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Commentary

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Is an investor founded to expect a continuity in the case law set by local courts which was applicable at the time of the investment in the host State? In situations where a major change in case law set by local courts ends up in frustrating the investment, would the investor be entitled to seek compensation from the host State based on investment treaties? Overruling of precedents is not uncommon in civil law and common law systems, although each try to mitigate its consequences over the parties. This phenomenon can be apprehended through the notion of legitimate expectations, which finds protection in different systems of law as well as in EU law and finds an expression in investment law through fair and equitable treatment principle which is found in most of modern investment treaties. It also shows that although most national legal systems do not attach any consequences to the overruling of precedents in terms of liability for the acts of the State's courts, application of investment treaties can give rise to such liability of the State. This discrepancy between most national systems and investment treaties is an expression of dualism in international law.

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"If we want things to stay as they are, everything will have to change". These are Tancred's well-known words in Visconti's film the *Leopard*. They echo our present concerns in international investment arbitration: are investors right to expect a stable legal environment? If so, how far are States entitled to impose changes in the legal environment without being exposed to a claim from investors? Change is consubstantial to a State's administration and policy and can sometimes be a condition of its survival. If the State accepts a stabilization clause and therefore commits not to reform its laws in the field of the investment, there will be little room for reform in the sector covered by the clause. But what should happen in other situations where the State has not offered such direct guarantees to investors? Some awards have ruled that even though it is free to change the content of its law, the State should not do so in a way that breaches the legitimate expectations of investors[1]. Therefore, the question shifts to *how*, by which means should the State anticipate those changes, inform investors and stakeholders, make them understandable to all parties, and make them transparent?

The issue is even more acute when the change comes from the judgments made by courts. Some awards have stated that the investor is entitled to rely on existing case law from the State courts at the time of the investment when this case law has been stable and continuous. Although the law can remain unchanged since the investment, its interpretation by courts can drastically impact the investment, if the interpretation has radically changed since the investment was made.

To illustrate this, an example can be taken from the factual background of the case *ADF Group v. USA*, which for our demonstration will be slightly modified[2]. A Canadian company has been awarded a public tender for the construction of a crossroads in the USA. The price mentioned in the reply to the tender was based on materials calculated by the company, among other steel produced in Canada. At the time of the investment, US

Courts had ruled an interpretation of the "Buy American Act" that authorizes imported steel for local construction projects with the condition that they are already "manufactured" – by opposition to "produced" – and are therefore to be integrated in the construction. However, local US authorities inform the company that it should use only locally produced steel, and reject this interpretation, although formerly admitted by US Courts. Consequently, the company claims that its forecasts on the investment are totally disrupted. The company brings the case to Courts, which reverse their prior interpretation of the legislative act and follow the interpretation given to it by local US authorities.

The topic of this article is to focus on the main questions that arise out of the responsibility of States for the acts of their Courts in the field of investment law, and to give some keys on how they could be handled by arbitrators and counsels.

Firstly, the question arises as to how the parties should be protected. Is there a principle of legitimate expectations that the parties can raise against the acts of a State because of a decision of their Courts that reverses so far well-established precedents? If it does exist, how close is this principle from the right to expect a stable legal framework, and the right to a transparent legal system? Could we use other principles or subjective rights, such as the right to a fair trial, to oppose the consequences of a radical change of case law in a specific situation?

Second, every legal system brings its own answers to these questions. A same factual situation can therefore lead to different solutions at the same time if it develops across different legal systems: one situation can be apprehended at the same time through the prism of one national law, EU law, the European Convention of Human Rights, and through a different prism in investment law. This is far from being an exception, as we shall see.

Although a convention on protection of investments can constitute the basis of a claim against the State, the fact that the legal system of this State does not provide any action to repair the consequences of an abrupt overruling of preexisting case law should be considered while assessing its responsibility. However, investment law brings its own solutions to this question, which can differ from the one adopted by the State. It is therefore possible that the liability of the State finds a basis in investment law, whereas the same situation is not sanctioned in the same State's domestic law. This is not surprising, since it is a logical consequence of dualism in public international law[3]. As will be seen later in this article, investment law brings original solutions, often at odds with the ones admitted by domestic legal systems, because it focuses on the result (were legitimate expectations effectively disrupted or not?) rather than on legal theory (are parties entitled to oppose legitimate expectations to a decision of justice if judgments rendered by Courts are not considered to be a source of law?).

In this study, we will analyze the solutions which are adopted to mitigate the consequences of overruling of precedents in different legal systems and see whether they admit to declare the State liable to repair the consequences of a disruption of the legitimate expectations of the parties **(1).** In this regard, we will see by comparison how EU law protects legitimate expectations through a principle of law **(2).** Investment law, as applied by arbitral tribunals, finds original solutions to this question **(3).** The consequence is the emergence of a dualist system where a similar factual situation can be sanctioned in public international law, and not in the domestic legal system, which creates potential discriminations between foreign and local investors in the host State **(4).**

1. Overruling of precedents in Civil and Common law

The role attributed to Courts broadly depends on the role attributed to justice in a given legal system. In this regard, the interpretation and the impact of overruling of precedents differs greatly in civil and in common law systems.

It is obvious that civil law systems are more subject to abrupt changes in case law than common law systems. A civil law judge is not bound by the rule of precedent. He is deemed to be free to depart from pre-existing case law on similar facts; and precedents, even though they may be important in the consideration of a case, are not the necessary basis of his reasoning[4].

