Investor Protection v. State Regulatory Discretion

Definitions of Expropriation and Shrinking Regulatory Competence

Ioannis Glinavos[*]

Abstract

The purpose of this paper is to offer support to the idea that the contemporary international legal framework offers opportunities to investors to challenge and control government action via what has been described as a 'regulatory freeze'. This regulatory freeze is the consequence of government reluctance to legislate/regulate in areas where claims of expropriation may be brought. The paper presents evidence from investment-treaty dispute resolution mechanisms, national and supranational judicial processes from both sides of the Atlantic. The paper concludes by suggesting that the potential for expanded definitions of expropriation is having a greater impact than actual case outcomes, as states seek to preempt any adverse developments by shying away from regulations that may provide fertile grounds for challenge. This effect is significant, as it is contrary to expectations of greater state involvement in economic management bred by the financial crisis.

Keywords: regulatory freeze, expropriation, investor protection, economic governance, environmental protection.

A. Introduction

The purpose of this paper is to demonstrate that the contemporary international legal framework offers opportunities to investors to challenge and control state action via what has been described as a 'regulatory freeze'. This means that changes to the way states behave are not being made because courts and tribunals have significantly expanded definitions of expropriation in order to massively restrict state regulatory discretion. On the contrary, a regulatory freeze is the consequence of states' own reluctance to legislate/regulate in areas where challenges might be brought. The costs of litigation and the potential of decisions adverse to the state mandating compensation for investors, even if they are largely remote in areas still considered an exercise of legitimate state 'police powers', make legislators doubly careful before upsetting market expectations via

* Dr. Ioannis Glinavos is Lecturer in Law at the University of Reading, School of Law, i.glinavos@reading.ac.uk.

expanding regulation, for example in pursuit of environmental objectives. As the focus of this paper is legislation concerning protection from state takings, the paper offers a comparative study examining definitions of expropriation in national and international law aiming to define the outer limits of curbs on state discretion. This discussion addresses the work of investment treaty based dispute resolution mechanisms and national provisions for private investor-state dispute resolution from both sides of the Atlantic. The paper concludes by suggesting that the potential for expanded definitions of expropriation is having a greater impact than actual case outcomes, as states seek to pre-empt any adverse developments by shying away from regulations that may provide fertile grounds for challenge.

B. State Takings or Unlucky Investors?

It is not a new idea in international law that foreign owned property should be protected from expropriation. Protection is commonly achieved by giving property owners a right to compensation for the value of the lost or expropriated property. Also, national constitutions contain to varying degrees mechanisms to protect economic rights, most specifically private property rights. One of the core functions of constitutional drafting in fact is to achieve a balance between the protection of the rights of citizens to enjoy their property and the ability of governments to control private actors' behaviour within the national economy. A balance is usually found on an intermediate point between absolute protection of private property rights and limitless government power. This balance in national constitutional provisions translates as limits on expropriation and provisions for compensation in the event of government takings. The following discussion offers a comparative exposition of provisions for the protection of property from state taking in international dispute resolution fora and nationally, drawing examples from Greece, the European Court of Human Rights (ECtHR), the European Court of Justice (ECJ) and the United States Supreme Court.

This discussion is of contemporary significance because in the last two decades (primarily) investors have made claims for compensation based on government regulations placing restrictions on the legal use of property affecting its value, but without actually removing the owner's title to the property.

This development has led to the creation of a doctrine of 'indirect expropriation' that is of concern because of its capacity to conflict with the till-recently dominant notion that states can regulate without having to pay compensation when such regulation constitutes an exercise of their legitimate 'police powers' such as taxation, the protection of public health and welfare. Concern stems from the argument that allowing a doctrine of indirect expropriation to eat away at the sphere of government discretion under the umbrella of police powers will severely limit the capacity of governments to legislate in order to promote general wel-

fare.[1] Obvious victims of these trends can be regulations to address environmentally damaging behaviour contributing to climate change, to use a single prominent example.

The core idea underpinning the framework of investor protection therefore is the requirement for the payment of compensation for expropriation. For there to be a recovery for expropriation, however, in almost all jurisdictions, there is a requirement that there must be a taking of property. Defining what constitutes expropriation or taking has been a matter of significant controversy both in dispute resolution fora and in national courts. The argument of this paper is that expanded definitions of expropriation that include regulatory measures that affect profitability, harm states' capacity to govern their sovereign territories and constitute part of an emerging global constitutional order that rates market freedoms as more important than other social and political objectives. The paper looks at case-law developed through various public and private dispute resolution fora in trying to tease out trends suggesting a global solidifying of a pro-market legal regime focused on the protection of business and property interests. The paper proceeds to look at these issues from the viewpoint of the Americas, looking at US law and NAFTA cases and then examines the European position by looking at Greece and the European Court of Human Rights. The following section begins an evaluation of definitions of takings under US law.

C. Takings under US Law

International law generally addresses the issue of expropriation by defining it as a compulsory transfer of property rights and refers to regulatory takings variably as indirect expropriation, disguised expropriation or creeping expropriation. While it is generally required that governments will need to offer compensation for actions amounting to expropriation, it is accepted that states are not liable for economic losses arising from bona fide regulation within the accepted scope of 'police powers' including the operation of competition law, consumer protection, securities regulation, environmental protection, land planning and other similar legislation.[2] In reviewing the decisions of the Iran-US Claims Tribunal for example, one of its members concluded that under international law, liability does not arise from actions that are non-discriminatory and are within the commonly accepted taxation and police powers of states.[3] The history of the conflict between protection of the public good with regulations at the discretion of government versus protection of private interests through constitutional curbs on government action is best displayed through a short presentation of the history of compensation for expropriation under the US Constitution. US jurisprudence, unlike that of its NAFTA partners Mexico and Canada, recognizes that regula-

1 Wagner, M. 'International Investment, Expropriation and Environmental Protection', Vol. 29 *Golden Gate University Law Review* (1999), p. 466.

