

# “Necessity,” Investor Rights, and State Sovereignty for NAFTA Investment Arbitration

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## Introduction

In recent years investment arbitrations, especially before the International Centre for Settlement of Investment Disputes (ICSID), have multiplied dramatically. Several of these arbitrations have contended with the legal concept of “necessity.”<sup>1</sup> An ancient and deeply rooted concept in international law, necessity is a defense doctrine that excuses a sovereign

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1. See José. E. Alvarez & Tegan Brink, *Revisiting the Necessity Defense: Continental Casualty v. Argentina*, in *Y.B. ON INT’L INVESTMENT L. & POL’Y* 319, 319-20 (Karl P. Sauvant ed., 2012); Frank Spoorenberg & Jorge E. Viñuales, *Conflicting Decisions in* 46 *CORNELL INT’L L.J.* 143 (2013)

state for violating a preexisting obligation.<sup>2</sup> As early as 1513, Niccolò Machiavelli recognized the doctrine in his famous work *The Prince*, writing: “Hence it is necessary for a prince wishing to hold his own to know how to do wrong, and to make use of it or not according to necessity.”<sup>3</sup> In 1841, U.S. Secretary of State Daniel Webster observed that a state acting in self-defense must have “a necessity of self-defence, instant, overwhelming, leaving no choice of means and no moment for deliberation.”<sup>4</sup> Recently, some countries, like Argentina, have invoked necessity to justify government actions contrary to the terms of their investment treaties, which are subject to ICSID arbitration.<sup>5</sup> In response, tribunals operating under ICSID rules have grappled with necessity, and some tribunals have relied on the analyses of World Trade Organization (WTO) arbitration panels.<sup>6</sup> Moreover, several scholars have argued that the WTO’s necessity analyses *should* inform investment arbitration under ICSID.<sup>7</sup>

Unlike investment tribunals under ICSID and WTO trade panels, the investment tribunals of the North American Free Trade Agreement (NAFTA) have not yet analyzed the necessity defense. In other words, the necessity defense has been analyzed in the investment and trade arbitration contexts, but has been curiously absent from the hybrid context of investment arbitration within a trade agreement. An explanation of why NAFTA investment tribunals have not encountered a necessity problem is beyond the scope of this Note, although one explanation may lie in the traditional view that necessity is a nonviable defense that poses an extremely high threshold for states to overcome.<sup>8</sup> Because adjudicative bodies have tradi-

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*International Arbitration*, 8 LAW & PRAC. INT’L CTS. & TRIBUNALS 91, 91–92 (2009) (discussing conflicting awards in recent ICSID cases in which Argentina was a party).

2. See Sarah F. Hill, *The “Necessity Defense” and the Emerging Arbitral Conflict in Its Application to the U.S.-Argentina Bilateral Investment Treaty*, 13 LAW & BUS. REV. AMS. 547, 551 (2007).

3. NICOLÒ MACHIAVELLI, *THE PRINCE* 22 (W.K. Marriott trans., William Benton 1952) (1513).

4. JAMES CRAWFORD, *THE INTERNATIONAL LAW COMMISSION’S ARTICLES ON STATE RESPONSIBILITY: INTRODUCTION, TEXT, AND COMMENTARIES* 179 (2002) (quoting Daniel Webster in 29 BRIT. & FOREIGN ST. PAPERS 1129 (1857)).

5. See, e.g., *Sempra Energy Int’l v. Arg. Republic*, ICSID Case No. ARB/02/16, Award, ¶ 98 (Sept. 28, 2007), [https://icsid.worldbank.org/ICSID/FrontServlet?requestType=CasesRH&actionVal=showDoc&docId=DC694\\_En&caselD=C8](https://icsid.worldbank.org/ICSID/FrontServlet?requestType=CasesRH&actionVal=showDoc&docId=DC694_En&caselD=C8) [hereinafter *Sempra Award*]; *Enron Corp. & Ponderosa Assets, L.P. v. Arg. Republic*, ICSID Case No. ARB/01/3, Award, ¶ 93 (May 22, 2007), <http://ita.law.uvic.ca/documents/Enron-Award.pdf> [hereinafter *Enron Award*].

6. See, e.g., *Cont’l Cas. Co. v. Arg. Republic*, ICSID Case No. ARB/03/9, Award, ¶ 192 (Sept. 5, 2008), <http://ita.law.uvic.ca/documents/ContinentalCasualtyAward.pdf> [hereinafter *Continental Award*].

7. See, e.g., Alberto Alvarez-Jiménez, *New Approaches to the State of Necessity in Customary International Law: Insights from WTO Law and Foreign Investment Law*, 19 AM. REV. INT’L ARB. 463, 463–64, 487–88 (2008); see also Luke Engan, Note, *In Search of Necessity: Congruence, Proportionality, and the Least-Restrictive Means in Investor-State Dispute Settlement*, 43 GEO. J. INT’L L. 495, 495 (2012); Andrew D. Mitchell & Caroline Henckels, *Variations on a Theme: Comparing the Concept of ‘Necessity’ in International Investment Law and WTO Law*, CHI. J. INT’L L. (forthcoming 2013) (manuscript at 7), available at [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2157250#%23](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2157250#%23).

8. See Alvarez-Jiménez, *supra* note 7, at 465.

tionally held the necessity defense to high standards, states have tended to avoid relying on the defense.

This Note argues that the necessity defense should play a significant role in NAFTA investment arbitration given how analogous treaties treat the defense. Although it has historically been a narrowly formulated and rarely used treaty exception, necessity has become increasingly popular in international disputes.<sup>9</sup> As of 2009, tribunals operating under the arbitration rules of ICSID heard necessity defense claims from Argentina in at least five of the country's forty-eight ICSID proceedings.<sup>10</sup> In addition, WTO panels and the WTO's Appellate Body (AB) have developed a lenient necessity test that makes necessity viable and operative.<sup>11</sup> In both institutions, recent panels have departed from traditional, narrow constructions of necessity and engaged in comprehensive analyses that tend to promote state deference.<sup>12</sup>

Investment arbitral tribunals have not collectively established an official interpretive approach to the necessity defense; however, this Note posits that recent years have seen a trend that effectively establishes a broad and usable necessity defense. Consequently, this Note argues that NAFTA investment tribunals will soon be forced to engage in necessity analysis and must follow similarly broad analyses for three reasons. First, the necessity defense will emerge in NAFTA disputes because of the structural similarities between NAFTA's arbitral provisions and arbitral provisions in bilateral investment treaties (BITs) and the WTO's General Agreement on Tariffs and Trade (GATT). Second, NAFTA has already broadened its approach to similar doctrines, such as the fair and equitable treatment standard (FETS). And third, political pressures affecting ICSID and the WTO will similarly prompt NAFTA tribunals to engage in a broad interpretation of the necessity doctrine.

This Note will proceed in four parts. Part I explains the origins of the necessity doctrine in customary international law and its emergence in international investment treaties. Part II discusses the necessity defense in the context of ICSID arbitration. Part III examines the WTO's broad and balanced necessity test. Finally, Part IV submits that NAFTA tribunals will soon encounter the necessity defense and should interpret it under the broad framework of recent ICSID and WTO decisions.

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9. See Robert D. Sloane, *On the Use and Abuse of Necessity in the Law of State Responsibility*, 106 AM. J. INT'L L. 447, 490 (2012) ("[I]t is noteworthy that the available precedents suggest that necessity has been raised about as frequently in the past three decades as it had been in the preceding three centuries.")

10. See Alec Stone Sweet, *Investor-State Arbitration: Proportionality's New Frontier*, 4 LAW & ETHICS HUM. RTS. 47, 69-70 (2010); William W. Burke-White & Andreas von Staden, *Private Litigation in a Public Law Sphere: The Standard of Review in Investor-State Arbitrations*, 35 YALE J. INT'L L. 283, 283-84 (2010) (citing U.N. Conf. on Trade & Dev., *Latest Developments in Investor-State Dispute Settlement*, IIA Monitor No. 1, at 2, U.N. Doc. UNCTAD/WEB/DIAE/IA/2009/6/Rev1 (2009), available at [http://www.unctad.org/en/docs/webdiaeia20096\\_en.pdf](http://www.unctad.org/en/docs/webdiaeia20096_en.pdf)).

