NUTCRACKER OR SLEDGEHAMMER? A TWAIL PERSPECTIVE ON PROPORTIONALITY TEST IN INDIRECT EXPROPRIATION

Rohan Karan Mehta[*]

Proportionality or trying to find the balance seems to have become ubiquitous; be it domestic law or international law, all over the globe, the adjudicatory authorities' primary imperative seems to be to find the balance. Through this paper, I challenge the prevalence of proportionality in International Investment Law. I shall employ TWAIL to problematise this application of proportionality. International Investment Law often pits developing nation-states against powerful corporations from the First World. This inherent inequality of International Investment Law has been subject to multiple criticisms from TWAIL scholars. Building on this rich tradition, I argue that the usage of proportionality in International Investment Law produces inequitable outcomes for the Third World. To build this critique, I shall focus on the locus classicus of Te´cnicas Medioambientales Tecmed S.A. v The United Mexican States *that introduced proportionality, and will analyse the subsequent cases that have used proportionality. What, then, can be a possible solution or a doctrine that the tribunals can rely upon? I suggest that perhaps going back to the roots of International Investment Law and adopting the doctrine of sole effects would lead to more equitable outcomes as compared to proportionality.*

TABLE OF CONTENTS

I. INTRODUCTION....28
II. TWAIL: THE OTHER SIDE OF INTERNATIONAL LAW....30
III. EXPROPRIATION- PROPORTIONALITY PREDICAMENT....32
A. TECMED V MEXICO....32
1. Proportionality and ECtHR Jurisprudence....33
2. Methodological Flaws and Legitimate Policy....38
B. CASES POST *TECMED*....40
IV. BACK TO BASICS: SOLE EFFECTS STRIKES BACK....42

[*] Student, National Law School of India University, Bangalore. The author would like to thank Rishabh Shivani, Anushka Kanabar, and Aumita Mishra for their invaluable support and discussions, which greatly contributed to the development of this paper.

V. CONCLUSION 45

I. INTRODUCTION

'A sledgehammer should not be used to crack a nut'.[1]

Through the above remark, Lord Diplock encapsulates the utility of the proportionality test. The often labeled 'precise and delicate' proportionality test has been used to crack a plethora of cases in constitutional and administrative law.[2] But now it finds itself in a previously uncharted domain: International Investment Law ('IIL').[3] Though proportionality is used in multiple areas of IIL, through this paper I focus on its application in indirect expropriation.[4]

The core concept of expropriation is reasonably clear: it is a governmental taking of property for which compensation is required.[5] The difference between a direct expropriation and an indirect expropriation is the question of whether the legal title of the owner is affected by the Government measure.[6] Indirect expropriation removes the investor's ability to use their investment in a meaningful way while retaining the title. A feature of indirect expropriation is the State's denial of expropriation and refusal to provide compensation.[7]

The underlying issue here then becomes distinguishing between indirect expropriation and a regulatory action of the host state.[8] This distinction is important because regulatory actions do not give rise to claims of compensation,

---

[1] *R v Goldstein* (1983) 1 WLR 151, 157.

[2] *Anuradha Bhasin v State of Jammu & Kashmir* (2020) 3 SCC 637; *Association for Democratic Reforms v Union of India* 2024 INSC 113.

[3] Over the last decade, both scholars and tribunals have increasingly resorted to principle of proportionality. See Alex Stone Sweet, 'Investor-State Arbitration: Proportionality's New Frontier' (2010) 4 Law & Ethics of Human Rights 47; Benedict Kingsbury and Stephan Schill, 'Investor-State Arbitration as Governance: Fair and Equitable Treatment, Proportionality and the Emerging Global Administrative Law' in Albert Jan van den Berg (ed), *50 Years of the New York Convention* (Series No 14, Kluwer Law International 2009).

[4] See Rudolf Dolzer, Ursula Kriebaum and Christoph Schreuer, *Principles of International Investment Law* (3rd edn, OUP 2022).

[5] Campbell McLachlan, Laurence Shore and Matthew Weiniger, *International Investment Arbitration: Substantive Principles* (OUP 2017).

[6] Dolzer, Kriebaum and Schreuer (n 4) 146.

[7] ibid 153.

[8] See August Reinisch, 'Expropriation' in Peter Muchlinski, Federico Ortino and Christoph Schreuer (eds), *The Oxford Handbook of International Investment Law* (OUP 2008) 753. For who is host state, see Collins Erin, 'Obligations of the Host State' (*Jus Mundi*, 2 April 2025) <https://jusmundi.com/en/document/publication/en-obligations-of-the-host-state> accessed 24 November 2024.

whereas indirect expropriation does. To elaborate, States have an inherent right to regulate themselves, and not every interference or regulatory action amounts to expropriation requiring compensation.[9]

Tribunals have espoused divergent perspectives to solve this dilemma.[10] Proportionality is the latest one to be thought of as the panacea to this issue.[11] The reason proportionality is starting to be used more correlates with the perceived failure of other doctrines.[12]

Much ink has been spilled on the above issue.[13] Overwhelmingly, the proportionality test has been favoured.[14] Though some scholars have critiqued proportionality, there has not been a Third World Approach to International

[9] For further explanation, see Ursula Kriebaum, 'Regulatory Takings: Balancing the Interests of the Investor and the State' (2007) 8 Journal of World Investment & Trade 717.

[10] For sole effects, see *Starrett Housing Corp v Government of the Islamic Republic of Iran* (1983) 4 Iran–US CTR 122, 156*; Saipem SpA v People's Republic of Bangladesh*, Case No ARB/05/7. For police powers, see *Too v Greater Modern Insurance Associates & the USA*, 23 Iran-US CTR*; Marvin Feldman v United Mexican States*, Final Award (2002) 18 ICSID Rev-FILJ 488 (2003).