2 Wagner (1999), p. 518.

3 Aldrich, G. 'What Constitutes a Compensable Taking of Property? The Decisions of the Iran-US Claims Tribunal', (1994), 88 *American Journal of International Law* p. 585, at p. 609.

tions that restrict the economic use of property may, in certain circumstances, qualify as compensable 'takings'. US law defines compensatable expropriations on the basis of case-law stemming from the Fifth Amendment of the US Constitution. The Fifth Amendment states that no person shall be deprived of life, liberty, or property without due process of law, nor shall private property be taken for public use without just compensation. While originally the courts interpreted this provision to require protection of real property or tangible assets, the definition has subsequently considerably widened. However, government action that causes economic loss is still largely considered to be non-compensable if it falls within the scope of the states' police powers (encompassing public health, safety and welfare).

A prime example of the widening definition of expropriation in US law is provided by the case of *Lochner v. New York* (1905, 108 US 45). In Lochner, the Supreme Court used a combination of the Fourteenth and the Fifth Amendments to invalidate regulations regarding taxation, minimum wage requirements, and labour relations.[4] In principle, there are two categories of takings that may attract compensation. The first is physical taking of property for which the owner must be compensated. In *Pennsylvania Coal Co v. Mahon* in 1922, (260 US 393), for example, the Supreme Court held that this rule would also apply to a regulation whose effect was to strip land of any economic use. A second category deals with regulations that adversely impact on the economic use of property but fall short of stripping it of all economic use, so-called partial takings. The Supreme Court has avoided setting definitive rules for determining when compensation will be awarded in such circumstances.[5] It could be argued that the court reacted to expanding government interference with private interests by seeking to define when compensation becomes payable according to the magnitude of the loss, an approach dubious in theory and problematic in application. The test (as developed in more recent case-law) seems to be based on an assessment of whether state regulation goes too far in reducing the value of the affected property. The subjective nature of this test has been recognized as problematic by the court itself and has resulted in a largely unsuccessful formula to use in distinguishing acceptable regulatory action from expropriation. In *Penn Central Transportation v. City of New York* (438 US 104) the court offered a three part test in determining whether a state action could amount to expropriation: one should examine the character of government action (seizure of property or regulatory intervention); interference with reasonable investment-backed expectations; and the extent of the diminution in value. Actions that lead to high levels of interference resulting in significant losses will warrant compensation. Even this test however does little to reduce the subjective elements of this determination, and is consequently of little practical value.

While the preceding section may create the impression of a uniform trend in US law towards expanding definitions of what constitutes expropriation, or tak-

4 Byrne, K. 'Regulatory Expropriation and State Intent', (2000) 38 *Can. Y.B. Int'l L.* p. 89, at p. 100.

5 Baughen, S., 'Expiration and Environmental Regulation: The Lessons of NAFTA Chapter II' (2006), Vol. 18, No. 2, *Journal of Environmental Law*, pp. 207-228, at p. 208.

ing, this has far from been the case. The desire of US courts to expand the scope of regulatory activity potentially caught by the definition of takings up to the 1930s was short-lived, as new appointments to the Supreme Court during the Depression and a recognition of the need for greater state involvement in the economy resulted in narrowing definitions of compensable expropriation. It was not till the 1980s where the politics and jurisprudence of the US courts changed direction again towards safeguarding interests wider than real property. This issue has been of interest because of concern that despite its differences with other neighbouring states, US jurisprudence on partial takings will infect the construction of Article 1110 of NAFTA.[6] It seems however, that to date American courts have rejected a number of claims for compensation arising out of loss of business value due to environmental or public health regulations. The question nevertheless remains: how do regulators react to the potential of obstructive litigation and do governments show willingness to test the court's appetite for expanding definitions of expropriation? While case-law generated by national courts shows a lesser desire to expand definitions of takings to include loss of profitability, the trends identified in investor arbitrations suggest otherwise. The next section demonstrates this by evaluating the jurisprudence of NAFTA.

D. The View from NAFTA

Like many international investment promotion agreements, NAFTA mandates compensation for direct and indirect expropriation of foreign investments. According to Wagner, in an unprecedented move, companies have started to use this protection to challenge measures instigated by governments aiming to protect the environment and public health.[7] This section looks into some detail at the investor protection provisions of NAFTA and their interpretations by tribunals. Article 1110 of NAFTA, entitles investors to compensation in the event of their investment being expropriated and extends this protection to measures "tantamount to nationalization or expropriation".[8] This brings us back to the question of whether the effects of regulations on the commercial prospects of investments could constitute expropriation. Decisions of tribunals making awards under BITs applying the principles of customary international law on expropriation can help us define the meaning of expropriation. In particular, some useful guidance on which state conduct (falling short of overt nationalization) can amount to expropriation can be derived from the awards of the Iran–US claims tribunals.[9] In *Tippetts, Abbett, McCarthy, Stratton v. TAMS-AFFA Consulting Engineers of Iran*[10] it was argued that a deprivation or taking of property may occur under international law through interference by a state in the use of that

6 Baughen (2006), p. 208.
7 Wagner (1999), p. 466.
8 Baughen (2006), p. 208.
9 Baughen (2006), p. 209.
10 6 Iran–U.S. Cl. Trib. Rep. 219 (1984) at pp. 225-226.

property or through interference in the enjoyment of its benefits, even where legal title to the property is not affected.

