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Fiscal Sovereignty and Investor-State Dispute Settlement

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The concept of sovereignty has commonly been traced back to the Peace of Westphalia, which ended the Thirty Years' War within the Holy Roman Empire in the 17th century. The Westphalian idea of sovereignty placed the state at the center of international relations, granting it absolute authority over its territory. However, today's understanding of sovereignty, a product of colonialism, 20th century wars, and contemporary globalization, has metamorphosed its Westphalian predecessor, subjecting states to international accountability. Non-state actors now occupy a pivotal position in international law: A prime example are foreign investors who benefit from a continually expanding territory of protection created by investment treaties, a crucial realm of which is access to investor-state dispute settlement. While investors often channel their legitimate grievances against a variety of sovereign conduct using this dispute settlement mechanism, on occasion, they also controversially misuse it as a backdoor to challenge measures that implicate a state's core fiscal policy. This Article argues that investor-state arbitral tribunals need to delimit the territory of investor protection by creating a jurisdictional dam to exclude specific matters that implicate the state's fiscal policy from attack in arbitration proceedings, in particular matters that are regulated through a state's legislative process and enactments concerning taxation measures. To this end, the Article presents several legal justifications, emanating notably from Article 31 of the Vienna Convention on the Law of Treaties, as to why such matters deserve the protection of a more stringent understanding and application of a general principle of "fiscal sovereignty," arguably the last bastion of the Westphalian legacy.

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Introduction

The creation of the modern state, and in turn its sovereignty, is often traced to the Peace of Westphalia in the 17th century, which ended the Thirty Years' War within the Holy Roman Empire between the Catholic Habsburgs and the Protestant princes of Germany. The peace was achieved through two treaties negotiated at the Congress of Westphalia, which saw delegates from ninety-six different sovereign entities represented.[1] The Congress, and the resulting peace, has been touted as "historic" in its ramifications on international relations.[2]

Regardless of whether this historical claim concerning the genesis of state sovereignty is accurate,[3] it is undisputed that by the middle of the 17th century,

1. Steven Patton, *The Peace of Westphalia and It Affects on International Relations, Diplomacy and Foreign Policy*, 10 Hists. 91, 92 (2019).

2. *See* Wyndham Bewes, *Gathered Notes on the Peace of Westphalia of 1648*, 19 Transactions Grotius Soc'y 61, 67 (1933).

3. Certain historians question the claim that state sovereignty, as a concept, can be traced back to the Peace of Westphalia, arguing that the concept of sovereignty began taking its current shape only in the 18th century. *See* Andreas Osiander, *Sovereignty, International Relations, and the Westphalian Myth*, 55 Int'l Org. 251, 262 (2001); Jonathan Havercroft, *Was Westphalia "All That"? Hobbes, Bellarmine, and the Norm of Non-Intervention*, 1 Glob. Constitutionalism 120, 121 (2012). Others trace the modern state defined by the principle of exclusive sovereignty over a bounded territory to the "fiscal crisis of medieval European feudalism, which by the 14th and 15th centuries was increasingly incapable of raising sufficient revenues to support the

the sovereign state became the central subject of legal and political commentary in international relations (which, at the time, was dominated by Western European scholarship).[4] A clear example of this is found in Chapter XVIII of Thomas Hobbes' *Leviathan,* published in the wake of the English Civil War in 1651, which constituted a pioneering attempt to delineate a sovereign's rights. Among a state's twelve principal rights, Hobbes' ninth right pertained to a state's sovereign right to tax: "Ninthly, is annexed to the Soveraignty, the Right of making Warre, and Peace with other Nations, and Common-wealths; that is to say, of Judging when it is for the publique good, and how great forces are to be assembled, armed, and *payd for that end; and to levy mony upon the Subjects, to defray the expenses thereof*."[5]

Hobbes positioned a state's right to levy money or taxes upon its subjects in the company of its right to make war and peace. This association is neither outlandish nor forced. Indeed, without the ability to raise revenues, a state is unable to engage in its most elemental functions: administering justice, defense, education, and healthcare; protecting the environment; building and maintaining infrastructure; and undertaking other fundamental tasks of statehood.[6] Moreover, in addition to being revenue-generating instruments, taxes also reflect a state's socio-economic ideologies on the distribution of wealth and income.[7] Therefore, there is an intrinsic connection between the nature and functioning of the state and its right to design its fiscal policy, including by levying taxes. In 1918, the political economist Joseph Schumpeter best articulated this proposition when he noted that "[t]axes not only helped to create the state. They helped to form it."[8] The term 'fiscal sovereignty' in this Article refers to this existential link between a state's sovereign being and its right to design its fiscal policy.

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mounting expenses of warfare." Roland Paris, *The Globalization of Taxation? Electronic Commerce and the Transformation of the State*, 47 Int'l Studs. Q. 153, 154 (2003).

4. There is a school of thought that disputes the relevance of the very notion of sovereignty to the plethora of indigenous communities that came to be colonized on the basis of justifications rooted in Westphalian sovereignty. Scholars of this school seek to distinguish the legal foundations of Westphalian sovereignty from the social and cultural foundations of indigenous sovereignty. *See* Taiaiake Alfred, *Sovereignty*, *in* Sovereignty Matters: Locations of Contestation and Possibility in Indigenous Struggles for Self-Determination 33, 33–36 (Joanne Barker ed., 2005). *See generally* Vine Deloria Jr., *Self-Determination and the Concept of Sovereignty*, *in* Native American Sovereignty 107 (J.R. Wunder ed., 1996).

5. Thomas Hobbes, Leviathan 138 (W.G. Pogson Smith ed., 1909) (emphasis added).

6. Jennifer Bird-Pollan, *The Sovereign Right to Tax: How Bilateral Investment Treaties Threaten Sovereignty*, 32 Notre Dame J.L. Ethics & Pub. Pol'y 107, 119 (2018).

7. *See* Sol Picciotto, International Business Taxation: A Study in the Internationalization of Business Regulation xiii (1992).

8. Joseph A. Schumpeter, *The Crisis of the Tax State*, *in* The Economics and Sociology of Capitalism 99, 108 (Richard Swedberg ed., 2020).

In light of the foundational nature of a state's fiscal sovereignty, the state has an interest in preserving, to the maximum extent possible, its exclusive authority to create, orient, and modulate its fiscal regime. However, in the past several decades, several limitations have been imposed upon states' fiscal sovereignty: some in the form of voluntary self-impositions and others in the form of involuntary burdens that are a product of market forces. One such involuntary burden—which states may have been surprised by[9]—came in the form of investor-state dispute settlement ("ISDS"), which is typically conducted through international arbitration proceedings instituted by investors against a state on the basis of their acceptance of the state's offer to arbitrate, as articulated in bilateral and multilateral investments treaties ("BITs" and "MITs"). This Article argues that ISDS arbitral tribunals have on several occasions, in the garb of exercising jurisdiction over investment disputes, overreached their mandate and inappropriately interfered with the host states' fiscal sovereignty on several occasions. Arbitral tribunals' laissez-faire exercise of jurisdiction is as much a function of open-ended drafting of BITs and MITs as it is a product of the tribunals ascribing generous interpretations to these BITs or MITs. This is unsurprising since ISDS, as a method of dispute resolution, was always emblematic of the moderate and interdependent version of sovereignty that exists in today's globalized world—as opposed to its more chiseled Westphalian predecessor. Still, it is imperative to critically examine the expansive jurisdictional distance that ISDS arbitral tribunals have traversed. As Toby Landau, KC, remarked in his recent award-winning 2023 Alexander Lecture at the Chartered Institute of Arbitrators, ISDS arbitral tribunals have left several "scars" along the way while going from ruling on "good old fashioned forms of investment" such as construction and infrastructure projects and "good old fashioned forms of state interference" such as direct expropriation or a clear denial of justice to now sitting in judgment of many "sensitive areas of sovereign discretion" such as healthcare, economic policy, and climate change.[10]

9. We may see evidence that states were surprised by this burden through recent state practice surrounding ISDS. Over the last decade, several states have proffered a "reformed approach to investment dispute settlement," abandoning the typical method of ISDS, i.e., international arbitration proceedings, and replacing it with either an "investment court system", which is the European Union's policy since 2015, *see Reform of the ISDS Mechanism*, Eur. Comm'n, https://policy.trade.ec.europa.eu/enforcement-and-protection/dispute-settlement/investment-disputes/reform-isds-mechanism_en [https://perma.cc/4PDW-63GE] (last accessed Apr. 14, 2025), or with State-State dispute settlement, i.e., international arbitration proceedings conducted between the home State and the host State of the investment, *see, e.g.*, Agreement on the Promotion and Protection of Investments, Austl.-U.A.E., Nov. 11, 2024, *available at* https://investmentpolicy.unctad.org/international-investment-agreements/treaties/bits/5161/australia---united-arab-emirates-bit-2024- [https://perma.cc/M7LK-446Z] (not yet in force).

10. Alison Ross, *The Scars Left by ISDS*, Glob. Arbitration R. (Apr. 12, 2024), https://globalarbitrationreview.com/article/the-scars-left-isds [https://perma.cc/CWS2-GNUQ].

This Article will first examine, from Part I onwards, the principle of fiscal sovereignty through the prism of how the concept of sovereignty has evolved over time. Against this backdrop, Part II will argue that fiscal sovereignty should be considered a general principle of international law, which should be considered while interpreting international treaties, including BITs and MITs, regardless of whether the treaty in question contains a so-called "tax carve-out." Throughout, this Article will also critique the methods of interpretation currently employed by ISDS arbitral tribunals to interpret these tax carve-outs, and show how these tribunals have, on many occasions, trespassed impermissibly into host states' fiscal sovereignty. Finally, this Article submits that ISDS arbitral tribunals should act with restraint when faced with an investor-state dispute that directly implicates a state's fiscal sovereignty.

I. Fiscal Sovereignty and Its Limitations

This Part outlines the theoretical foundation of the Article's argument. Section A provides a historical evolution of the concept of sovereignty from a normative lens. Section B defines and places the concept of fiscal sovereignty within that historical framework, while addressing the possible limitations that may be imposed on a state's fiscal sovereignty.

A. Evolution of the Concept of Sovereignty

Sovereignty has been referred to as "the most important . . . structural principle of international law that shapes the content of nearly all rules of international law,"[11] while also being criticized for being a quintessentially "European term and idea" that has been force-fit into "cultures that had their own systems of government since the time before the term *sovereignty* was invented in Europe."[12] Both characterizations of the concept of sovereignty are pertinent and speak to its multi-faceted nature.[13] Indeed, as noted by American political scientist Professors Michael Ross Fowler and Julie Marie Bunck, sovereignty may be viewed as a "chunk" or a "basket" of rights that do not necessarily go together.[14]

Over time, there have been several definitional strings attached to the cloth of sovereignty. There exists at the same time the notion of domestic or internal sovereignty, which refers to "authority structures within states and the ability of

11. Franz Xaver Perrez, Cooperative Sovereignty from Independence to Interdependence in the Structure of International Environmental Law 13 (2000).

12. Alfred, *supra* note 4, at 39 (emphasis in original).

13. Bardo Fassbender, *Sovereignty and Constitutionalism in International Law*, *in* Sovereignty in Transition 115, 139–43 (Neil Walker ed., 2003).

14. Michael Ross Fowler & Julie Marie Bunck, Law, Power, and the Sovereign State: The Evolution and Application of the Concept of Sovereignty 116–17 (1995).

these structures to effectively regulate behaviour," as well as international legal sovereignty, which refers to "recognition . . . accorded to juridically independent territorial entities which are capable of entering into voluntary contractual agreements" in the form of treaties.[15] International relations theory also presents several distinct approaches to viewing sovereignty. The so-called constructivist approach views sovereignty as a dynamic "social construct."[16] The classical realist and structuralist approaches view sovereignty as a fixed construct based on discernible elements, such as territory and political independence.[17] The neo-realist and neo-liberal schools of thought, by contrast, have sought to contextualize how a sovereign state can be considered to be functionally separate from its counterparts in the modern world.[18]

These seemingly varied conceptions of sovereignty owe their allegiance, in different measures, to the overarching cloud of Westphalian sovereignty, which was rooted in the treaties emanating from the Peace of Westphalia, described by G. W. F. Hegel as "one of the most important basic laws governing the possession of any state."[19] It was this Westphalian idea of sovereignty that placed the modern nation-state at the center of international law and granted the state absolute authority over its territory and its people. In particular, Westphalian sovereignty is understood to have created three building blocks of sovereignty. First is the absolute authority that a state possesses over its territory (which came to be known as internal sovereignty). Second is the independence of a state from foreign interference (which, to varying degrees, is reflected in the realist notions of sovereignty as well as its neo-realist and neo-liberal variants). Third is the equality of states, which formed the foundation stone of international law.[20]

When understanding the concept of sovereignty, it is important to pay homage to its historical Westphalian foundations. However, it is equally important to adapt that understanding beyond those foundations and examine how it has bent to subsequent historical contexts. The Westphalian idea of sovereignty grew in prominence at the impetus of several philosophers from the 16th through the 20th century, including Emmerich de Vattel, Christian Wolff, and Thomas Hobbes.[21] However, in the 21st century, the Westphalian

15. Stephen D. Krasner, *Rethinking the Sovereign State Model*, 27 Rev. Int'l Studs. 17, 21 (2001).

16. Navid Pourmoukhtari, *A Postcolonial Critique of State Sovereignty in IR: The Contradictory Legacy of a 'West-Centric' Discipline*, 34 Third World Q. 1767, 1783 (2013).

17. *Id.* at 1782.

18. *See generally* Hidemi Suganami, *Understanding Sovereignty through Kelsen/Schmitt*, 33 Rev. Int'l Studs. 511 (2007).

19. Will Hickey, The Sovereignty Game: Neo-Colonialism and the Westphalian System 13 (2020).

20. *Id.* at 3.