[11] *Tecnicas Medioambientales Tecmed, SA v Mexico*, ICSID Case No. ARB (AF)/00/2, Award (29 May 2003) 43 International Legal Materials 133; *Azurix Corp v Argentine Republic*, ICSID ARB/01/12, Award (14 July 2006).

[12] Other doctrines include sole effects, police powers etc. All of them are criticised because they focus on a particular aspect, like effect or purpose of the regulation. Whereas proportionality is thought to be balancing multiple interests.

[13] Jaunius Gumbis and Rapolas Kasparavicius, 'State's Right to Regulate: What Constitutes a Compensable Expropriation in Investor-State Arbitration' (2017) 5 Yearbook on International Arbitration 153; Mojtaba Dani and Afshin Akhtar-Khavari, 'The Uncertainty of Legal Doctrine in Indirect Expropriation Cases and the Legitimacy Problems of Investment Arbitration' (2016) 22 Widener Law Review 1.

[14] Giovanni Zarra, 'Right to Regulate, Margin of Appreciation and Proportionality: Current Status in Investment Arbitration in Light of Philip Morris v. Uruguay' (2017) 14 Brazilian Journal of International Law 95; Mojtaba Dani and Afshin Akhtar-Khavari (n 13); Kiratipong Naewmalee, 'Indirect Expropriation: Property Rights Protection, State Sovereignty to Regulate and the General Principles of Law' (PhD thesis, University of Wollongong 2017); Stephen Olynyk, 'A Balanced Approach to Distinguishing between Legitimate Regulation and Indirect Expropriation in Investor-State Arbitration' (2012) 15 International Trade & Business Law Review 254; Prabhash Ranjan, 'Police Powers, Indirect Expropriation in International Investment Law, and Article 31(3)(c) of the VCLT: A Critique of Philip Morris v. Uruguay' (2019) 9 Asian Journal of International Law 98; Jeffrey Waincymer, 'Investor-State Arbitration: Finding the Elusive Balance between Investor Protection and State Police Powers' (2014) 17 International Trade & Business Law Review 261; Omer Erkut Bulut, 'Drawing Boundaries of Police Powers Doctrine: A Balanced Framework for Investors and States' (2022) 13 Journal of International Dispute Settlement 583.

Law ('TWAIL') appraisal of this issue.[15] I attempt to fill this gap by using TWAIL to evaluate the proportionality test.

I argue that the current application of the proportionality test produces inequitable outcomes for the third world. Then I argue that a more equitable solution would be the utilisation of the sole effects doctrine. Therefore, in Part II, I elaborate on how I employ TWAIL. Subsequently, in Part III, I use TWAIL to evaluate the *locus classicus* of *Te´cnicas Medioambientales Tecmed S.A. v The United Mexican States* ('Tecmed') that introduced proportionality and analyse the subsequent cases that have used proportionality.[16] Through this part, I highlight the flaws of this doctrine. Finally, in Part IV, I argue for the invocation of the sole effects doctrine by demonstrating how it resolves the flaws of proportionality and then demonstrate its practical application through a concise hypothetical.

II. TWAIL: THE OTHER SIDE OF INTERNATIONAL LAW

TWAIL has famously been described as a network of third-world scholars using their unique perspective to critique the history, structure, and process of evolution of international law.[17] The third world here refers to a geographical as well as a political space.[18] There are further generations within the TWAIL scholarship. However, due to the limited scope of this paper, it aims to contribute towards the general TWAIL scholarship.[19]

But, despite the above amorphous description, the aims and purposes of TWAIL lend a semblance of consistency in its usage. Broadly, TWAIL aims to

---

[15] For an introduction to TWAIL, see BS Chimni, 'Third World Approaches to International Law: A Manifesto' (2006) 8 International Community Law Review 3. For other approaches of critiques, see Prabhash Ranjan, 'Using the Public Law Concept of Proportionality to Balance Investment Protection with Regulation in International Investment Law: A Critical Appraisal' (2014) 3 Cambridge Journal of International and Comparative Law 853; Caroline Henckels, 'Indirect Expropriation and the Right to Regulate: Revisiting Proportionality Analysis and the Standard of Review in Investor-State Arbitration' (2012) 15 Journal of International Economic Law 223.

[16] ICSID Case No. ARB(AF)/00/2. ('*Tecmed*').

[17] BS Chimni, *International Law and World Order: A Critique of Contemporary Approaches* (CUP 2017) 10-30.

[18] ibid. Third world united by common ties against the capitalist regimes that continue to produce colonial or neo-colonial ideologies.

[19] ibid. The primary reason being that the differences themselves are contested. Therefore, it is hard to conclusively come to common ground or a demarcating line.

deconstruct the international law norms that perpetuate racialised ideas and instead propose more equitable alternatives.[20]

This perspective becomes especially important considering the international investment law where due to the nature to proceedings itself, States are pitted against corporations. More specifically even within IIL, expropriation represents the crudest iteration of this inherent inequality. For instance during the Argentinian financial crisis, the state was forced fight multiple expropriation claims before ICSID tribunals which further exacerbated its financial issues.[21] However, symbolically, let us visualise the imagery of a third world country battling is financial issues, being questioned in an adversarial setting about the ambit of its sovereign right to regulate through expropriation cases by massive conglomerates from the Global North. This visual is enough as Chimni argues to cast doubt on the entire IIL regime.[22]

All this becomes even more problematic when proportionality is thought of as a panacea that would bring balance to the table when the question of expropriation arises.[23] Therefore, given this context, TWAIL becomes particularly important to highlight the inherent biases within the balancing framework that is proportionality which seems to gloss over the inherent inequity and paper over the fault lines within the IIL regime.

