

B. Kuzhatov 

Queen Mary University of London,
KazGUU named M. Narikbayev, Kazakhstan, Nur-Sultan
e-mail: k_bagdat@kazguu.kz

REGULATORY SPACE AS A FACTOR OF CHANGE OF INTERNATIONAL INVESTMENT TREATY REGIME

At present time, the quest of balance between public and private interests under investment treaty provisions has become a serious challenge for all of the concerned parties, namely for host states, foreign investors, arbitral tribunals, scholars and arbitration lawyers. This quest is driving the international investment treaty regime to drastic changes. In this sense, this Article aims to determinate the role of regulatory space factor in the light of changing investment treaty jurisprudence. For this purpose, the Article analyses current fundamental shifts in international investment treaty regime and attempts to explain the roots of these shifts, inter alia, by focusing on the regulatory space factor. It reveals the drawbacks of current treaty regime, the lack of balance between regulatory space and investment protection, the role of the regulatory space in new investment treaties. In conclusion, it would argue that regulatory space plays a pivotal role in overall shifts of treaty regime. It could not resolve the current issues of balance in the treaty regime, but to some extent will serve to strike a balance between the regulatory space and the investment protection. The scientific novelty of the article is determined by the fact that this research attempts to justify the determination of factor of regulatory space in changing investment treaty regime by building a chain of roots of the matter and further development. The subject of the research is international investment law, particularly treaty regime. The Article employs doctrinal methodology to legal research from the perspective of historical, comparative and empirical analysis. The research under this Article is text-based and if applicable supported by the results of empirical studies.

Key words: investment treaty regime, regulatory space, investment protection, foreign direct investment, host state, investor, arbitration tribunal, ICSID, BIT, MIT, UNCTAD.

Б. Құжатов

Мәри патшайым атындағы Лондон Университеті,
М. Нәрікбаев ҚазГЗУ, Нұр-Сұлтан қ.
e-mail: k_bagdat@kazguu.kz

Қабылдаушы мемлекеттердің реттеу құқығы халықаралық инвестициялық келісімдер режимінің өзгеріс факторы тұрғысында

Қазіргі уақытта инвестициялық келісімдердің ережелері аясында мемлекеттік және жеке мүдделер арасындағы тепе-теңдікті қалпына келтіру барлық мүдделі тараптар, атап айтқанда қабылдаушы мемлекеттер, шетелдік инвесторлар, арбитраждық соттар, ғалымдар және төрелік заңгерлер үшін күрделі дилеммаға айналды. Теңгерімді іздеу халықаралық инвестициялық келісімшарт режимінің күрт өзгеруіне әкеледі. Осы өзгеріске орай, бұл мақаланың мақсаты – инвестициялық келісімдер тәжірибесіне әсер ету тұрғысынан қабылдаушы мемлекеттердің реттеуші құқықтарының рөлін анықтау. Мақалада халықаралық инвестициялық келісімдер режиміндегі соңғы маңызды өзгерістер талданады. Атап айтқанда, қабылдаушы мемлекеттердің реттеуші факторына назар аударылады және қолданыстағы шарттық режимнің кемшіліктерін, реттеуші кеңістік пен инвестицияларды қорғау арасындағы тепе-теңдіктің болмауының себептерін және жаңа инвестициялық келісімдерде қабылдаушы мемлекеттердің реттеуші құқықтарының рөлін түсіндіреді. Мақаланың ғылыми жаңалығы зерттеуде дилемманың себептік байланысын және оларды әрі қарай дамыту арқылы инвестициялық келісімдер режиміндегі өзгерістер тұрғысынан реттеуші кеңістік факторының анықтамасын негіздеуге талпыныс жасайтындығымен анықталады. Зерттеу нысаны – халықаралық инвестициялық құқық, атап айтқанда инвестициялық келісімдердің режимі.