21. *See* Krasner, *supra* note 15, at 20.

notion of sovereignty, propagated by these philosophers, has been criticized for being "a narrow Eurocentric and one-size-fits-all perspective that has inspired and replicated the practice of sovereignty as an absolute and enduring feature of the modern state."[22] This shift in mindset is largely attributable to the end of the two World Wars and the development of post-colonial narratives of international law. After all, the concept of sovereignty, which developed pursuant to the Peace of Westphalia, has been used as much to define the parameters of international law as to justify the colonial conquest of territories where indigenous communities had been living for centuries, if not millennia. In noting this connection, it warrants further mentioning that some post-colonial scholars have attempted to advance distinct underpinnings to the concept of sovereignty, for instance, "indigenous sovereignty," which positions sovereignty as "not purely a legal source of political authority, but rather a social and cultural way of defining community."[23] However, most post-colonial representations of sovereignty, be it the constructivist, the neo-liberal, or the neo-realist, continue to develop under the foundational epithet of Westphalian sovereignty, which constitutes an "enduring feature" of global reality.[24]

It is also important to bear in mind that in the previous century Westphalian sovereignty has been critiqued as being inadequate "in an interdependent world," where cross-border trade and commerce—and, in turn, influence—is inevitable.[25] Some scholars have proposed that the non-interventionist notions of Westphalian sovereignty should be diluted, resulting in what has been referred to as 'interdependent sovereignty.' Proponents of this concept argue that sovereignty, as traditionally understood, "is being eroded by globalization resulting from technological changes that have dramatically reduced the costs of communication and transportation," which renders the state unable to "engage in activities that have traditionally been understood to be part of their regulatory portfolio."[26] Others advance the view that, since it is impossible to dilute the non-interventionist notions intrinsic to Westphalian sovereignty, the time is ripe to "drop the anachronistic idea of Westphalian sovereignty and replace it with the notion of 'sovereignty as responsibility,'" which views sovereignty as a bundle of rights and obligations.[27] Either way, these criticisms of Westphalian sovereignty seek to predicate the concept of state sovereignty on interdependence rather than independence and global cooperation.

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22. Pourmoukhtari, *supra* note 16, at 1776.

23. Harald Bauder & Rebecca Mueller, *Westphalian vs Indigenous Sovereignty: Challenging Colonial Territorial Governance,* 28 Geopols. 156, 165 (2021).

24. Pourmoukhtari, *supra* note 16, at 1784.

25. Peter Dietsch, *Rethinking Sovereignty in International Fiscal* Policy, *in* Catching Capital: The Ethics of Tax Competition 167, 173 (2015).

26. Krasner, *supra* note 15, at 19.

27. Dietsch, *supra* note 25, at 175.

It would be remiss at this juncture to not also discuss the contribution of Austrian philosopher Hans Kelsen to the development of this line of thought in the previous century. Kelsen most famously introduced the philosophical conundrum of the *grundnorm*, which intended to examine whether positive international law logically precedes the national legal systems in the hierarchy of norms. Kelsen left the conundrum unresolved (although, according to some scholars, he sympathized with the prioritization of international law).[28] That notwithstanding, Kelsen envisaged the possibility that international law could precede national legal systems and, in such a situation, stated that "the conclusion is also drawn that the sovereignty of the state is fundamentally limited, making possible the efficacious organization of world law."[29] This conclusion, per Kelsen, plays a "decisive role . . . within the political ideology of pacifism" as distinct from the political ideology of imperialism, which is given an impetus if national legal systems precede international law.[30]

It is apparent from the above that within the basket of sovereignty reside several ingredients that co-exist, albeit not necessarily in normative harmony. Indeed, the paradoxical nature of sovereignty is that it's very exercise on the international plane often limits its scope. While seemingly contradictory, this is an inherent feature of the "organized hypocrisy" that is sovereignty.[31] Accordingly, delineating the contours of the notion of sovereignty in today's post-colonial, interdependent world is a delicate balancing act. On the one hand, force-fitting the pre-colonial framework of state sovereignty onto newly independent former colonial states is not an equitable solution, as it is representative of the so-called post-colonial mission "to civilize those considered uncivilized" and to "entrench a formidable West-centric ideology" into the practice of international organizations, such as the United Nations, the International Monetary Fund ("IMF"), and the World Bank.[32] On the other hand, to disentitle newly independent colonized states from benefiting from the discernable advantages of non-interventionism that stem from the Westphalian origins of sovereignty also amounts to a convenient, cherry-picked conceptualization of the concept. This sentiment rings true in the words of Algerian jurist, Mohammed Bedjaoui, who, while pointing out the hypocrisies surrounding the differential application of similar notions to European and non-European states in the wake of decolonization, stated that "it is ironical to see how the same imperial Powers of the nineteenth century which, in their colonial policies, vigorously denied the existence of any rule . . . have felt able, in connexion [sic] with the reverse

28. Suganami, *supra* note 18, at 518–20.

29. Hans Kelsen, *Sovereignty*, *in* Normativity and Norms: Critical Perspectives on Kelsenian Themes 525, 532 (Stanley L. Paulson & Bonnie Litschewski Paulson eds., 2007).

30. *Id.* at 535–36.

31. Krasner, *supra* note 15, at 19.

32. Pourmokhtari, *supra* note 16, at 1777.

modern phenomenon of decolonization, to demand the application of the same [rule] that they once sought to emasculate."[33]

To lay down a definitive understanding of sovereignty falls beyond the realm of this Article. However, in order to meaningfully discuss the central theme of this Article, i.e., fiscal sovereignty, which exists as a subset within the basket of sovereignty, it is incumbent to recognize that the notion of sovereignty should be evolutively construed to accommodate within this basket its Westphalian foundations as well as certain inevitable ingredients of interdependence arising out of today's juridico-political climate. One such ingredient is the increasing role of non-state actors on the international plane, a prime example of which are foreign investors who, in the past few decades, have been afforded the right to directly sue sovereign states in international arbitration proceedings; a right they have exercised extensively.

B. Fiscal Sovereignty

One of the most fundamental features of a state's sovereignty is its authority to levy taxes to finance itself.[34] Scholars and philosophers have long acknowledged this, starting with Hobbes' enumeration of the principal rights associated with state sovereignty, going to Jean Bodin's statement that taxation constitutes the "financial nerves of the state,"[35] and articulated, more recently, in Michel Focault's writings.[36]

Indeed, a state can perform none of the other functions associated with its being without raising revenue, tying a state's existence closely to its so-called "fiscal sovereignty." The term "fiscal sovereignty" has been subjected to several related definitions. Professor Ilias Bantekas, one of the few who has forayed into defining the term, describes it as states' freedom "to choose when and how to finance themselves."[37]Another international fiscal law specialist, Professor Arnold Knechtle, characterizes it as "the non-derivative sovereignty of a state, which is in principle internally as well as externally unlimited, and which manifests itself vis-à-vis other states in exercising sole (exclusive) authority in

33. Mohammed Bedjaoui (Special Rapporteur on the Economic and Financial Acquired Rights and State Success), *Second Rep. on Succession of States in Respect of Matters Other than Treaties*, ¶ 91, U.N. Doc. A/CN.4/216/Rev.1.

34. Allison Christians, *Sovereignty, Taxation and Social Contract*, 18 Minn. J. Int'l L. 99, 104 (2009).

35. *See* Mireille Abelin, Fiscal Sovereignty: Reconfigurations of Value and Citizenship in Post-Financial Crisis Argentina 72 (2012) (Ph.D. Dissertation, Columbia University) (on file with author).

36. *Id.* at 87 (discussing how Focault wrote that "[t]he fundamental objective of governmentality will be . . . state intervention with the essential function of ensuring the security of the natural phenomena of economic processes or processes intrinsic to population.").

37. Ilias Bantekas, *The Contractualization of Fiscal and Parliamentary Sovereignty: Towards a Private International Finance Architecture?*, 11 Glob. Constituionalism 139, 144 (2022).

respect of acts of legislation, administration and justice within its territorial power sphere."[38] The United Nations Conference on Trade and Development ("UNCTAD") defines fiscal sovereignty as "the jurisdiction to tax . . . based on the domestic legislative process, which is an expression of national sovereignty, thus heightening the sensitivity of the surrounding issues. There are no restrictions under international law to the legislative jurisdiction to impose and collect taxes."[39]

These conceptions of fiscal sovereignty have undertones of the traditional Westphalian understanding of sovereignty. Across them, one can draw a consistent line of thought that fiscal sovereignty constitutes, at a minimum, the state's exclusive jurisdiction to formulate tax rules as part of its fiscal policy without interference from other states, and, by extension, the authority to apply these tax rules and adjudicate disputes arising from the rules. In line with the UNCTAD's definition of fiscal sovereignty, the matters in respect of which a state's entitlement to formulate tax rules should typically be unfettered are matters that fall within its legislature's competence; as distinct from matters that fall within the rule-making competence of the executive.[40] After all, matters that require proper legislative scrutiny will typically lie at the heart of a state's fiscal policy, and thus would always warrant protection as part of the state's fiscal sovereignty. This idea of a chasm between matters of legislative policy and those that fall within the executive's competence will be discussed in greater detail below, particularly in the context of the purpose behind tax carve-outs often stipulated in BITs or MITs. At this stage, it suffices to note that the understanding of a state's unencumbered fiscal sovereignty to tax that this Article seeks to cover—what the international taxation law specialist Professor Tsilly Dagan refers to as "substantive tax sovereignty"—encapsulates "the ability of a political community to design its fiscal system in ways that support its collective self-determination," not based on "[t]he coercive power of

38. Arnold A. Knechtle, Basic Problems in International Fiscal Law 34 (1979).

39. U.N. Conf. Trade & Dev., Taxation, at 1–2, 7, U.N. Sales No. E.00.II.D.5 (2000).

40. Accordingly, the spate of executive orders issued by the President Donald Trump of the United States in early 2025, whereby President Trump seeks to unilaterally impose tariffs on import of goods and services from foreign states, are excluded from this general understanding of fiscal sovereignty. *See* Proclamation No. 14257, 90 Fed. Reg. 15041 (Apr. 7, 2025). This is principally because these tariffs are not (at least, at the time of this Article's publication) backed by a formal legislative process. *See id.* Moreover, tariffs may not be comparable to quintessential tax rules covered by a state's fiscal sovereignty, since they are intended as fiscal impositions on goods and services imported from foreign states, as distinct from taxes, which are typically intended as fiscal impositions on goods and services that derive value from the resources of the state imposing the taxes. Accordingly, the arguments presented in the Article should not be considered to cover such executive orders issuing tariffs.

the state" to tax, but on the exercise of "legitimate authority" best represented through legislative processes.[41]

Although not nearly enough has been written about the notion of fiscal sovereignty, scholars who have explored the subject generally agreed that fiscal sovereignty, as conceptualized above, is a domain of international law where "Westphalian sovereignty is still dominant,"[42] with some calling it the "last bastion" of Westphalian sovereignty.[43] Some scholars have sought to advance the counter-argument that, just as the broader notion of sovereignty has undergone a dilution in respect of other facets of state functioning in the modern world, the same dilution is warranted in the context of taxation. As a result, fiscal sovereignty should be viewed as a bundle of rights and obligations. With this change of lens, tax cooperation at a global level may be viewed as "required by, and conducive to, the protection of sovereignty," as opposed to being a constraint on it.[44] Relatedly, other scholars, such as Canadian political scientist Professor Roland Paris, have also asserted the so-called "globalization of taxation."[45] However, they also recognize associated limitations, clarifying that such globalization may not extend to components of a tax system intrinsic to the state's fiscal sovereignty.[46] For example, the rate of taxation, be it for direct or indirect taxation, is one such "fiercely defended component of each country's tax system . . . also the most subject to change, as well as the most political," which would be the "least likely to be completely harmonized" into a global perspective.[47]

41. Tsilly Dagan, *Substantive Tax Sovereignty Under Globalization*, 29 Tilburg L. Rev. 1, 3 (2024).

42. Dietsch, *supra* note 25, at 180.

43. Itai Grinberg & Joost Pauwelyn, *The Emergence of a New International Tax Regime: The OECD's Package on Base Erosion and Profit Shifting (BEPS)*, 19 Am. Soc'y Int'l L. Insights (Oct. 28, 2015), https://www.asil.org/insights/volume/19/issue/24/emergence-new-international-tax-regime-oecd's-package-base-erosion-and [https://perma.cc/TV73-GZ9K].

44. Dietsch, *supra* note 25, at 187.

45. Paris, *supra* note 3, at 153.

46. *Id.* at 174 (recognizing that "[c]oncerns about *popular* sovereignty might . . . generate opposition to the transnational harmonization of tax policy" (emphasis in original)); Insop Pak, *International Finance and State Sovereignty: Global Governance in the International Tax Regime*, 10 Ann. Surv. Int'l & Compar. L. 165, 205 (2004) (Even though there has been a dilution of Westphalian sovereignty in the domain of fiscal policy, "[n]evertheless, nation-states are, and will remain the main actors in international economic affairs under international law.").

47. Yariv Brauner, *An International Tax Regime in Crystallization*, 56 Tax L. Rev. 259, 283 (2003).

Regardless, there is no doubt the notion of taxation has undergone a transformation from the time Hobbes imagined it as a hierarchical social payment linked to military sacrifice. Today, taxation has become the expression of what has been christened the "juridico-political" contract between the state and its subjects that forms the connection between the state's economy and its sovereignty.[48] Further, given the advent of globalization and the ensuing flow of capital, there is a need for tax harmonization to ensure that sovereign states can coordinate, especially to exchange information and apportion tax bases so as to avoid tax evasion loopholes that permeate the said juridico-political contract.[49] However, this transformation does not, and should not, entail an unencumbered dilution of a state's control over its fiscal policy, either by isolating the state's fiscal policy from its juridico-political sovereignty or from introducing limitations to the state's control over its fiscal policy without explicit or implicit consent. To that end, one scholar posits that a state's fiscal policy should be subsumed within the traditional juridico-political understanding of its sovereignty, i.e., sovereignty tied to the state's "territorial power and defense from external enemies," not least because delineating the state's fiscal policy from these facets of sovereignty does it disservice.[50] This is because a state cannot meaningfully retain the unencumbered sovereignty to regulate such elemental features of its statehood without a similar preservation of its sovereignty over its fiscal repositories, which are essentially a means to this end.