While the assumption of control over property by a state does not automatically and immediately justify a conclusion that the property has been 'taken' by the government (warranting compensation under international law), compensation will be payable whenever the owner of the property has been deprived of fundamental rights of ownership and such deprivation is permanent. Interestingly enough, the intent of the state agency responsible for the regulation is less important than the effects of the measures on the owner. Equally, the form this interference takes is less important than the reality of its effects. The tribunal in Tippetts therefore conceptualizes expropriation as the result of state actions resulting in pragmatic results detrimental to the investor, regardless of the form of the measure or its intent. Solutions consistent with this approach of the Iran-US Claims Tribunal have also been reached in different contexts. In *Middle Eastern Shipping and Handling Co v. Egypt*[11] the tribunal described indirect expropriation using the terms "depriving the investor of the use and benefit of his investment, even though he may retain nominal ownership of the respective rights". Similarly, in *Lauder v. Czech Republic*[12] takings amounting to expropriation included those that were not overt, but effectively neutralized the 'enjoyment' of property.[13] It is also generally accepted that expropriations outside the scope of a state's police powers (referring to public health, safety and welfare) will entail an obligation to compensate, notwithstanding the public interest considerations behind the state's action or the fact that such action is lawful. In *Cia del Desarollo de Santa Elena SA v. Republic of Costa Rica*[14] the tribunal decided that the purpose of protecting the environment for which the property was taken does not alter the legal character of the taking for which adequate compensation must be paid. The tribunal then went on to state that expropriatory environmental measures are similar to any other expropriatory measures that a state may take in order to implement its policies. The tribunal concluded that where property is expropriated, even for environmental purposes, (mandated by domestic or international policies), the state's obligation to pay compensation remains; a conclusion at odds with public expectations of action on behalf of governments to tackle climate change, seen to be caused to a large extent by the actions of private, profit seeking entities. Dicta to the effect that environmental regulations may be seen as 'takings' requiring compensation were also followed in *Tecmed v. Mexico*.[15]

Continuing with our discussion of NAFTA, it is worth offering some further detail on the substantive protections to investors offered by its Chapter 11. Under this chapter, foreign investors are entitled to the benefit of 'national treatment' (Art. 1102); to the application of most-favoured-nation principles (Art. 1103); and to the minimum treatment to which they are entitled to under

11 2002, ICSID ARB/99/6 para. 107.
12 2001, IIC 205 (2001), para. 54.
13 M. Sornarajah, *The International Law of Foreign Investment*, Cambridge University Press, Cambridge 2004, p. 350.
14 2000, 15 ICSID Rev. 169.
15 2003, ICSID ARB(AF)/00/2 para. 21.

international law, including fair and equitable treatment and full protection and security (Art. 1105). Performance requirements, as regards both foreign and domestic investors, are prohibited (Art. 1106), subject to some limited exceptions. While successful claims by investors challenging state actions under NAFTA mostly involve breaches of Articles 1102 and 1105, the major focus of concern (primarily by environmental groups) has been on the potential of Article 1110 to inhibit environmental regulation, the so-called 'regulatory chill', which is the core issue of this paper. Chapter 11 (Art. 1110) provides that no party shall directly or indirectly nationalize or expropriate an investment of an investor of another party in its territory or take a measure tantamount to nationalization or expropriation of such an investment except: for a public purpose; on a nondiscriminatory basis; in accordance with due process of law; and on payment of compensation. The key concept of investment is defined (Art. 1139) as including an enterprise, but also includes: equity security, a debt security of an enterprise, a loan to an enterprise as well as an interest in an enterprise that entitles the owner to share in income or profits of the enterprise, or to share in the assets of that enterprise on dissolution. Definitions of investment under NAFTA also encompass real estate or other property, tangible or intangible, acquired in the expectation or used for the purpose of economic benefit or other business purposes, plus interests arising from the commitment of capital or other resources in the territory of a party to the treaty to economic activity in such territory. The wordings of these last headings are particularly open to interpretation and liable to encompass expectations of future trading profits in another NAFTA party.[16]

To police the enforcement of these rules, NAFTA creates a system of international investment arbitration whereby aggrieved foreign investors may challenge host states' actions that allegedly interfere with their rights. These challenges to the exercise of public authority by sovereign states are heard by international arbitral panels that operate under rules designed for the settlement of international investment disputes on the example of ICSID (International Convention on the Settlement of Investment Disputes). Similar rights and remedies are found in hundreds of bilateral investment treaties (BITs). The resulting global network of investment rules creates powerful rights for international capital and a powerful new jurisdictional universe of adjudication to enforce them.[17] Are, however investor protection provisions interpreted in dispute resolution fora in ways that severely restrict the state's ability to regulate in areas till recently considered as legitimate exercise of state authority? The following section answers this question by focusing on evidence from the NAFTA area.

16 Baughen (2006), p. 225.

17 S. Wood & S. Clarkson, 'NAFTA Chapter 11 as Supraconstitution', (2009), CLPE Research Paper 43/2009 Vol. 5 No. 8, pp. 4-5.

