatment" *requires/includes* that investors of one contracting party shall not be willfully rejected to fairly judicial proceedings by the other contracting party

¹⁹⁵⁵ An example of this treaty preamble is China-Uzbekistan BIT (n 1064).

or be treated with obvious discriminatory or arbitrary measure.

3 A determination that there has been a breach of other articles of this agreement, or articles of other agreements, does not establish that there has been a breach of this article.¹⁹⁵⁶ [italic added]

Similar to a balanced treaty preamble, a clarified FET clause can also restrict the tribunals' discretionary power to make broad treaty interpretations. The word "require" presents an exhaustive list of FET's components, while "include" expresses an exemplified list. The precise scope and components of FET depend on the actual negotiations between China and another contracting state.

8.3.3 The Clear but Flexible Exception Clause

According to the systemic interpretative approach, the treaty in which the questioned words appear should be regarded as a whole. In this respect, if there are provisions emphasising the significance of non-investment values, then such clauses must be considered by the tribunals to make a balanced interpretation. Meanwhile, these provisions list particular situations in which the measures taken by the host state are still justified even if they are against its treaty obligations *vis-à-vis* foreign investors, leaving certain room for the host state to exercise its regulatory power for the public interest and pursue sustainable foreign investment. The more commonplace and increasingly emphasised non-investment values, to a certain extent, contribute to a better-balanced investor-state relationship and achieve the optimisation of both parties' value.

From the perspective of protecting the host state's right to regulate in the public interest, more details should be provided in the exception clause to remove doubts and diffuse debates over the actual application of proportionality in practice. Although the exception clause has been stipulated in some Chinese BITs, there are still some continued uncertainties that can affect the practical proportionality analysis in balancing the investor-state relationship. This can be due to a lack of qualifying language in such a clause and a poorly defined criterion, or even no criterion at all for "necessity". Therefore, more details should be provided in the exception clause to avoid doubts and debates on proportionality's actual application in practice. The researcher puts recommendations on the exception clause as below.

Essential Security Interests

This agreement shall not be construed:

- (a) to require any contracting party to furnish or allow access to any information the disclosure of which will *it determines* to be contrary to *its essential security interests*.
- (b) to prevent a contracting party from adopting measures that *it considers proportional* for the purpose of protecting *its essential security interests* to its domestic law on a non-discriminatory basis / to prevent a contracting party from adopting *less restrictive means that it considers* to pursue the purpose of protecting *its essential security interests* to its domestic law on a non-discriminatory basis.
- (c) to prevent the host country from taking any actions to perform the duty of maintaining

¹⁹⁵⁶ A prime example of clarified FET is CETA (n 545) Article 8.

international peace and security under the Charter of the United Nations.¹⁹⁵⁷ [*italic added*]

General Exceptions

Provided that such measures are not applied in an arbitrary or unjustifiable manner, or do not constitute a disguised restriction on international trade or investment, nothing in this agreement shall be construed to prevent a contracting party from adopting or maintaining measures, which

- (a) are *proportional* / less restrictive means to preserve public order;
- (b) are *proportional* / less restrictive means to protect human, animal or plant life or health;
- (c) are *proportional* / less restrictive means to ensure compliance with laws and regulations that are not inconsistent with the provisions of this agreement;
- (d) aim to protect cultural industries;
- (e) aim to protect the environment.¹⁹⁵⁸ [*italic added*]

As highlighted by the researcher, based on the different objectives pursued by the host state, the exception clauses can be generally classified into two types. The qualifying language varies according to the significance or nature of the actual protected non-investment values, clarifying the decision-maker in each particular exceptional situation. Concerning the essential security interests, the host state is the decision-maker because it has a comprehensive understanding of its national condition and reacts to the emergency immediately, compared with the tribunals. Therefore, the qualifying language "it considers" explicitly appears in the provision of essential security interests. The qualifying language disappears in the provision of general exception, expressing the tribunal is the decision-maker when reviewing the measures taken for other non-investment values, such as environmental protection. Such flexible exception clauses guarantee the host state's right to ensure its essential security interests; On the other hand, the tribunals have discretionary power to make decisions on other non-investment values, somewhat avoiding the situations in which the exceptions are used by the host state as excuses to impair foreign investors' rights.

Meanwhile, the researcher also explicitly stresses the criterion for necessity to avoid confusion and eliminate any potential issues arising from its criteria. The need for such a defined criterion was emphasised in the Argentinian cases earlier examined. Therefore, as recommended by the researcher, the sole word "necessary" in the exception clause is replaced by more detailed phrases, such as "proportional to the desired purpose" or "less restrictive means to the pursued purpose".

As recommended by the researcher, the above issues need to be settled or clarified by China with another contracting party during their negotiations to conclude new treaties or amend old BITs. All of these contribute to rebalancing the investor-state relationship in the context of international investment, benefiting the protection and protection of China's inbound and outbound FDI.

¹⁹⁵⁷ Similar examples can be seen in China-Turkey BIT (n 15) and Canada-China BIT (n 421), which use the wording "necessary".

¹⁹⁵⁸ Similar examples can be seen in Canada-China BIT (n 421) and China-Colombia BIT (n 124).

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