Recurring Themes / Thèmes récurrents

Indirect Expropriation in International Law / L’expropriation indirecte en droit international

Introduction

Investment-treaty litigation, so popular in recent years, has kindled the debate on indirect expropriation of property under international law. In the context of the North American Free Trade Agreement ("NAFTA") investor-state arbitration mechanism in particular, foreign investors have asserted claims that certain regulatory measures taken by NAFTA State Parties constituted indirect expropriations of their property. Some point to the NAFTA experience to argue that affording foreign investors access to investor-state arbitration mechanisms that allow them to challenge, as "expropriations" or "measures tantamount to expropriation," regulatory measures will lead to a wave of litigation and will result in states’ unwillingness or inability to regulate areas of public concern, such as health and the environment. With respect to NAFTA itself, critics assert that the dispute-resolution mechanism available under its Chapter 11 has been hijacked by private corporations seeking to broaden the definition of expropriation under international law and force State Parties to settle claims for huge amounts. Others argue, by contrast, that the inclusion of takings clauses in investment treaties and the availability of investor-state arbitration mechanisms ensure a non-discriminatory and fair treatment of foreign investors and consequently are necessary to create a favorable investment environment that benefits everyone.

As the foregoing suggests, the debate on the definition of indirect expropriation revolves, to a great extent, around the need to strike the appropriate balance, in investment treaties, between the interests of foreign investors and the right of a state to regulate in the public interest. How much protection should be afforded the property rights of foreign investors? Some argue that the state – and, ultimately, the taxpayer – should not be required to act as the insurer of last resort of the value of foreign investments affected by governmental regulations pursuing a legitimate public purpose; the effects of regulations on the value of foreign property represent the materialization of a political risk, the consequences of which the foreign investor must bear. Others argue, in contrast, that it is not for the foreign investor to bear, in each and every case, the financial brunt of governmental regulations aimed at some public welfare purpose; if the effect of a regulation on an
investment is that of an expropriation, the state must compensate the foreign property owner.

Against this background, two doctrines have emerged from the indirect expropriation jurisprudence – one that favors the interests of foreign investors – the “sole-effect” doctrine, as Rudolf Dolzer and Felix Bloch have termed it – and another that favors the right of the state to regulate – the “police-powers” doctrine, as Veijo Heiskanen calls it. Pursuant to the “sole-effect” doctrine, the crucial factor in determining whether an indirect expropriation has occurred is solely the effect of the governmental measure on the property owner; the purpose of the governmental measure is irrelevant in making that determination. In the oft-cited Tippetts case, the Iran-United States Claims Tribunal ably encapsulated the essence of the “sole-effect” doctrine: “The intent of the government is less important than the effects of the measures on the owner, and the form of the measures of control or interference is less important than the reality of their impact.”1 The “police-powers” doctrine, on the other hand, also considers, in establishing whether a regulatory measure amounts to an expropriation, the purpose and context of the measure.

Rudolf Dolzer and Felix Bloch point out that, thus far, neither of the two doctrines can be characterized as dominant or as representing the mainstream of international thinking, though the more recent jurisprudence of arbitral tribunals seems inclined to shift the focus of the analysis “away from the context and the purpose to the effects on the owner.” In connection with the latter, the recent award by a NAFTA Chapter 11 arbitral tribunal in Metalclad Corp. v. United Mexican States epitomizes, along with Tippetts, the “sole-effect” approach.

In 1993, Metalclad Corporation, a United States company, purchased the Mexican company Confinamiento Tecnico de Residuos Industriales, S.A. de C.V. (“COTERIN”) in order to acquire, develop, and operate the latter’s hazardous-waste transfer station and landfill in Guadalcazar, Mexico. Although the Mexican federal and state governments had authorized COTERIN to construct and operate the landfill, the Municipality of Guadalcazar denied the municipal construction permit; subsequently, the local Governor issued an ecological decree, declaring the area encompassing the landfill to be a “Natural Area for the protection of rare cactus.” As a result, the operation of the landfill was precluded. The Metalclad Tribunal, among other things, held that the Municipality’s conduct in denying the construction permit, “taken together with the representations of the Mexican fed-

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