Generally, this is carried out by a critical evaluation of narratives through their global historicisation.[24] An example of this approach would be Chimni's analysis of customary international law by historicising it.[25] Therefore, in a similar vein, I attempt to carry out my TWAIL analysis by historicising the usage of the proportionality test in IIL cases dealing with expropriation.

Historicisation of the jurisprudence is important and relevant in this case. The reason is that as I will demonstrate in later parts, proportionality is not a concept that has always been prevalent in IIL. To contextualise, IIL lies at the

---

[20] Makau Mutua and Antony Anghie, 'Proceedings of the Annual Meeting (American Society of International Law)' (April 5-8, 2000) 94 ASIL Proc 31-40.

[21] ICSID Case No ARB/02/1; ICSID Case No ARB/03/9; ICSID Case No ARB/03/15. Also see Charity L Goodman, 'Uncharted Waters: Financial Crisis and Enforcement of ICSID Awards in Argentina' (2007) 28 University of Pennsylvania Journal of International Law 449.

[22] BS Chimni, 'Customary International Law: A Third World Perspective' (2018) 112 American Journal of International Law 1.

[23] Reinisch, 'Expropriation' (n 8) 773.

[24] Obiora Chinedu Okafor, 'Critical Third World Approaches to International Law (TWAIL): Theory, Methodology, or Both?' (2008) 10 International Community Law Review 371.

[25] Chimni (n 22).

intersection of international private and public law. Whereas traditionally proportionality as a remedy was common only in domestic administrative courts, even then usually when adjudicating upon rights.

Therefore, assessing the roots of how this balancing act came to the fore in IIL is essential for the primary reason of it being vital to uncover the hidden agenda, if any behind the reliance of this supposedly foreign concept in a then new and emerging field of law. By appreciating the historical context behind the usage of proportionality in IIL, we can ascertain whether it is politically charged or tends to favor certain outcomes/states over others. Consequently, only through historicisation can we understand the million dollars 'why' question: why does proportionality seem to lead to certain outcomes in IIL.

III. EXPROPRIATION- PROPORTIONALITY PREDICAMENT

In this section, I first critique the *Tecmed* usage of proportionality due to it being the most relied-upon conception of proportionality in IIL.[26] Then I trace and analyse cases that have relied on proportionality since *Tecmed*. Through this, I highlight that proportionality produces inequitable outcomes for the third world.

A. TECMED V MEXICO

In *Tecmed*, a subsidiary of a Spanish company acquired land, buildings, and other assets to operate a hazardous waste landfill in Mexico. Subsequently, the Mexican Government denied the license renewal for the operation of the landfill to the subsidiary. The company alleged indirect expropriation, whereas Mexico argued that this was done for environmental interests and public health.[27]

According to the tribunal, the main question was whether the State's actions were *proportional* to the concerns of public interest and the protection of foreign investments.[28] For this, there must be a legitimate aim.[29] Additionally, there must be a relationship of proportionality between the burden on the foreign investor and the aim in question.[30] Interestingly the tribunal found the

[26] *Tecmed* (n 11).
[27] See generally Mexico-Spain BIT (1995) art 5.
[28] *Tecmed* (n 11) 122.
[29] ibid. Citing *James v UK*, App No 8793/79 (ECtHR, 21 February 1986).
[30] ibid.

basis for these principles in the jurisprudence of the European Court of Human Rights ('ECtHR').[31]

In *Tecmed*, the tribunal first determined the aim for regulation, which was a hostile reception from the local community.[32] Then, it evaluated the legitimacy of the aim and concluded that this cannot amount to an aim that denies investors rights.[33] Thus, as an investor was affected disproportionately, there was indirect expropriation.[34]

I critique this conception of proportionality on two grounds. Firstly, on its reliance on the ECtHR jurisprudence and secondly, on the discretion granted to tribunals to make value judgments.

1. Proportionality and ECtHR Jurisprudence

To clarify, here I do not deal with the overall history of the proportionality test, but rather its origin in IIL from the ECtHR. *First,* I argue that the proportionality test is not a rule of customary law or even a general principle recognised by all nations.[35] It is often a tendency of the 'Developed World' to universalise their principles, a TWAIL perspective would therefore entail questioning such claims. The phrasing of Article 38(1) of the International Court of Justice statute mentions that international custom and general principles recognised by civilised nations should be applied when disputes are before the Court. The phrase 'civilised nations' in this article when evaluated from a TWAIL lens underscores the inherent inequality.

As Akehurst argues custom is constituted by two elements, the objective one of 'a general practice', and the subjective one 'accepted as law' (opinio juris). The main evidence of customary law is in the actual practice of states. This can be ascertained from published material, newspaper reports of actions taken by states, statements made by government spokesmen to Parliament, to the press,

[31] ibid.
[32] ibid 127-38.
[33] ibid 133-148.
[34] ibid 148-149.
[35] Chinese constitutional-administrative law appears not to recognise a principle of proportionality at all. See Han Xiuli, 'The Principle of Proportionality in Tecmed v. Mexico' (2007) 6 Chinese Journal of International Law 635, 650. Similarly, there is a lack of evidence that proportionality is recognised as a rule of customary international law. See Rosalyn Higgins, *Problems and Process: International Law and How We Use It* (OUP 1994) 236.

at international conferences and meetings of international organisations; and also, state laws and judicial decisions.[36]