This is especially true for a developing world constituted by the formerly colonized states (representing the so-called "Global South"), which "have long struggled with dependence upon foreign debt and the establishment of monetary authority—even when they had juridico-political sovereignty."[51] This proposition is supported by a post-colonial historical analysis. In the previous century, especially after the Second World War ended, the formerly colonized states inherited their juridico-political sovereignty—in some cases, almost overnight—from their European colonizers. However, most, if not all the newly recognized states did not have a mature fiscal policy backing their sovereignty at the time. These states have had to develop, from the ground up, a fiscal policy that enabled growth and development. Through the process, these states have often had to completely "dispose of their sovereign decision-making power as well as their ability to make fiscal or other social policy" due to certain "structural or quantitative conditionalities" that are imposed upon them by Western, Euro-centric institutions, be it the developed states or institutions

48. Abelin, *supra* note 35, at 94–96.
49. *See* Pak, *supra* note 46, at 205.
50. Abelin, *supra* note 35, at 94–96.
51. *Id.* at 347.

such as the IMF, the World Bank, or the London and Paris Clubs.[52] The stark disparity between the financial state of affairs of the formerly colonized states and their former colonizers widens when one maps the history of the creation of tax havens, which is "intimately linked" to the decolonization process. Specifically, several of these tax havens were set up as overseas territories of colonizers starting in the 1950s to enable European capitalists to siphon off their capital to these havens, avoiding the high taxes in their home jurisdictions.[53] This resulted in the novel phenomenon of investments being routed into developing states through said tax havens, enabling capital exporters to avoid paying taxes to the developing states hosting their investments by, for instance, gaining capital based on the exploitation of natural resources of developing states but then declaring those gains, for the purposes of capital gains taxation, in tax havens (e.g., taking advantage of exemptions or reductions of source-based taxation for capital gains in developing states). Indeed, as one historian notes, the reason why "tax avoidance disproportionately drains the wealth of countries in the global South is that modern tax havens are quintessentially colonial and imperial institutions."[54]

In light of this post-colonial context, it is imperative that academic discourse on state sovereignty accounts for a state's (and particularly Global South states') control over its fiscal policy. This ensures that additional external limitations are not lightly imposed upon the state's fiscal sovereignty over their explicit, voluntary limitations or those that are market-induced. The following Section delineates the parameters of these limitations to fiscal sovereignty.

1. Voluntary Limitations to Fiscal Sovereignty

Voluntary limitations to fiscal sovereignty are those that states explicitly agree to for the purposes of international cooperation on taxation, including treaties known as double tax avoidance agreements ("DTAs"). At the time of writing, there are well over 3,000 such treaties.[55]

DTAs are detailed and technically complex legal instruments through which states agree on a cross-border dividing line where the exercise by one state of

52. Bantekas, *supra* note 37, at 150–54.

53. Examples of such tax havens, all of which are either formerly colonized territories or current dependencies of former colonizers, include the British Virgin Islands, Jersey and Guernsey, the Bahamas, Bermuda, the Cayman Islands, Mauritius, the Seychelles and Vanuatu.

54. Vanessa Ogle, *The End of Empire and the Rise of Tax Havens: How Decolonisation Propelled the Growth of Low-Tax Jurisdictions, with Lasting Economic Implications for Former Colonies*, New Statesman (Dec. 18, 2020), https://www.newstatesman.com/ideas/2020/12/end-empire-and-rise-tax-havens [https://perma.cc/4PDK-R5G4]; *see also* Vanessa Ogle, *Tax Havens: Legal Recoding of Colonial Plunder*, LPE Project (Oct. 11, 2020), https://lpeproject.org/blog/tax-havens-legal-recoding-of-colonial-plunder/ [https://perma.cc/C73X-68EJ].

55. *Tax Treaties*, OECD, https://www.oecd.org/tax/treaties/ [https://perma.cc/U4H4-JHG3] (last accessed Apr. 12, 2024).

its jurisdiction to tax overlaps with that of the other state. This dividing line is defined in what constitutes a DTA's core part: the 'distributive rules.' These rules have been developed and fine-tuned since the 1920s in models agreed upon in international forums such as the League of Nations and, currently, the Organization for Economic Cooperation and Development ("OECD")[56] and the United Nations.[57] Through their distributive rules, DTAs aim to ensure that the same income is not double taxed (i.e., by the source state and the residence state) to ensure certainty and to assure non-discrimination for investors. In essence, DTAs reflect a careful balance between the jurisdictional interests of the two states concerned in their alternating roles as residence state and source state.[58]

In addition to distributive rules, DTAs almost always contain a specific mechanism for tax dispute settlement, known as mutual agreement procedure ("MAP"). MAPs require tax authorities of the two states concerned endeavor to resolve a disputed case by mutual agreement with a view to eliminate taxation that is not in accordance with the DTA. Given the complexities of cross-border disputes on tax issues, states intend the MAP to make use of expert adjudicators.

Apart from DTAs, which are typically bilateral, states also embrace certain concessions on their fiscal sovereignty through multilateral agreements. These multilateral agreements, once executed, may result in (automatic) modifications to the scope or content of the DTAs that state parties to the multilateral agreements have signed. An example of this type of voluntary limitation to fiscal sovereignty is the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting ("BEPS MLI"), which was negotiated by several states in 2016 and 2017 via the OECD. Since then, around 1,900 DTAs that have been modified pursuant to the entry into force of the BEPS MLI.[59]

2. Market-Induced Limitations to Fiscal Sovereignty

Generally, market-induced limitations to fiscal sovereignty take one of two forms in today's globalized world: (1) those that states agree to as a means of encouraging foreign investments; and (2) those that states are compelled to

56. *See generally* OECD, Model Tax Convention on Income and on Capital: Condensed Version 2017 (10th ed., 2017), https://www.oecd.org/ctp/treaties/model-tax-convention-on-income-and-on-capital-condensed-version-20745419.htm [https://perma.cc/VV27-SRSS].

57. *See generally* U.N. Dep't of Econ. & Soc. Affairs, Double Taxation Convention Between Developed and Developing Countries, U.N. Doc. ST/ESA/PAD/SER.E/213, Sales No. xix.804 (2017).

58. Charles E McLure, *Globalization, Tax Rules and National Sovereignty,* 55 Bull. for Int'l Fiscal Documentation 328, 328–30 (2001).

59. *Azerbaijan Signs Landmark Agreement to Strengthen its Tax Treaties*, OECD (Nov. 20, 2023), https://www.oecd.org/tax/treaties/azerbaijan-signs-landmark-agreement-to-strengthen-its-tax-treaties.htm [https://perma.cc/TFD7-C7JC].

agree to because of their excessive, non-performing debts. Distinctly from voluntary limitations, these market-induced limitations typically do not operate under treaties negotiated and executed between states.

Examples of the first kind of market-induced limitations include reductions of the effective or statutory rates of taxation that apply to capital generated within the state. Source-based taxation, the classical method of taxation over residence-based taxation, might serve to discourage economic activity and investment. This is especially true for capital-importing states, such as countries in the Global South, where there already exists a perception of a higher amount of political and regulatory risk that makes foreign investors hesitant, if not reluctant, to invest. Thus, in order to attract investments, capital-importing states often reduce source-based tax rates on income derived from capital or other kinds of financial activities in the state. This, in turn, has a consequential impact on the overall tax structure and policy of the state in question, since the state could try to offset low tax revenues from foreign investments against other revenue generating opportunities from domestic income.[60]

The second kind of market-induced limitation typically leads states to seek monetary assistance from global financial institutions like the IMF, the World Bank, or the London and Paris Clubs. In exchange for financial assistance, states are often compelled to agree to institutionally imposed structural or quantitative conditionalities. The difference between such market-induced limitations and those of the former kind, however, is that when a state needs financial salvaging, their consent to the conditionalities imposed by the above listed institutions is, for all effects and purposes, fictitious. As Professor Ilias Bantekas explains, "[t]he international finance architecture is structured in such a way that developing states or states in distress are unable to make alternative choices."[61] This is because an over-indebted state could be facing any number of issues, including exclusion from private financial markets; imposition of extremely high interest rates on loans; and currency devaluation "to such an extent that it is internationally undesirable" so as to cause trade deficits.[62] Therefore, "in the absence of liquidity and constant pressure, indebted states are forced to submit to the demands of their creditors in the form of conditionalities."[63] While these conditionalities—structural as well as qualitative—may take the shape of agreements or memoranda of understanding that appear to be negotiated between the debtor and creditor, "in practice the negotiating power of the debt is diminished significantly, if not outright extinguished."[64]

60. McLure, *supra* note 58, at 328–30.
61. Bantekas, *supra* note 37, at 149.
62. *Id.*
63. *Id.*
64. *Id.*

The types of structural conditionalities that a debtor state may be compelled to consent to include political, legislative, and institutional reforms.[65] A good example is the post-2010 bail-out deal that Greece was constrained with, which included conditionalities such as transferring parliamentary powers and decision-making authority, including decisions on fiscal policy, to "a supervisory authority known as the 'troika' and composed of the European Union (Commission), the European Central Bank, [and] the IMF."[66] The types of quantitative conditionalities that a debtor state may be subjected to include "the achievement of macroeconomic targets, such as the reduction of fiscal deficits and the accumulation of international reserves."[67] The objectives that the IMF has recently set for states such as Pakistan, Sri Lanka, and St. Kitts and Nevis exemplify such qualitative conditionalities on states' fiscal regimes. For instance, as of 2024, the IMF is requiring Pakistan to "broaden [sic] the tax base (especially in undertaxed sectors) and improve [sic] tax administration to improve debt sustainability" in order to restore "the energy sector's viability by accelerating cost reducing reforms" and promote "private-led activity."[68] Similarly, as part of its examination of Sri Lanka's financial crisis since 2024, the IMF has revisited the state's tax exemptions for foreign investors and suggested "new tax proposals to attract investments."[69] Regarding St. Kitts and Nevis as well, the IMF is working on a complete overhaul of the state's fiscal policy, including by drawing up a set of fiscal rules to reform the nation's tax base and resulting revenue.[70] These examples demonstrate the sheer extent of fiscal control that debtor states are compelled to renounce in dire situations. Needless to say, this relinquishment of fiscal control, which takes the form of structural or qualitative conditionalities imposed by international institutions to regulate state market conditions, exists over and above the voluntary limitations on fiscal sovereignty that these states may have previously consented to through DTAs.

In light of such expansive limitations on states' fiscal sovereignty that exist on the international economic plane, it is incumbent upon other actors that operate on the peripheries of this plane, such as ISDS arbitral tribunals, to

65. *Id.*

66. *Id.*

67. *Id*.

68. Press Release, International Monetary Fund, Pakistan: IMF Reaches Staff-Level Agreement on the Second and Final Review of the 9-Month Stand-By Arrangement, IMF Press Release No. 24/91 (Mar. 20, 2024).

69. IMF, *Sri Lanka: 2024 Article IV Consultation and Second Review Under the Extended Fund Facility, Request for Modification of Performance Criterion, and Financing Assurances*, Country Reports 2024 (June 13, 2024).

70. IMF Staff, St. Kitts and Nevis: Staff Concluding Statement of the 2025 Article IV Mission (Feb. 26, 2025), https://www.imf.org/en/News/Articles/2025/02/27/st-kitts-and-nevis-cs-of-the-2025-article-iv-mission [https://perma.cc/E7ES-CXSU].

refrain from assuming that states have agreed to limit their fiscal sovereignty in any manner other than by such voluntary or market-induced limitations. To that end, from a normative point of view, the perspective surrounding any discussion implicating states' fiscal sovereignty must be adjusted. The default assumption in such a discussion should consistently be that states have full control over their fiscal policies, and any restrictions on this control should be treated as exceptions, reasonably qualified as either voluntary or market induced. This adjustment is necessitated even further in cases where the underlying object of taxation constitutes a natural resource of a state, which is often the case in ISDS arbitrations. Indeed, in such circumstances, a state's fiscal control over its natural resources "is further linked to a state's permanent sovereignty over natural resources, including the state's ability to dispose of and regulate depletion of the natural resources as best deemed fit."[71]

Notably, this adjustment of perspective regarding fiscal sovereignty can be realized by recognizing its historical roots in Westphalian sovereignty or by, at the very least, identifying that such roots still persist in some characteristics of states' fiscal sovereignty today. Even though the notion of state sovereignty has evolved over time, taxation remains one of the most fundamental policy items over which a modern state desires to retain control in as absolute and reasonable terms as possible.[72] This aspect is especially true for the developing countries of the Global South, which deserve a greater emphasis on and preservation of their fiscal sovereignty—by reinforcing its traditional, independent Westphalian status—not least because these countries are already subjected to systemic involuntary market-induced limitations on their fiscal sovereignty in the post-colonial era. After all, recognizing that interdependence is the other side of the coin of modern, globalized sovereignty is one thing; however, to perpetrate systemic inequality at the behest of an interdependent society of nations is quite another. The delicate balancing act of delineating state sovereignty requires that the values associated with such interdependence should not be unreasonably exalted. Indeed, it is only reasonable to allow the formerly colonized states to benefit from the very Westphalian facets of sovereignty—to the extent that they are reasonable and necessary—that were used to colonize them in the first place. This proposition is most resonant for such states' fiscal (including taxation) policy, since no "policymaking competence is more central to the idea of the modern state than taxation."[73]

A prime example of an unreasonable exaltation of such interdependence, which results in the dilution of states' fiscal sovereignty that is neither voluntary

71. Cornel Marian, The State's Power to Tax in the Investment Arbitration of Energy Disputes: Outer Limits and the Energy Charter Treaty 239 (2020).

72. Brauner, *supra* note 47, at 262–63.

73. Paris, *supra* note 3, at 157.

nor market-induced, is how ISDS arbitral tribunals have treated claims instituted by investors challenging states' fiscal policies. Having laid down the normative groundwork for the forthcoming discussion, this Article now turns to critiquing this treatment by ISDS arbitral tribunals of challenges to fiscal policies. Through this critique, the Article seeks to establish that ISDS, as a system, is in dire need of the aforementioned normative change in perspective when it comes to preservation of states' fiscal sovereignty. The pragmatic impact of this normative shift in perspective would require questioning, from a clean slate, whether ISDS arbitral tribunals have the jurisdiction to rule on matters that directly implicate a state's core fiscal (including taxation) policy. Before creating this clean slate, however, the harm perpetuated by ISDS arbitral tribunals, which have consistently assumed the authority to adjudicate upon matters of core fiscal policy, must be undone. This Article therefore argues that the existing and systematically entrenched assumption of arbitral jurisdiction has resulted from a disregard of states' fiscal sovereignty, amounting to an imposition of an extraneous limitation on states' fiscal sovereignty that is neither voluntary nor market induced.

In conjunction with this adjustment of perspective, a robust legal basis simultaneously warrants a greater regard in international law for the notion of fiscal sovereignty, particularly in order to ensure that investors do not trespass into sacred sovereign territory using the backdoor of dispute resolution privileges granted by BITs and MITs. The forthcoming Part presents the grounds for this legal basis, together with a discussion on the ISDS jurisprudence as it stands on issues of fiscal (including taxation) policy.