Қорытындылай келе, автор қабылдаушы мемлекеттердің реттеуші құқықтары шарт режимінің қазіргі мәселелерін шеше алмайды, бірақ белгілі бір дәрежеде реттеуші кеңістік пен инвестицияларды қорғау арасындағы тепе-теңдікке қол жеткізуге көмектеседі деп тұжырымдайды. Мақалада тарихи, салыстырмалы және эмпирикалық талдау тұрғысынан құқықтық зерттеудің доктриналық әдісі қолданылады. Осы мақаладағы зерттеу мәтінге негізделген және мүмкін болған жағдайда эмпирикалық зерттеулермен расталады.

Түйін сөздер: инвестициялық келісім режимі, реттеуші кеңістік, инвестицияларды қорғау, тікелей шетелдік инвестициялар, қабылдаушы мемлекет, инвестор, төрелік сот, ICSID, BIT, MIT, UNCTAD.

Б. Кужатов

Лондонский Университет имени Королева Мэри,
Казахский государственный юридический университет имени М. Нарикбаева, Казахстан, г. Нур-Султан
*e-mail: k_bagdat@kazguu.kz

Регуляторные права принимающих государств как фактор изменения режима международных инвестиционных соглашений

В настоящее время восстановление баланса между государственными и частными интересами в рамках положений инвестиционных соглашений стало серьезной дилеммой для всех заинтересованных сторон, а именно для принимающих государств, иностранных инвесторов, арбитражных судов, ученых и арбитражных юристов. Поиск баланса ведет к резкому изменению режима международного инвестиционного соглашения. В свете такого изменения цель настоящей статьи направлена на определение роли регуляторных прав принимающих государств с точки зрения влияния на практику инвестиционных соглашений. Статья анализирует последние существенные изменения в режиме международных инвестиционных соглашений. В частности, она фокусируется на факторе регуляторных прав принимающих государств и объясняет недостатки текущего режима инвестиционных соглашений, причины отсутствия баланса между регуляторными правами принимающих стран и защитой инвестиций, роль регуляторных прав принимающих государств в новых инвестиционных соглашениях. Научная новизна статьи определяется тем, что в данном исследовании делается попытка обосновать определение фактора регуляторного пространства в свете изменений режима инвестиционных соглашений путем выстраивания причинно-следственных связей дилеммы и их дальнейшего развития. Предметом исследования является международное инвестиционное право, в частности режим инвестиционных соглашений. В заключение автор приходит к выводу, что регуляторные права государства имеют значительное влияние на изменения режима инвестиционных соглашений. Регуляторное пространство не может решить текущие проблемы баланса в режиме инвестиционных соглашений, а в некоторой степени будет способствовать достижению баланса между регуляторным пространством и защитой инвестиций. В статье применяется доктринальный метод правового исследования с точки зрения исторического, сравнительного и эмпирического анализа. Исследование по данной статье основано на тексте и, если применимо, подтверждается результатами эмпирических исследований.

Ключевые слова: режим инвестиционных соглашений, регуляторное пространство, защита инвестиций, прямые иностранные инвестиции, принимающее государство, инвестор, арбитражный трибунал, ICSID, BIT, MIT, UNCTAD.

Introduction

The nature of investment treaties has begun to change. It could be seen in the light of the recent termination and withdrawal from treaties by a number of states, revision of treaty clauses, and conclusion of a new wave of balanced treaties (UNCTAD 2019). Several factors have been pointed out by scholars as main factors of this change (Sornarajah 2011; Kaushal 2009; Mills 2011). They include overall shift in a political and economic landscape between developed and developing states, the dominant power of arbitration in the interpretation of treaty provisions, one-sided investment protection focused provisions of treaties, restriction of sovereignty and regulatory space of host states.

Flaws of current investment treaty regime

International investment treaties have been playing a crucial role in providing protection to foreign investors in the host states. In addition to this role, international investment treaties enforce the host states to make their regulatory framework more transparent, stable, predictable and secure in relation to foreign investors (UNCTAD 2003, 91).