On the other hand, the ambit of general principles is contested. One view is that it refers to the 'general principles of international law'. While another is that it refers to general principles of national law. According to the first definition (general principles of international law) – the phrase is not a source of law as a method of using existing sources – extending existing rules by analogy, inferring the existence of broad principles from more specific rules using inductive reasoning. According to the second definition of general principles of law (general principles of national law), gaps in international law may be filled by borrowing principles that are common to all or most national systems of law.[37]

Therefore, it seems that to establish proportionality as either CIL or general principle, it has to be shown that it is ubiquitous in the domestic legal system or practices of states. To this end, scholars like Bücheler analyse the German, Canadian, South African, and Israeli domestic courts and argue that proportionality is a general principle of law.[38] However, while proportionality is commonly used for adjudication in domestic legal systems of Europe and North America, there are nations where proportionality is not used, with China being the biggest example among other Asian nations.[39] Additionally, proportionality does not exist in all 'civilised nations'.[40] Consequently from a critical third world lens, it seems arrogant of the 'civilised nations' to place a principle which might be ubiquitous in their domestic systems at a pedestal and universalise it. Even among the countries where it exists, it is not uniformly applied as cultural factors shape judicial review in different legal systems.[41] Most investment treaties do not refer to proportionality.[42] At the present juncture, according to Scholars like

---

[36] Alexander Orakhelashvili, *Akehurst's Modern Introduction to International Law* (Routledge 2022).

[37] RB Schlesinger, 'Research on the General Principles of Law Recognized by Civilized Nations' (1957) 51 American Journal of International Law 734, 739.

[38] Gebhard Bücheler, 'Proportionality as a General Principle of Law' in Valentina Vadi (ed), *Proportionality, Reasonableness and Standards of Review in International Investment Law and Arbitration* (Edward Elgar Publishing 2018) 37.

[39] ibid.

[40] Abdulkadir Gülçür, 'The Necessity, Public Interest, and Proportionality in International Investment Law: A Comparative Analysis' (2019) 6(2) University of Baltimore Journal of International Law 215.

[41] Valentina Vadi, *Proportionality, Reasonableness and Standards of Review in International Investment Law and Arbitration* (Edward Elgar Publishing 2018).

[42] ibid.

Vadi, further study is required and any decisive conclusion would be premature.[43] Furthermore, none of the IIL tribunals try to justify it as a custom or general principle, rather they adopt it from ECtHR jurisprudence. Therefore, proportionality cannot be justified as a part of CIL or a general principle of law.

Second, the proportionality test necessarily has some normative content. It cannot be seen as merely an analytical tool. The test entails considering whether a state action is proportionate to its aims.[44] The tribunal considers whether the means are necessary, suitable, and the least restrictive alternative for the aim.[45] In answering these questions, the tribunal moves away from 'what is' to 'what ought to be'.[46] To illustrate, suppose a tribunal is adjudicating on whether measure X is necessary to achieve goal Y. The tribunal here is considering whether measure X should be employed or whether some other measure Z ought to be sufficient.[47] Engaging with this normative content requires an understanding of the roots of the principle.

Therefore connectedly, *third*, this normative content of proportionality in ECtHR is contingent on and made coherent through European constitutionalism. The character of proportionality in ECtHR jurisprudence is constitutional. To elaborate, the European Convention on Human Rights is treated as a constitutional charter, specifically a European constitutional charter.[48] An example would be the ECtHR jurisprudence on Protocol No. 1.[49] This protocol suggests a balancing test between an individual's possession of the property and the state's right to regulate.[50] The ECtHR courts, while using proportionality to balance interests, also have to rely on other considerations to

---

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

[44] Michael Fordham and Thomas de la Mare, 'Identifying the Principles of Proportionality' in Jeffrey Jowell and Jonathan Cooper (eds), *Understanding Human Rights Principles* (Hart Publishing 2001) 27.

[45] Moshe Cohen-Eliya and Iddo Porat, Proportionality and Constitutional Culture (CUP 2013)

[46] N Jansen Calamita, 'The Principle of Proportionality and the Problem of Indeterminacy in International Investment Treaties' in Andrea K Bjorklund (ed), *Yearbook on International Investment Law and Policy 2013-2014* (OUP 2015) 157-200.

[47] The argument is inspired from Prof Lon Fuller's classic examples in 'Positivism and Fidelity to Law: A Reply to Professor Hart' (1958) 71(4) Harvard Law Review 630.

[48] *Ireland v United Kingdom* (1978) 2 EHRR 25; *Loizidou v Turkey* (1995) 20 EHRR 99.

[49] European Convention on Human Rights, Protocol No 1. Also, interestingly the case that *Tecmed* has relied upon was relating to Protocol No. 1 of the Convention.

[50] *Sporrong & Lönnroth v Sweden* (1983) 5 EHRR 35, 69. See generally Camilo B. Schutte, *The European Fundamental Right of Property* (Kluwer 2004) 51–58.

determine the hierarchy of interests.[51] This hierarchy is influenced by the constitutional nature of the convention.[52]

Thus, I argue that considering its normativity and embeddedness in European constitutionalism, the ECtHR proportionality test cannot be used in IIL expropriation disputes. Considering that European constitutionalism influences its normative nature, the test may be appropriate when governing ECtHR disputes between European nations. But from a TWAIL perspective it cannot be universalised to adjudicate on investment issues concerning the third world. The reason is that a particular set of European values cannot act as a universal standard governing the particular policies of other nation-states, especially one peculiar to the third world.