II. Fiscal Sovereignty as a General Principle of International Law

Fiscal sovereignty should be considered a general principle of international law: one that is necessarily taken into account when interpreting BITs and MITs under Article 31(3)(c) of the Vienna Convention on the Law of Treaties 1969 ("VCLT"). Section A of this Part explains the role of general principles of international law under VCLT Article 31(3)(c), and Section B posits how fiscal sovereignty may consequently qualify as a general principle of international law. Applying this framework, Section C investigates whether and how ISDS arbitral tribunals consider fiscal sovereignty while interpreting BITs and MITs, particularly focusing on dispute resolution clauses contained therein. The Section then proceeds to examine how ISDS arbitral tribunals' interpretations and assumptions of jurisdiction under such clauses may change when accounting for the general international legal principle of fiscal sovereignty. Throughout this discussion, the author delineates cases where the relevant BIT or MIT

contained a so-called 'tax carve-out' from cases where the treaty in question did not contain such a carve-out.

A. General Principles of International Law under Article 31(3)(c) of the VCLT

The VCLT, which opened for signature in 1969 and entered into force in 1980, is the foundational text that lays down the 'law of treaties.' At the time of writing this Article, the VCLT has 116 contracting parties and 45 signatories, thus constituting one of the most ubiquitously accepted treaties in international law. As such, it has, in varying respects, been characterized as codifying the customary international law on the interpretation and application of treaties.[74]

The VCLT prescribes the scheme for interpreting treaties in Articles 31 and 32 thereof, which are themselves also widely recognized as representing customary international law.[75] Article 31 of the VCLT contains the 'general rule' of treaty interpretation, which requires that "[a] treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose." Distinctly, Article 32 of the VCLT permits recourse to certain 'supplementary means' of interpretation, such as a treaty's *travaux préparatoires*,[76] only if: (1) the interpretation arrived at using the general rule in Article 31 needs to be confirmed, (2) the interpretation leaves the meaning ambiguous or obscure, or (3) the interpretation leads to a result which is manifestly absurd or unreasonable.

One criticism levied against the VCLT's interpretation scheme is its heavy reliance upon the text of a treaty being "the most authentic expression of the intentions of the parties," which perpetuates the risk of excessively literal treaty interpretations that are devoid of sufficient context.[77] However, this criticism is absorbed by the wide aperture that Articles 31(2) and 31(3) of the VCLT afford to the context surrounding the text of the treaty. For the purposes of the present Article, the most significant of these absorbents is contained in VCLT Article 31(3)(c), which requires that an interpretation take into account "together with the context . . . any relevant rules of international law applicable in the

74. *See* Land and Maritime Boundary between Cameroon and Nigeria (Cameroon v. Nigeria), Judgment, 2002 I.C.J. Rep. 303, ¶ 263 (Oct. 10); *see also* Maritime Delimitation in the Indian Ocean (Som. v. Kenya), Judgment, 2017 I.C.J. Rep. 3, ¶¶ 42–50 (Feb. 2).

75. Arbitral Award of 31 July 1989 (Guinea-Bissau v. Sen.), Judgment, 1991 I.C.J. Rep. 53, ¶ 48 (Nov. 12) ("These principles are reflected in Articles 31 and 32 of the Vienna Convention on the Law of Treaties, which may in many respects be considered as a codification of existing customary international law on the point."); *see* Vienna Convention on the Law of Treaties arts. 31, 32, May 23, 1969, 1155 U.N.T.S. 331 [hereinafter VCLT].

76. A treaty's "*travaux préparatoires*" constitutes its preparatory works for negotiations of the terms agreed upon by the state parties to the treaty. *See* VCLT , *supra* note 75, art. 32.

77. Pratyush Panjwani, *The Role of Travaux in Interpreting BIT Provisions: Are Tribunals Over-Prepared to Resort to Preparatory Works?*, 20 J. World Inv. & Trade 473, 479 (2019).

relations between the parties." Article 31(3)(c) represents the principle of "systemic integration" in international law, which ensures that treaties are not interpreted in isolation of the elements of international law beyond the treaty.[78] The International Court of Justice ("ICJ") has qualified the application of this tenet of interpretation as "an integral part of the task of interpretation,"[79] such that, if the "general rules of international law are of a peremptory nature, . . . then the principle of interpretation . . . turns into a legally insurmountable limit" if these rules of international law are not applied.[80]

It is generally accepted in scholarly writing that the expression "rules of international law" in Article 31(3)(c) of the VCLT corresponds to the enumerated sources of international law in Article 38(1) of the Statute of the ICJ, which include, inter alia, "international custom, as evidence of a general practice accepted as law" as well as "the general principles of law recognized by civilized nations."[81] Therefore, there is no uncertainty that general principles of international law play a crucial role in the exercise of interpretation, pursuant to Article 31(3)(c) of the VCLT, so long as they are "relevant" to the subject matter of the treaty being interpreted. What is not as certain, however, is what the qualifier "applicable in the relations between the parties" in Article 31(3)(c) means in the context of general principles of international law. Scholars of international law are currently divided over whether this phrase envisages only strictly "binding" general principles,[82] or if such a vision is too myopic for the purposes of systemic integration. As one scholar points out, "it is sometimes considered possible that rules extrinsic to the treaty under interpretation which . . . are not binding on all parties to the treaty . . . may under certain circumstances nevertheless become relevant for the interpretation" of the treaty in question.[83] The latter, more liberal understanding, while not the dominant scholarly view, has received the occasional nod from international courts and tribunals, including the ICJ. Under such a view, courts and tribunals have referred to non-binding treaties to interpret another (binding) treaty, pursuant

78. Campbell McLachlan, *The Principle of Systemic Integration and Article 31(3)(c) of the Vienna Convention*, 54 Int'l & Compar. L.Q. 279, 310 (2005); s*ee also* Liliana E. Popa, *The Holistic Interpretation of Treaties at the International Court of Justice*, 87 Nordic J. Int'l L. 249 (2018).

79. Oil Platforms (Iran v. U.S.), Judgment, 2003 I.C.J. Rep. 161, ¶ 41 (Nov. 6).

80. Oil Platforms (Iran v. U.S.), Judgment, 2003 I.C.J. Rep. 324, ¶ 9 (Nov. 6) (separate opinion by Simma, J.).

81. Mark E. Villager, Commentary on the 1969 Vienna Convention on the Law of Treaties 433 (2009); Oliver Dörr, *Commentary on Article 31 VCLT*, *in* Vienna Convention on the Law of Treaties: A Commentary ¶¶ 95, 99 (Oliver Dörr & Kirsten Schmalenbach eds., 2018).

82. Villager, *supra* note 81, at 433.

83. Dörr, *supra* note 81, at 611; *see also* Richard Gardiner, Treaty Interpretation 268 (2008).

to Article 31(3)(c) of the VCLT,[84] on the ground that "signed but unratified treaties may constitute an accurate expression of the understanding of the parties at the time of signature."[85] Notwithstanding this scholarly and jurisprudential divide, for the purposes of the present Article, it suffices to note that the manner in which general principles of international law can be used to ensure a systemically integrated interpretation is by keeping in mind that "in entering into treaty obligations, the parties intend not to act inconsistently with generally recognized principles of international law."[86]

B. Fiscal Sovereignty as a General Principle of International Law

State sovereignty constitutes a long-recognized, general principle of international law. The ICJ and previously the Permanent Court of International Justice ("PCIJ") have both, on many occasions, granted the principle of state sovereignty the elevated status of customary international law, thereby axiomatically recognizing it as a general principle as well.[87] For instance, in the *Case of the S.S. Lotus* in 1927, the PCIJ noted that "[r]estrictions upon the independence of [s]tates cannot . . . be presumed" and "all that can be required of a [s]tate is that it should not overstep the limits which international law places upon its jurisdiction; within these limits, its title to exercise jurisdiction rests in its sovereignty."[88] The ICJ, in its 1986 judgment in the *Military and Paramilitary Activities in and against Nicaragua* case, explicitly recognized that "[t]he basic legal concept of [s]tate sovereignty in customary international law, [is] expressed in, *inter alia*, Article 2 paragraph 1, of the United Nations Charter," which provides that "[t]he Organization is based on the principle of the sovereign equality of all its Members."[89] The ICJ further observed that sovereignty over the internal waters and territorial sea of every state and to the air space

84. OSPAR Arbitration (Ir. v. U.K.), 2003 PCA Case Repository, ¶¶ 7–19 (July 2) (Griffith, J., dissenting); Southern Bluefin Tuna Cases (N.Z. and Austl. v. Japan), Case Nos. 3–4, Order of Aug. 27, 199, 1999 ITLOS Rep. 280, ¶ 10 (separate opinion by Treeves, J.).

85. Maritime Delimitation and Territorial Questions between Qatar and Bahrain (Qatar v. Bahr.), 2001 I.C.J. Rep. 40, ¶ 89 (Mar. 16).

86. McLachlan, *supra* note 78, at 311.

87. *Id.* at 310. Ordinarily, it is obvious that a principle that meets the higher threshold of being part of customary international law must also satisfy the lower threshold of being a general principle of international law. As Professor Campbell McLachlan puts it, "customary international law and the general principles of law form two of a set of progressive concentric circles, each one constituting a field of reference of potential assistance in treaty interpretation" under Article 31(3)(c) VCLT. *Id.*

88. The Case of the S.S. Lotus (Fr. v. Turk.), Judgment, 1927 P.C.I.J. (ser. A) No. 10, at 19 (Sept. 7). *See generally* S.S. Wimbledon (U.K. et al. v. Ger.), Judgment, 1923 P.C.I.J. (ser. A) No. 01 (Aug. 17).

89. Military and Paramilitary Activities in and Against Nicaragua (Nicar. v. U.S.), Judgment, 1986 I.C.J. Rep. 14, ¶ 212 (June 27).

above its territory constitute "firmly established and longstanding tenets of customary international law."[90]

It is, therefore, evident that the principle of state sovereignty qualifies as customary international law, at least insofar as territorial sovereignty is concerned. However, at no point has the PCIJ or ICJ explicitly ruled that the domain of the customary international legal principle of state sovereignty subsumes within itself the state's fiscal sovereignty, either as a customary international legal principle or as a general principle of international law. While the customary international law status of the principle of sovereignty arguably encapsulates the protection of a sovereign state's *domaine réservé* and freedom from external interference and intervention, which is recognized in Article 2(7) of the United Nations Charter, the scope of a state's *domaine réservé* has undergone a significant undercutting in recent years. However, this undercutting does not diminish the inviolability of a state's fiscal sovereignty: As a component of its overall sovereignty, fiscal sovereignty must be recognized as a general principle of international law because it is not only a principle "common to the various legal systems of the world," but it is also a principle that has been transposed to the international legal system and, must, be considered an "intrinsic" part thereof.[91]

First, the characterization of fiscal sovereignty as a general principle of international law is supported by the existence of the more than 3,000 double-tax avoidance agreements ("DTAs") in force at the time of writing. After all, as already noted above, the paradoxical nature of sovereignty is that its limitation on the international plane, through the execution of international treaties, often serves as proof of its existence. As noted by the PCIJ in the *S.S. Wimbledon* case, "the right of entering into international engagements is [itself] an attribute of [s]tate sovereignty."[92] Thus, the very fact that states have negotiated and consented to be bound by DTAs (and for that matter multilateral agreements such as the BEPS MLI) may, if coupled with a recognition by other jurisprudential sources, be considered as reflective of a general principle of fiscal sovereignty.

Second, together with the DTAs and other multilateral agreements that operate on the international scale, a state's fiscal policy, especially its authority to impose taxes, is perhaps the domain of state sovereignty most commonly endorsed, and regulated, in states' constitutions.[93] A simple comparative

90. *Id.*

91. Memorandum, Int'l Law Comm'n, Draft Committee, General Principles of Law, U.N. Doc. A/CN.4/L.982 (2023), *at* Draft Conclusions 4, 5 & 7.

92. U.K. et al., v. Ger., 1923 P.C.I.J. at 25.

93. *See generally* Politics, Taxation, and The Rule of Law: The Power to Tax in Constitutional Perspective (Donald P. Racheter & Richard E. Wagner eds., 2002).

analysis shows that, be it in civil law nations[94] or common law nations,[95] it is rare for states' constitutions to not mention the power to tax. This ubiquitous constitutional endorsement is not afforded to all domains of state sovereignty, which, in the author's view, is itself testament to the general importance of the principle of fiscal sovereignty.

Third, certain court decisions have implied support for the proposition that fiscal sovereignty may qualify as a general principle of international law. Most notably, in 1932, the PCIJ implicitly recognized and applied the general principle of a state's fiscal sovereignty in *Free Zones of Upper Savoy and the District of Gex*. The context surrounding the PCIJ's judgment[96] was a dispute brought by Switzerland against France, alleging that France had imposed taxes in violation of a treaty between the two parties prohibiting customs duties on imported goods at the frontier. The PCIJ relied on its earlier conceptualization of state sovereignty laid down in the *S.S. Lotus* case and implicitly encapsulated a state's fiscal sovereignty within the domain of the general principle of sovereignty:

> [W]hile it is certain that France cannot rely on her own legislation to limit the scope of her international obligations, it is equally certain that French fiscal legislation applies in the territory of the free zones as in any other part of French territory . . . .
>
> The tax to which the Swiss Agent had drawn the particular attention of the Court is the tax on importation, a form of the turnover tax which is levied at the frontier on goods imported as the result of a contract. It is impossible at present to say whether this tax . . . is now levied at the frontier as a customs duty or as a fiscal tax, or whether the French Government would claim to continue to levy it at the frontier if the customs line were withdrawn. However that may be, the Court neither desires nor is able to consider whether the collection at the political frontier of any particular French tax is or is not contrary to France's obligations . . . .
>
> [T]herefore, considerations connected with its own jurisdiction and with the respect due to the sovereignty of France over the free zones prevent the Court from entertaining certain requests made on behalf of the Swiss Government.[97]

Ultimately, in its dispositif, the PCIJ ordered France to withdraw the customs line while noting that the withdrawal did "not affect the right of the French Government to collect at the political frontier fiscal duties not

94. *See* Gw. [Constitution] art. 104. (Neth. 2018); 1958 Const. art. 47 (Fr.).

95. *See Australian Constitution* s 55; India Const. Part XII.