E. Canadian Freezing

The tribunal in *Methanex v. USA*[18] observed that regulatory conduct by public authorities is unlikely to be the subject of legitimate complaint under Article 1110 of NAFTA, although it did not rule out that possibility. The tribunal suggested that expropriations tend to involve the deprivation of ownership rights, while regulations involve a lesser interference.[19] The argument could be made therefore that the distinction between expropriation and regulation screens out most potential cases of complaints concerning economic intervention by a state and reduces the risk that governments will be subject to claims as they go about their business of managing public affairs.[20] On the facts of Methanex, the closure of the border under consideration had been temporary, whereas expropriation usually amounts to a lasting removal of the ability of an owner to make use of its economic rights although the tribunal made it clear that, in some contexts and circumstances, it would be appropriate to view a deprivation as amounting to an expropriation, even if it were partial or temporary. The position is similar to that in the *S.D. Myers v. Canada* (para. 283) discussed later in this section. In *Metalclad v. United Mexican States*[21] expropriation under NAFTA was held to include not only open, deliberate and acknowledged takings of property, such as outright seizure or formal or obligatory transfer of title in favour of the host state, but also covert or incidental interference with the use of property. This interference was deemed illegitimate when it had the effect of depriving the owner, in whole or in significant part, of the use (or reasonably-to-be expected economic benefit) of property even when such interference was not necessarily to the obvious benefit of the host state. According to Sornarajah[22] these dicta illustrate the expansive scope given to expropriation. To return to one of the main focal points of this discussion, which is concern as to the effect of NAFTA on progressive environmental regulation, it is worth stating that the wording of Article 1110 clearly requires the payment of compensation for an expropriation, notwithstanding that the measure in question is directed at the protection of the environment. Sornarajah[23] voices concern that as the same arbitrators are involved in various tribunals, passing judgment on similar disputes, expanding notions of expropriation used by NAFTA tribunals are likely to spill over to other areas of international law as well.

It is worth repeating here the reason for concern arising from the requirement for compensation for indirect expropriation. If states are threatened with the need to compensate in increasing regulatory spheres when regulation affects the profitability of investments, states will be less likely to legislate in the common good, especially on environmental protection issues, when doing so incurs costs of preventing or defending litigations. In principle, NAFTA (Art. 1110) does not prevent a state from introducing an expropriatory measure to ensure that

18 2005 Final Award of the Tribunal on Jurisdiction and Merits, 3 August 2005
19 Baughen (2006), p. 217.
20 *Ibid.*, p. 219.
21 ICSID Case No. Arb (AF) 97/1, Award 30 August 2000.
22 Sornarajah (2004), p. 355.
23 *Ibid.*

investment activity in its territory is undertaken in a manner sensitive to environmental concerns. References to 'public purpose' clearly allow this, provided that compensation is paid to the investor.[24] But it is the payment of compensation in itself that is exactly the problem here. Why should a state be forced to compensate polluters when exercising its legitimate power to control their damaging behaviour?

There are already cases illustrating the existence and evolution of the trends described above within NAFTA. The case of *Ethyl Corporation v. Canada*[25] which was settled before the tribunal had the chance to make an award, involved Canadian environmental regulations that prohibited the import and trade in certain chemical components (MMT) of gasoline due to their potentially harmful effects on health and the environment. Immediately upon the bill becoming law the US Corporation Ethyl and its wholly owned Canadian subsidiary filed a notice of arbitration pursuant to NAFTA's investment chapter. Ethyl claimed amongst other things that the Canadian law constituted an expropriation of its business in Canada and was as such subject to compensation under Article 1110. The reason for the damage to Ethyl's business was that its Canadian subsidiary was the sole Canadian importer, processor and distributor of the substance.[26] Ethyl's argument was that BITs containing similar provisions to NAFTA's investment protection provisions, required compensation for 'indirect expropriation' where the effect of regulatory measures is tantamount to direct expropriation. Ethyl claimed that the purpose of Article 1110 was to protect investors' property rights from government infringement by requiring compensation. This supposedly did not negate the government's sovereign rights to legislate over its territory, while at the same time protecting the expectations of investors. Ethyl also drew arguments from the jurisprudence of the GATT dispute resolution panel on Article XX(b) which permits trade restrictions where necessary to protect human, plant or animal life or health. They suggested that Article XX(b) requires governments to choose the least trade restrictive measures, and Canada's action in banning trade in these substances was not necessary to achieve the stated objectives or environmental protection. The Ethyl case did not get the chance to lead to an award as the Canadian government repealed the law after losing before a domestic trade panel on a separate action. Similar arguments were employed in the *S.D. Myers* case[27] which involved a claim for compensation against Canada for losses arising out of a ban on the export of PCBs which the US company claimed to amount to expropriation of its contracts to treat Canadian PCBs. The result of the case was similar to the one in Ethyl, as Canada repealed the law instead of defending the action.