The principle of proportionality is at its core a principle of constitutional and administrative law.[53] The migration of constitutional ideas in international law is a contested topic.[54] Methodologically, there are as Vadi argues two views, the first, a functionalist and the second, a cultural approach.[55]

In a functionalist approach, law can be taken from one place and used in any other.[56] On the other hand, in a cultural approach, law cannot be separated from its context.[57] The assumption underlying the functional approach is that law is a tool meant to address social issues and that all societies have similar issues.[58]

Considering this, I argue that a cultural approach is more aligned with the realities of the present world and the divide between the global north and the third world. Different societies do indeed face different issues, from a TWAIL lens, the most glaring example, to illustrate this point would be the struggles of the third world, be it apartheid or the imposition of a hegemonic capitalist order.

---

[51] Vadi (n 41).

[52] ibid.

[53] VC Jackson, 'Constitutional Law in an Age of Proportionality' (2015) 124 Yale Law Journal 3094, 3098.

[54] G Teubner, 'Fragmented Foundations: Societal Constitutionalism beyond the Nation State', in P. Dobner and M. Loughlin (eds), *The Twilight of Constitutionalism?* (OUP 2010) 327, 328.

[55] Vadi (n 41).

[56] A Watson, 'Comparative Law and Legal Change' (1978) 37 Cambridge Law Journal 313–36, 314–15.

[57] Otto Kahn-Freund, 'On Uses and Misuses of Comparative Law' (1974) 37 Modern Law Review 1.

[58] R Michaels, 'The Functional Method of Comparative Law', in M. Reimann and R. Zimmermann (eds), *The Oxford Handbook of Comparative Law* (OUP 2006) 339–82.

These struggles are not present in the first world, as they are the ones who are if not playing the role of oppressors are the ones who are complicit.

A cultural approach realises that law cannot be separated from its context. Legal systems and principles are embedded in particular cultures. A meaningful usage of proportionality would be engaging with its particular ECtHR context and the values underlying it. However, IIL in their usage of proportionality has lacked such nuance. Rather, instead of nuance, a 'balancing' principle based in European constitutionalism has been relied upon by Europeans against the third world.

Scholars argue the historical, political, and cultural background of the principles have to be closely evaluated.[59] The reason is that constitutional principles are formed in very particular connotations of power and relationships between different institutions. Considering the international setting of IIL, such principles of particular jurisdiction cannot be incorporated at the international level.

A meaningful engagement with the principles entails more than blindly copy-pasting excerpts from ECtHR, it entails consideration of whether the principle has proven to be satisfactory in its field of origin, and whether it would be satisfactory to solve the unique concerns of the IIL regime. To clarify, I am not opposed to the usage of proportionality in IIL. However, its current conception based on ECtHR constitutionalism is not something that can be utilised without deliberation and taking cognisance of values underlying the same.

Now, it may be argued that another way to use proportionality in IIL is not by taking on from ECtHR, but rather using it as an analogy to transplant the concept, essentially a legal transplant.

To contextualise, constitutional ideas such as proportionality migrate across disciplines through predominantly three ways: (a) cross-judging (essentially referring to the jurisprudence of other tribunals); (b) legal transplant (transplanting legal principles or law from one country to another), and (c) when they become general principles of law. As argued before, ECtHR cannot be used for cross-judging because of its peculiar character, for instance: IIL is concerned with investor-state disputes in a neo-liberal world where capitalistic

[59] P Zumbansen, 'Transnational Comparisons: Theory and Practice of Comparative Law as a Critique of Global Governance' (Research Paper No 1/2012, Osgoode Hall Law School 2012).

interests play a predominant role. Whereas ECtHR is concerned with human rights violations; legal instruments in ECtHR such as Protocol No.1 underlies the logic of proportionality, but there is no such backing in the IIL framework. Similarly, as argued before, proportionality at the current stage cannot be said to be a general principle of law. Therefore, (a) and (c) cannot be used to justify proportionality in IIL.

However, I argue that even the logic of legal transplant cannot be used to justify proportionality in IIL. The reason is because of the issues inherent in the legal transplant of constitutional principles in international law.[60] The major issue is selection bias. There is the possibility that arbitrators would choose the cases or principles that they are familiar with (European arbitrators and EtCHR jurisprudence) rather than ones that reflect the position of law or are more suited to the present issue. Additionally, given that in IIL cases, there are already BITs that govern any dispute between the parties, going out of their way to choose principles such as proportionality is in some sense altering the very text of the treaty chosen by parties. Finally, for transplants, the legal systems have to be comparable. But considering the supranational law setting of IIL, it is not desirable to transpose the experience of any national jurisdiction, especially one where the principle seems to more often than not weighed against a particular group, that is the third world.

To conclude, *Tecmed* encapsulates this point. It highlights how Mexico's particular policy considerations were delegitimised by a supposedly universal standard. Thus, the infusion of ECtHR jurisprudence, particularly its proportionality test is problematic for third-world countries. In the next subsection, I *arguendo* ignore the infusion of ECtHR and focus on the fallacies of the test itself.

2. Methodological Flaws and Legitimate Policy

Even in the ECtHR, proportionality has three steps, namely necessity, suitability, and then a balancing analysis.[61] The tribunal in *Tecmed* however skipped the first two prongs and proceeded directly to balancing.[62] In the third step, benefits from

[60] Vadi (n 41).

[61] Takis Tridimas, 'Proportionality in Community Law: Searching for the Appropriate Standard of Scrutiny' in Evelyn Ellis (ed), *The Principle of Proportionality in the Laws of Europe* (Hart Publishing 1999) 65.

[62] *Tecmed* (n 11) 122. There is also no apparent reason why *Tecmed* didn't use the complete test, see Henckels (n 15).

the measure are weighted against the restriction of the investor's right. But in *Tecmed* this was done without deciding whether the regulatory measure is suitable or whether less restrictive alternative measures are available to the host country.