Under civil law systems, judges are deemed to deliver an interpretation of statutory law. Therefore, the interpretation of the law given by courts can change over time although the law that is interpreted remains unmodified. In this sense, it is traditionally taught in law schools that case law is *not* a source of law, because

judges merely interpret the law rather than they create it[5]. Along the same lines, some authors suggest that a judgment reversing an interpretation of the law that was so far widely admitted is *not* retroactive, because the law itself has not changed and the judgment is supposed to deduce the solution of the case from the law[6]. Such views deny any right to a specific interpretation by the parties, and therefore exclude the idea that their legitimate expectations can be harmed because of a change of case law. As such, this view is rather artificial: one can say that there is no retroactivity because the law has not changed, but this retroactivity has a consequence on the parties' legal situation that can rarely be anticipated by them. *It is a fact* that the legal situation of the parties is affected by the decision rendered by the judicial body, and it is a fact also that their basic expectations are disrupted by the abrupt change taken by the judges.

This has led civil lawyers to look for solutions to avoid these detrimental effects, for instance by imposing transitional arrangements on the new ruling. In France, the Cour de Cassation has developed a set of techniques aimed at avoiding this consequence. One technique consists in announcing in advance, in its annual report (the "*Rapport annuel de la Cour de Cassation*", which compiles official commentaries, given by the Court, on the main decisions of the past year and gives its position on important pending legal issues) the changes that it is contemplating adopting before they are effectively adopted. A second technique consists in defining the moment when the new case ruling applies, with the aim to avoid a retroactivity that would harm the interests of the parties[7]. The Cour de Cassation has, in very rare cases, reversed its former case-law in relation to the prescription applicable to a claim but has decided not to apply this change to the case at hand, the reason given being that *"the immediate application of this rule of prescription would deprive the victim of its right to a fair trial, in the sense of article 6.1 of the European Convention of Human Rights"*[8]. Some authors admit that case law is to some extent a source of law on which the parties are legitimately relying[9]. However, it is worth noting that the principle of legitimate expectations is not universally used as a basis of the protection of the parties against a reversal of case-law. In French law, the Cour de Cassation is reluctant to admit that such a principle of legitimate expectations, or "legal safety" ("sécurité juridique") could exist and form the basis of subjective rights for the parties[10]. In the above quoted judgment rendered in 2004, the Cour de Cassation, using the form of a "prospective overruling", rejected an immediate application of its new interpretation to the case at hand, considering it would be against the right to a fair trial based on article 6.1 of the European Convention of Human Rights rather than on a hypothetical principle of legitimate expectations. This "prospective overruling" was also used by the European Court of Justice, which decided in several occurrences to apply a new interpretation of law only to future cases, in order not to trouble rights regularly obtained through a former interpretation of law[11]. As suggested by some authors, a means to mitigate the retroactivity of a new case law could consist in recognizing the right for the parties to seek the State's responsibility towards any party that based its behavior on an interpretation of law which the Courts later reversed[12]. However, it is broadly considered in civil law countries that retroactivity of case-law is not a cause of liability for the State.

The European Court of Human Rights, for its part, considers that the retroactive applicability of a new interpretation of the law can be a violation of the right to a fair trial as stipulated by article 6.1 of the Convention in that this change could not reasonably be anticipated by the parties[13]. Moreover, this Court considered in several judgments that courts which change their interpretation of a legal disposition have a special duty to explain the reasons why they are departing from previous decisions, failing which the State shall be held responsible for a violation of article 6 of the European Convention of Human Rights[14]. The French Cour de Cassation followed this pattern, thereby changing drafting habits that were firmly anchored in its traditions[15]. Thus, the European Court of Human rights exerts considerable influence on national courts, including Supreme Courts, to draft more explanatory judgments, and detail the steps of their reasoning, sometimes by developing the chronology of case law precedents over a single issue.

In common law systems, retroactivity of case law is to some extent mitigated by the doctrine of precedent. The doctrine of precedent refers to the doctrine that courts are to follow judicial decisions in earlier cases when the same questions are raised before it in subsequent matters. This doctrine is designed by the aims attached to the rule of law. As underlined by an author *"the basic reason behind the doctrine of stare decisis is the maintenance of consistency and certainty. Certainty, predictability and stability in law are considered to be major*

objectives of the legal system, and the doctrine of stare decisis aims at achieving these objectives"[16]. The judge might decide to depart from prior case law, but he will do so not only considering the need to adapt the law to the case at hand, but also taking into consideration the rule of law in its entirety to assess the consequences of this change on the whole system.

This is also reflected in the structure of the reasoning in common law judgments. It is generally recognized that common law systems proceed by induction from facts to a decision. The judge has creative powers to decide on a case, but will usually weigh several possible options, and discuss the best approach to adopt. Dissenting opinions are not rare before Supreme Courts. If a change is always possible despite the rule of precedent, it will rarely come "out of the blue" but will have been anticipated in former decisions and discussed as a possible option in *Obiter dicta* in previous decisions, therefore allowing the parties to anticipate a change. As theorized by Dworkin in his "law as integrity" theory the judge has a duty of consistency in the application of law, and the law is seen as a coherent phenomenon, rather than a set of discrete decisions[17].

Interestingly enough, one finds the same debates on decision-making in common law and in civil law systems. In a "realist" conception of law making, the judge undertakes a "quasi-legislative" function in the process where *"in order to achieve a fair and just result the court may find it necessary to depart from the statement of law in the precedent case"*[18]. On the other hand, in the "declaratory" theory "*the entire common law already exists awaiting judicial declaration"*[19]. Therefore *"if the judges change their mind about a particular common law rule or principle, they are not changing the law »*[20]. Echoing civil law, common law systems tend to overtake this rather theoretical debate to look for ways to mitigate the negative consequences of abrupt changes, such as prospective overruling, i.e. judgments where the judge overturns a precedent but decides not to apply this change to the case at hand.