It is widely accepted that the international investment arbitration regime embodied in NAFTA and BITs was intended to limit governments' exercise of public power by giving international capital enforceable protection against certain

24 Baughen (2006), p. 222.
25 38 of *International Legal Materials* 1999, pp. 708-731.
26 Wagner (1999), pp. 491-492, at p. 496.
27 40 ILM 1408 (2001), para. 250.

forms of state intervention in the economy, including protection against expropriation. As a result, market actors have invoked treaty rights aggressively to inhibit public welfare regulation, with at least some success. Even though governments have won most Chapter 11 cases, arbitral panels have taken a broad view of what can count as measures "tantamount to expropriation", effectively restricting governments' ability to regulate corporate activities in what they see as the public interest.[28] Wood and Clarkson argue that despite the fact that investors have actually lost in most cases challenging regulation that reached their conclusion, there is still room for concern in the wake of *Methanex*. While *Methanex* ruled that non-discriminatory regulation of general application does not amount to expropriation unless the regulating government gave the investor a commitment not to regulate, other Chapter 11 tribunals have held that Article 1110 does cover non-discriminatory regulation that might be said to fall within an exercise of a state's so-called police powers.[29]

The Canadian cases discussed above seem to confirm the concerns of commentators. One result of NAFTA's provisions is not so much that governments actually lose cases brought against them by investors, but that governments choose to shy away from regulation when faced with a risk of losing. When the effect of this 'regulatory freeze' is to prevent regulation from coming into place, then the effect is the same as outlawing the legislation on the basis of a hard core, pro-market interpretation of treaty provisions. It is a win for business and investor interests, but is it a win for society, and is it a win for democratically expressed popular choices? The next section examines the existence and evolution in Europe of similar trends to those in North America.

F. Protection of Fundamental Rights

The Charter of Fundamental Rights of the EU (2000/C 364/01), provides in Article 17 on the Right to Property that: Everyone has the right to own, use, dispose of and bequeath his or her lawfully acquired possessions. No one may be deprived of his or her possessions, except in the public interest and in the cases and under the conditions provided for by law, subject to fair compensation being paid in good time for their loss. The use of property may be regulated by law in so far as is necessary for the general interest. The article also specifically mentions that intellectual property shall be protected. This article is based on Article 1 of the Protocol to the ECHR:

> Every natural or legal person is entitled to the peaceful enjoyment of his possessions. No one shall be deprived of his possessions except in the public interest and subject to the conditions provided for by law and by the general principles of international law. The preceding provisions shall not, however, in any way impair the right of a State to enforce such laws as it deems neces-

28 Wood & Clarkson (2009), p. 5.
29 *Pope & Talbot Inc. v. Canada,* interim award, 26 June 2000, p. 32

sary to control the use of property in accordance with the general interest or to secure the payment of taxes or other contributions or penalties.

The rights in Article 1 are fundamental rights, common to all national constitutions of states party to the EU. This has been recognized on numerous occasions by the case-law of the European Court of Justice, initially in the *Liselotte Hauer v. Land Rheinland-Pfalz* judgment.[30] The general principles to be applied in determining whether or not there has been a violation of Article 1 were set out in *James v. United Kingdom*.[31] The first question is whether the deprivation was in the 'public interest'. In deciding this, national authorities enjoy wide discretion. The court argued that the judgment of national authorities will be respected unless it is "manifestly without reasonable foundation". Given the courts' reluctance to challenge the state's view as to what constitutes public interest, it is not surprising there have not been many successful challenges to a measure on this ground. Secondly, it is examined whether a reasonable relationship of proportionality exists between the means employed and the aim sought to be realized, meaning that a 'fair' balance must be struck between the demands of the general interests of the community and the requirements of the protection of the individual's fundamental rights. The balance would not be fair if the applicant had to bear "an individual and excessive burden". The taking of property without payment reasonably related to its value would normally constitute a disproportionate interference.[32] It follows, therefore, that where the applicant has received no compensation, a breach of Article 1 will generally be established. However, this should not be interpreted as requiring the state to compensate for all actions affecting property entitlements. Only claimants arguing for "deprivation of possessions" will be entitled to compensation, and the threshold for this heading is a high one. The measure in question must completely remove any economic value from the affected right. A mere reduction in value will not suffice, as is shown by a series of decisions by the European Court of Human Rights.[33]

There is concern however that the interpretation of fundamental rights could lead to expanded definitions of expropriation giving opportunities to investors to bring new claims. The Openeurope thinktank suggests that Article 17 of the Charter was a result of pressure from the European Landowners Organization and represented a win of landowner interests over environmental campaigners. The problem for environmental groups was centred on the requirement that fair compensation must be paid in good time for loss of property. Such strict requirement for compensation may mean that environmental regulations have to be considered against expensive tradeoffs with claims for compensation by affected owners. For Openeurope, the consequences of this article are not restricted to environmental regulation, but pose a more general threat to government regulatory policy. For example, adoption of the Charter could have meant that the UK Gov-

30 Case 44/79, 1979, ECR 3727.
31 1986, 8 EHRR 123.
32 Baughen (2006), p. 214.
33 *Ibid.*, p. 215.

ernment would have had to pay compensation after it brought Railtrack under public ownership.[34] These being political decisions, it is questionable whether the appropriate forum to debate and resolve them is the ECJ. A similar argument can be made when looking at national constitutions. The following section examines the Greek constitutional position as to the right to compensation for expropriation.