Thus, going directly to the third prong entails the making of a judgement about the importance of achieving the objective vis-a-vis the importance of preventing harm to the investor's interests.[63] It may be argued that since proportionality is a conjunctive test, ultimately all prongs must be analysed, which would mean that the order of the analysis is irrelevant. However, the point I am trying to establish is not that the order of the proportionality test was misapplied by the tribunal. Rather the tribunal altogether skipped the first two prongs. In any case, despite proportionality being a conjunctive test, the balancing stage has to be at the last, as the earlier two prongs inform the content of the balancing stage. In *Tecmed*, the tribunal is balancing the benefits and harms of the restriction without deferring to the host state regarding the suitability of the measure or the presence of less restrictive alternative measures.

The lack of deference, combined with the methodological fallacies, creates problems for host states. As shown by *Tecmed*, it grants the tribunal the discretion to decide which public objectives are worth pursuing and legitimate, instead of the State. This casts doubt over the host state's sovereignty and undermines its right to regulate itself.

This application of proportionality also intensifies the TWAIL critiques of IIL and BIT as being neo-colonial institutions that undermine the host state's right to make decisions for public objectives.[64] Some major TWAIL critiques of the international investment regime are that they are based upon an understanding of the law that does not align with considerations relating to human rights, environmental protections, and the sovereignty of host states, an issue that is particularly exacerbated in the cases of developing countries acting as host states.[65]

---

[63] Henckels (n 15) 232.

[64] Nicolás M Perrone, 'Foreign Investment Law: A TWAIL View' in Tony Anghie, Michael Fakhri, Vasuki Nesiah, Karin Mickelson and B.S. Chimni (eds), *TWAIL Handbook* (Edward Elgar) (forthcoming).

[65] Centre for Trade and Investment Law, 'International Investment Law and TWAIL' (ctil.org.in, 2023) <https://ctil.org.in/cms/docs/Papers/Publish/02International%20Investment%20Law%20and%20TWAIL.pdf> accessed 14 November 2024.

Another connected critique TWAIL critique that can be made here is one of the 'chilling effect' thesis, which posits that the entire regime of IIL deters host states from making decisions for public purposes, in fear of facing penalties from tribunals.[66] All of these ultimately hamper the development of nations, usually third-world countries, thus replicating the current hegemonic and inequitable systems. In the next subsection, I evaluate other IIL cases that have applied the proportionality test.

B. Cases Post *Tecmed*

Despite there being no stare decisis in IIL, the majority of indirect expropriation awards following *Tecmed*, have cited and applied its proportionality test.[67] Soon after *Tecmed*, the tribunal in *Azurix v Argentina*, applied a *Tecmed*-esque proportionality test, and the award was eventually won by the investor.[68] Following that, an interesting award was *Fireman's Fund Insurance v The United Mexican States*.[69] Here, the tribunal questioned *Tecmed's* application of the proportionality test because it imported the test from ECtHR without any basis. This case was won by the host state.

However, it appears that *Fireman's Fund Insurance* was an aberration. The dominant trend has been that cases have used *Tecmed's* proportionality without any questions. As in future cases like *LG&E v Argentina*,[70] *Continental Casualty v The Argentine Republic*,[71] and *El Paso v Argentina*,[72] the holdings have favoured the investor.

---

[66] Maryam Malakotipour, 'The Chilling Effect of Indirect Expropriation Clauses on Host States' Public Policies: a Call for a Legislative Response' (2020) 22 International Community Law Review 235.

[67] Jan Paulsson, 'The Role of Precedent in Investment Treaty Arbitration' in Katia Yannaca-Small (ed), *Arbitration under International Investment Agreements: A Guide to the Key Issues* (2nd edn, OUP 2018) ch 4.01.

[68] *Azurix Corp v Argentine Republic*, ICSID Case No ARB/01/12, Award (14 July 2006).

[69] *Fireman's Fund Insurance Company v United Mexican States*, ICSID Case No ARB(AF)/02/1, Award (17 July 2006).

[70] *LG&E Energy Corp., LG&E Capital Corp., and LG&E International Inc. v Argentine Republic*, ICSID Case No ARB/02/1, Award (25 July 2007).

[71] *Continental Casualty Company v Argentine Republic*, ICSID Case No ARB/03/9, Award (5 September 2008).

[72] *El Paso Energy International Company v Argentine Republic*, ICSID Case No ARB/03/15, Award (31 October 2011).

However, the award in *Occidental Petroleum Corporation v Ecuador,*[73] is particularly interesting. Here the Ecuadorian constitution and local laws were in support of proportionality. However, the tribunal stated that proportionality is a matter of general international law and cited *Tecmed*. However, as I have argued above, proportionality is not a general international law principle. Merely because it has been cited by a few tribunals does not make it a general principle or customary international law.[74] Still, the trend of *Tecmed's* proportionality being applied and investors winning continues in subsequent cases like *Deutsche Bank AG v Sri Lanka*,[75] *Total v Argentina*,[76] and *Suez and InterAgua v Argentina* prevails.[77]

The last award I will highlight is *Philip Morris v Uruguay*.[78] Here, the tribunal also attempted to use the proportionality test from *Tecmed*. Interestingly, however, the host state won. Here, the tribunal equated the meaning of proportionality with reasonableness. This award highlights another flaw with the underlying current proportionality test – its unclear content. This is problematic because it grants ad hoc tribunals the leeway to mould the content of the proportionality test.

To clarify, this is different from my previous critique of methodology. There, due to the flawed methodology, the tribunals determined the legitimacy of state policy. Here, I argue that as there is no basis in IIL, there is ambiguity regarding what proportionality entails in investor-state disputes. Combining this

---

[73] *Occidental Petroleum Corporation and Occidental Exploration and Production Company v Republic of Ecuador*, ICSID Case No. ARB/06/11, Award (5 October 2012).