This discrepancy between civil and common law approaches is somehow mitigated by the fact that civil law judges tend to discuss, in their judgments, the merits of different approaches in the interpretation of the law, before adopting one of them, at the same time making clear the interpretation they might want to adopt in the future. However, the discrepancy remains true in principle. Both systems have in common that although they recognize the potential harm to the legitimate expectations of the parties, the State should not be held liable for this.

This theoretical analysis of the decision-making system is irrelevant to the law of responsibility of States, where *only the result* is scrutinized in itself, without taking into consideration the theoretical background that lies behind each legal system: when it comes to evaluating the material consequences on the parties of the judgment rendered by a local court, it is irrelevant that case law is seen as a source of law or that the judge is seen as a mere interpreter of a norm which does not change. This result is seen from outside of the State legal system: were legitimate expectations disrupted or not? Was a party entitled to rely on a given legal background – which includes its corpus of case-law – at a certain point in time? Investment law, as a branch of public international law, reasons along the same lines. It stems from this that a situation which does not give rise to the liability of a State under the host State's law can leave the way open to its liability for the same acts based on public international law principles. This is a normal consequence of dualism in public international law.

2. EU law: legitimate expectations protected as a principle of law

Legitimate expectations are closely related to *legal certainty*, which assumes the maximum predictability of the State's behavior and requires that "*there be no doubt about the law applicable at a given time in a given area and, consequently, as to the lawful or unlawful nature of certain acts or conduct"*[21]. Beyond this principle of legal certainty are several judgments of the European Court of Justice where the Court has put forward *legitimate expectations* of the parties as a principle of law which falls within the realm of EU law[22]. The principle was found by the Court to be in relation to retroactive application of the law but, as will be seen, has a necessary impact on the question of retroactivity of judgments as well as it teaches us how the Court sanctions this principle, therefore showing us the way to its transposition to the question at hand.

In Case 265/ 85 *Van den Berg and Jurgens BV v/ Commission* the Court held that *«. . . any trader in regard to whom an institution has given rise to justified hopes may rely on the principle of the protection of legitimate expectations"*[23]. In *Mudler v. Minister van Landbouwen Visseri*[24]

and *Von Deetzen v. HZA Hamburg-Jonas*[25], the Court partially invalidated retroactive EU legislation on milk production, because its application would be detrimental to the producers' legitimate expectations based on the former law. Assurances can be of a general nature, and the economic operators do not need to be individually named to benefit from such protection. In *Mudler v. Minister van Landbouwen Visseri* the individual applied a scheme that had been applied by others before him for a period, against the position of the authorities that this operator had not been mentioned individually as a beneficiary of this scheme. Along the same lines, in some situations the European Court limited the consequences to its decision to invalidate an EU regulation by ordering that this annulation be effective only in the future to avoid detrimental consequences on stakeholders who had relied on the regulation. In the same decisions, the Court invited the EU institutions (Commission, Council. . .) to modify the legislation so as to integrate this invalidation[26]. This was the case when the consequences of a full retroactivity of the annulment judgment would have had major effects on the economic situation of social protection services or institutions[27].

The Court does not prohibit *per se* retroactive legislation or State intervention but sets conditions to this retroactivity. In Case 98/78 A. *Racke v. HZA Mainz*[28]and *Weingut Gustav Decker KG v. HZA Landau*[29], the European Court expressly accepted that retroactive legislation was not invalidated by the principle of legitimate expectations if certain conditions were met. It held that, *"although in general the principle of legal certainty precludes a Community measure from taking effect from a point in time before its publication, it may exceptionally be otherwise where the purpose to be achieved so demands and where the legitimate expectations of those concerned are duly respected".* The Court therefore imposes a balance of interests, to enable the measure to operate retroactively as much as is necessary for the public interest without jeopardizing legitimate expectations of private interests.

The criteria might rely on the possibility the trader had to anticipate the change. In the case of a sudden change of policy having unexpected effects, where the change could not be anticipated by a prudent trader, the Court ruled that it could be considered as a violation of legitimate expectations[30]. On the other hand, in situations where *"a prudent and discriminating trader could have foreseen the adoption of a Community measure likely to affect his interests, he cannot plead that principle if the measure is adopted"*[31]. The investor should therefore not be protected each time he is expected to have reasonably anticipated the change[32].

As seen, the Court sets a principle of legitimate expectations and sanctions it by imposing its application into the rule of law, each time the parties have not been able to anticipate the change. The Court sets the guidelines on how it should handle retroactive application of the law, which should encompass situations where such retroactivity comes from its interpretation by the judges.

3. Investment law: the protection of legitimate expectations through fair and equitable treatment principles

Should States be held internationally liable for retroactive case-law although in their own legal system retroactivity is not a source of State liability?

There is little doubt that violation of legitimate expectations, and its consequences in terms of detrimental effects arising from a judgment rendered by local Courts can be internationally imputed to the State. It is well established in International law that a State can be held responsible for the actions of its judicial bodies. Resolution n°56/83 dated 28 January 2002 adopted by the General Assembly of the United Nations formally expressed the imputation to the State of the decisions rendered by its judicial bodies. In its article 4.1 it is stated that *"the conduct of any State organ shall be considered an act of that State under international law, whether the organ exercises legislative, executive, judicial or any other functions, whatever position it holds in the organization of the State, and whatever its character as an organ of the central government or of a territorial unit of the State".* The same resolution, in its article 7, extended this imputation in situations where such decision would be considered as illegal or exceeding the powers vested in such organ of the State: *"the conduct of an organ of a State or of a person or entity empowered to exercise elements of the governmental authority shall be considered an act of the State under international law if the organ, person or entity acts in that capacity, even if it exceeds its authority or contravenes instructions"*[33].