11. See Alvarez-Jiménez, *supra* note 7, at 468.

12. *Id.* at 468, 484.

## I. The Necessity Doctrine in International Investment Treaties

### A. Definition of the Necessity Doctrine

In international law, scholars traditionally discuss necessity within the International Law Commission's (ILC) narrow and rigid formulation.<sup>13</sup> The necessity defense "permit[s] an otherwise illegal act in an emergency not of the perpetrators' making and with severe consequences if the act is not done."<sup>14</sup> Consequently, a successful necessity defense imposes costs on a person or private entity other than the perpetrating state actor. The necessity doctrine justifies this allocation of costs by presuming that the state's actions intended to protect an "essential interest" of higher value than the interest protected in the breached obligation.<sup>15</sup> In so far as the obligations that the state breached protected private entities, a successful necessity defense subordinates this protection in favor of a higher state interest.<sup>16</sup>

Generally, the ILC reflects the customary international law defense of necessity through Article 25 of the 2001 *Draft Articles on the Responsibility of States for Internationally Wrongful Acts (Articles)*.<sup>17</sup> According to Article 25, a state may not present a necessity argument for violating an international obligation unless the state acted in the *only way* it could have to safeguard an "essential interest against a grave and imminent peril" and did not "seriously impair an essential interest" of that state, other states, or the international community.<sup>18</sup> Although Article 25 does not mention harm to private entities, the ILC has recognized through commentary the article's application to private entities.<sup>19</sup> Regardless, necessity is a traditionally narrow exception that "entitles [a] [s]tate to pass [certain] measures . . . for the maintenance of public order or the protection of . . . security interests," within a limited time frame.<sup>20</sup>

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13. See, e.g., Jorge E. Viñuales, *State of Necessity and Peremptory Norms in International Investment Law*, 14 LAW & BUS. REV. AMS. 79, 79-80 (2008) (noting that the International Law Commission articulates necessity in Article 25 of its Articles on State Responsibility). But see Sloane, *supra* note 9, at 452-53, 498 (arguing against the notion that Article 25 reflects the customary international law defense of necessity).

14. JAMES R. FOX, DICTIONARY OF INTERNATIONAL AND COMPARATIVE LAW 226 (3d ed. 2003).

15. Viñuales, *supra* note 13, at 82. Notably, "essential interest" is a vague expression that has incited extensive discourse. *Id.* at 82 n.10

16. See *id.* at 82.

17. See Stone Sweet, *supra* note 10, at 71 (citing Rep. of the Int'l Law Comm'n, *Draft Articles on the Responsibility of States for Internationally Wrongful Acts*, 53rd Sess., Apr. 23-June 1, July 2-Aug. 10, 2001, U.N. Doc. A/56/10).

18. *Id.*; see also Viñuales, *supra* note 13, at 102 (asserting that the term "essential interest" evolves with the development of international law). See generally *id.* (discussing the interaction between the necessity defense and peremptory norms, which are the core content of "essential interests"); Jürgen Kurtz, *Adjudging the Exceptional at International Investment Law: Security, Public Order and Financial Crisis*, 59 INT'L & COMP. L.Q. 325, 338 (2010) (discussing the self-defense origins of the narrowly defined necessity defense under international law).

19. See CRAWFORD, *supra* note 4, at 180-86.

20. Kurtz, *supra* note 18, at 326 (internal quotation marks omitted); see BORZU SABAH, COMPENSATION AND RESTITUTION IN INVESTOR-STATE ARBITRATION: PRINCIPLES AND

## B. Role of the Necessity Doctrine in International Investment Treaties

In addition to necessity's function as a customary international principle, necessity has also appeared in agreements between foreign investors and host states. Within this particular context, necessity functions in at least two capacities. First, the necessity doctrine provides a basis for balancing investor rights with a state actor's interests.<sup>21</sup> Second, necessity provisions in international investment treaties distinguish between "legitimate regulatory choices" and illegitimate "excuses for protectionism."<sup>22</sup>

International investment treaties incorporating the necessity doctrine have modified the doctrine and enabled bodies interpreting the treaties to affect the doctrine's identity.<sup>23</sup> Although necessity has a particular definition in international law, specifically in customary international law as articulated by the ILC, treaties such as BITs, the GATT, and the NAFTA have included provisions that allude to, or at least provide a context for, the necessity doctrine.<sup>24</sup> Indeed, several BITs and the GATT contain provisions that excuse a signatory state from violation of its treaty obligations if it violated these obligations out of "necessity."<sup>25</sup> In addition, although NAFTA Chapter 11 does not have specific "necessity" language, NAFTA Article 1131 on governing law allows NAFTA tribunals to decide an issue under "applicable rules of international law," through which a tribunal can introduce necessity as a rule of international law.<sup>26</sup> Against these treaty frameworks, tribunals under ICSID Rules and the WTO have formulated their own approaches to the necessity doctrine. Although tribunal deci-

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PRACTICE 180 (2011) ("A state of necessity does not annul or terminate the international obligation; rather it provides a justification or excuse for nonperformance while the circumstances in question subsists.") (internal quotation marks and alterations omitted).

21. Burke-White & von Staden, *supra* note 10, at 295.

22. Benn McGrady, *Necessity Exceptions in WTO Law: Retreaded Tyres, Regulatory Purpose and Cumulative Regulatory Measures*, 12 J. INT'L ECON. L. 153, 154 (2008).

23. See, e.g., Treaty Concerning the Encouragement and Reciprocal Protection of Investment, U.S.-Ecuador, art. IX, Aug. 27, 1993, S. TREATY DOC. NO. 103-15 (1997) [hereinafter U.S.-Ecuador BIT]; North American Free Trade Agreement, art. 1131, Dec. 17, 1992, 32 I.L.M. 289 (1993) [hereinafter NAFTA], available at <http://www.nafta-sec-alena.org/en/view.aspx?conID=590>; Treaty Concerning the Reciprocal Encouragement and Protection of Investment, U.S.-Arg., art. XI, Nov. 14, 1991, S. TREATY DOC. NO. 103-2 (1994) [hereinafter U.S.-Argentina BIT]; Treaty Concerning the Reciprocal Encouragement and Protection of Investments, U.S.-Turk., art. X, Dec. 3, 1985, S. TREATY DOC. 99-19 (1990) [hereinafter U.S.-Turkey BIT]; General Agreement on Tariffs and Trade arts. XX, XXI, Oct. 30, 1947, 61 Stat. A-11, 55 U.N.T.S. 194 [hereinafter GATT];

24. See, e.g., NAFTA, *supra* note 23, art. 1131; U.S.-Argentina BIT, *supra* note 23, art. XI; GATT, *supra* note 23, art. XX.

25. Compare U.S.-Ecuador BIT, *supra* note 23, art. IX(1) ("This Treaty shall not preclude the application by either Party of measures necessary for the maintenance of public order, the fulfillment of its obligations with respect to the maintenance or restoration of international peace or security, or the protection of its own essential security interests."), with U.S.-Argentina BIT, *supra* note 23, art. XI (similar language), and U.S.-Turkey BIT, *supra* note 23, art. X(1) (similar language). In addition, GATT Articles XX and XXI allow a contracting party to take measures necessary "to protect public morals," "to protect human, animal or plant life or health," "to secure compliance with laws or regulations [consistent with the GATT]," or "necessary for the protection of its essential security interests . . ." GATT, *supra* note 23, arts. XX(1)(a)-(d), XXI(b).