[74] Peter Malanczuk, *Akehurst's Modern Introduction to International Law* (7th revised edn, Rutledge 2002) ch 3 – Sources of International Law.

[75] *Deutsche Bank AG v Democratic Socialist Republic of Sri Lanka*, ICSID Case No ARB/09/2, Award (31 October 2012).

[76] *Total SA v The Argentine Republic,* ICSID Case No ARB/04/1, Award (27 November 2013).

[77] *Suez, Sociedad General de Aguas de Barcelona SA and Interagua Servicios Integrales de Agua SA v Argentine Republic*, ICSID Case No ARB/03/17, Award (9 May 2010). Here, the award was granted based on FET violation rather than indirect expropriation. Interestingly, *Tecmed's* proportionality was applied for both standards. The interplay between proportionality and FET is out of the scope of the paper. However, current academic scholarship suggests a close relationship between the claims. See also Christoph H Schreuer, 'Fair and Equitable Treatment (FET): Interactions with Other Standards' (2007) 4(5) Transnational Dispute Management; Dalia Višinskytė, *Indirect Expropriation in Investor-State Arbitration* (PhD thesis, Mykolas Romeris University 2023).

[78] *Philip Morris Brand Sàrl (Switzerland), Philip Morris Products SA (Switzerland) and Abal Hermanos SA (Uruguay) v Oriental Republic of Uruguay*, ICSID Case No ARB/10/7, Award (8 July 2016).

with the no *stare decisis* aspect and the flawed approach of *Tecmed*, the ad hoc tribunals usually composed of Western and privileged sections of the society are empowered to determine its content.[79] This is problematic as proportionality then becomes a catch-all term for the tribunal to consciously or unconsciously impose their Eurocentric conceptions of values. A perusal of parties that usually end on the losing side (Mexico, Argentina, Sri Lanka) brings into the fore the issue of proportionality and challenge the veracity of using the principle without being cognisant of its inherent biases. From a critical third world lens, is proportionality's supposed balancing act able to actually weigh investor interests with goals of third world?

To sum up, in this section, I posited a broad critique of proportionality in IIL with two prongs. The proportionality test in IIL traces its roots to the ECtHR. This conception of proportionality is embedded in European constitutionalism and cannot be used as a universal standard. In the particular context of how IIL tribunals have used proportionality, this critique has two implications. Firstly, due to the flawed methodology of proportionality, it has granted ad hoc tribunals the discretion to determine the legitimacy of public policy. This raises concerns about the third world's right to regulate their sovereignty and even their development. Secondly, due to a lack of stare decisis and no basis for proportionality in IIL, the tribunals have the discretion to use proportionality as a catch-all term and impose their values to adjudicate. In the subsequent section, I suggest an alternative and present a hypothetical.

IV. BACK TO BASICS: SOLE EFFECTS STRIKES BACK

To hark back to Part I, the underlying issue is the difficulty in distinguishing between indirect expropriation and regulatory action. I argue that instead of a qualitative measure like proportionality. A quantitative measure like the 'sole effects doctrine' should be used to solve this issue.[80] The doctrine looks at the *effect* of the regulation or government action on investment.[81] This provides a more equitable resolution. Here, the effect is not only limited to economic loss but extends also to the loss of control that investors have suffered.[82] The loss must

[79] Sergio Puig, 'Social Capital in the Arbitration Market' (2014) 25(2) European Journal of International Law 387.

[80] Kriebaum (n 9).

[81] Dolzer, Kriebaum and Schreuer (n 4) 169.

[82] August Reinisch and Christoph Schreuer, *International Protection of Investments: The Substantive Standards* (CUP 2020).

cause substantial deprivation to the investor.[83] It is to be noted that substantial deprivation grants the tribunal discretion to determine what exactly is substantial.

To illustrate with a few classic examples of sole effects in IIL, per Dolzer, the authority from sole effects doctrine in IIL comes from the practice of the Iran-US Claims Tribunal.[84] There, in awards such as *Starrett Housing v Iran*,[85] the tribunal focused on the *effect* of interference with property rights. This doctrine has further been expanded to see the effect on use or control and value or income.[86]

However, I argue that this discretion is much lower than what the tribunal enjoys when it employs proportionality. As it is primarily a quantitative measure, the discretion of the tribunal is significantly lower and does not in any circumstance culminate in the tribunal determining the legitimacy of policy. This also resolves one of my primary critiques of proportionality. Therefore, from a TWAIL lens, this seems more appetible than proportionality.

There may be some element of normative judgment about the clear boundaries of substantial deprivation. However, the scope is limited as compared to proportionality. It may be argued that even the sole effects doctrine, being a legal principle, can be developed by tribunals in a manner to alter its existing contours, hence making it similar to proportionality. The tribunals, as scholars like Kammerhofer argue, have expanded or rather muddled the contours of sole effects by highlighting questions such as sole effect on what (value, use, income, etc.)? and the extent of effect (total or substantial)?[87] Therefore if the argument is that sole effect doctrine is also not inherently clear, I accept it. However, my claim is that the sole effect, no matter how much it is altered by the tribunals, cannot ever lead to tribunals making normative judgments about the aims and concerns of nation-states, at least not to the level of proportionality. This in turn alleviates the one of the primary concerns that

[83] ibid.

[84] Dolzer, Kriebaum and Schreuer (n 4) 170.

[85] *Starrett Housing Corporation v Iran* (1983) 4 Iran-USCTR 122.