A lack of protection provided by customary international law and uncertain foreign investment protection laws of the host states principally has led developed states to conclude investment treaties with developing states (Kaushal 2009, 513). In this sense, investment treaty provisions have been designed to ensure investment protection guarantees

for foreign investors in addition to those contained in the host states' national system (Dolzer 2005, 953). Investment treaty represents that foreign investor's property and contract rights are protected and enforceable under international law (Kaushal 2009, 513; Elkins et al 2008, 825). Therefore, at the outset, the investment treaty regime was driven by developed states as a tool to reduce the political risk for investments of companies of home states in the host states.

Earlier 1960s the World Bank and International Monetary Fund took the lead to address the emerging international legal framework of foreign investment, pointing to its mandate and to the link between economic development, international cooperation, and the role of private international investment (Dolzer 2015, 7; Muchlinski 2009, 38). Thus, the treaty regime initially made a clear focus on the rights of investors and responsibilities of host states in the provision of protection to alien's property. To achieve the goal, classic investment treaties incorporated standards of treatment such as fair and equitable treatment, expropriation, national treatment and most favoured nation. If the host state expropriates the investment, changes applicable governing laws in relation to foreign investors, restricts the transfer of profits or takes discriminatory measures against a foreign investor, then the foreign investor may bring a claim for compensation of damages or deprived investment. These standards of treatment have binding obligations on host states by constraining their national regulatory sphere of action.

Moreover, the focus of protection under investment treaties covered not only the post-establishment phase of investment, but also admission. In the light of such a clause, the host state has an obligation to treat foreign investors not less favourable than their own nationals. This goal has been achieved through proper incorporated national treatment and most-favoured nation clauses.

Initiatives of the World Bank brought to a search of a dispute settlement mechanism which resulted in the adoption of the Convention on the Settlement of Investment Disputes between States and Nationals of Other States (ICSID Convention) establishing the International Centre for Settlement of Investment Disputes (ICSID) in 1965 (Dolzer 2015, 7). It provided investors of the ICSID member states to seek a remedy before ICSID tribunal.

The classical investment treaty regime of the past decade has addressed only issues of foreign investment protection. At the same time, investment treaties are understood to attract and promote foreign investment by reducing the discrimina-

tion and unpredictability of state actions (Dolzer 2005, 953). Therefore, this regime was expected to contribute to the development of the host states economy through transfer of capital, technology and skills.

However, the assumption that investment treaties promote investment flow has been subject to the observation of numerous studies. These studies have come divergent outcomes on the correlation between the investment treaties and foreign investment flow, thus positive effects of the investment treaties on the promotion of foreign investment have been doubted (Kaushal 2009, 525; UNCTAD 1988, 1998, 2003; Driemeier 2003).

In the light of this regime to date over 3000 bilateral (BITs) and multilateral investment treaties (MITs), including trade-investment partnership agreements have been concluded. The majority of current BITs and MITs were negotiated during 1960 to 1990s based on a narrow investor protection model stemming from the 1962 OECD Draft Convention on the Protection of Foreign Property.

What is a regulatory space?

The meaning of regulatory space in international investment law is used interchangeably with the concepts of sovereignty, national space, regulatory rights, right to regulate, police power, regulatory autonomy, regulatory measures and regulatory freedom of states to regulate (Mann 2003, 211).

In general, the term is reflected as attribute of sovereignty under international law that represents freedom of state to involve in political, economic, legislative and other regulatory activity as the state sees fit.

In terms of sovereignty, the term is related to the concept that decision making authority and power of a state to legislate should not be allocated to private investors and international arbitration tribunals (Kaushal 2009, 511). In particular, sovereignty is understood as the superiority of national and governmental power.

In recent scholars' contributions, this term is widely mentioned as a right to regulate. It is understood as the right of the host state to regulate foreign investment in order to promote domestic priorities and to protect the public welfare from possible negative impacts of foreign and domestic investment. More narrowly the term is discussed in recent scholar contributions, where the term is defined as the legal right of the host state that permits it exceptionally to regulate in derogation of international commitments it has undertaken in the framework of

investment agreements without incurring a duty to compensate (Titi 2013, 33).