26. NAFTA, *supra* note 23, art. 1131(1).

sions have been confusing and conflicting, tribunals are decidedly driving the necessity doctrine toward a broad, or at least balanced, framework.<sup>27</sup>

## II. Necessity in BITs

BITs, like all investment treaties, are highly compatible vehicles for the necessity doctrine. BITs are popular treaties between states that enable investors to operate smoothly in a foreign state; at the end of 2008 there were 2,676 BITs in existence.<sup>28</sup> As instruments that protect foreign investors and “mitigate the risks” of operating in particular countries, BITs also take into consideration state interests by including clauses that incorporate language of necessity.<sup>29</sup> In a practical sense, necessity clauses offer state actors the possibility of avoiding the negative consequences of breaching obligations in certain circumstances.<sup>30</sup> Accordingly, necessity clauses have been included in most BITs.<sup>31</sup>

Recently, Argentina has cited the necessity provision in Article XI of the U.S.-Argentina BIT in investment arbitration disputes, and ICSID tribunals have chosen to treat the provision broadly. Article XI provides that:

This Treaty shall not preclude the application by either Party of measures necessary for the maintenance of public order, the fulfillment of its obligations with respect to the maintenance or restoration of international peace or security, or the Protection of its own essential security interests.<sup>32</sup>

After Argentina’s monumental economic crash in 2001, United States foreign investors initiated arbitration against Argentina based on the country’s failure to honor its promises to foreign investors under the U.S.-Argentina BIT.<sup>33</sup> Argentina’s actions in response to its economic crisis changed the business environment on which investors had relied, but considering the magnitude of the Argentine economic crisis, Argentina justified its actions as being necessary.<sup>34</sup> However, tribunals operating under the ICSID Rules

27. See Alvarez-Jiménez, *supra* note 7, at 468, 482; Stone Sweet, *supra* note 10, at 76.

28. See, e.g., U.S.-Argentina BIT, *supra* note 23, pmb. (asserting that the U.S.-Argentina BIT seeks to “stimulate the flow of private capital” and “maintain a stable framework for investment”); Burke-White & von Staden, *supra* note 10, at 284.

29. See Kurtz, *supra* note 18, at 331. Compare U.S.-Ecuador BIT, *supra* note 23, art. IX(1) (“This Treaty shall not preclude the application by either Party of measures necessary for the maintenance of public order, the fulfillment of its obligations with respect to the maintenance or restoration of international peace or security, or the protection of its own essential security interests.”), with U.S.-Argentina BIT, *supra* note 23, art. XI (similar language), and U.S.-Turkey BIT, *supra* note 23, art. X(1) (similar language).

30. For example, under the U.S.-Argentina BIT necessity clauses, states are excused from their obligations towards investors when there is a necessity to preserve “public order,” “international peace or security,” or the state’s own “essential security interests.” See U.S.-Argentina BIT, *supra* note 23, art. XI.

31. Stone Sweet, *supra* note 10, at 70; see also William W. Burke-White & Andreas von Staden, *Investment Protection in Extraordinary Times: The Interpretation and Application of Non-Precluded Measures Provisions in Bilateral Investment Treaties*, 48 VA. J. INT’L L. 307, 311, 313 (2008).

32. U.S.-Argentina BIT, *supra* note 23, art. XI.

33. Stone Sweet, *supra* note 10, at 69.

34. *Id.* at 69-70.

initially rejected Argentina's necessity defense in efforts to protect investors.<sup>35</sup> Specifically, the tribunals emphasized the traditional construction of necessity, as articulated by the ILC, and applied a narrow approach to the necessity defense. The tribunals' rejection of necessity in these cases arguably caused state actors to react negatively. For example, the rejection gave rise to threats on the legitimacy of investment treaties. In response, tribunals have recently expanded their analyses of the necessity doctrine and accepted Argentina's necessity defense.<sup>36</sup>

### A. The Argentina Crisis

The economic crisis that sparked the proliferation of foreign investor claims against Argentina began between 1999 and 2002.<sup>37</sup> Argentina signed onto the ICSID Convention on May 21, 1991,<sup>38</sup> and by 1994 had sold 90% of its holdings in state-run companies and utilities to foreign investors.<sup>39</sup> Before the crash, Argentina pegged its currency to the American dollar, fixing its exchange rate to that of the United States.<sup>40</sup> Pegging the Argentine currency to the American dollar enabled investors to know what exchange rate to expect for their transactions and caused investors to expect dollars in return for their investments. In addition, Argentina promised to allow capital to move out of Argentina freely and enacted laws that promoted investor participation and negotiation in fixing utility rates.<sup>41</sup> However, between 1999 and 2002, Argentina took measures that violated the promises the country had made to its foreign investors under the BIT.<sup>42</sup> Argentina's economy crashed due to an enormous budget deficit, skyrocketing foreign debt, and a payments crisis.<sup>43</sup> In response, Argentina implemented economic policy initiatives, but these initiatives failed and dramatically cut foreign investments. Argentina's economic crisis intensified, causing riots, a plague of unemployment and poverty, and the appointment of five presidents within ten days between December 2001 and January 2002, which marked a surge of political instability.<sup>44</sup>

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35. *Id.* at 71.

36. *Id.* at 63, 76 (arguing that legitimacy concerns prompted the use of the more comprehensive approach of proportionality).

37. *Id.* at 69.

38. INT'L CTR. FOR SETTLEMENT INV. DISPUTES, LIST OF CONTRACTING STATES AND OTHER SIGNATORIES OF THE CONVENTION (AS OF JULY 25, 2012) (2012), available at <https://icsid.worldbank.org/ICSID/FrontServlet?requestType=ICSIDDocRH&actionVal=ShowDocu ment&language=English>.

39. *Id.*

40. See, e.g., Continental Award, *supra* note 6, ¶ 104 (citing a 2004 statement by the International Monetary Fund); Kurtz, *supra* note 18, at 330.

41. Stone Sweet, *supra* note 10, at 69.

42. *Id.* Argentina's measures included drastic budget cuts, renegotiation of foreign debt, currency devaluations, limits on bank account withdrawals and "Pesification," which forced the conversion of dollar deposits into pesos. *Id.*

43. *Id.*

44. *Id.*; *Las semanas de los cinco presidentes* [The Weeks of the Five Presidents], BBC MUNDO (Dec. 31, 2001), [http://news.bbc.co.uk/hi/spanish/latin\\_america/newsid\\_1735000/1735611.stm](http://news.bbc.co.uk/hi/spanish/latin_america/newsid_1735000/1735611.stm). On December 20, 2001, Argentine President Fernando de la Rúa resigned due to the social riots, *id.*, without a vice president, as Vice President Carlos

Foreign investors reacted to the harm that the Argentine economic collapse caused and sent out requests for arbitration at ICSID. The investors claimed that Argentina had violated investment treaties and had treated foreign investors below the “fair and equitable treatment” standard (FETS) of the BITs.<sup>45</sup> In response, the Argentine republic pled the necessity defense. Thus far, eight rulings under the ICSID Rules—five arbitral awards and three Annulment Committee rulings—have assessed whether the measures that Argentina adopted during its meltdown were necessary to preserve public order and security.<sup>46</sup>

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Alvarez had previously resigned in October 2000 following disagreements with the President over a corruption scandal. James Reynolds, *Argentina's Vice-President Quits*, BBC NEWS (Oct. 7, 2000), <http://news.bbc.co.uk/2/hi/americas/960418.stm>. The next day, the Argentine congress assigned a provisional presidency to Senate leader Ramón Puerta. *The Weeks of the Five Presidents*, *supra*. Then, Congress elected Adolfo Rodríguez Saá as interim president, who was sworn in on December 23. *Id.* After just seven days, Mr. Rodríguez Saá resigned on December 30, claiming that he had lost the support of his political party. *Id.*; *Argentina President Resigns*, CNN (Dec. 30, 2001), [http://articles.cnn.com/2001-12-30/world/argentina.resignation\\_1\\_ramon-puerta-adolfo-rodrieguez-saa-argentina?\\_s=PM:WORLD](http://articles.cnn.com/2001-12-30/world/argentina.resignation_1_ramon-puerta-adolfo-rodriguez-saa-argentina?_s=PM:WORLD). Following Mr. Rodríguez Saá's resignation, Congress once again assigned the presidency to Senate leader Ramón Puerta, but Mr. Puerta resigned soon after, and on December 31, Congress temporarily assigned the presidency to the Chamber of Deputies leader Eduardo Camaño. *The Weeks of the Five Presidents*, *supra*. Finally, on January 1, 2002, Congress elected Senator Eduardo Duhalde to serve as president until December 2003. *Id.*; *see also*, *New Man Takes Helm in Argentina*, BBC NEWS (Jan. 2, 2002), <http://news.bbc.co.uk/2/hi/americas/1737562.stm> (reporting that Congress elected Mr. Eduardo Duhalde after a special session); *Argentina's New President Sworn In*, BBC NEWS (Jan. 2, 2002), <http://news.bbc.co.uk/2/hi/americas/1738175.stm> (reporting that Mr. Eduardo Duhalde was sworn into the presidency as Argentina's fifth leader in two weeks).