G. The Greek Constitution of 2008

The Greek Constitution, as amended in 2008, offers a very good illustration of governments' attempts to balance the need for protection and respect of private property rights with the government's discretion to guide the national economy in the public interest. The Greek solution offers a pro-market interpretation of the state-market relationship that is remarkable in creating a constitutional duty to compensate takings under almost any circumstances. For example, while the constitution reserves the right to nationalize enterprises (but not to the extent that such nationalization affects the right of foreign investors to repatriate profits, Art. 107), nationalization is possible only for enterprises that are considered monopolies or are of vital importance to the development of sources of national wealth or are primarily intended to offer services to the community as a whole (Art. 106.3). While initially, the constitution proclaims that the use of private rights of property cannot be exercised contrary to the public interest (Art. 17.1) and states that private economic initiative shall not be permitted to develop at the expense of freedom and human dignity, or to the detriment of the national economy (Art. 106.2), it proceeds to state that no state interference with private property is allowed, even in order to protect that public interest, without full compensation (Art. 17.2). Indeed before the payment of such compensation begins (although it does not need to be paid in full in advance in the case of important works of an emergency nature), state interference on the private domain is not even allowed to start (Art. 17.4). Also, every expropriation needs to be compensated within a year and a half, otherwise it is to be reversed, and the amounts paid to the private owners are not subject to tax and charges (Art. 17.4). Compensation is also offered to shareholders of nationalized enterprises (Art. 106.4), and minority shareholders are even offered a buy-out option in cases of part nationalization, where the government attains a controlling state in the enterprise (Art. 06.5).

The only instance where the right to compensation is not recognized is for subterranean works that do not affect the use of the over ground properties (Art. 17.7). However, a very important question is what is considered in Greek law to be a 'taking'? Even the strongest constitutional protections from expropriation will not be particularly restrictive of government activity if very few government actions are actually given the label of expropriation. This reservation ought

34 OpenEurope, 'The EU Charter of Fundamental Rights: Why a Fudge Won't Work', p. 8 (June 2007), available at: <www.openeurope.org.uk/research/charteranalysis.pdf> (last accessed 8 June 2010).

not to worry private owners of properties in Greece. It is important to state first of all that the Greek Constitution seeks to protect property rights in a general sense, as those arising from contractual and real property transactions. This is consistent with the approach of the the ECHR (Protocol 1, Art. 1) discussed above, which guarantees all property rights and interests, not limiting protection to real (land based) rights. Spyropoulos and Fortsakis[35] argue that Greek courts prefer to base protection of wider economic rights on the ECHR, and not Article 17 of the Constitution, but that does not alter the practical effect of protection from expropriation being extended beyond land based rights. According to the aforementioned authors, definitions of property for these purposes include acquired rights (like profits). In this view, the state's right to levy taxation (Art. 78) is limited by the expropriation provisions of Article 17 insofar as excessive taxation will be deemed as equivalent to a taking, and therefore subject to the compensation provisions of the constitution.

At this point in the discussion, the reader may wonder what is contentious about offering compensation for expropriation. Is it not a greater concern that the government reserves for itself the power to expropriate to begin with? In fact the provision for compensation for all takings is a very significant curb on government policy discretion. While it is difficult to draft a constitution in a way that government is directly prohibited from expropriating private property (this in any case is not desirable as in some circumstances expropriation is the only way to safeguard the national interest: think of taking control over the production of pharmaceutical products in case of severe epidemics, or taking control of productive resources during wartime), it is far more beneficial to private owners to acknowledge the legal power to expropriate property, but to make it prohibitively expensive to do so. Costs considerations will ensure that any government will think very hard before proceeding to take property either on an ad hoc or on a sectoral basis. Disincentives to takings are even higher when measures affecting profitability of investments are deemed as equivalent to expropriation. The following section offers some case illustrations of how the rights to compensation are interpreted by courts and tribunals.

H. European Jurisprudence

While in Europe a different institutional framework of course exists in comparison to NAFTA, a careful examination of cases appearing before investment tribunals, the European Court of Justice (ECJ) and the European Court of Human Rights (ECtHR) show that common trends can be identified on both sides of the Atlantic. Defining expropriation in Europe to a great extent depends on what has been historically defined as property. In the *Oscar Chinn* case,[36] market access was held not to amount to property. The United Kingdom argued that the provision of subsidies to a shipping carrier (allowing them to charge nominal freight

35 P. Spyropoulos & T. Fortsakis, 'Constitutional Law in Greece', Kluwer Law, Sakkoulas 2009.
36 *UK v. Belgium*, 1934 PCIJ, ser A/B, no. 63.

charges) amounted to a breach of the general principles of international law (respect for vested rights). The Permanent Court of International Justice (the precursor to the International Court of Justice) , however, rejected this position, reasoning that it is not possible to see in the claimant's original position, which was characterized by the retention of customers and the possibility of making a profit, anything in the nature of a genuine vested right. In contrast, vested contractual rights have been regarded as property which is capable of being expropriated. In *SPP (Middle East) v. Arab Republic of Egypt*,[37] a claim for expropriation succeeded in respect of losses sustained by the claimant under a contract to develop a site near the Pyramids for tourism that the Egyptian government cancelled when it introduced legislation preventing further development on the site.[38]

In the European context there are not many examples of successful actions where investors have complained for non-compensated expropriation with reference to loss of profits, or regulatory measures that adversely affect business prospects. However, as noted above in relation to the effects of growing litigation over NAFTA, the fact that claims have largely been unsuccessful is not a complete answer and should not lead to complacency as to the ability of governments to determine national economic policy for two reasons. First, as Sornarajah noted, arbitrators of investment disputes are a relatively closed group, and ideas and attitudes tend to circulate between panels. Second, there is already evidence of greater acceptance of wider notions of what constitutes expropriation, as the following cases involving Greece show. Greece has been selected as a jurisdiction of interest for the purposes of this examination, because it is an example of a jurisdiction where traditional legal mechanisms for investor protection have been greatly multiplied by pressures of a political and economic nature under the auspices of a pro-investor constitution. In fact, while most claimants in investment disputes involving Greece have failed, they seemed to have failed on jurisdictional or technical grounds unrelated to the merits of the substantive claim. The danger is therefore that while the courts have mostly favoured the government in these cases, they have not done so because they share the government's argument that the type of regulation under discussion does not amount to a taking. In fact, the judges' comments suggest a degree of sympathy for the claimant on the substantive issues. There might be a short time therefore before the legal situation catches up with a decidedly pro-market regulatory environment.