96. The PCIJ's judgment is most notable for explaining the distinction between customs duties and taxes. *See* Joined Cases 2/62 and 3/62, Comm'n of the Eur. Econ. Cmty. v. Lux. and Belg., ECLI:EU:C:1962:45, ¶¶ 432–33 (Dec. 14, 1962).

97. Free Zones of Upper Savoy and the District of Gex (Fr. v. Switz.), Judgment, 1932 P.C.I.J. (ser. A/B) No. 46, at 166–68 (Jun. 7).

possessing the character of customs duties."[98] The PCIJ effectively limited its consideration to France's obligation to abstain from erecting customs barriers. However, the court notably refrained from determining the nature or legality of the taxes imposed by France in the free zones. The PCIJ's finding that it "neither desires nor is able to consider" the nature and legality of the taxes imposed by France is clear evidence of the court's reluctance and jurisdictional incompetence to render any determination on an issue that falls within France's fiscal sovereignty.[99] After all, in the PCIJ's own words, such an issue is "connected with its own jurisdiction."

The PCIJ's judgment in the *Free Zones of Upper Savoy and the District of Gex* case is by no means an isolated instance of recognition of a state's fiscal sovereignty in case law. In a similar vein, the PCIJ and the ICJ recognized territorial sovereignty through *effectivités*, whereby administrative acts, like taxation, demonstrate a state's effective exercise of territorial sovereignty.[100] Such *effectivités*, according to the ICJ, evidence "the intention and will to act as sovereign."[101] In addition, there are many awards and decisions rendered by international tribunals in the ISDS context[102] and otherwise[103] that have more explicitly recognized the existence of the principle of fiscal sovereignty. For instance, in the case of *Euratom v. United Kingdom Atomic Energy Authority*, the arbitral tribunal noted that "[i]t is quite clear that a State under its own sovereignty decides, as a general rule, any question of taxes to be imposed on residents in that State or on income derived from or paid in that State."[104] Similarly, the findings of the ISDS arbitral tribunal in the case of *Murphy v. Ecuador*, while warranting criticism for several reasons that are discussed in the forthcoming Subsection, paid homage to the distinctive position that fiscal sovereignty occupies, explaining "while [states] may be willing to accept international discipline over state

98. *Id.* at 170.

99. *See generally* Céline Braumann, *The Settlement of Tax Disputes by the International Court of Justice*, 36 Leiden J. Int'l L. 907 (2023).

100. *Id.*; *see also* Territorial and Maritime Dispute between Nicaragua and Honduras in the Caribbean Sea (Nicar. v. Hond.), 2007 I.C.J. Rep. 659, ¶¶ 207–08 (Oct. 8).

101. *See* Legal Status of Eastern Greenland (Den. v. Nor.), 1933 P.C.I.J. (ser. A/B) No. 53, at 46 (Sept. 5) (finding Norway could not contest Denmark's claim to Greenland due to a unilateral act by Norway).

102. *See, e.g.*, Sun Reserve Luxco Holdings SRL v. Italy, 5 SCC Case No. 132/2016, Award, ¶ 510 (Mar. 25, 2016) [hereinafter Sun Reserve] ("This is particularly in light of the object and purpose behind treaty provisions such as Article 21 ECT, which the Tribunal considers are intended for the Contracting Parties to preserve fiscal sovereignty over tax related matters.").

103. *See, e.g.*, George Cook v. Mexico, 4 Reps. Int'l Arb. Awards 593, 595 (Oct. 8, 1930) ("The right of the State to levy taxes constitutes an inherent part of its sovereignty; . . . legislatures, whether of states or of the Federation cannot legally create exemptions which restrict the free exercise of the sovereign power of the State in this regard.").

104. Case Concerning the Taxation Liability of Euratom Employees (Comm'n of the Eur. Atomic Energy Cmty. (Euratom) v. U.K. Atomic Energy Auth.), 8 Reps Int'l Arb. Awards 497, 507 (Feb. 25, 1967).

conduct, they are reluctant to accept such oversight as regards their powers of taxation."[105]

Scholars have largely affirmed courts and tribunals' recognition of the fundamental importance of the general principle of fiscal sovereignty, including on the basis that a state's jurisdiction over its fiscal policy is also closely guarded in national laws.[106] Indeed, a state's sovereignty over its fiscal or tax policy is frequently codified in nation-state constitutions. This near ubiquitous endorsement of the general principle of fiscal sovereignty in case law and scholarly writings validates the statement of Professor Diane Ring that "[n]o significant issue in international tax can be discussed without raising the question of 'sovereignty.'"[107]

C. Application of the General Principle in ISDS

The consequence of considering fiscal sovereignty as a general principle of international law is that it ought to be taken into account, together with the context of the treaty under interpretation, pursuant to VCLT Article 31(3)(c). This Section critically examines the jurisprudence of ISDS arbitral tribunals to determine whether the general principle of fiscal sovereignty has been appropriately accounted for in treaty interpretation. In particular, this Section identifies where ISDS arbitral tribunals have fallen short and posits how their decisions or awards may have been different had they properly applied the general principle of fiscal sovereignty as part of the VCLT's interpretation scheme. Before delving into this analysis, it is, however, imperative to make three preliminary remarks on this issue.

First, it is important to recall that the default assumption on any discourse on fiscal sovereignty must, as discussed in detail in the previous section, be

105. Murphy Exploration & Production Company International v. Republic of Ecuador, 2012 PCA Case Repository No. 2012-16 (formerly AA 434), Partial Final Award (May 6) [hereinafter Murphy].

> The purpose of [the tax carve-out] specifically is to preserve the states' sovereignty in relation to their power to impose taxes in their territory. Most governments view these powers as a central element of sovereignty. Therefore, while they may be willing to accept international discipline over state conduct, they are reluctant to accept such oversight as regards their powers of taxation. This has led most state parties to modern investment treaties to omit taxation from a treaty's ambit, or restrict the treaty's application to certain types of taxes.

Id. ¶ 165.

106. Edwin van der Bruggen, *State Responsibility under Customary International Law in Matters of Taxation and Tax Competition*, 29 INTERTAX 115, 120–21 (2001). *See generally* Harold Wurzel, *Foreign Investment and Extraterritorial Taxation*, 38 COLUM. L. REV. 809 (1938); Martin Norr, *Jurisdiction to Tax and International Income,* 17 TAX L. REV. 431 (1962); Paris, *supra* note 3; Christians, *supra* note 34; McLure, *supra* note 58.

107. Diane Ring, *What's at Stake in the Sovereignty Debate? International Tax and the Nation State*, 49 VA. J. INT'L L. 155, 156 (2009).

adjusted so as to treat the imposition of limitations on it as the exception to the default general rule that states have full control over their fiscal policies. This default assumption is neither a unique nor an uncorroborated proposition as a matter of jurisprudence. It was stipulated by the PCIJ in *S.S. Lotus*, where the court noted, while laying out the contours of the principle of state sovereignty, that "[r]estrictions upon the independence of [s]tates cannot . . . be presumed."[108] In fact, even before the PCIJ's judgment, an award of a five-member arbitral tribunal in the 1910 *North Atlantic Fisheries* case between the United Kingdom and the United States confirmed that "a line which would limit the exercise of sovereignty of a [s]tate within the limits of its own territory can be drawn only on the ground of express stipulation, and not by implication from stipulations concerning a different subject-matter."[109] The idea that limitations on sovereignty in general, and fiscal sovereignty in particular, can only be imposed by explicit agreement of the state waiving its sovereignty claim is thus incontrovertible. Even in the case of market-induced limitations to fiscal sovereignty, discussed in Subsection I.B.2. above, these limitations in most instances are products of an agreement that the states in question are compelled to reach. While the consent of severely indebted states may in practice be a myth, in theory it is difficult to envisage any state limiting its sovereignty on any matter, let alone one closely tied to its fiscal policy, without having thoroughly considered and consented to such a limitation.

Second, the majority of the host states that have been sued in investor-state disputes are in the Global South. Empirical studies have shown that while the "home state of the claimant-investor is strongly represented by the United States, followed by the Netherlands, the United Kingdom, Germany, Canada, and Spain," host states are "overwhelmingly middle-income states."[110] On the other hand, researchers have found that "investors from developing countries almost never file arbitration claims against governments of developed states."[111] These quantitative analyses are also supported by the annual investments reports of the UNCTAD; the most recent one in 2023 noted that "[a]s in previous years, the majority of new cases (about 65 percent) were brought against developing countries."[112] These countries are the ones that often find themselves in situations—due, to a considerable extent, to the residual impacts

108. Fr. v. Turk., 1927 P.C.I.J. at 19.

109. The North Atlantic Coast Fisheries Case (Gr. Brit. v. U.S.), 1909 PCA Case Repository No. 1909-01, Final Award, ¶ 15 (Sept. 7).

110. Daniel Behn et al., *Empirical Perspectives on Investment Arbitration: What Do We Know? Does It Matter?*, 21 J. World Inv. & Trade 188, 192 (2020).

111. Thomas Schultz & Cédric Dupont, *Investment Arbitration: Promoting the Rule of Law or Over-empowering Investors? A Quantitative Empirical Study*, 25 Eur. J. Int'l L. 1147, 1156 (2014).

112. U.N. Conf. Trade & Dev., World Investment Rep. 2023, at 78, U.N. Doc. UNCTAD/WIR/2023 (July 5 2023).

of colonization—where they are compelled to agree to the aforementioned market-induced limitations on their fiscal sovereignty.[113]

Third, it is not uncommon for BITs or MITs to contain provisions that effectively carve out matters of taxation from the scope of application of the treaty in question. These provisions are referred to as 'tax carve-outs.' A prime example of such a tax carve-out is Article 21(1) of the Energy Charter Treaty 1994 ("ECT"), which, inter alia, provides that "nothing in this Treaty shall create rights or impose obligations with respect to Taxation Measures of the Contracting Parties." Such general carve-outs are most commonplace in BITs and MITs. There is broad jurisprudential consensus that their coverage is not limited to matters of substance but also extends to the jurisdiction of tribunals.[114] In other words, if a taxation measure falls within the scope of a carve-out, ISDS arbitral tribunals will usually decline jurisdiction with respect to that taxation measure.[115] That said, certain BITs also contain standard-specific tax carve-outs, which exclude the application of the BIT in question to taxation measures with respect to claims raised under certain standards, such as the national treatment or most-favored-nation standard.[116] However, given that such standard-specific tax carve-outs are not the norm, the present Section shall focus primarily on cases involving generic carve-outs.

Tax carve-outs, especially those that are generic in scope, have themselves been recognized as a codification of the state parties' fiscal sovereignty.[117] However, given that fiscal sovereignty is a general principle of international law, it should continue to be relevant and applicable before an ISDS arbitral tribunal interpreting a BIT or MIT, notwithstanding whether the treaty contains a tax carve-out. Indeed, fiscal sovereignty, as a general principle, deserves a position in the interpretation scheme pursuant to VCLT Article 31(3)(c), regardless of its

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113. Bantekas, *supra* note 37, at 149.

114. *See, e.g.*, Duke Energy Electroquil Partners & Electroquil S.A. v. Republic of Ecuador, ICSID Case No. ARB/04/19, Award, ¶ 188 (Aug. 18, 2008); EnCana Co. v. Republic of Ecuador, LCIA Case No. UN3481, Award, ¶ 145 (Feb. 3, 2006).

115. *See id.*

116. *See, e.g.*, Agreement for the Promotion and Protection of Investments, Gr. Brit.-India, Jan. 6, 1995, 27 U.N.T.S. 1.

> The provisions of this Agreement relative to the grant of treatment not less favourable than that accorded to the investors of either Contracting Party or of any third State shall not be construed so as to oblige one Contracting Party to extend to the investors of the other the benefit of any treatment, preference or privilege resulting from: (a) any existing or future customs union or similar international agreement to which either of the Contracting Parties is or may become a party, or (b) any international agreement or arrangement relating wholly or mainly to taxation or any domestic legislation relating wholly or mainly to taxation.

Id. art. 4(3).

117. *See* Murphy, 2012 PCA Case Repository No. 2012-16, ¶ 165; Sun Reserve, 5 SSC Case No. 132/2016, ¶ 510.

codification in the form of a tax carve-out. This position is further strengthened when those state parties have also entered into a DTA in exercise of their fiscal sovereignty. When two states have already agreed to limit their fiscal sovereignty by executing a DTA, the default assumption that states have full control over their fiscal policies warrants that no further limitation to fiscal sovereignty be presumed under a BIT, especially since BITs or MITs are purposefully distinct from DTAs. As explained by UNCTAD, "[t]he principal purpose of [DTAs] is to deal with issues arising out of the allocation of revenues between countries; the principal purpose of BITs is to protect the investments that generate these revenues (and tax issues are excluded from their provisions)."[118] That said, even when the two state parties in question have not entered into a DTA, the relevance or the applicability of the general principle of fiscal sovereignty under Article 31(3)(c) of the VCLT should not be diminished. In other words, this principle should continue to influence the interpretation of a BIT or MIT, like any other general principle of international law, regardless of whether the state parties to the treaty have executed a separate DTA or the treaty in question contains a tax carve-out.

The ideal solution to account for the general principle of fiscal sovereignty when a BIT or MIT is interpreted is to place a jurisdictional dam that cautions ISDS arbitral tribunals against assuming jurisdiction on matters that are too closely tied to the host state's fiscal sovereignty. This jurisdictional dam can be constructed against the backdrop of the interpretation of not only the tax carve-out but also the investor-state dispute resolution clause contained in a BIT or MIT. This ensures that such a dispute resolution clause, which typically applies to disputes relating to an investment, prohibits ISDS arbitral tribunals from adjudicating over claims that implicate the host state's core fiscal policy. In other words, the consideration of the host state's fiscal sovereignty as a factor relevant to the examination of the investor's claims should not be deferred until the adjudication of the merits of the said claims. Instead, such claims should, from the outset, be considered beyond an ISDS arbitral tribunal's jurisdiction. Inspiration for such a solution is available not only in the ISDS jurisprudence that attaches tax carve-outs (when they exist) to arbitral tribunals' jurisdiction, but also in the PCIJ's judgment in *Free Zones of Upper Savoy and the District of Gex*, wherein the PCIJ was obviously cautious in exercising jurisdiction over an issue within France's fiscal sovereignty. The forthcoming Subsections examine the current positions ISDS arbitral tribunals hold on their jurisdiction over matters closely tied to the host state's fiscal sovereignty. Cases are organized by those in

118. U.N. Conf. Trade & Dev., Taxation, *supra* note 39, at 27.

which the treaty under interpretation contained a tax carve-out and those where a tax carve-out was absent.