General limitation of the regulatory space

As an ordinary international agreement, the investment treaty reduces the scope of sovereignty for state parties of the treaty. There are two common ways of limitation of the regulatory space by the investment treaty.

Firstly, the nature of the investment treaty functions to define and narrow the permissible types of domestic administrative regulation to which foreign investors could be subject. This limitation on the host state's administrative right to regulate in the public interest covers not only economic matters, but also extends to environmental, tax and labor as well. In this sense, host states are obliged to bring their domestic legislation into a balance with a treaty regime (Dolzer 2006, 954). Such limitation is a response to the investors' concern for the predictability and stability of the legal framework of the host state governing the investments.

Secondly, investment treaties virtually permit any type of public policy regulation affecting foreign investors to be challenged before international arbitration tribunals. In this way, investment treaties limit the power of the host state to subject foreign investors to its domestic legal system.

Excessive limitation factor

There is rising public concern about excessive limitation of regulatory space by investment treaty provisions. *Inter alia*, it is about the suitability and the legitimacy of the existing international investment law system for dealing with the tension between investment protections and competing for the right to regulate host states. This is due to the fact that the functioning of the investment treaty regime has become no longer suitable for the host states. In particular, extensive investment protection focused treaty regime led to an increase in arbitration disputes over the world (Kingsbury and Schill 2010; UNCTAD 2003). The broadly worded and open-textured standard provisions of investment treaties provided foreign investors with the right to challenge nearly any regulatory measure regardless legitimate or not, as well arbitral tribunals with significant discretion in interpreting obligations of states towards their treatment to foreign investors (Roberts 2010, 179-225).

In theory, treaty parties are supreme when creating the law and tribunals are supreme when ap-

plying it in particular cases. In this sense, tribunal awards in particular cases informally contribute to the interpretation, and thus the creation of law (Roberts 2010, 179-225).

However, there are two critical issues for the host states on this. In the first place, it is frequently difficult for tribunals to set criteria to determine whether a breach has occurred and thus a host state is liable to compensate. A concern is that treaty provisions may unduly expose states to compensate investors for non-discriminatory, legitimate laws, regulations, and administrative decisions adopted to sustain public welfare. Determination of borderline between legitimate regulatory rights and discriminatory measures was widely discussed in earlier arbitration cases (Tecmed 2003, Metalclad 2000, Methanex 2005). Currently, a significant share of arbitration disputes on challenging the regulatory space is primarily related to regulatory measures on sensitive sectors such as environment, energy security, climate change, the ban on tobacco and etc. (Philip Morris 2017; Charanne Construction 2016; NextEra Energy 2019; Eiser Infrastructure 2017; Novenergia II 2018; Masdar Solar 2018; Antin Energia 2018). Merely the Kingdom of Spain is facing over 40 arbitration disputes for regulatory measures in the sector of renewable energy under the Energy Charter Treaty.

In the second place, for states any investment dispute in arbitration involves financial stakes large enough despite win or lose outcomes of the dispute (Muchlinski 2009, 347-378). Since even a single award can place "onerous" demands on the budgetary resources of states (Muchlinski 2009, 347-378). As a result, host states, mostly developing states had to pay a high cost of national sovereignty instead of foreign investment flow (Elkins et al 2008, 299).

New wave of treaties

A factor of regulatory space, *inter alia*, has been leading to a nascence of new investment treaty regime. The new investment treaty regime is intended to shift well entrenched investment protection focused treaty regime. It is meant that new treaties should resolve the accumulated issues of the current investment treaty regime. Primarily, it should preserve the host state's regulatory space in the public interest, balance investor rights and duties, acknowledge the importance of sustainable development and environmental goals (Muchlinski 2016, 41).

International organizations such as UNCTAD and the Commonwealth Secretariat took the leading

role in developing guidelines for the design of new investment treaties. At the same time, model treaties have also been designed by the United States, Canada, Norway and ASEAN member states. There are also newly designed treaties such as the US-EU Transatlantic Trade and Investment Partnership (TTIP), Trans-Pacific Partnership (TPP) Agreement and Canada-EU Comprehensive Economic and Trade Agreement (CETA), which have reconsidered approaches on standards of protection.