45. *See, e.g.*, *Sempra Award*, *supra* note 5, ¶ 95; *LG&E Energy Corp. v. Arg. Republic*, ICSID Case No. ARB/02/1, Decision on Liability, ¶¶ 72, 105 (Oct. 3, 2006) [hereinafter *LG&E Decision on Liability*], [https://icsid.worldbank.org/ICSID/FrontServlet?requestType=CasesRH&actionVal=showDoc&docId=DC627\\_En&caseId=C208](https://icsid.worldbank.org/ICSID/FrontServlet?requestType=CasesRH&actionVal=showDoc&docId=DC627_En&caseId=C208).

46. *Stone Sweet*, *supra* note 10, at 69–70. The eight rulings are: *Enron Corp. & Ponderosa Assets, L.P. v. Arg. Republic*, ICSID Case No. ARB/01/3, Decision on Application for Annulment, ¶¶ 406–08, 414–15 (July 30, 2010) [hereinafter *Enron Annulment*], <http://italaw.com/documents/EnronAnnulmentDecision.pdf> (annulling partially the Enron award, rejecting the tribunal's decision that Argentina could not rely on necessity or Article XI of the U.S.-Argentina BIT, but not finding that Argentina ultimately succeeded on its necessity claim); *Sempra Energy Int'l v. Arg. Republic*, ICSID Case No. ARB/02/16, Decision on Application for Annulment, ¶¶ 208–09, 219, 223 (June 29, 2010) [hereinafter *Sempra Annulment*], [https://icsid.worldbank.org/ICSID/FrontServlet?requestType=CasesRH&actionVal=showDoc&docId=DC1550\\_En&caseId=C8](https://icsid.worldbank.org/ICSID/FrontServlet?requestType=CasesRH&actionVal=showDoc&docId=DC1550_En&caseId=C8) (annulling the Sempra award on the ground of manifest excess of powers because the tribunal had relied on Article 25 of the ILC's Articles over Article XI of the U.S.-Argentina BIT); *Continental Award*, *supra* note 6, ¶ 304 (determining that Argentina could avail itself of the necessity defense under Article XI of the U.S.-Argentina BIT); *Sempra Award*, *supra* note 5, ¶¶ 355, 363, 390 (rejecting Argentina's invocation of necessity on several grounds); *CMS Gas Transmission Co. v. Arg. Republic*, ICSID Case No. ARB/01/8, Decision of the Ad Hoc Committee on the Application for Annulment of the Argentine Republic, ¶¶ 145–46, 150, 158 (Sept. 25, 2007) [hereinafter *CMS Annulment*], [https://icsid.worldbank.org/ICSID/FrontServlet?requestType=CasesRH&actionVal=showDoc&docId=DC687\\_En&caseId=C4](https://icsid.worldbank.org/ICSID/FrontServlet?requestType=CasesRH&actionVal=showDoc&docId=DC687_En&caseId=C4) (finding errors of law in the CMS tribunal's decision on necessity but refusing to annul the tribunal's decision); *Enron Award*, *supra* note 5, ¶ 321 (finding against Argentina on the matter of necessity); *LG&E Decision on Liability*, *supra* note 45, ¶ 267(d) (determining that Argentina was in a state of necessity for a



Despite similar factual backgrounds, the eight ICSID rulings reached inconsistent determinations on whether Argentina's actions in the early 2000s were necessary.<sup>47</sup> In three early cases, *CMS Gas Transmission*, *Enron*, and *Sempra*, ICSID tribunals rejected Argentina's necessity defense.<sup>48</sup> However, in *LG&E* and *Continental Casualty*, the tribunals accepted the defense.<sup>49</sup> The decisions of the annulment committees are more complex. The *CMS* annulment committee found that the *CMS* tribunal had made a manifest error of law in rejecting Argentina's necessity defense,<sup>50</sup> but the committee nevertheless refused to annul the original *CMS* award.<sup>51</sup> In contrast, the *Sempra* annulment committee annulled the *Sempra* award due to the tribunal's reliance on Article 25 of the ILC's *Articles* over Article XI of the U.S.-Argentina BIT, which the committee considered a "manifest excess of powers."<sup>52</sup> Finally, the *Enron* annulment committee partially annulled the *Enron* award, finding error in the tribunal's necessity analysis.<sup>53</sup> To varying degrees, each ICSID tribunal and annulment committee involved in the Argentina cases assessed necessity in terms of both customary international law and treaty law.<sup>54</sup>

## B. Conflicting Attitudes Towards Necessity in ICSID Proceedings

Initially, ICSID tribunals in the Argentina cases relied extensively on customary international law as reflected in Article 25 of the ILC's *Articles*.<sup>55</sup> Notably, the tribunals that relied on Article 25 were among the first to ever confront a dispute under Article XI of the U.S.-Argentina BIT.<sup>56</sup> In the early cases of *CMS*, *Enron*, and *Sempra*, the tribunals relied extensively on customary law as articulated in Article 25 of the ILC's *Articles*. Under customary law, the necessity defense required that Argentina show *inter alia* that its actions "were the *only* ones available to the government to respond to the crisis."<sup>57</sup> Although the tribunals did not always explain their approach, they were strict in reviewing Argentina's economic responses and ruled in favor of investors' rights.<sup>58</sup> For example, in *CMS*

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specified time period); *CMS Transmission Co. v. Arg. Republic*, ICSID Case No. ARB/01/8, Award, ¶¶ 4, 331 (May 12, 2005), [https://icsid.worldbank.org/ICSID/FrontServlet?requestType=CasesRH&actionVal=showDoc&docId=DC504\\_En&caseId=C4](https://icsid.worldbank.org/ICSID/FrontServlet?requestType=CasesRH&actionVal=showDoc&docId=DC504_En&caseId=C4) (determining that Argentina's acts in suspending a tariff adjustment formula for gas transportation applicable to a *CMS* investment did not meet the requirements of necessity).

47. See Viñuales, *supra* note 13, at 81 (noting the dissimilarities between two awards despite similar factual backgrounds in the Argentine economic crisis).

48. *Burke-White & von Staden*, *supra* note 10, at 297-98.

49. *Id.* at 298-99.

50. *CMS Annulment*, *supra* note 46, ¶¶ 145-46.

51. *Id.* at ¶¶ 150, 158.

52. *Sempra Annulment*, *supra* note 46, at ¶¶ 208-09, 219, 223.

53. *Enron Annulment*, *supra* note 46, at ¶¶ 406-08, 414-15. See generally Engan, *supra* note 7, at 496 (citing to the *Sempra* and *Enron* Annulments).

54. See, e.g., Viñuales, *supra* note 13, at 84.

55. See Kurtz, *supra* note 18, at 327, 335.

56. *Stone Sweet*, *supra* note 10, at 75.

57. *Burke-White & von Staden*, *supra* note 10, at 297 (emphasis added).

58. *Id.* (observing that the tribunals "applied an extraordinarily strict standard"); *Stone Sweet*, *supra* note 10, at 75. *Stone Sweet* proposes that among the reasons why the

the tribunal initiated its analysis of necessity under the strict terms of customary international law and subsequently applied its analysis to Article XI of the U.S.-Argentina BIT.<sup>59</sup> Although the tribunal did not give reasons for its application of customary law or explain its understanding of the economic crash, the tribunal held Argentina's actions to the ILC's stringent standards and refused to accept a necessity defense.<sup>60</sup>

In subsequent proceedings, however, ICSID tribunals increasingly relied on the necessity language in the BITs, relied less on the customary international law definition reflected in Article 25 of the ILC's *Articles*, and broadened its approach to necessity. In *LG&E*, the ICSID tribunal first focused on Article XI of the U.S.-Argentina BIT and referred to Article 25 of the ILC's *Articles* to a limited extent.<sup>61</sup> Without the initial influence of the customary definition of necessity, the tribunal decided necessity on the basis of Article XI and clearly identified the doctrine's trade-off between competing interests.<sup>62</sup> In *Continental Casualty*, the tribunal also decided in favor of Argentina based on an extensive and broad necessity analysis.