The following cases present efforts by investors to present investment disputes over contractual issues as government takings requiring compensation. The first example of the desire to portray contractual disputes in this light, is the *Rosemarie Marra and Marrecon Enterprises, S.a./cross v. Vaso Papandreou, et al.* case[39] where the claimant sued in the US courts, seeking $1.6 billion in damages from the Greek government for breach of contract and unlawful expropriation of property stemming from the revocation of a license to build and operate a casino. The trigger for the action was the Greek government's decision to issue a resolu-

37 ICSID Award, 32 ILM 933, 1993.
38 Baughen (2006), pp. 223-224.
39 216 F3d 1119, 2000.

tion identifying legal defects in the licensing process, and accordingly revoking the Ministry of Tourism's earlier decision to grant a casino license to Marra and her partners. The Greek government won the case on the basis of a choice of law clause in the contract that gave jurisdiction to the Greek courts to hear the dispute, causing Marra to fall foul of the national statute of limitations.

Another instance of investors complaining about indirect expropriation on a contractual basis, this time brought before the ECtHR can be found in the case of *Agrotexim and others v. Greece*.[40] The ECtHR noted at the outset that the applicant companies had not complained of a violation of the rights vested in them as shareholders of Fix Brewery. Their complaint had been based exclusively on the proposition that the alleged violation of the Brewery's right to the peaceful enjoyment of its possessions by the Greek government had adversely affected their own financial interests because of the resulting fall in the value of their shares. They had considered that the financial losses sustained by the company and the latter's rights had to be regarded as their own, and that they had therefore been victims, albeit indirectly, of the alleged violation. In its report the Court seemed to accept that a violation of a company's rights (protected by Art. 1 of Protocol No. 1, ECHR) resulted in a fall in the value of its shares. Therefore it found that there was automatically an infringement of the shareholders' rights under that article. However, the Court found that such a set of circumstances did not give the shareholders *locus standi*. It was the Brewery, as the corporate entity whose rights had been violated, that could sue to recover any losses. The investors therefore again failed on account of a technicality, despite the fact that the court indicated its agreement with important arguments on the substance of the claimant's case. A third example where the European Court of Human Rights actually found for the applicants in their claim for compensation for a violation of Article 1, Protocol 1 of the ECHR is *Stran Greek Refineries and Stratis Andreadis v. Greece*.[41] According to the applicants' submission, although no property was transferred to the state, the combined effect of legislative actions resulted in a de facto deprivation of their possessions. The loss to Stran arose by the cancellation of a debt set in a final and binding arbitral award. The Court considered this to be an infringement of the right to the peaceful enjoyment of possessions, because interference with the arbitral award constituted an interference with the applicants' property right.

This last case offers a good illustration of competing objectives weighing on the judges minds. The Court did not doubt that it was necessary for the democratic Greek state to terminate a contract concluded by the dictatorship of 1967-1974, which it considered to be prejudicial to its economic interests. The ECtHR recognized according to the case-law of international courts and of arbitral tribunals that any state has a sovereign power to amend or even terminate a contract concluded with private individuals, provided it pays compensation. This conclusion supposedly reflected recognition that the superior interests of the state take precedence over contractual obligations and took into account of the

40 330-A Eur. Ct. H.R. ser. A, 1995.
41 13427/87, 1994, ECHR 48.

need to preserve a fair balance in a contractual relationship. However, the court noted, the unilateral termination of a contract does not extend to an arbitration clause.

According to Subedi[42] the tendency to treat contractual rights as equivalent to property rights in disputes related to takings, blurs the line between public and private law, between treaty obligations and private obligations. An example from the ICSID jurisprudence dealing with the similar issues as those discussed above in the Greek cases involved a US investor complaining that Turkey[43] caused them loss in violation of the US-Turkey BIT by not proceeding with sanctioning the construction of a proposed power station. While the tribunal did not go as far as saying that compensation was payable, it found a violation of the principle of fair and equitable treatment. Perhaps the best illustrations of efforts to stretch the notion of expropriation come from cases where businesses have challenged planning laws as equivalent to takings.[44]