These recent negotiated treaties have sought to safeguard the state's regulatory space and regulatory autonomy by narrowing down and clarifying treaty guarantees, and by limiting the opportunities for a broad interpretation of protection standards by arbitral tribunals. Newly designed treaties use renewed and novel approaches in relation to the preservation of regulatory space. Common approaches include:

- an explicit confirmation of the host state's regulatory rights;
- more precise definitions of investment and investor, standards of treatment, general exceptions clauses;
- affirmation of other non-investment values and concerns such as protection of labor and environment;
- more precise dispute settlement clauses on access to ISDS;
- provisions curbing arbitral tribunal's power to interpret the investment treaty.

Kazakhstan's perspective

In the context of this topic, the Article notes that the issue of the regulatory space is important also for Kazakhstan. To date, Kazakhstan has concluded over 40 (forty) bilateral investment treaties on the encouragement and reciprocal protection of investment (Ministry of Foreign Affairs of the Republic of Kazakhstan 2020). There are also multilateral treaties that contain investment protection provisions such as the Energy Charter Treaty and the Eurasian Economic Union Treaty. The majority of them were concluded between 1992 and 2005, which based on the old investment treaty regime.

In the framework of these investment treaties, Kazakhstan is Respondent in 19 (nineteen) international investment arbitrations (Investment Policy Hub of UNCTAD, 2020). 5 (five) of them were initiated under the Energy Charter Treaty and 7 (seven) of them under the bilateral investment treaty between Kazakhstan and the United States.

One of the most challenged treaties is the Energy Charter Treaty that Kazakhstan is a member state. As recent trend demonstrates that investors overly rely on the substantive protection provisions of the Energy Charter Treaty to protect their investments in the host states. To date 125 investment disputes have been raised under the Energy Charter Treaty. According to statistics of the Energy Charter Treaty, over the last two years, 50 applications for arbitration have been submitted under the Energy Charter provisions (The Energy Charter Secretariat information). From 2015 to 2019 years 60 arbitration claims were submitted against host states under the Energy Charter Treaty. It brought an overwhelming burden for member countries in the protection of their public interests and implementation of internal laws.

The trend raises a matter of concern among member countries about harmonizing investment protection provisions towards their regulatory rights and striking a balance between them. In 2018, the Energy Charter Conference has started the long-awaited negotiations on the modernization of the treaty. Ten topics have been adopted by the Energy Charter Conference for discussion and further elaboration of viable solutions for member states. One of the included 10 topics is the right to regulate, i.e. regulatory space issue.

Conclusion

This article attempted to explain current fundamental shifts in international investment treaty regime and the roots of these shifts, *inter alia*, by focusing on the regulatory space factor. The Article demonstrated the drawbacks of current treaty regime, the lack of balance between regulatory space and investment protection, the role of the regulatory space in new investment treaties. There is a number of factors which affected this shift such as political and economic landscape between developed and developing states, the dominant power of arbitration in the interpretation of treaty provisions, one-sided investment protection focused provisions of treaties. However, massive claims of investors to ISDS on challenging legitimate regulatory rights of the host states, *inter alia*, led to the reconsideration of the treaty regime.

Currently, states seek to develop new types of investment treaties that strike a balance between regulatory space and investor protection. The number of new model treaties has been elaborated. There is no doubt that a new wave of treaties will also touch upon Kazakhstan since most of the treaties

have been concluded in the late 1990s and 2000s. Regulatory space matter is also under discussion in the framework of the modernization process of the Energy Charter Treaty.

In conclusion, it is argued that regulatory space plays a pivotal role in overall shifts of treaty regime.

However, it is early to point out the effectiveness of new treaties on balancing regulatory space and investment protection, as well as on stopping the increase of arbitration disputes, but to some extent certainly, new treaties help to resolve current flaws of the investment treaty regime.

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