This resolution was not an innovation in international law. In the PCIJ case *concerning certain German interests in Polish upper Silesia*, the court judged that *"a law is the*

expression of the State's authority, as can be attributed to the State the judicial decisions rendered by Courts or administrative measures"[34]. In *Metalclad v. Mexico,* the tribunal judged that the State's responsibility may arise when *"the court decision itself constitutes a violation of the treaty"*[35], as well as the procedure followed by the court can constitute a violation[36].

The main question resides in whether the State should be held liable for the interpretation given by courts of a national existing law. Interpretation given by judges is retroactive, because it applies to situations that are already constituted at the time the new interpretation is given by the judge. In this regard, it is broadly recognized in doctrinal writings that a change in the interpretation of law by the courts is detrimental to the parties' interests, because they relied on a formerly admitted interpretation of the law.

Awards rendered in the scope of investment law have broadly admitted the existence of a principle of legitimate expectations. Although this principle illustrates cases of responsibility to sanction change in the host States administrative regulations and enactment of new statutes **(a),** there are signs of a shift in the application of this principle to situations where legitimate expectations are frustrated by an overturn of precedents decided by the host State courts **(b).**

a) The principle of protection of legitimate expectations in investment law...

The principle of legitimate expectations is not *stricto sensu* based on conventions of protection of investments, but rather on a constructive interpretation of fair and equitable treatment. As underlined by the comity ad hoc in *CMS v. Argentina* on 25 September 2007, "*although legitimate expectations might arise by reason of a course of dealing between the investor and the host State, these are not, as such, legal obligations, though they may be relevant to the application of the fair and equitable treatment clause"*[37]. Therefore, legitimate expectations are not contained in a principle protected by itself, but are protected through the prism of fair and equitable treatment clauses in investment treaties, and therefore analyzed through this legal standard on a case by case basis. Along the same lines as EU law, legitimate expectations are often quoted through, or in parallel with, transparency and stability of the legal system, here again protected through the fair and equitable treatment standard. In the *Enron* case, it was stated that *"stability of the legal and business framework is an essential element of fair and equitable treatment"*[38]. In *TECMED v. Mexico* the arbitral tribunal considered that *"the Contracting Parties [must] provide international investment treatment that does not affect the basic expectations that were considered by the foreign investor to make the investment. The foreign investor expects the host State to act in a consistent manner, free from ambiguity and totally transparently in its relations with the foreign investor, so that it may know beforehand any and all rules and regulations that will govern its investments, as well as the goals of the relevant policies and administrative practices or directives, to be able to plan its investment and comply with such regulations"*[39].

Several awards quote it as an essential rule of protection of investors. Most of these awards describe examples where States intervene through their government or their central or decentralized administrations. In some rare occasions, arbitral tribunals were led to deal with the situation of « acts » (i.e. judgments) attributable to courts, as will be seen hereafter[40]. However, all awards which had to consider whether legitimate expectations of the parties should be considered to ground their claim against States can be analysed in the light of the question of reversal of case law before courts. The main reason lies in public international law principles, which admit that States can be held internationally liable for the acts of their judicial bodies, as seen above.

As can be imagined there is no single guideline. Most arbitral tribunals follow an *in concreto* assessment. In this sense, a right to protection based on legitimate expectations was recognized in various situations. For instance, when specific commitments were made by the State to the investor. In *TECMED v. Mexico*[41], the tribunal found that *"The foreign investor also expects the host State to act consistently, i.e. without arbitrarily revoking any preexisting decisions or permits issued by the State that were relied upon by the investor to assume its commitments as well as to plan and launch its commercial and business activities".*

It is possible however that the State did not make any specific commitment to the investor, but the change affects the general legal framework in the host State. In *Total v. Argentina* and *El Paso v. Argentina* it was held that the protection can be claimed *"even in the absence of specific promises by the government"* if the change was drastic *"in the essential features of the transaction*", in

particular *"for regimes which are applicable to long term investments and operations"*[42]. This is in particular the case if the legal framework that had been designed to attract investments is totally dismantled[43]. In *Suez & Vivendi v. Argentina* the tribunal decided that *"investors, deriving their expectations from the laws and regulations adopted by the host country, acted in reliance upon those laws and regulations and changed their economic position as a result (. . .). It was the existence of such expectations created by host country laws, coupled with the fact of investing their capital in reliance on them, and a subsequent sudden change in those laws that led to a determination that the host country had not treated the investors fairly and equitably"*[44]. In *Parkerings v. Lithunania,* it was admitted that the investor's expectations can be frustrated by the instability of the legal framework[45].

In the case *Eiser and Energia Solar v. Spain*, an ICSID tribunal considered that the investor was entitled to rely on regulation set by the State at the time of the investment[46]. The issue was in relation to the tariff set by the Spanish government for buying electricity produced by solar farms. The price level was aimed to encourage investment in this sector, which was an equivalent of subsidies. After the 2008 financial crisis and its consequences over States' booming debts, the Spanish government unilaterally reduced this tariff, which resulted in a significantly negative effect on the profitability of the sola companies' investment. Based on the *Methanex v. USA* award[47], Spain argued that the legislative changes introduced in the sector were an expression of its sovereign right to regulate and maintained that there was no acquired right to a tariff. Along the same lines as in the case *Suez Vivendi v. Argentina*, which was invoked by the claimant, the tribunal admitted that the investor was entitled to rely on the price set at the time of the investment and condemned the State accordingly[48]. The tribunal admitted the respondent's view that *"While the investor is promised protection against unfair changes, it is well established that the host State is entitled to maintain a reasonable degree of regulatory flexibility to respond to changing circumstances in the public interest. Consequently, the requirement of fairness must not be understood as the immutability of the legal framework (. . .)"*. However, it considered that the regulatory change did not consist only in a reasonable reduction of the tariff but was so drastic to induce huge losses for the investors that could not have been anticipated at such a scale.