In *Continental Casualty*, the tribunal accepted Argentina's necessity defense under Article XI of the BIT under a rationale that looked broadly at "public order" and "essential security interests" in Article XI.<sup>63</sup> In the *Continental Casualty* arbitration, the tribunal decided the issue of whether Article XI was applicable to the dispute between Continental Casualty, an employment compensation insurance provider, and Argentina.<sup>64</sup> In its award, the tribunal reasoned that actions falling under Article XI included those "to preserve or to restore civil peace and the normal life of society (especially of a democratic society such [as] that of Argentina) . . . even when due to significant economic and social difficulties . . ." <sup>65</sup> The tribunal reasoned that Argentina's particular situation showed how "[a] severe economic crisis may . . . qualify under Article XI as affecting an essential security interest."<sup>66</sup> Finally, the tribunal referred to the process of weighing and balancing in a WTO case, *EC-Tyres*.<sup>67</sup> The tribunal ultimately determined that Argentina was entitled to the necessity defense after assessing the challenged measures, the contribution of the measure to its

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first ICSID tribunals ruled as they did are: (1) "these tribunals saw their central mission as the protection of investors' rights"; (2) "a necessity clause such as that contained in Article XI, had not previously been pleaded before an ICSID panel"; and (3) the adoption of a proportional analysis would have placed arbitrators "in the position of the balancing judge as perhaps something quite different than arbitrators traditionally conceived." *Id.*

59. Viñuales, *supra* note 13, at 84.

60. *Id.* at 81, 84. Notably, the ad hoc committee criticized the tribunal's use of Article 25 of the ILC's *Articles* in the case of a U.S.-Argentina BIT Article XI dispute. *Id.* at 85.

61. *Id.* at 86.

62. *Id.* at 85-87, 101 (noting that the *LG&E* tribunal identified necessity's inherent value trade-off).

63. Stone Sweet, *supra* note 10, at 70, 74.

64. *Id.* at 73.

65. *Id.* at 74.

66. *Id.* (quoting the Continental Award, *supra* note 6, ¶ 174).

67. *Id.* at 74-75 (quoting the Continental Award, *supra* note 6, ¶ 194).

ends, and the measure's impact on international commerce.<sup>68</sup>

### C. Assessing ICSID Tribunals' Response to Necessity

As their decisions bind only the parties that submit themselves to a dispute, ICSID tribunals are not bound by *stare decisis* when rendering awards.<sup>69</sup> Although the tribunals hearing the Argentina cases are showing more responsiveness to state interests by accepting Argentina's necessity defense, because of the lack of *stare decisis* recent decisions cannot individually assure that tribunals will continue to accept Argentina's necessity defense. Indeed, after *LG&E* some refused to "read too much into" the decision.<sup>70</sup> Nevertheless, commentators such as Alec Stone Sweet, William W. Burke-White, and Andreas von Staden have designed coherent frameworks for tribunals proceeding under the ICSID rules to adopt in hearing necessity cases.<sup>71</sup>

The respective frameworks of Stone Sweet, Burke-White, and von Staden suggest that necessity will not fall to the wayside as an extremely rigid and unusable exception, but will instead emerge as a powerful defense for sovereign states. Stone Sweet presents a proportionality framework under which arbitrators "deploy means-ends testing to evaluate the impact of the State's measures on the investment . . ." <sup>72</sup> In the necessity phase of proportionality, Stone Sweet posits that arbitrators will engage in "a least-restrictive means test."<sup>73</sup> This test asks whether a respondent state "[took] measures that infringed more on investors' rights than was necessary for the State to achieve its purpose[.]"<sup>74</sup> *Continental Casualty*, according to Stone Sweet, presented proportionality's "grand entrance."<sup>75</sup>

On the other hand, Burke-White and von Staden present a necessity framework based on the European Court of Human Rights' (ECtHR) broader "margin of appreciation" balancing approach.<sup>76</sup> The "margin of appreciation" analysis in the European Human Rights Treaty can be applied to investment issues, as both human rights and investment issues share situations in which rights are in conflict.<sup>77</sup> Burke-White and von

68. *Id.*

69. *Id.* at 60.

70. Hill, *supra* note 2, at 562 n.120 (quoting Todd Weiler, *ICSID Grants Argentina's Necessity Plea*, GLOBAL ARB. REV. (2006) ("My impression is that the [LG&E] decision is a prudent, political one. I would not read too much into it, at least with respect to the substantive necessity defence.")).

71. See generally Stone Sweet, *supra* note 10; Burke-White & von Staden, *supra* note 10.

72. Stone Sweet, *supra* note 10, at 63.

73. *Id.* at 70.

74. *Id.*

75. *Id.* at 76. *But cf.* Burke-White & von Staden, *supra* note 10, at 344 (refusing to accept that the *Continental Casualty* award "mark[ed] an explicit turn toward proportionality analysis . . .").

76. See generally Burke-White & von Staden, *supra* note 10 (describing the framework); Stone Sweet, *supra* note 10, at 68 n.65 (acknowledging Burke-White and von Staden's framework).

77. See Burke-White & von Staden, *supra* note 10, at 342.

Staden's analysis is premised on the view that although standards of review were originally developed from private law commercial arbitration, investor-state arbitration today significantly operates in a public law context.<sup>78</sup> Customary international law, as reflected in Article 25 of the ILC's *Articles*, precludes the public law elements from affecting a decision on necessity, and as a result Burke-White and von Staden recommend the "margin of appreciation" standard.<sup>79</sup> The "margin of appreciation" is a concept that the European Court of Human Rights first announced in 1976 in *Handyside v. United Kingdom*.<sup>80</sup> Under this framework, arbitral tribunals determine how much "breadth of deference" to give to state action based on the nature of the rights in conflict and ECtHR jurisprudence, which, like investment cases, balances private rights with social and economic policies.<sup>81</sup> Although the proportionality and "margin of appreciation" frameworks have different analytical steps, these frameworks admittedly lead to the same result: a more successful necessity defense.<sup>82</sup>

### III. WTO Necessity & Investment Arbitration

In the WTO context, necessity is expressed in at least two exception provisions that require a state's measure to be "necessary" to avoid a violation of treaty obligations.<sup>83</sup> Although WTO provisions do not apply to investment protection, these provisions are relevant because ICSID awards, such as *Continental Casualty*, have cited to the WTO's reasoning. Moreover, the necessity analysis under WTO law provides an example of a balance between market-based rights and regulatory government goals. Unlike ICSID tribunals, WTO panels and the AB, the adjudicating bodies of the WTO, already apply a consistent and sophisticated framework to determine necessity. WTO panels and the AB examine the necessity exception through a test that assesses the link between the respondent state's measure and its policy objective.<sup>84</sup> Although the WTO has developed a more consistent framework for necessity than ICSID tribunals, the WTO's analysis is similarly flexible, "balanced[,] and deferential."<sup>85</sup>

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78. *Id.* at 287-88.

79. *See id.* at 298 (asserting that customary international law "preclude[s] public law elements" from affecting a decision on necessity).

80. *Handyside v. United Kingdom*, 24 Eur. Ct. H.R. (ser. A) ¶ 48 (1976), available at <http://www.echr.coe.int/ECHR/EN/hudoc> (accepting the margin of appreciation in the human rights context of freedom of expression).

81. Burke-White & von Staden, *supra* note 10, at 342 (internal quotations omitted).

82. *Id.* at 339-40.

83. Kurtz, *supra* note 18, at 337, 339 (citing GATT, *supra* note 23, arts. XX, XXI(b)-(c)) (internal quotations omitted).

84. Nicolas F. Diebold, *The Morals and Order Exceptions in WTO Law: Balancing the Toothless Tiger and the Undermining Mole*, 11 J. INT'L ECON. L. 43, 68 (2007).

85. *See* Michael Ming Du, *The Rise of National Regulatory Autonomy in the GATT/WTO Regime*, 14 J. INT'L ECON. L. 639, 665 (2011).