1. Cases Where Investment Treaties Contain a Tax Carve-Out

There are several instances of ISDS arbitral tribunals denying jurisdiction over a claim, or a portion of a claim, that implicates a tax measure on the basis of a tax carve-out contained in the treaty in question.[119] Indeed, this solution has been relatively consistently adopted in a line of cases, for instance in respect of the seven percent tax levied by Spain on the production of electrical energy through renewable sources in 2012,[120] or the Robin Hood Tax levied by Italy on the windfall profits of oil, gas, and other conventional energy companies.[121] However, there are a significant instances in which ISDS arbitral tribunals have interpreted tax carve-outs in a way that enabled them to breach the jurisdictional dam. Recently, scholars have correctly questioned the effectiveness of tax carve-outs in barring taxation-based investment claims, going so far as to argue that "arbitral tribunals have shown a willingness to read down or even ignore carve-out clauses."[122]

The author delineates decisions where ISDS arbitral tribunals have breached the jurisdictional dam of tax carve-outs into two schools of interpretation, one concerning the imposition of the condition that the carved-out taxation measures be bona fide and the other concerning the understanding of the term "taxation measures" and what it covers insofar as the material scope of the carve-out is concerned.

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119. *See* ACF Renewable Energy v. Bulgaria*,* ICSID Case No. ARB/18/1, Award, ¶ 1511 (Jan. 5, 2024).

120. *See* JGC v. Spain, ICSID Case No. ARB/15/27, Award, ¶ 465 (Sept. 9, 2021); *see also* Foresight Luxembourg Solar 1 S. Á.R1., et al. v. Spain, 5 SCC Case No. 2015/150, Final Award, ¶ 260 (Nov. 14, 2018) [hereinafter Foresight]; Isolux Netherlands, BV v. Spain, 5 SCC Case No. 2013/153, Final Award, ¶ 741 (July 17, 2016); Novenergia II-Energy & Environment (SCA) (Lux.) SICAR v. Spain, SCC Case No. 2015/063, Final Award, ¶ 525 (Feb. 15, 2018) [hereinafter Novenergia]; Eiser Infrastructure Limited and Energia Solar Luxembourg S.À.R.L. v. Spain, ICSID Case No. ARB/13/36, Final Award, ¶¶ 266, 270–71 (May 4, 2017) [hereinafter Eiser Infrastructure]; 9REN Holding S.a.r.l v. Spain, ICSID Case No. ARB/15/15, Award, ¶ 207 (May 31, 2019) [hereinafter 9REN].

121. *See* Sun Reserve, 5 SSC Case No. 132/2016, ¶ 533; *see also* ESPF Beteiligungs GmbH, et al. v. Italy, ICSID Case No. ARB/16/5, Award, ¶ 355 (Sept. 14, 2020); Athena Investments A/S (formerly Greentech Energy Systems A/S) et al. v. Italy*,* 5 SCC Case No. 2015/095, Final Award, ¶ 227 (Dec. 23, 2018); CEF Energia BV v. Italy, 5 SCC Case No. 158/2015, Award, ¶ 204 (Jan. 16, 2019).

122. Matthew Davie, *Taxation-Based Investment Treaty Claims,* 6 J. Int'l Disp. Settlement 202, 223 (2015); *see also* Colin Cherian, *Between the Scylla and Charybdis: Tax Carve-outs and Tribunal Jurisprudence*, 10 Indian J. Arb. L. 156 (2021).

The first school of interpretation comprises arbitral tribunals that seek to limit the applicability of tax carve-outs to only bona fide taxation measures. The harbinger of this school of interpretation is the line of cases brought by shareholders of the Yukos Oil Company challenging the Russian Federation's allegedly expropriatory taxation measures against the company. Specifically, the seeds of this school were sowed in 2009 by the tribunal in *Quasar de Valors v. Russian Federation*, which rendered the following finding that ultimately inspired the tribunal in the seminal *Hulley/Veteran/Yukos v. Russian Federation* case:

> Russia also argues preliminarily that the Danish BIT is automatically excluded from application here because it states in Article 11(3): 'The provisions of this Agreement shall not apply to taxation.' The present Claimants could therefore not have proceeded even if they were Danish investors because they complain precisely of tax measures taken with respect to Yukos. This argument was not pursued with great insistence. Nor should it have been. The Claimants allege that Russia imposed a bogus reassessment of taxes in order to effect a spoliation of Yukos assets. To think that ten words appearing in a miscellany of incidental provisions near the end of the Danish BIT would provide a loophole to escape the central undertakings of investor protection would be absurd. Complaints about types and levels of taxation are one thing. Complaints about abuse of the power to tax are something else. A 'decree' to the effect that 'all tax inspectors are henceforth instructed to collect everything they can get their hands on from Danish investors' would not be insulated because of Article 11(3) of the BIT. Abuse and pretext are at the heart of the Claimants' allegations.[123]

Rendered in the context of the investors' reliance on a BIT between Denmark and the Russian Federation, the finding was reached by invoking the most favored nation clause contained in the BIT between Spain and the Russian Federation. While the award of the *Quasar de Valors* tribunal was ultimately set aside by the Svea Court of Appeal due to its erroneous interpretation of the limited dispute resolution clause,[124] the finding pioneered an interpretative solution that spread like wildfire.[125]

The most prominent and explicit constriction of a tax carve-out to so-called 'bona fide' taxation measures came in 2014, when the arbitral tribunal in *Hulley/Veteran/Yukos v. Russian Federation* rendered the following finding while interpreting ECT Article 21(1):

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123. Renta 4 S.V.S.A et al. v. Russian Fed'n, 5 SCC Case No. 24/2007, Award on Preliminary Objections, ¶ 74 (Mar. 20, 2009).

124. Renta 4 S.V.S.A et al.. v. Russian Fed'n, Case No. T 9128-14, Judgment of Svea Court of Appeal (Jan. 18, 2016).

125. For its first application, see RosInvestCo UK Ltd. v. Russian Fed'n, 5 SCC Case No. 079/2005, Award, ¶¶ 264, 628 (Sept. 12, 2010).

> Article 21 of the ECT can apply only to *bona fide* taxation actions, i.e., actions that are motivated for the purpose of raising general revenue for the state. By contrast, actions that are taken only 'under the guise' of taxation, but in reality aim to achieve an entirely unrelated purpose (such as the destruction of a company or the elimination of a political opponent), . . . cannot qualify for exemption from the protection standards of the ECT under the taxation carve-out in Article 21(1).[126]

The award of the *Hulley* tribunal was set aside by the Hague District Court in 2016, only to be reinstated by the Hague Court of Appeal in 2020. Commenting on the status of the proceedings before the Dutch judiciary is complicated, especially after the Hague Court of Appeal's judgment was overturned by the Supreme Court of the Netherlands. However, interestingly, the Court of Appeal endorsed the tribunal's interpretation of the tax carve-out in ECT Article 21(1), while curiously also rendering the anomalous determination that the carve-out does not have any jurisdictional relevance.[127] Notwithstanding this ill-deserved fate of the ECT's tax carve-out before the Dutch judiciary (which is without company on this issue), the *Hulley* tribunal's assumption of jurisdiction, despite the presence of the tax carve-out in Article 21(1), set ablaze the wildfire sparked by the *Quasar de Valors* tribunal. Most arbitral tribunals since 2014, when faced with a claim challenging a taxation measure in the face of a tax carve-out, have sought to examine whether the taxation measure in question is 'bona fide.'[128] The notable exceptions to this jurisprudence are primarily cases where arbitral tribunals have directly considered whether the taxation measure in question is bona fide without determining whether this constitutes a condition under the tax carve-out.[129] Apparently only one arbitral tribunal has explicitly refused to read this condition into the tax carve-out in ECT Article 21(1): the tribunal in *Stadtwerke München GmbH, RWE Innogy GmbH, and others v. Spain.* Its anti-establishment findings in this respect are worth reproducing here:

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126. Hulley Enter. Ltd. (Cyprus) v. Russian Fed'n, 2005 PCA Case Repository No. 2005-03/AA226, Final Award, ¶ 1431 (July 18).

127. Hulley Enter. Ltd. (Cyprus) v. Russian Fed'n, 2005 PCA Case Repository No. 2005-03/AA226, 2020 Hague Court of Appeal, Case No. 200.197.071/01, ¶¶ 5.2.4–5.2.20 (Feb. 18).

128. *See, e.g.*, Novenergia, SCC Case No. 2015/063, ¶¶ 509–11; ACF Renewable Energy, ICSID Case No. ARB/18/1, ¶ 1494; Infrastructure Serv. Luxembourg S.à.r.l. and Energia Termosolar B.V. (formerly Antin Infrastructure Serv. Luxembourg S.à.r.l. and Antin Energia Termosolar B.V.) v. Spain, ICSID Case No. ARB/13/31, Award, ¶ 314 (June 15, 2018); RREEF Infrastructure (G.P.) Ltd. and RREEF Pan-European Infrastructure Two Lux S.à r.l. v. Spain, ICSID Case No. ARB/13/30, Decision on Responsibility and on the Principles of Quantum, ¶ 188 (Nov. 30, 2018); Photovoltaic Knopf Betriebs GMBH v. Czech Republic, 2014 PCA Case Repository No. 2014-21, Award, ¶¶ 255–56 (May 15); Cube Infrastructure Fund SICAV et al. v. Spain, ICSID Case No. ARB/15/20, Award, ¶ 221 (June 26, 2019); RENERGY S.à r.l. v. Spain, ICSID Case No. ARB/14/18, Award, ¶¶ 477–78 (May 6, 2022).

129. *See, e.g.*, JGC, ICSID Case No. ARB/15/27, ¶ 465; Foresight, 5 SCC Case No. 2015/150, ¶ 150.

> The Claimants in their pleadings argue that the obligation of good faith (*bona fide*) derives from Article 31(1) of the VCLT which provides that ". . . a treaty shall be interpreted in good faith . . ." That provision, of course, says nothing about a government's obligation of good faith in imposing taxes.
>
> The context of Article 21 of the ECT is a Contracting Party's power to tax. In this connection, one must bear in mind that the power to tax is a fundamental sovereign right that belongs to all governments; a sovereign right they have wide discretion in exercising. Moreover, the power to tax is fundamental to the power to govern since it provides governments with the necessary means to carry out their governmental functions. As a result, all governments jealously protect the power to tax and strongly resist any external limitations on it. The negotiators of the ECT sought to protect their power to tax from such external constraints by specifically exempting Taxation Measures from their obligations owed to protected investors by negotiating and agreeing to a separate and specific provision to that effect. The last sentence of Article 21(1) underscores the importance that the Contracting Parties attached to it. It states: "In the event of any inconsistency between this Article and any other provision of the Treaty, this Article shall prevail to the extent of the inconsistency." It is a recognition that governments have superior obligations to provide for the public good and that meeting those obligations will depend on a wide variety of complex circumstances that no one, including treaty negotiators, can predict. As a result, governments must be left free to use their discretion as they see fit to do so.
>
> The Claimants are no doubt correct that there must be some limitations on a Contracting State's power to tax in international law. These limitations in customary international law are that a tax cannot be confiscatory or discriminatory. It is precisely these limitations that are endorsed in Article 21 of the ECT, in relation to Article 10(2) and (7) and to Article 13 of the ECT. This Tribunal has no mandate to graft further limitations on the Contracting States' taxation powers that are not reflected in the text of the ECT itself.[130]

A handful of other arbitral tribunals have stressed that "[t]he power to tax is a core sovereign power that should not be questioned lightly"[131] and "[i]t is not easy to overthrow the presumption that a tax measure introduced by a state is enacted *bona fide,*"[132] when interpreting tax carve-outs. However, none have gone as far as the *Stadtwerke München* tribunal to abrogate the indiscriminate power to read into a tax carve-out any additional and extra-textual (i.e., beyond the treaty's text) limitations on the host state's fiscal sovereignty. Unsurprisingly,

130. Stadtwerke München GmbH, RWE Innogy GmbH et al. v. Spain, ICSID Case No. ARB/15/1, Award, ¶¶ 168–70 (Dec. 2, 2019) (internal citations omitted).

131. Eiser Infrastructure, ICSID Case No. ARB 13/36, ¶ 270; *see also* 9REN, ICSID Case No. ARB/15/15, ¶ 207; Sun Reserve, 5 SSC Case No. 132/2016, ¶ 510.

132. Novenergia, SCC Case No. 2015/063, ¶ 524.

most tribunals have gone the other way. These tribunals have read the condition of good faith into tax carve-outs at the expense of the host state's fiscal sovereignty while half-heartedly paying lip service to the sovereign function of taxation. A notable example comes in the finding in *Photovoltaic Knopf Betriebs GMBH v. Czech Republic*:[133]

> Accepting the existence of international limits on the Contracting Parties' right to exclude taxation measures from certain provisions of the ECT does not strip the Contracting Parties from one of their 'most quintessential sovereign powers.' Instead, it acknowledges that any sovereign prerogative has its limits, which are, in the present case, imposed by the text and purposes of Article 21 of the ECT.[134]

This finding resulted in the exclusion of a solar levy imposed by the Czech Republic on the electricity produced from solar radiation from the tax carve-out on the ground that even though "one purpose of the [s]olar [l]evy was to raise revenue for the [s]tate (to finance the subsidies to solar energy producers)," the solar levy was structured to "adjust the level of the [feed-in tariffs] payable to certain renewable energy producers rather than to raise revenue."[135] This reasoning, relying on "the importance of good faith in the application of" the carve-outs,[136] is a quintessential misapplication of the principle of fiscal sovereignty. If one accepts, as the *Photovoltaic Knopf* tribunal did, that the state's power to tax is a fundamental sovereign function, the tax carve-out must be interpreted by taking into account this proposition. Otherwise, the tribunal ends up adding "implicit limits"[137] to this sovereign function over and above the text of the treaty in question. Moreover, such limitations should not be introduced from the back end by relying on the "purposes" of the tax carve-out—after all, the tax carve-out has no greater purpose than to preserve the state's fiscal sovereignty.

Such an interpretative fallacy, which also taints other awards dealing with the same solar levy,[138] is easily alleviated if the state's fiscal sovereignty is

133. The same tribunal also heard and decided other cases by way of awards rendered on the same date. *See generally* ICW Eur. Inv. Ltd v. Czech Republic, 2014 PCA Case Repository No. 2014-22, Award (May 15) [hereinafter ICW]; WA Inv. Europa Nova Ltd. v. Czech Republic, 2014 PCA Case Repository No. 2014-19, Award (May 15) [hereinafter WA Inv.].