In *PSEG Global Inc. v. Turkey*, the tribunal recognized that the State's right to modify the legal background could be detrimental to the investor if those changes were constant to a point where they harmed the basic planning of the investment: the tribunal *"finds that the fair and equitable treatment was seriously breached by what has been described above as the "roller-coaster" effect of the continuing legislative changes"*. In the same judgment, the tribunal conceded that the change can stem from a moving interpretation of the law or the conditions of applicability of the law[49].

However, the parties' expectations must be seen from an objective legitimate and reasonable standpoint rather than "single-mindedly" through the Claimant's subjective expectations[50]. The investor's fair expectations cannot fail to consider parameters such as business risk or industry's regulatory patterns. Accordingly, *"the investor must anticipate that the circumstances could change, and thus structure its investment in order to adapt it to the potential changes of the legal environment"*[51]. The level of development of the country where the investment was made must be considered. One should reasonably expect legislative changes in developing countries[52]. In *Parkerings v. Lithuania* the tribunal rejected the investor's claim, conceding that the legal framework in Lithuania was in constant change, a fact the investor should have anticipated because Lithuania was a transitional economy stepping out of communism at the time of the investment. The investor had taken a business risk which the investor should have anticipated by negotiating a stabilization clause with the State[53]. Therefore, the tribunal considered that the State had not acted unfairly, and there was no breach in the equitable treatment obligation set by the treaty. Such changes should be anticipated in some industries which are more subject to changes due to evolution of technology.

The investor's rights to a stable legal environment should not be interpreted as a denial of the State's authority and right to adapt the legislative context and make reforms. In *Saluka BV v. Czech Republic*,[54] it was held that *"it is now established in international law that States are not liable to pay compensation to a foreign investor when, in the normal exercise of their regulatory powers, they adopt in a non-discriminatory manner bona fide regulation that are aimed at the general welfare*". The State should therefore be able to defend the change by substantiating the goals in terms of general welfare

through means that are not discriminatory. In a way, investor should reasonably expect that a change can happen. The question is which change can be reasonably anticipated for a normal investor in a given context? In *Eureko BV v. Slovakia* the Slovakian State had modified the legal background regulating its health system to make it non-profitable to private operators[55]. Private insurance was not prohibited as such, but the reform instituted measures that were equivalent to a ban on profits. This rendered this market non-profitable to operators. The tribunal considered that this measure was not an expropriation and could not be considered as discriminatory (it applied to all insurance actors in Slovakia). Therefore, it admitted that the State was free to enact reforms in the interest of welfare. However, it considered that Eureko BV, a foreign investor, had not been able to anticipate a change in a way so drastic that its investment would be totally ruined because of a ban on profits in this sector: *"the tribunal is satisfied that the ability to distribute profits (. . .) [was] an essential precondition of Eureko's decision to invest in the Slovak Republic (. . .). It accepts that, while Eureko's management were aware of the possibility of far-reaching reforms being introduced in the organization of health insurance in the Slovak Republic after the 2007 election, they were not aware that such reforms would include a ban on profits and a ban on transfers that would prevent the realization of any profits from their investment"*. The tribunal underlined that the reform voted by the government was by itself incompatible with the notion of investment: *"to characterize expenditure on the establishment of a business operation in another State as an "investment" necessarily implies the right to enjoy the possibility of a return on the investment, if it proves profitable. Locking in accrued profit is incompatible with that right"*. Therefore, it considered that the measure was a violation of the dispositions of the BIT regarding fair and equitable treatment.

b) . . . and its extension to the overruling of precedents by courts in the host State.

The above principles have recently found interesting applications in the context of overruling of precedents by State courts.

In *ADF Group v. USA*, the claimant asserted that he was entitled to rely on existing case law from the State Courts at the time of the investment and that this case law was stable and continuous[56]. Although the tribunal denied that the change affected the claimant, the tribunal did not reject this assertion but rather considered that the case law which was invoked by the investor was not applicable to his situation. An *a contrario* interpretation of this case reasonably allows for a principle that an investor could count on a stable and continuous legal context created by consolidated precedents, if they are relevant to the situation at hand at the time of the investment, and therefore give rise to a liability of the State whose Courts have reversed their prior well-established precedents.

In *Elly Lilly v. Canada* this analysis was conceded in a clearer expression[57]. In this case, the investor openly argued that the State was liable because of its Courts, based on an overturn of their prior precedents, on which he asserted he was entitled to rely at the time of his investment.

The arbitral tribunal first admitted that the State can be liable for the acts of its Courts. It also conceded that there can be reasonable expectations of the investor based on the law applicable at the time of the investment, and that these expectations can be jeopardized in case of *"dramatic change in the law"*. It did not take part in the somewhat theoretical debate on the qualification of case law as a constitutive part of law[58]. The arbitrators rather focused on whether the claimant was right to rely on Courts precedents. However, in this situation, the claim was dismissed, as they considered the overturn could have been anticipated by a diligent investor. The tribunal was persuaded by Canada's evidence, which included client alerts issued by the investor's outside counsel in the arbitration that there was an incremental and evolutionary change in Canadian law. The arbitrators noted that the investor had access to doctrinal writings available which announced a possible change in case law, and therefore could not claim this change was unexpected. One finds there a similar approach as the one used in the *"prudent trader"* criterium[59].

The lessons learned from these decisions are that arbitrators are usually inclined to recognize that States can potentially be held liable for the acts of their courts when their judgments harm legitimate expectations of investors based on precedents that are overturned in a way that constitutes a drastic change of the legal framework. The condition is that the investor should be able to demonstrate that he could legitimately rely on a legal

context grounded on stable precedents and that he had no reasons to anticipate that they could be overturned based on a reasonable a careful assessment of the legal context at the time of the investment.