The possibility of claims for protection from taking/expropriation to be used in areas where it was not originally (at least by the drafters of the Greek Constitution) anticipated is high in planning regulations, which stem from a wide range of public decisions including determining sites for public open spaces such as roads and squares, sites for public service buildings or uses, such as schools and hospitals and involving the conservation of natural areas, the protection of archaeological sites and monuments, or the construction of public works.[45] According to Giannakourou and Balla, physical invasions are not critical to the takings issue controversy in Greece. It is land-use restrictions that seem to generate most disputes that reach the courts. Land-use restrictions are regulatory measures and do not 'de jure' constitute acts of taking as title remains with the landowner and are thus a good example of evolving notions of 'indirect' expropriation. The courts in these cases have a challenging task in trying to identify the line between normal regulations, which require landowners to bear the economic consequences, and takings, which may place obligations on public authorities to compensate landowners. Greek planning laws rarely grant compensation rights for reductions in property values due to planning or development control decisions. Judicial practice indicates that the severity of the regulatory measures taken under planning legislation is the key criterion when it comes to deciding whether an indirect expropriation or an equivalent measure has taken place. In cases dating from the 1920s and 1930s courts recognized that the total and permanent prohibition of construction on a parcel of land constitutes a deprivation of property, if pragmatically no other use is possible or economically beneficial. However, according to Giannakourou and Balla, starting in the 1980s, these same courts have been reluctant to find compensable injuries on the property even when regulatory measures eliminated most of the substantial uses of property. Decisions seem to

42 S. Subedi, *International Investment Law: Reconciling Policy and Principle*, Hart Publishing, Oxford 2008, p. 161.

43 *PSEG Global Inc. and Konya v. Republic of Turkey*, 2007 ICSID, final award 19 January 2007

44 G. Giannakourou & E. Balla, 'Planning Regulation, Property Protection and Regulatory Takings in the Greek Planning Law', (2006), Vol. 5 *Washington University Global Studies Law Review* p. 535.

45 The Greek Ombudsman 2005.

suggest that a diminution in land value is not sufficient to establish a 'takings' claim when the affected property has not been rendered valueless. Instead, it seems that all uses or values of a parcel must be eliminated by a planning regulation before the takings claim is viable. It seems therefore that Greek jurisprudence resists the expansion of the definition of compensable expropriation at least in relation to real property.

The European Court of Human Rights has developed a doctrine similar to the Greek one, which looks at the degree of interference with property rights to decide whether a deprivation of property has occurred within the meaning of Article 1 of Protocol No. 1 to the ECHR. In *Papamichalopoulos v. Greece*,[46] where the applicants' land had been taken over by the military, the Court found that, although there was never any formal expropriation, the loss of all ability to dispose of the land in issue entailed sufficiently serious consequences for the applicants property to be considered de facto expropriated in a manner incompatible with their right to the peaceful enjoyment of their possessions. In *Pialopoulos v. Greece*,[47] despite the authorities having imposed a building freeze and having announced plans for the expropriation of the applicants' properties, the Court held that despite there being no reasonable balance struck between the demands of the general interest and the requirements of the protection of the individual's fundamental rights, the effect of these measures did not involve a deprivation of property or a control of the use of property. What can we conclude therefore, as to the expansion of notions of expropriation requiring compensation in European jurisdictions, especially in the case of Greece which we more closely examined? While there has been less success in European Courts in expanding notions of indirect expropriation, the trend identified in NAFTA, of investors seeking to prevent regulatory state action by using treaty rights, or definitions of fundamental rights emanating from the ECHR, is present in the European context, at least in the desire of investors to test the waters by bringing actions. A point of particular interest in this enquiry is whether courts are favouring the states because they are convinced as to their substantive legal argument, or on the basis of technicalities.

I. Conclusion

The protection of private property seen from the point of view of national constitutions presents an incomplete picture of an international situation that is becoming increasingly homogenized. As David Schneiderman has suggested,[48] it is not so much the constraints of national laws on government powers that determine the shape of the state-market relationship currently, but constraints imposed by international legally binding obligations. The centrality of private property rights in modern economic organization results in a necessarily liberal

46 16 Eur. H.R. Rep. 440, para. 45, 1993.

47 33 Eur. H.R. Rep. 977, 2001.

48 D. Schneiderman, *Constitutionalizing Economic Globalization: Investment Rules and Democracy's Promise*, Cambridge University Press, Cambridge 2008.

interpretation of the state–market relationship and leads to an international legal regime increasingly geared towards the protection of investor expectations. As Wood and Clarkson state,[49] investor rights for example in NAFTA and under BITs (and the arbitral decisions applying them) are directly effective and enforceable in the host state. By virtue of international treaties on enforcement of arbitral awards like the New York Convention of 1958, investor-state arbitration awards are enforceable in domestic legal systems as if they were awards of a domestic court. Moreover, they are greatly insulated against challenge in the domestic courts. International investor rights thus take effect in national legal systems without the need for the intervening step of enacting or amending domestic legislation or constitutions. This is precisely why NAFTA Chapter 11 claims that aim to invalidate existing regulatory measures, as we saw earlier, can have effects despite conflicting national provisions.

Consider, for example, the issue of environmental protection that the arguments in this paper have returned to frequently. If national, regional or multilateral obligations for the protection of investments and private property rights inhibit environmental legislation by making it prohibitively expensive to enact, or outright illegal, how can states pursue worthwhile long term objectives that may in the short run violate market expectations? Considering the low levels of success of investor claims involving indirect expropriation, are states justified in being reluctant to regulate? The argument of this paper is that states have valid reasons to feel threatened and there is danger that the desire to expand definitions of expropriation found in NAFTA jurisprudence will spill out to other courts and tribunals. This development, if true, will set yet another barrier to effective government action to fight climate change especially in an economic environment that leaves states with little spare funds to spend in compensating aggrieved polluters. The ultimate question is whether state policy objectives should be dependant on the evolution of jurisprudence which proceeds on a decidedly pro-market treaty based legal framework, or whether the treaties themselves should be amended to safeguard state sovereign rights to regulate activities within their territories.

49 Wood & Clarkson (2009), p. 12.