134. Photovoltaic Knopf, 2014 PCA Case Repository No. 2014-21, ¶ 251.

135. *Id.* ¶ 258; *see also* Antaris Solar GmbH and Dr. Michael Göde v. Czech Republic, 2014 PCA Case Repository No. 2014-01, Award, ¶ 250 (May 2) [hereinafter Antaris]; ICW, 2014 PCA Case Repository No. 2014-19, ¶ 317; WA Inv., 2014 PCA Case Repository No. 2014-19, ¶ 336.

136. Photovoltaic Knopf, 2014 PCA Case Repository No. 2014-21, ¶ 256.

137. *Id.* ¶ 251; *see also* ICW, 2014 PCA Case Repository No. 2014-19, ¶ 310; WA Inv., 2014 PCA Case Repository No. 2014-19, ¶ 329.

138. *See generally* Antaris, 2014 PCA Case Repository No. 2014-01; ICW, 2014 PCA Case Repository No. 2014-19; WA Inv., 2014 PCA Case Repository 2014-No. 19.

elevated to a general principle of international law. This principle would therefore get its deserved position in the interpretation scheme under Article 31(3)(c) of the VCLT, thereby mandating that tribunals apply this principle when interpreting tax carve-outs. The solar levy in the cases brought against the Czech Republic is typical of a taxation measure that should have been excluded from an ISDS arbitral tribunal's jurisdictional supervision, not in the least because one of its purposes was admittedly to raise revenue. Indeed, the fact that the solar levy might have been structured to adjust the level of tariffs payable to certain energy producers is immaterial, since—as will be further discussed below—when determining whether a taxation measure is excludable, the central inquiry focuses on its legal operation and not economic effect. However, the devoted reliance of ISDS arbitral tribunals on good faith imposed an unsolicited condition on the tax carve-out that the Czech Republic's solar levy could not fulfil. This imposition is more bizarre in the face of the consistent recognition by the arbitral tribunals that examined the solar levy that the Czech Republic did not exhibit a hint of bad faith in the taxation measure.[139] In fact, the *Photovoltaic Knopf* tribunal "emphasize[d] that this case does not involve conduct comparable to . . . *Quasar de Valores*" since there is no evidence the Czech Republic acted "abusively, duplicitously or with similar bad faith."[140] Nonetheless, the solar levy ended up on the other side of the jurisdictional dam, to be assessed by the tribunals against the investment protection obligations undertaken by the Czech Republic under the ECT.[141] The fate of the Czech Republic's solar levy shows that the limitation on fiscal sovereignty first imposed by the *Quasar de Valors* tribunal has been applied in much more liberal ways than it was originally stipulated.

This has resulted in a gradual yet systemic shifting of the burden of proof in ISDS cases, since states must now establish at the outset that the taxation measure was enacted in good faith. This burden is difficult to surmount in a vacuum, especially given the policy-based justifications that ISDS arbitral tribunals readily use to protect investors by, at the very least, giving them their day in court. As one scholar remarks, the line of jurisprudence stemming from the *Quasar de Valors* and *Hulley decisions* has ended up "rotat[ing] the taxation-related kaleidoscope of the taxation-related case law to put the *bona fide* inquiry at the outset of the application of the . . . carve-out."[142] The unfortunate consequence of this reversal of the burden of proof is "that a claimant can bring a taxation-based investment claim under [a BIT or MIT] with a taxation carve-out clause

139. Antaris, 2014 PCA Case Repository No. 01, ¶ 253.

140. Photovoltaic Knopf, 2014 PCA Case Repository No. 2014-21, ¶ 261; ICW, 2014 PCA Case Repository No. 2014-19, ¶ 320; WA Inv., 2014 PCA Case Repository No. 2014-19, ¶ 339.

141. Antaris, 2014 PCA Case Repository No. 2014-01, ¶ 253.

142. MARIAN, *supra* note 71, at 243.

and, providing that it makes an allegation of bad faith, be confident that the claim will survive a preliminary objection and be accorded a hearing on the merits."[143] On the face of it, this could not have been the intention of the states that are party to the BIT or MIT in question when including a tax carve-out.

The second school of interpretation affecting tax carve-outs is defined by arbitral tribunals that have interpreted the term "taxation measures" or the like term contained in tax carve-outs narrowly, to the exclusion of certain kinds of measures. This school of interpretation was pioneered by the arbitral tribunal in *EnCana v. Ecuador*. The *EnCana* tribunal found that a legal provision (and any ensuing executive act thereunder, however "idiosyncratic") pertaining to VAT refunds qualified as a "taxation measure" and thus fell outside its jurisdiction. The tribunal enumerated, *inter alia,* the following factors in support of its interpretation of the term "taxation measures":

> (1) It is in the nature of a tax that it is imposed by law . . . The Tribunal is not a court of appeal in Ecuadorian tax matters, and provided a matter is sufficiently clearly connected to a taxation law or regulation (or to a procedure, requirement or practice of the taxation authorities in apparent reliance on such a law or regulation), then its legality is for the courts of the host state . . . .
>
> (3) Having regard to the breadth of the defined term 'measure', there is no reason to limit Article XII(1) to the actual provisions of the law which impose a tax. All those aspects of the tax regime which go to determine how much tax is payable or refundable are part of the notion of 'taxation measures'. Thus tax deductions, allowances or rebates are caught by the term.
>
> (4) *The question whether something is a tax measure is primarily a question of its legal operation, not its economic effect*. A taxation law is one which *imposes a liability on classes of persons to pay money to the state for public purposes*. The economic impacts or effects of tax measures may be unclear and debatable; nonetheless a measure is a taxation measure if it is part of the regime for the imposition of a tax . . . .[144]

In addition to these factors, the *EnCana* tribunal also examined Ecuador's domestic legal regime to understand the characterization of the measure in question under domestic law.[145] The relevance of the domestic law characterization of a taxation measure is not a matter of much jurisprudential cacophony among arbitral tribunals, although its precise status in the inquiry of taxation measures has received slightly diverging considerations from tribunals. Some tribunals have considered the domestic law characterization to be "the

143. Davie, *supra* note 122, at 226.
144. EnCana, LCIA Case No. UN3481, ¶ 145 (emphasis added).
145. *Id.* ¶¶ 146–50.

appropriate starting point" in determining whether the measure qualifies as a taxation measure. This interpretation could supplement an autonomous understanding of the taxation measure as a matter of international law.[146] Others have afforded the domestic law characterization an independent and determinative stature separate from whether the measure qualifies as a taxation measure as a matter of international law. This interpretation rests on the ground that unless the host state "has itself chosen to characterize a measure as a tax measure in its own domestic legal order, that measure does not fall within the scope of [the tax carve-out]."[147] However, no arbitral tribunal has completely sidestepped the domestic law characterization of a taxation measure, nor has any tribunal ruled it out as irrelevant.

It is in respect of the autonomous international law understanding of taxation measures, i.e., its understanding over and above its domestic law characterization, where investor-state jurisprudence appears to have gone astray in the second school of interpretation. The most solemn victim of this jurisprudential disarray is the (in)famous Law No. 2006-42 enacted by Ecuador in 2006 ("Law 42"), which gave rise to several ISDS arbitrations against Ecuador: Law 42 constituted an amendment to Ecuador's Hydrocarbons Law and, in its most relevant part, imposed on "[c]ontracting companies having Hydrocarbons exploration and exploitation participation agreements in force with the Ecuadorian State pursuant to this Law" the obligation to "grant the Ecuadorian State a participation of at least 50% over the extraordinary revenues caused by such price difference."[148] As the tribunal in *Burlington v. Ecuador* put it, "Law 42 imposed a participation of 50% over so-called 'non agreed or unforeseen surpluses from oil selling prices' on private contractors."[149]

The question of whether and to what extent Law 42 would qualify as a "taxation measure" as a matter of international law under tax carve-outs stemming from various treaties kept many ISDS arbitral tribunals busy in the ensuing

146. Sun Reserve, 5 SSC Case No. 132/2016, ¶ 515; Antaris, 2014 PCA Case Repository No. 2014-01, ¶ 225; Perenco Ecuador v. Republic of Ecuador, ICSID Case No. ARB/ 08/6, Decisions on Remaining Issues of Jurisdiction and Liability, ¶ 585 (Sept. 12, 2014) ("[I]t is possible for a measure to be characterized differently under different legal systems, the municipal and international . . . .").

147. Photovoltaic Knopf, 2014 PCA Case Repository No. 2014-21, ¶ 238 ICW, 2014 PCA Case Repository No. 2014-19, ¶ 297; WA Inv., 2014 PCA Case Repository No. 2014-19, ¶ 316.

148. Burlington Resources Inc. v. Republic of Ecuador, ICSID Case No. ARB/08/5, Decision on Liability, ¶ 30 (Dec. 14, 2012); *see generally* Murphy, 2012 PCA Case Repository No. 2012-16, ¶ 102; Occidental Petroleum Corporation and Occidental Exploration and Production Company v. Republic of Ecuador, ICSID Case No. ARB/06/11, Award (Oct. 5, 2012) [hereinafter Occidental]; Perenco Ecuador v. Republic of Ecuador, ICSID Case No. ARB/ 08/6; Repsol YPF Ecuador, S.A. v. Republic of Ecuador, ICSID Case No. ARB/08/10, Award (Sept. 27, 2019); Chevron Corporation and Texaco Petroleum Company v. Republic of Ecuador (II), 2009 PCA Case Repository No. 2009-23, Second Partial Award on Track II (Aug. 30).

149. Burlington Resources, ICSID Case No. ARB/08/5, ¶ 39.

years. Concerningly, their answers to this seemingly straightforward question have varied considerably. First came the 2010 *Burlington* tribunal, which analyzed whether the investor's claims implicating Law 42 qualified as "matters of taxation" under the tax carve-out contained in Article X of the Treaty between the United States and Ecuador concerning the Encouragement and Reciprocal Protection of Investments ("U.S.-Ecuador BIT").[150] Basing its understanding of a "tax" on the *EnCana* tribunal's "apposite" analysis, the *Burlington* tribunal found that Law 42 constituted a tax for the purposes of the carve-out in Article X of the U.S.-Ecuador BIT, citing the following reasons:

> First, Law 42 is, as its very name indicates, a law. Second, that law imposes a liability on "classes of persons", namely, on contracting companies having [Production Sharing Contracts] in force with Ecuador whenever the currently prevailing price of oil exceeds a preset reference price. Third, in accordance with this liability, these "classes of persons" must pay money to the state on a monthly basis. Fourth and finally, the monies so collected are available for the state to use for public purposes. As Ecuador indicated, the money collected under Law 42 "goes directly into the account of the state . . . as all taxes do, in the Cuenta Unica of the state at the Central Bank" . . . The Tribunal also notes that Burlington paid the monies due under Law 42 through the same Tax Consortium which is liable for income taxes in Blocks 7 and 21.[151]

On the basis of this finding, the *Burlington* tribunal denied jurisdiction "over those Law 42 non-expropriation claims which raise 'matters of taxation' within the meaning of Article X, that is, (i) the fair and equitable treatment claim . . ., (ii) the arbitrary impairment claim . . .; and (iii) the full protection and security claim."[152] However, the tribunal exercised jurisdiction over certain umbrella clause claims raised by Burlington, and "join[ed] to the merits its final determination on whether it has jurisdiction over Burlington's outstanding umbrella clause claims pending resolution of the question whether these claims require

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150. Treaty Concerning the Encouragement and Reciprocal Protection of Investment, U.S.-Ecuador, May 5, 1997, 21 ILM 1227 (1982).

> [T]he provisions of this Treaty, and in particular Article VI and VII, shall apply to matters of taxation only with respect to the following: (a) expropriation, pursuant to Article III; (b) transfers, pursuant to Article IV; or (c) the observance and enforcement of terms of an investment agreement or authorization as referred to in Article VI (1) (a) or (b), to the extent they are not subject to the dispute settlement provisions of a Convention for the avoidance of double taxation between the two Parties, or have been raised under such settlement provisions and are not resolved within a reasonable period of time.

Id. art. X(2).

151. Burlington Resources, ICSID Case No. ARB/08/5, ¶¶ 165–66.

152. *Id.* ¶ 249.

privity between Burlington and Ecuador."[153] Importantly, the tribunal's exercise of jurisdiction over some of the umbrella clause claims was predicated on the fact that Burlington "does not bring this claim on the ground that Law 42 is unlawful or that Law 42 should not be enforced."[154] In contrast, the tribunal's renunciation of jurisdiction over the remainder of Burlington's claims was principally based on the fact that those claims "challenged Law 42" and thus qualified as matters of taxation excluded by the tax carve-out.[155]

The 2012 *Occidental v. Ecuador (II)* arbitral tribunal, which also adjudicated claims under the U.S.-Ecuador BIT, was the next to consider the issue of the characterization of Law 42, albeit only incidentally during the quantum phase of the arbitration proceedings. Although even at this late stage the tribunal did consider the existence of the tax carve-out in Article X of the U.S.-Ecuador BIT to be "a compelling procedural reason why the Tribunal must characterize Law 42,"[156] it ultimately decided to find that Law 42 was "not a tax," since Ecuador "throughout the Hearing on Quantum, was loath to characterize Law 42," and considering Law 42 as a tax "is contrary to the plain text of Law 42 and, in any event, as stressed by [Ecuador], it was not 'created' in accordance with the Ecuadorian Constitution."[157] Thus, the tribunal exclusively focused on the domestic law characterization of Law 42 and did not at all consider the contrary characterization of the *Burlington* tribunal as a matter of international law.

Next came the *Murphy v. Ecuador* arbitral tribunal, which, like the *Burlington* and *Occidental (II)* tribunals, also adjudicated claims under the U.S.-Ecuador BIT. However, the *Murphy* tribunal's characterization of Law 42, rendered in a partial final award in 2016, went in the exact opposite direction from the analysis of the *Burlington* tribunal:

> Law 42 operated similarly to a tax in that it imposed economic burdens (50% and later 99% of additional participation) upon a class of persons (contractors with participation contracts for oil exploration and exploitation in Ecuador) to pay money to the state, ostensibly for public purposes (to allocate a larger share in revenues derived from the country's natural resources to its citizens via state expenditure) without there being any direct benefit to the taxpayer. Law 42 and the subsequent *Ley de Equidad Tributaria* had similar effects.
>
> Notwithstanding these similarities, the Tribunal holds that, taking into account all circumstances, the more accurate characterisation of Law 42's operation is that it was not a tax, or a matter of taxation at international

153. *Id.* ¶¶ 198–99. In its Decision on Liability, the tribunal ultimately denied jurisdiction over these umbrella clause claims for lack of privity. *See id.* ¶¶ 220, 234.