4. Dualism and its consequences: a case of discrimination between foreign investors and nationals of the host State?

As seen above, domestic States usually admit no liability towards parties who may have been frustrated in their rights because of an abrupt change of case law by their local courts. Therefore, if international treaties lead to sanctioning the same States - thus benefitting foreign investors who can base their claims on those treaties - the same act may potentially bring different sanctions in domestic legal systems of law and in the sphere of public international law.

This is not surprising if one admits the predicate of dualism in international law, which finds acceptable a discrepancy between the domestic and international systems in the application of the rule of law.

It also enhances the difference between the treatment given to nationals of the host State and investors from foreign States who satisfy foreign nationality requirements to benefit from the protection of a treaty in the same host State. As such, it is at the heart of recent criticisms raised against investment treaties underlining that "*international standards of protection may be greater than those available to nationals under the host State's constitutional or administrative law*"[60].

This discrepancy is also harshly illustrated in the integrated legal and economic system of the European Union which led to a ban on bilateral investment treaties within the EU sphere in the *Achmea* judgment rendered by the ECJ[61].

One of the contradictions was pointed out in relation to the prohibition of discrimination set by EU law, based on article 18 of the TFUE (European Treaty) which prohibits discrimination between nationals of EU States and is a cornerstone of the main principles of freedom of transit of services and goods within the EU. Some have claimed that this principle should apply both ways, in other words that not only should foreign EU investors be given the same treatment as local investors within the host State, but also that foreign EU investors *should not be treated* better than the nationals of the host State (doctrine of "reverse discrimination").

This raises the question of the compatibility of some of the principles based on bilateral investment treaties, as discussed above in relation to the sanction of legitimate expectations by the prohibition of discrimination in EU law. If the foreign investor is an EU national, why would he find himself in a better position than other nationals of the State where he invests? Why should he be protected against an overturn of a well-set precedent while nationals of the same State are not protected by the host State's administrative and constitutional law?

This argument of reverse discrimination is not condoned by the ECJ, which considers that the State cannot impose local rules on foreign EU investors if those rules constitute a restriction on freedom of transit of goods and services[62]. More specifically concerning the compatibility of investment treaties with EU Law, in the case *Achmea BV v. Slovakia*, the Attorney General Wathelet pleaded that the Slovakia-Netherlands bilateral investment treaty does not discriminate between EU members according to their nationality[63]. The Attorney General held that all nationals of the EU are entitled to ground a claim on their respective investment treaty signed with Slovakia. Therefore, article 18 of the TFUE (European Treaty) is not obstructed. However, in its judgment rendered on March 6, 2018 the Court does not follow the conclusions of the Attorney General, but for different reasons not strictly based on the discrimination argument.

Our view is that nationals of the host State can hardly insist that they should be given the same treatment as other EU foreign investors who can base their claims on an investment treaty. In the case *Knoors v. Staatssecretaris van EconomischeZaken*, the ECJ judged that the dispositions of the European treaty on freedom of service and establishment cannot be applied to purely internal legal situations. As stated by the Court it "*cannot be applied to situations which are wholly internal, in other words, where there is no factor connecting them to any of the situations envisaged by community law*"[64]. As observed by some authors, the principle of legal certainty, which is sometimes used by the ECJ to mitigate retroactivity, is typical to ECJ case-law and is not found in most domestic legal systems, including French law[65] Therefore, local nationals would not be able to ground a claim built on the argument that they are not given the

same treatment as those who satisfy foreign nationality requirements and can benefit from a treaty, because their local situation does not fall into the realm of EU law, as stated by the ECJ in the *Knoors v. Staatssecretaris van EconomischeZaken* case.

Despite this, the European Commission has repeatedly expressed its hostility to the recourse to bilateral investment treaties arbitration to sanction disputes arising between nationals of a EU State against another EU host State and supports negotiations for the establishment of a multilateral investment Court to settle investment disputes as an alternative to the existing network of investment treaties[66]. This bold political move was followed by the decision rendered by the ECJ in the case *Achmea BV v. Slovakia*, where the Court rejected the applicability of bilateral investment treaties in the relations between foreign EU investors and other EU States[67].

Seen from the theory of international law perspective, this bold reaction against the recourse to investment treaties between EU State members expresses a rejection of the dualism theory which characterizes public international law. As such it is consistent with a progressive attempt to build a legal system to rule UE as a unified integrated economic and legal entity.

However, it does not address the question of the protection of legitimate expectations of investors within the EU. As observed by some authors, it does not preclude the use of other forums, like the ICSID -whose awards do not require a local enforcement - to continue benefitting from the aforementioned treaties and executing them, including within the UE[68].

It also demonstrates that dualism is still a living concept in the theory of international law[69]. Potential discrimination between investors and nationals of the host State should therefore be seen as a normal consequence of dualism in international law. By the same token, the argument of discrimination in the host State between nationals and foreign investors does not exclude *per se* a potential liability of the host State towards a foreign investor whose legitimate expectations are frustrated by a radical overturn of case law decided by its domestic courts.

CONCLUSION

The principle of legitimate expectations has been recognized by EU law, the European Court of Human Rights, and most awards in investment arbitration cases as a principle of law.

Investment treaties can justifiably ground claims for violation of legitimate expectations based on an abrupt change of case law since the time of the investment took place in the host State, as long as certain conditions are met, in particular when it can be demonstrated that the change could not be reasonably anticipated by the investor.

Such change can be attributed to the State, because Courts are public bodies acting on its behalf.

This does not mean that States are prohibited from modifying their legislation, or that interpretation of law is fixed once and for all, but rather that judges and legislators should use every available tool to mitigate the consequences of the change in the best way possible so that investors can reasonably anticipate the change; if it is proven that the investors should have anticipated the change, they should not be able to claim their legitimate expectations were frustrated.