### A. GATT Article XX General Exceptions and Article XXI Security Exceptions

The first formulation of necessity in WTO law appears in Article XX of the GATT, among the treaty's "General Exceptions" provisions.<sup>86</sup> Article XX sets forth a list of ten exceptions to WTO trade obligations, and three of these exceptions invoke necessity. Specifically, provisions XX(a), XX(b), and XX(d) provide exceptions for measures that are necessary (1) "to protect public morals"; (2) "to protect human, animal or plant life or health"; or (3) to comply with certain laws or regulations.<sup>87</sup>

WTO law's second formulation of necessity appears in Article XXI(b) and (c) of the GATT.<sup>88</sup> In these provisions the WTO presents a formulation of necessity significantly similar to the formulation in several bilateral investment treaties, including the U.S.-Argentina BIT. Article XXI(b) allows a state to take "any action which it considers necessary for the protection of its essential security interests."<sup>89</sup> Further, Article XXI(c) allows a state to take "any action in pursuance of its obligations . . . for the maintenance of international peace and security."<sup>90</sup>

### B. WTO's Traditional Approach to Necessity

Early in GATT/WTO's history, some argue, panels exhibited trade-biased interpretations of GATT provisions equivalent to ICSID's early pro-investor bias in Argentina cases.<sup>91</sup> Indeed, Article XX's own structure juxtaposes trade *obligations* against regulation *exceptions*, which implies an inherent structural bias towards trade over legitimate state regulation.<sup>92</sup> Some argue that early GATT tribunals interpreted Article XX exceptions narrowly and thus never found these exceptions to apply to any case.<sup>93</sup> In determining whether a state measure was "necessary," WTO panels would traditionally assess whether the measure constituted the "least trade restrictive" means, but could potentially do so without considering the respondent state's prerogative to issue regulations.<sup>94</sup> Further, WTO panels were prone to proposing alternatives arbitrarily, failing to take practical approaches to regulation, and disregarding the impracticality of proposed alternatives.<sup>95</sup>

### C. Current WTO Approach to Necessity

Current WTO panels and the AB interpret the necessity exception using a weighing and balancing approach based on discrete factors and an

86. GATT, *supra* note 23, art. XX.

87. *Id.*

88. *Id.* art. XXI(b)-(c).

89. *Id.* art. XXI(b).

90. *Id.* art. XXI(c).

91. *See, e.g.,* Du, *supra* note 85, at 664-65.

92. *Id.*

93. *See id.* at 665.

94. *Id.* (internal quotations omitted).

95. *Id.*

alternative-measure analysis.<sup>96</sup> WTO panels now consider a comprehensive set of relevant variables in analyzing necessity under Article XX.<sup>97</sup> In addition, the AB considers alternative measures in light of a respondent state's particular situation, taking into consideration political, cultural, and economic issues.<sup>98</sup> Further, the AB in *Brazil–Retreaded Tyres* determined that the “fundamental principle” in the analysis of a necessary measure is “the right that WTO Members have to determine the level of protection that they consider appropriate in a given context.”<sup>99</sup>

As a preliminary matter, the WTO has a broad understanding of the concept of necessity. Necessity in WTO law can refer to a range of situations and operate in a variety of settings.<sup>100</sup> The WTO has developed this approach through its decisions in *Korea–Beef*, *EC–Asbestos*, *Dominican Republic–Cigarettes*, *US–Gambling*, and *Brazil–Retreaded Tyres*.<sup>101</sup> In *Korea–Beef*, the AB held that a necessary measure could have any of several meanings, ranging from “indispensable” to “making a contribution to” a certain policy goal.<sup>102</sup> Notably, *Continental Casualty* cited to this section of the decision, indicating that the WTO's necessity approach is consistent with the decisions of recent tribunals operating under ICSID.<sup>103</sup> The *Korea–Beef* panel ultimately decided that “necessary” was “significantly closer to the pole of ‘indispensable’ than to the opposite pole of simply ‘making a contribution to’” the policy goal.<sup>104</sup> In contrast, the AB in *Brazil–Retreaded Tyres* moved along the spectrum and required that a necessary measure make a “material” contribution.<sup>105</sup> Besides reflecting the value that the AB places on the regulatory goal involved, the distinct results of *Korea–Beef* and *Brazil–Retreaded Tyres* noticeably indicate the AB's flexible approach to necessary measures.

In addition to adopting a flexible understanding of necessity, the WTO has established an elaborate framework to determine whether a challenged regulatory measure is necessary. The WTO's framework consists of a three-factor analysis, followed by a determination of whether alternative measures are reasonably available. The AB delineated this three-factor

96. Note, however, that some have expressed that “under Article XX of the GATT 1994, although the new case law has loosened the rigidity of the sub-paragraphs, there are legitimate concerns that some of the rigidities in the old GATT case law may be read into the chapeau.” Du, *supra* note 85, at 674.

97. See *id.* at 665–66.

98. See *id.*

99. Appellate Body Report, *Brazil–Measures Affecting Imports of Retreaded Tyres*, ¶ 210, WT/DS332/AB/R (Dec. 3, 2007) [hereinafter *Brazil–Retreaded Tyres*].

100. See *id.*; Du, *supra* note 85, at 666; see, e.g., Daniel C. Etsy, *Governing at the Trade–Environment Interface*, in *THE WTO AND GLOBAL GOVERNANCE: FUTURE DIRECTIONS*, 115, 122 (Gary P. Sampson ed., 2008) (addressing WTO necessity in the context of environmental concerns).

101. Du, *supra* note 85, at 666.

102. *Id.*

103. See *Continental Award*, *supra* note 6, ¶ 193.

104. Appellate Body Report, *Korea–Measures Affecting Imports of Fresh, Chilled and Frozen Beef*, ¶ 161, WT/DS161/AB/R (Dec. 11, 2000) [hereinafter *Korea–Beef*].

105. *Brazil–Retreaded Tyres*, *supra* note 99, ¶ 210.

analysis in *Korea–Beef*.<sup>106</sup> Under the analysis, the WTO first looks at the challenged state measure and the “relative importance of the . . . interests” that it furthers.<sup>107</sup> Second, the WTO considers the contribution that the challenged measure makes towards its goal.<sup>108</sup> Third, the WTO assesses the challenged measure’s “restrictive effects on international commerce.”<sup>109</sup>

After this three-factor analysis, the WTO looks at alternative measures.<sup>110</sup> Specifically, the WTO determines whether an alternative measure is “reasonably available,” which requires the WTO to determine whether the alternative measure “contributes to the realization of the end pursued.”<sup>111</sup> The significance of an alternative measure is that a state that claims a necessity exception under Article XX may fail if the WTO finds an alternative measure that is “less restrictive” on trade and reasonably available to policymakers.<sup>112</sup>

Although an alternative measure is adverse to a successful necessity argument, existing WTO procedural rules limit the availability of alternative measures, which ultimately contributes to a broad approach to necessity. Indeed, while the respondent state bears the burden of proof to make a prima facie case of necessity, the party opposing the respondent state bears the burden of raising a challenging alternative measure.<sup>113</sup> In addition, the WTO can determine that any given regulatory measure, instead of being an alternative, complements a challenged measure.<sup>114</sup> By removing at least some measures that tribunals could qualify as alternatives, WTO tribunals are more likely to consider challenged measures necessary.<sup>115</sup> In sum, the current practice of the WTO regarding necessity involves a broad approach that respects state regulatory autonomy.

#### D. Responses to WTO Necessity

While the WTO’s established approach to necessity largely confirms national regulatory autonomy, some concerns plague its effectiveness and perhaps its durability. First, Michael Du characterizes the WTO AB’s weighing and balancing test as a “*de facto* value-based approach.”<sup>116</sup> In other words, if “the value at stake is high,” such as a threat to health and

106. *Korea–Beef*, *supra* note 104, ¶¶ 162–63.

107. *Id.* ¶ 162.

108. *Id.* ¶ 163.

109. *Id.* ¶ 163.

110. See Appellate Body Report, *European Communities–Measures Affecting Asbestos and Asbestos-Containing Products*, ¶¶ 171–72, WT/DS135/AB/R (Mar. 12, 2001).

111. *Id.* (quoting *Korea–Beef*, *supra* note 104, ¶¶ 165–66).

112. *Id.*

113. See Du, *supra* note 85, at 667 (citing Appellate Body Report, *United States–Measures Affecting the Cross-Border Supply of Gambling and Betting Services*, ¶¶ 309–11, WT/DS285/AB/R (Apr. 7, 2005)).