[86] *Burlington Resources Inc. v Republic of Ecuador,* ICSID Case No ARB/08/5, Decision on Liability, (14 December 2012) 397; *Alpha Projektholding GmbH v Ukraine,* ICSID Case No ARB/07/16, Award, (8 November 2010) 408; *I.P. Busta & J.P. Busta v Czech Republic* (SCC Case No V 2015/014, Final Award, 10 March 2017) [389-390]; *Cargill, Incorporated v Republic of Poland,* ICSID Case No ARB(AF)/04/2, Award, (29 February 2008) 587

[87] Jörg Kammerhofer, *International Investment Law and Legal Theory* (CUP 2021).

TWAIL scholars might have as using sole effects. The reason being that it does not amount to adjudicating on policy and due to its limited scope does not lend itself easily to judicial discretion.

The reason being, at its core, the doctrine is concerned with the deprivation of investment. Akin to Dworkin's chain novel thesis, even if there is discretion afforded to tribunals, ultimately, they cannot mold or alter the principle into what it is not.[88] The principle's core cannot be eviscerated, and as long as that is the case, the sole effect is better suited for the needs of the third world as compared to proportionality. Thus, its content cannot be decided by the tribunal.

Finally, unlike proportionality, the sole effects doctrine arguably has its basis in general principles of investment law.[89] As mentioned before, the doctrine has been used in IIL for over 40 years, though the its basis is unlikely to be found in domestic legal systems, as it is concerned with expropriation, which by definition does not arise in domestic scenarios. The basis can be found, unlike proportionality in treaty practice. For instance, Article 1110 of NAFTA defines expropriation itself in terms of affecting the investment.[90] Many expropriation clauses expressly state that the state measure is to be deemed expropriatory due to its effects.[91] These clauses use terms like 'having the same effect' or 'having a similar effect'.[92]

The main argument against the sole effects doctrine is that it infringes upon the state's right to regulate. I argue that this is not the case, since the threshold for substantial deprivation as established by tribunals is very high.[93]

---

[88] Ronald Dworkin, 'Law as Interpretation' (1982) 9(1) Critical Inquiry 179.

[89] Rudolf Dolzer and Felix Bloch, 'Indirect Expropriation: Conceptual Realignments?' (2003) 5 International Law Forum 155, 164; *Pope & Talbot v Canada,* UNCITRAL (NAFTA) Interim Award (26 June 2000); Jason Gudofsky, 'Shedding Light on Article 1110 of the North American Free Trade Agreement (NAFTA) Concerning Expropriations: An Environmental Case Study' (2000) 21 Northwestern Journal of International Law and Business 243, 287–88; J Martin Wagner 'International Investment, Expropriation and Environmental Protection' (1999) 29 Golden Gate University Law Review 465.

[90] North American Free Trade Agreement (NAFTA) art 1110. This interpretation was also supported by *Pope & Talbot*.

[91] Jenny Santikko, 'When regulation is expropriation' (Master's thesis, University of Helsinki 2019).

[92] ibid.

[93] Ben Mostafa, 'The Sole Effects Doctrine, Police Powers and Indirect Expropriation under International Law' (2008) 15 Australian International Law Journal 151; Todd Weiler, 'Interpreting Substantive Obligations in Relation to Health and Safety Issues', in Todd Weiler

Usually, regulations do not meet this threshold and this grants the host state ample leeway.[94] Thus the third world concern of it hampering on them making independent policy decisions is resolved. If despite this a regulatory action meets the threshold, then it is more equitable for the investor to be compensated.

To illustrate briefly how the sole effects approach would have been applied, I use a basic hypothetical with facts akin to *Tecmed*. A Spanish company 'X' has a waste recycling plant in Mexico with a one-year permit. The community surrounding it did not like it due to generation of noise, smell, etc. The local government found some procedural error and canceled the permit. Mexico claims environmental and public health reasons for its decision whereas X claims indirect expropriation. Here, based on a subtle difference of fact: namely whether Mexico offered relocation in good faith,[95] I present two scenarios to argue how it is equitable to both parties:

Scenario A: No relocation offered – The effect of the regulation has substantially deprived the investors of the value that they paid for the plant. As relocation has not been offered, the company has no recourse left. In this case, there has been indirect expropriation.

Scenario B: Relocation offered – Here, the effect of the regulation has not substantially deprived X of their investment. They still have access to it, albeit its value may be reduced. But it cannot be said to be an indirect expropriation. However, they may have other remedies like violation of fair and equitable treatment.

V. CONCLUSION

To end as I began, proportionality in IIL expropriation claims seems like a sledgehammer that is not precise enough to crack the tough nut of indirect expropriation. To establish this, I have done three things. First, I have argued how the proportionality test in IIL is derived from the ECtHR jurisprudence that is embedded in European Constitutionalism. Second, I have argued that the proportionality analysis eventually leads to the ad hoc tribunal to determine the

(ed), *NAFTA: Investment Law and Arbitration: Past Issues, Current Practice, Future Prospects* (2004). See also Ranjan (n 14) 123.

[94] Ranjan (n 14).

[95] Interestingly in *Tecmed*, it was argued by Mexico that it would offer relocation. However, in actuality it never came into fruition and the dispute started. To resolve all of these issues as Kriebaum argues, we may need to move away from "all or nothing" approach we rethink IIL regime. See Kriebaum (n 9).

legitimacy of public policy. Thirdly, the ambiguity surrounding the contents of proportionality grants tribunals enormous discretion. All of these have cumulatively disadvantaged the host states which are usually third world countries. Finally, I proposed a solution via a quantitative determination of expropriation, by reverting to the sole effects doctrine and illustrated a hypothetical for the same.