The discrepancy in the treatment of a same legal situation in the domestic law of the host State - which does not admit such liability towards parties frustrated by such change, but see it as a normal consequence of the authority attached to Courts to decide on cases while interpreting the law – and in the sphere of public international law through the application of investment treaties - where the same State can be held liable towards the investor – can be seen as a normal consequence of dualism in public international law.

Endnotes

1. See §3b.
2. *ADF Group Inc. V. the United States of America*, ICSID, ARB (AF) 00/1, award, 9 January 2003.
3. The dualist or pluralist view on the relationship between internal law and international law was initially presented by Triepel in his book "Volkerrecht and Landrecht" (Leipzig, 1899). It was later developed by other authors, in particular Anzilotti (Cours de droit international, 1921, reedited by LGDJ in 1999), Virally and Oppenheim (T.Olsen, P. Cassia, Le droit international, le droit européen et la hiérarchie des

normes, PUF, 2006, p.37); see also Pierre-Marie Dupuy and Yann Kerbrat, Droit international public, Dalloz, 2016, p.447 and seq. Dualism considers that between internal and international law there can be no conflict since internal provisions are applied exclusively within the State's borders and have no influence on the international legal system. International law cannot rule over the relationships between individuals at an internal level (B.Marian, The dualist and monist theories. International law's comprehension of these theories, http://revcurentjur.ro/old/arhiva/attachments_200712/recjurid071_22F.pdf).

4. In this study, we will take our examples from the French Civil law system.

5. F. Terré, Introduction générale au droit, Précis Dalloz, 10e édition, 2015, §360 and seq.

6. See in French theory Th. Bonneau, "Brèves remarques sur la prétendue rétroactivité des arrêts de principe et des arrêts de revirement », Dalloz, 1995, Chron., p.24; M. Troper and C. Grzegorczyk, « Precedent in France », in D. Neil Mac Cormick and Robert S. Summers (eds), Interpreting precedents: A comparative study (Aldershot : Dartmouth publishing Co, 1997), p.107.

7. See for instance, C. Com., 15 July 1986, Bull. Civ., IV, n°160, p.135, regarding the calculation of the interest rate of a loan.

8. Civ. 2, 8 July 2004, D. 2007, p.835, with a commentary of P. Morvan: « Le sacre du revirement prospectif sur l'autel de l'équitable »; see also another recent exemple of a judgment of the Supreme Court: Com., 21 March 2018, n°16-28.412, commented by N. Mathey in C.C.C, 2018, n°89.

9. P. Deumier, Introduction générale au droit, LDGJ, 4th Ed., 2017, n°435.

10. See for instance Molfessis, in RTDCiv, 2000, p. 670.

11. ECJ, 27 March 1980, *Denkavit*, n° 61/79, Rec. p. 1205; ECJ, 8 April 1976, *Defrenne*, n°43/75, Rec. p.455; ECJ, 17 May 1990, *Barber*, C-262/88; ECJ, 26 April 1994, *Roquette*, C-228/92, Rec., p.455; ECJ, 9 March 2000, *EvangelischerKrankenhausverein Wien*, C437-97.

12. See D. Pouyaud, « La responsabilité du fait du contenu d'une décision juridictionnelle », AJDA, 2008, p. 1178.

13. ECHR, 12 July 2018, *Allègre v. France*, 22008/12.

14. *ECHR, Atanovski v. Macedonia*, 14 January 2010, 36815/03; see also *Gorou v. Greece*, 11 February 2010, 12686/03; *Mamatkoulov and Askarov v. Turkey*, 4 February 2005, 46827/99 and 46951/99.

15. Cour de cassation, Ch. Mixte, 24 February 2017, D. 2017, p. 793, with a commentary from B. Fauvarque-Causson.

16. Dipti Khatri, Stare Decisis, Academike, January 12, 2015 (www.lawctopus.com/academike/stare-decisis/).

17. R. Dworkin, Law's Empire, Belknap Press (1986).

18. Jesse Wall, « Prospective overruling. It's about time » [2009] OtaLawRw7; (2009).

19. Ibid.

20. Ibid, quoting A Mason, 'Legislative and judicial law-making: can we locate an identifiable boundary?' [2003] AdelLawRw 4; (2003) 24 Adelaide Law Review 15, 21.

21. ECJ, case C-331/88 R v *MAFF c. Fedesa* (1990) ECR I-4023; C-345/06, *Heinrich*, Judgment of 10 March 2009, §44.

22. ECJ case C-107-97, *Max Rombi* (2000); ECJ case 175/78, *Saunders* (1979).

23. 1987 E. Comm. Ct. Rep. 1155.

24. ECJ, case 120/86, *Mudler v. Minister van Landbouwen Visseri* (1988).

25. ECJ, case 170/86, *Von Deetzen v. HZA Hamburg-Jonas* (1988).

26. ECJ, case C-164/97 and C-165/97.

27. ECJ case 43/75, *Defrenne* (1976); case 41/84, *Pinna I* (1986); case C-262/88, *Barber* (1990).

28. ECJ case 162/96, *Racke v. HZA Mainz* (1998).

29. ECJ case C 99/78, *Weingut Gustav Decker KG v. HZA Landau (1979)*.

30. ECJ case 74/74, *CNTA v. Commission* (1975).

31. *Van den Berg and Jurgens BV v/ Commission* above quoted.

32. On this subject, see E. Sharpston, European Community Law and The Doctrine of Legitimate Expectations:

How Legitimate and for whom? 11 Nw.J. Int.L. & Bus.87 (1990-1991).