114. See McGrady, *supra* note 22, at 153–54.

115. See Du, *supra* note 85, at 667; McGrady, *supra* note 22, at 154.

116. Du, *supra* note 85, at 667 (citing Michael M. Du, *Autonomy in Setting Appropriate Level of Protection under the WTO Law: Reality or Rhetoric?*, 13 J. INT’L ECON. L. 1077, 1100–01 (2010)).

safety or the environment, then the WTO will consider a pertinent measure necessary.<sup>117</sup> However, if the regulatory objective is less important, such as prevention of commercial fraud, then the WTO may overrule a necessity objection.<sup>118</sup> In other words, the AB gives less deference to member states when the value of the regulatory end is low. This approach is somewhat problematic because it implies that the WTO ranks the importance of regulatory goals even though it is not necessarily an institution best suited for such a role.<sup>119</sup>

Second, there is also a concern with the WTO panel's characterization of respondent states' regulatory goals. A panel's characterization of a regulatory goal can affect the outcome of a case by, for example, affecting the availability of alternative measures.<sup>120</sup> Nevertheless, the liberties that the WTO panel took when describing and discussing Brazil's regulatory goal in *Brazil—Retreaded Tyres* suggest that the WTO may not apply a consistent approach to characterization.<sup>121</sup> Benn McGrady, a Georgetown professor who regularly advises non-governmental organizations on issues of trade, adds that "it is more worrying that panels rarely engage in detailed analysis of a member's regulatory goal."<sup>122</sup> However, the concerns of arbitrariness in goal characterization and improper goal ranking may be overemphasized. For one, WTO members have voluntarily entered into a treaty in which they explicitly agreed to submit disputes for ultimate determination by a third-party tribunal. Moreover, a certain degree of variation in the approaches that the WTO uses when dealing with trade disputes is inevitable; the facts of any given case almost always vary from those of the last, as do considerations of trade against particular measures. Finally, the safeguards for state regulations that the elaborate WTO approach to necessity has instituted should sufficiently protect state regulatory interests.

#### IV. Necessity and NAFTA

NAFTA Chapter 11 does not contain language explicitly creating a necessity defense. However, such a defense may be introduced under international principles as allowed under NAFTA Article 1131. Interestingly, while several claims that investors brought under NAFTA Chapter 11 have asserted member state violations such as expropriation and discriminatory treatment, no NAFTA member has claimed necessity as a defense.<sup>123</sup> As

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117. *Id.*

118. *Id.* at 667-68.

119. *Id.*

120. See McGrady, *supra* note 22, at 165, 168.

121. See *id.* at 153, 172-73 (noting that the inconsistency in the panels' approach to necessity may, justifiably, seem arbitrary to observers).

122. *Id.* at 154.

123. See, e.g., *Gallo v. Gov't of Can.*, Statement of Defence, ¶¶ 202, 262 (Sept. 15, 2008) (NAFTA Ch. 11 Arb. Trib.), <http://www.naftaclaims.com/Disputes/Canada/Gallo/Gallo-Canada-Defence-15-09-08.pdf>; *Merrill & Ring Forestry L.P. v. Gov't of Can.*, Statement of Defence, ¶¶ 6, 8-10, 113 (Oct. 30, 2007) (NAFTA Ch. 11 Arb. Trib.), [http://www.naftaclaims.com/Disputes/Canada/Merrill/Merrill\\_Ring-Canada-Defence.pdf](http://www.naftaclaims.com/Disputes/Canada/Merrill/Merrill_Ring-Canada-Defence.pdf); *Ethyl Corp. v. Gov't of Can.*, Statement of Defence, ¶¶ 12, 103 (Nov. 27, 1997) (NAFTA



such, Chapter 11 tribunals have yet to face a necessity defense. This trend may change, however, as the proportional treatment between investor protection and state sovereignty that ICSID and the WTO have adopted prompts NAFTA members to assert necessity as a defense.<sup>124</sup> Although NAFTA Chapter 11 does not contain necessity language, a party may introduce a necessity defense under international principles as allowed under NAFTA Article 1131. For example, a necessity defense may be appropriate in an expropriation claim, such as the recent claim that the U.S. company AbitibiBowater filed against Canada.<sup>125</sup> With the potential appearance of necessity in future NAFTA proceedings, NAFTA will face the challenge of devising its own necessity analysis framework. Given the clear advantages of a consistent and sturdy framework, NAFTA tribunals should adopt a framework that exhibits the proportional and balancing approaches of recent ICSID panels and the WTO.

While NAFTA tribunals have not yet encountered a necessity claim, NAFTA has both investment provisions and a governing law provision that allow for the exception.<sup>126</sup> In 1993, Mexico, Canada, and the United States executed NAFTA to eliminate customs and tariffs in their trade relations.<sup>127</sup> NAFTA Chapter 11 contains investment provisions that list obligations that signatory parties must accord its investors, which include non-discriminatory treatment and non-expropriation.<sup>128</sup> In addition, Chapter 11 may incorporate a necessity exception through its governing law provision at Article 1131. While not technically a BIT, Chapter 11 shares the comprehensive structure and central elements of bilateral and multilateral investment agreements.<sup>129</sup> Thus, Chapter 11 is popularly described as a

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Ch. 11 Arb. Trib.), <http://www.naftaclaims.com/Disputes/Canada/EthylCorp/EthylCorpStatementOfDefense.pdf>; see also *Metalclad Corp. v. United Mex. States*, ICSID Case No. ARB(AF)/97/1, Award, ¶ 1 (Aug. 30, 2000), [https://icsid.worldbank.org/ICSID/FrontServlet?requestType=CasesRH&actionVal=showDoc&docId=DC542\\_En&caseId=C155](https://icsid.worldbank.org/ICSID/FrontServlet?requestType=CasesRH&actionVal=showDoc&docId=DC542_En&caseId=C155) (addressing challenge by Metalclad that Mexican regulations were “tantamount to . . . expropriation” of their investment in connection to Metalclad’s hazardous waste facility in Mexico).

124. See, e.g., Ian Laird, *The Emergency Exception and the State of Necessity*, in INVESTMENT TREATY LAW: CURRENT ISSUES II 235, 238 (Federico Ortino et al. eds., 2007) (advocating the use of necessity as a tool for the Canadian government in its dispute before NAFTA regarding the softwood lumber industry).

125. See generally Charmaine Noronha, *AbitibiBowater Files NAFTA Expropriation Claim*, BLOOMBERG BUSINESSWEEK (Feb. 25, 2010, 11:29 AM), <http://www.businessweek.com/ap/financialnews/D9E3AANO1.htm>.

126. NAFTA, *supra* note 23, arts. 1105 (concerning a minimum standard of treatment), 1110 (concerning expropriation and compensation), 1131 (concerning governing law).

127. See generally *id.*

128. *Id.* arts. 1105, 1110.

129. See Howard Mann & Konrad von Moltke, *Protecting Investor Rights and the Public Good: Assessing NAFTA’s Chapter 11* 18 (Int’l Institute for Sustainable Dev. 2002, Background Paper to ILSD Tri-National Policy Workshops), available at <http://www.iisd.org/publications/pub.aspx?id=573>; see also Jessica S. Wiltse, Comment, *An Investor-State Dispute Mechanism in the Free Trade Area of the Americas: Lessons from NAFTA Chapter Eleven*, 51 BUFF. L. REV. 1145, 1155 n.50 (2003).

“trilateral investment treaty contained within a free-trade arrangement.”<sup>130</sup>

#### A. Structural Statutory Similarities

In addition to essentially being a trilateral investment treaty, NAFTA Chapter 11 shares the statutory structure of BITs and the GATT regarding certain obligations. This suggests that NAFTA should follow a similarly broad framework in its own necessity analysis. Like Article XI of the U.S.-Argentina BIT and Article XXI of the GATT, Chapter 11 sets up obligations within a normative structure. Through an application of necessity under Article 1131, NAFTA tribunals may, like former ICSID and WTO tribunals, excuse a violation of these rights. Given the structural similarities between the necessity exceptions discussed and NAFTA’s investment provisions, a proportional and balanced treatment of the necessity exception in NAFTA investment arbitration arguably “fits” NAFTA’s structure of rights.<sup>131</sup>

NAFTA Article 1110, on expropriation and compensation, states that NAFTA members may not

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 (“expropriation”) except: (a) for a *public purpose*; (b) on a non-discriminatory basis; (c) in accordance with due process of law and Article 1105(1); and (d) on payment of compensation . . . .<sup>132</sup>

Similarly, Article XI of the U.S.-Argentina BIT allows for “the application by either [p]arty of measures necessary for the maintenance of *public order*, . . . restoration of international peace or security, or the [p]rotection of its own essential security interests.”<sup>133</sup> Thus, NAFTA and the U.S.-Argentina BIT both contain provisions allowing for regulatory goals involving a public purpose. Although NAFTA does not contain the necessity language found in Article XI, a state may introduce a necessity defense through Article 1131, which states: “A Tribunal established under this Section shall decide the issues in dispute in accordance with this Agreement and applicable rules of international law.”<sup>134</sup> A party may construe necessity as an applicable rule of international law,<sup>135</sup> allowing a NAFTA tribunal thereafter to apply the necessity defense.