33. This solution was also extended to issues where the State argued that the decision taken by its organ was illegal under its own law. In *SPP v. Egypt* (ICSID/ ARB/ 84/3), 20 May 1992 (§82 and seq.), the tribunal stated that *'it is possible that under Egyptian law certain acts of Egyptian officials, including even Presidential decree n°475, may be considered legally non-existent or null and void or susceptible of invalidation. However, these acts were clocked with the mantle of Governmental authority and communicated as such to foreign investor who relied on them in making their investment ».* One must add, however, that this solution should be followed unless the act is undoubtedly null according to the applicable law, or that the investor should have reasonably seen that the organ had no power to take such decision. In such situation, the investor cannot reasonably argue that he was misled by the act (see for instance *Framatome v. Atomic Energy Organization of Iran*, ICC award, 30 April 1982 (Journal du Droit International, 1984, p.58).

34. PCIJ, 25 May 1926; see also ICJ, *Barcelona Traction Light and Power Company,* 5 February 1970 (ICJ Reports 1970, p.3); *Compania de Aguas and Vivendi v. Argentina* (ICSID/ ARB/ 97/3), 21 November 2000.

35. *Metalclad v. Mexico* (ICSID/AF/ 97/1), 30 August 2000.

36. See ICJ, *Lagrand (Germany v/ United States of America*), 27 June 2001, ICJ Reports, 2001, p.466.

37. *CMS v. Argentina,* Ad hoc committee (ICSID, ARB/01/8), 25 September 2007, §89.

38. *Enron Corporation Ponderosa Assets v. Argentina* (ICSID, ARB/01/3), 22 May 2007, §239; see also *Enron,* above quoted*; LGE v. Argentina* (ICSID/ARB/ 02/1), 3 October 2006.

39. See also *Emilio Augustin Maffezini v. Spain* (ICSID/ ARB/97/7), 13 September 2000, §83; *Saluka BV v. Czech Republic* (CNUDCI), partial award, 17 March 2006, §309.

40. See §3b).

41. Above quoted.

42. *El Paso v. Argentina* (ICSID/ ARB/ 03/15), 31 October 2011.

43. *LGE v. Argentina* (ICSID/ARB/02/01), 3 October 2006.

44. *Suez & Vivendi v. Argentina* (ICSID/ ARB/ 03/19), 30 July 2010.

45. *Parkerings Companiets v. Lithuania* (ICSID/ARB/ 05/8), 11 September 2007, §321.

46. *Eiser and Energia Solar v. Spain* (ICSID/ARB/ 13/36), 4 May 2017.

47. *Methanex v. USA,* UNCITRAL, 3 August 2005.

48. *Suez & Vivendi v. Argentina* above quoted.

49. *PSEG Global Inc. v. Turkey* (ICSID/ARB/02/5), 19 January 2007, §254.

50. *Suez & Vivendi v. Argentina* above quoted.

51. *Saluka v. Czech Republic* (UNCITRAL, 2006), 17 March 2006; *Parkerings Companiets v. Lithuania*, above quoted.

52. J. Cazala, « La protection des attentes légitimes de l'investisseur dans l'arbitrage international », Revue Internationale de droit économique, 2009/1, t. XXIII, 1, p.5, §3.2.

53. *Parkerings Companiets v. Lithuania*, above quoted, §336.

54. *Saluka BV v. Czech Republic*, Above quoted.

55. Eureko BV (Achmea) v. Slovak State (PCA case n°2008/13), 7 December 2012.

56. *ADF Group Inc. V. the United States of America*, ICSID, ARB (AF)00/1, award, 9 January 2003, §72.

57. *Elly Lilly v. Government of Canada*, ICSID, case UNCT/14/2.

58. See §1.

59. See §2.

60. R. Wisner and N. Campbell, Bringing the Home State Back in: in the Case for Home State Control in Investor-State Dispute Resolution Settlement, (2018) 19 BLI, p. 6.

61. ECJ, *Achmea BV v. Slovakia*, n°C-284/16; See below.

62. ECJ, 18 February 1987, case 98/86, Rec., 1987, p. 809; ECJ, 7 February 1984, case 237/82, Rec., 1984, p. 483.

63. ECJ, Press Release n°101/17.

64. ECJ, *Knoors v. Staatssecretaris van EconomischeZaken*, 7 February 1979, C 115/78; see also ECJ, *La Reine c/ Saunders,* 28 March 1979, aff. 175/78, Rec. 1129; ECJ, *Omalet v/ Rijkdienst van SocialeZekerheid*, 22 December 2010, C-245/09.

65. P. Morvan, *« Le sacre du revirement prospectif sur l'autel de l'équitable »,* Rec. Dalloz, 2007, p. 835, §6.

66. L. Yong, « EU to begin negotiations for a multilateral investment court », Global Arbitration Review, 12 September 2017; Factsheet on the Multilateral Investment Court, European Commission, http://www.consilium.europa.eu/en/press/press-releases/2018/03/20/multilateral-investment-court-council-gives-mandate-to-the-commission-to-open-negotiations.

67. The discrimination argument had been discussed by the Attorney General Wattelet, as seen above. However, it was not the argument used by the ECJ to justify its decision to reject the application of bilateral investment treaties in the EU. The Court rather founded its decision on the idea that arbitration set up by bilateral investment treaties are not jurisdictions of national States, within the meaning of article 267 of the TFUE, and were not bound to refer interpretation of EU law to the ECJ. Therefore, the Court considered that they did not offer any guarantee of a unified application of EU law, and were therefore not compatible with EU Law.

68. As underlined by one author ICSID (S. Lemaire, Rev.Arb., 2018, n°2, p. 424, §48), the *Micula* case demonstrates that an incompatibility between ICSID arbitration and European Law could turn into the advantage of the latter.

69. See footnote 3. ■

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