130. Wiltse, *supra* note 129, at 1169; *see also id.* at 1155 (describing NAFTA Chapter 11 as “a trilateral investment treaty grafted onto an arrangement which is otherwise largely directed at establishing liberalization and fairness in the trade of goods and services.”) (quoting David R. Haigh, Q.C., *Chapter 11- Private Party vs. Governments, Investor-State Dispute Settlement: Frankenstein or Safety Valve?*, 26 CAN.-U.S. L.J. 115, 129 (2000)).

131. *See* Stone Sweet, *supra* note 10, at 76 (internal quotations omitted).

132. NAFTA, *supra* note 23, art. 1110 (emphasis added).

133. U.S.-Argentina BIT, *supra* note 23, art. XI (emphasis added).

134. NAFTA, *supra* note 23, art. 1131(1) (emphasis added).

135. *See* Sloane, *supra* note 9, at 469. Article 1131 does not define “applicable rules of international law,” but necessity is usually considered a general principle of law, *id.*, and a principle of international customary law through Article 25 of the ILC’s *Articles*, even if some scholars contest the accuracy of Article 25’s articulation of necessity as customary law, *see, e.g., id.* at 451-52.

Similarly, GATT's Articles XX and XXI directly and indirectly share structural elements with NAFTA Chapter 11 provisions. GATT's Article XX(a) allows for measures "necessary to protect *public morals*," which is consistent with Article 1110's "public purposes."<sup>136</sup> Further, GATT's Article XXI(b) shares an exception for "essential security interests" with Article XI of the U.S.-Argentina BIT.<sup>137</sup> Likewise, XXI(c) adds that nothing shall be construed to prevent a state "from taking any action in pursuance of its obligations . . . for the maintenance of *international peace and security*."<sup>138</sup> NAFTA Chapter 11 does not mention security interests directly, but security interests may arguably fit within "public purposes." As mentioned above, NAFTA can incorporate the necessity doctrine in these provisions through Article 1131.

#### B. NAFTA's Fair and Equitable Treatment Framework

Despite the fact that NAFTA has not directly addressed a necessity defense under Chapter 11, it has already employed somewhat proportional and broad frameworks within other doctrines. In *S.D. Myers v. Canada* in 2000, an Ohio corporation that processed PCB waste sued Canada under NAFTA Article 1105, among other provisions.<sup>139</sup> Article 1105 states that each NAFTA party shall accord "fair and equitable treatment and full protection and security."<sup>140</sup> Finding in favor of the Canadian government, a NAFTA tribunal assessed Article 1105's fair and equitable treatment in a manner that took into consideration both investor rights and state regulatory autonomy. Specifically, the tribunal stated that when assessing a violation of fair and equitable treatment, the "determination must be made in the light of the high measure of deference that international law generally extends to the right of domestic authorities to regulate matters within their own borders."<sup>141</sup> Thus, NAFTA tribunals have already considered the kind of broad analytical approach that such tribunals should take when encountering a future necessity defense.

#### C. International Investment Pressures in NAFTA

Finally, NAFTA tribunals should adopt a broad framework when encountering a necessity claim because NAFTA reasonably faces political pressures regarding legitimacy similar to those affecting ICSID and the WTO. While the impetus for ICSID's recent acceptance of Argentina's necessity is uncertain, ICSID's analysis arguably shifted due to political pressure from Argentina and other Latin American countries.<sup>142</sup> Signifi-

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136. GATT, *supra* note 23, art. XX (emphasis added).

137. *Id.* art. XXI(b).

138. *Id.* art. XXI(c) (emphasis added).

139. *S.D. Myers, Inc. v. Gov't of Can., Partial Award*, ¶ 135 (Nov. 13, 2000) (NAFTA arbitration under UNCITRAL rules) [hereinafter *S.D. Myers*], <http://www.italaw.com/sites/default/files/case-documents/ita0747.pdf>.

140. NAFTA, *supra* note 23, art. 1105(1).

141. *S.D. Myers*, *supra* note 139, ¶ 263.

142. See Burke-White & von Staden, *supra* note 10, at 285 (observing a threat to the "perceived legitimacy of investor-state arbitration"); see also Erlend M. Leonhardsen,

cantly, ICSID's legitimacy in Latin America is fragile given that 45% of all defendants in pending cases are Latin American countries.<sup>143</sup> Likewise, some commentators have argued that states questioned the WTO's legitimacy as an international trade court after concluding that GATT/WTO jurisprudence leans too much towards private trade.<sup>144</sup> Indeed, supporters of Canadian state actions have criticized the WTO for limiting Canada's ability to handle issues like climate change.<sup>145</sup>

NAFTA also faces legitimacy concerns that should prompt future tribunals reviewing a necessity claim to adopt an analytical framework that balances investor and state regulatory interests. Although NAFTA is steadily moving towards transparency,<sup>146</sup> many generally question its legitimacy due to its lack of transparency.<sup>147</sup> The U.S. federal government has also questioned whether NAFTA claims pose threats to democracy and the country's regulatory powers.<sup>148</sup> Others view NAFTA as "an assault on state sovereignty" and as an instrument that "chills the ability of democratic governments to protect public health and the environment . . . ."<sup>149</sup> Moreover, state legislatures in the United States have expressed concern that "investor-state dispute mechanisms threaten state authority and sovereignty."<sup>150</sup> Considering the pressures that NAFTA currently faces from state sovereigns, NAFTA should adopt a broad analytical framework in considering necessity.

## Conclusion

Given the lack of investment arbitrations to demonstrate how NAFTA treats the necessity doctrine, the doctrine's application in NAFTA is empirically unknown. Nevertheless, ICSID and WTO tribunals' interpretation of the necessity defense has been increasingly broad and balanced between investor rights and state sovereignty. Due to its increased acceptance among ICSID tribunals and the WTO, the necessity defense will likely reach NAFTA tribunals. Accordingly, similarities in statutory language,

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*Looking for Legitimacy: Exploring Proportionality Analysis in Investment Treaty Arbitration*, 3 J. INT'L DISP. SETTLEMENT 95, 107-08 (2012).

143. Stone Sweet, *supra* note 10, at 68.

144. See, e.g., Du, *supra* note 85, at 641, 674.

145. See Andrew Green, *Climate Change, Regulatory Policy and the WTO: How Constraining are Trade Rules?*, 8 J. INT'L ECON. L. 143, 143 (2005).

146. Gary B. Born & Ethan G. Shenkman, *Confidentiality and Transparency in Commercial and Investor-State International Arbitration*, in THE FUTURE OF INVESTMENT ARBITRATION 5, 31 (Catherine A. Rogers & Roger P. Alford eds., 2009).

147. See, e.g., Mann & Moltke, *supra* note 129, at 19-20 (citing *Methanex v. United States*, Decision of the Tribunal on Petitions from Third Persons to Intervene as Amici Curiae, ¶ 49 (Jan. 15, 2001), [http://italaw.com/sites/default/files/case-documents/ita0517\\_0.pdf](http://italaw.com/sites/default/files/case-documents/ita0517_0.pdf)) (NAFTA arbitration under UNCITRAL rules).

148. Leonhardsen, *supra* note 142, at 110.

149. Wiltse, *supra* note 129, at 1183 (citing Ray C. Jones, *NAFTA Chapter 11 Investor-to-State Dispute Resolution: A Shield to Be Embraced or a Sword to be Feared?*, 2002 BYU L. REV. 527, 545 (2002)).

150. *Id.* at 1193 (citing Tripp Baltz, *State Lawmakers Worry About Sovereignty in Dispute Resolution Language of TPA Bill*, 19 INT'L TRADE REP. (BNA) 32, 1385 (2002)).

current treatment of other doctrines, and political pressures should prompt NAFTA tribunals to incorporate and interpret the necessity doctrine in a broad fashion similar to ICSID tribunals and the WTO.