154. *Id.* ¶ 181.

155. *Id.* ¶¶ 211, 215.

156. Occidental, ICSID Case No. ARB/06/11, ¶ 488.

157. *Id.* ¶¶ 489, 495.

> law, but a unilateral change by the state to the terms of the participation contracts that were governed by the Hydrocarbons Law. The stated purpose of the law was to amend certain oil contracts held by certain oil companies, all of which were foreign companies. The obligation to pay 50% in additional participation stemmed from the contractual obligations in the participation contracts. The revenue earned by the state under Law 42 was classified as nontax revenue. After the enforcement of Law 42, Ecuador's 'non-tax' revenue from hydrocarbon exploitation increased, while the contractors' decreased, essentially modifying the participation formula in the contracts.[158]

Importantly, the findings of the *Murphy* tribunal are tainted by two severe shortcomings.

First, the *Murphy* tribunal's determination that Law 42 does not constitute a tax or a matter of taxation, although accompanied by the qualifier "at international law," was effectively a determination focused on *domestic* law. The primary reason underlying the tribunal's determination is the (admitted) fact that "Law 42 was not enacted under Ecuadorian tax legislation" pursuant to the relevant provisions of the Ecuadorian Constitution but was rather "an amendment to the Hydrocarbons Law."[159] This reasoning is circular. On one hand, the tribunal stated that it must determine whether or not Law 42 constitutes a "matter of taxation at international law for the purposes of Article X(2)" of the U.S.-Ecuador BIT, "notwithstanding that Law 42 was clearly enacted outside of the Ecuadorian tax regime" as a matter of domestic law. The tribunal also accepted explicitly that "the domestic characterization of a measure is not determinative at international law."[160] On the other hand, the tribunal's reasoning under international law followed precisely the same footsteps as its reasoning under domestic law, namely that Law 42 did not operate as a tax but as "a unilateral change by the state to the terms of the participation contracts that were governed by the Hydrocarbons Law."[161]

The above critique is not to suggest that an international law characterization of whether a particular measure is a "taxation measure" should come at the complete exclusion of a domestic law assessment. The domestic law characterization of a measure is indicative of the host state's systemic intentions and should be assessed to at least derive evidentiary support of such intentions, even if not as a decisive element. The flaw in the *Murphy* tribunal's approach was instead its misunderstanding of the distinction, from a purely international

158. Murphy, 2012 PCA Case Repository No. 2012-16, ¶¶ 189–90.

159. *Id.* ¶¶ 167–70, 185.

160. *Id.* ¶ 185; *see also id.* ¶ 161 ("Even though the domestic characterization of a law is not decisive in the treaty context, it is a strong indication as to how the law should be characterized.").

161. Murphy, 2012 PCA Case Repository No. 2012-16, ¶ 190.

law perspective, between a taxation measure and a taxation law. It is widely accepted that the term "measure" is of much broader import than law (or legislation) concerning taxation.[162] This distinction was alluded to most recently by the tribunal in *Freeport-McMoRan v. Peru,* which examined a taxation measure enacted under Peruvian law in the nature of imposition of penalties and interest. That tribunal found the taxation measure caught by the tax carve-out contained in the United States-Peru Trade Promotion Agreement to "nevertheless constitute 'tax measures,'" even though "penalties and interest are not taxes under Peruvian law."[163] It reasoned that the term "measure" includes but is not limited to matters enacted under a tax legislation.[164] Indeed, even the *EnCana* tribunal had envisaged precisely this when it alluded to "the breadth of the defined term 'measure,'" finding "no reason to limit" the tax carve-out "to the actual provisions of the law which impose a tax."[165] The *Murphy* tribunal's justification that Law 42 was not, strictly speaking, a tax law, but rather an amendment to the Hydrocarbons Law clearly runs afoul of this consistent understanding of taxation measures in international law.

Second, even though the *Murphy* tribunal alluded to the *EnCana* tribunal's prioritization of the "legal operation" over the "economic effect" of the measure in question, it is evident that the *Murphy* tribunal's analysis actually rests on the effect, and not the operation, of Law 42. For instance, the *Murphy* tribunal highlighted that Law 42 is "a unilateral change by the state to the terms of the participation contracts that were governed by the Hydrocarbons Law," such that it results in "amend[ing] certain oil contracts held by certain oil companies, all of which were foreign companies." The very phrasing of this finding suggests that it has much more to do with the effect of Law 42 than its legal operation. Similarly, the tribunal's myopic focus on the fact that Law 42 was not part of the Ecuadorian "tax regime" does not automatically disqualify it as a tax.

The fundamental flaw in the *Murphy* tribunal's application of the *EnCana* formula is its normative outlook that "not every mandatory payment made by a class of persons to the state for public purposes without direct benefit is necessarily a tax."[166] But that is precisely what the *EnCana* formula requires. As per that formula, "a taxation law is one which imposes a liability on classes

162. *See, e.g.*, Terminal Forest Products Ltd. v. United States, UNCITRAL, Decision on Preliminary Question, ¶ 258 (June. 6, 2006) ("Within the terminology used in the NAFTA, 'measure' is indeed broader than 'law.'"), https://www.italaw.com/cases/200 [https://perma.cc/DH8V-LK6P]; Ethyl Corporation v. Canada, UNCITRAL, Award on Jurisdiction, ¶ 66 (June. 24, 1998), https://www.italaw.com/cases/409 [https://perma.cc/28LP-E9WH].

163. Freeport-McMoRan Inc. v. Republic of Peru, ICSID Case No. ARB/20/8, Final Award, ¶ 551 (May 17, 2024) [hereinafter Freeport].

164. *Id.* ¶¶ 546–49.

165. EnCana, LCIA Case No. 2012-16, ¶ 145.

166. *Id.* ¶ 191.

of persons to pay money to the state for public purposes."[167] Not only should every mandatory payment made by a class of persons to the state for public purposes without direct benefit qualify as a tax, but any such measure that legally operates to add to the state's revenue, in any manner whatsoever, should also qualify as such. This is regardless of whether that measure has been enacted by the taxation department of the government or under the constitutional provisions associated with taxation. This includes, for instance, measures that are enacted or implemented simply to adjust the distribution of refunds or to change the qualification of a particular asset, which do not directly appear to be enacted within a "tax regime" but directly result in a rise of the state's revenue.[168] Indeed, the myopic outlook professed by the *Murphy* tribunal has enabled many tribunals to breach the jurisdictional dam to exercise jurisdiction over taxation measures that legally operated to raise the revenue of the state exchequer through the imposition of mandatory payments on a class of people. An important example again is the solar levy imposed by the Czech Republic, to which, as discussed above, tribunals have frequently refused to extend the protection of the tax carve-out on many occasions, even though "one purpose of the [s]olar [l]evy was to raise revenue for the [s]tate."[169]

Even more egregiously, the *Murphy* tribunal chose to breach the jurisdictional dam by disqualifying Law 42 from the protection of the tax carve-out despite paying homage to the principle of fiscal sovereignty. For instance, the tribunal, while noting that the purpose of the tax carve-out was "specifically . . . to preserve the States' sovereignty in relation to their power to impose taxes in their territory," found that "[m]ost governments view these powers as a central element of sovereignty. Therefore, while they may be willing to accept international discipline over State conduct, they are reluctant to accept such oversight as regards their powers of taxation."[170] This ostensible homage to the principle of fiscal sovereignty is nothing more than lip service. Had the *Murphy* tribunal given appropriate value to the principle of fiscal sovereignty, its characterization of Law 42 might have been different. At the very least, a proper recognition of this principle might have prompted the tribunal to apply the *EnCana* tribunal's formula more earnestly by cleanly delineating the legal operation of Law 42 from its economic

167. *Id.* ¶ 142

168. *See, e.g.*, Sun Reserve, 5 SSC Case No. 132/2016, ¶¶ 556–61 ("Claimants' claims concerning the classification of photovoltaic plants as immovable property are, in essence, claims relating to the underlying taxation measures . . . . The characterization of photovoltaic plants is important, because immovable and movable property are subject to different depreciation rates and thus different effective tax rates, as well as different municipal charges"); Athena Investments, 5 SCC Case No. 2015/095, ¶¶ 231–33.

169. Photovoltaic Knopf, 2014 PCA Case Repository No. 2014-21, ¶ 258; *see also* Antaris, 2014 PCA Case Repository No. 2014-01, ¶ 240; ICW, 2014 PCA Case Repository No. 2014-19, ¶ 317; WA Inv., 2014 PCA Case Repository No. 2014-19, ¶ 336.

170. *See generally* Murphy, 2012 PCA Case Repository No. 2012-16.

effect, as the *Burlington* tribunal did. In other words, a more careful assessment of Law 42 and its legal operation would have manifested a genuine regard to Ecuador's fiscal sovereignty. Moreover, instead of drawing comfort from the fact that Law 42 was not enacted as part of Ecuador's tax regime but was instead enacted as an amendment to the Hydrocarbons Law, which enabled the tribunal to breach the jurisdictional dam, the tribunal could have used precisely this legal foundation of Law 42 to better appreciate the attack on Ecuador's fiscal sovereignty. As already mentioned, in ISDS cases that involve at their crux the host state's natural resources, an adjustment of perspective as to matters of fiscal policy could make it incumbent upon ISDS arbitral tribunals to judiciously assess a state's legitimate interest in exercising fiscal control over such natural resources since this interest lies at the cusp of the state's fiscal sovereignty as well as its permanent sovereignty over natural resources.

Such a misapplication of the principle of fiscal sovereignty, coupled with perfunctory lip service to it, has created a dangerous lack of jurisprudential consistency in the characterization of the same measure on the international plane. A disciplined and well-grounded application of the principle of fiscal sovereignty under Article 31(3)(c) of the VCLT would significantly reduce this cacophony and add much-needed objectivity and consistency in the jurisprudence of ISDS arbitral tribunals. Moreover, it would compel ISDS arbitral tribunals to adopt the more apposite and overarching line of inquiry, such as whether the measure under attack operates as an exercise of the host state's legitimate interest in preserving its sovereignty over natural resources, including by imposing an obligation upon investors to contribute to the state's exchequer. It will likewise discourage a more inapposite and myopic line of questioning, such as whether the measure under attack was enacted under the domestic tax regime or as an amendment to the law regulating the natural resources in question.

2. Cases Where Investment Treaties Do Not Contain a Tax Carve-Out

The jurisprudential fate of ISDS claims advanced under BITs or MITs that do not contain a tax carve-out is substantially different. The UNCTAD, for instance, noted in a 2021 guide that "[m]ost old-generation [investment treaties] do not exclude tax measures . . . which means that tax-related measures, whether of general or specific application, are covered by [investment treaties]. This includes tax measures that fall within the scope of a [DTA] between the two countries."[171] The UNCTAD justifies the possibility of dual coverage of certain taxation measures by DTAs and investment treaties by asserting that "[a] specific tax-related matter may simultaneously fall within the scope of a

171. U.N. Conf. Trade & Dev., *International Investment Agreements and Their Implications for Tax Measures: What Policymakers Need to Know*, 16, U.N. Doc. UNCTAD/DIAE/PCB/INF/2021/3 (2021).

[DTA] as well as an [investment treaty] between the relevant countries. Most [investment agreements] are silent on their relationship with [DTAs] and generally no special mechanism exists for addressing tax-related claims under [investment treaties]."[172]

This is an unfortunate, albeit accurate, exposition of the approach that ISDS arbitral tribunals have taken in the past—and are likely to take in the future—when faced with a claim that challenges the imposition or application of a tax or taxation measure of a host state. Indeed, in the absence of a tax carve-out in the BIT or MIT in question, an arbitral tribunal may never even bother to question their jurisdiction over tax claims. This is not to say that no ISDS arbitral tribunal has adopted a judicious approach when adjudicating over such a taxation measure in the absence of a tax carve-out in the BIT or MIT in question. One such example is the tribunal in *Paushok v. Mongolia*, which was faced with a claim under the BIT between Mongolia and the Russian Federation challenging a legislative enactment of the Mongolian Parliament, the Great Khural, that imposed a windfall profit tax of 68% on any gold sales at prices in excess of USD 500 per ounce on the amount exceeding the said base price.[173] The tribunal dismissed this claim, noting that even though the windfall profit tax may have been "considered excessive" in certain respects, "arbitrary and unreasonable," specifically noting the circumstance "when it comes to dealing with fiscal legislation which on its face is not targeting Claimants in particular or foreign investors in general."[174] The finding of the tribunal in *Paushok* shows that it was cautious of trespassing into matters of fiscal policy. However, this cautious approach, judicious as it may be, warrants being accelerated or repositioned into the tribunal's assessment of its own jurisdiction before entering into the merits of any claims that implicate taxation measures that lie dangerously close to matters of fiscal policy. This repositioning of the discourse can be achieved by taking into consideration the general principle of fiscal sovereignty while interpreting the dispute resolution clause contained in the BIT or MIT in question under Article 31(3)(c) of the VCLT.

To exemplify this proposition, the author shall use, and in the process critique, the findings of the arbitral tribunal in *Cairn v. India.* This was a rare case where the tribunal was faced with a claim that directly challenged a legislative taxation measure that impacted the investor, but before it could assess the merits of the claim, the tribunal was required to determine India's jurisdictional objection that was in essence predicated on the principle of fiscal

172. *Id.*

173. Sergei Paushok, CJSC Golden East Co. and CJSC Vostokneftegaz Co. v. Mongolia, UNCITRAL, Award on Jurisdiction and Liability, ¶ 104 (Apr. 2, 2011), https://www.italaw.com/sites/default/files/case-documents/ita0622.pdf [https://perma.cc/3CK3-LZ7D].

174. *Id.* ¶ 321.

sovereignty. The challenged taxation measure was a capital gains tax retrospectively imposed by India in 2012 on any offshore transaction that relates to shareholding in an Indian company "if the share or interest derives, directly or indirectly, its value substantially from the assets located in India."[175] The measure gave rise to several ISDS arbitrations against India.[176] Although several of these arbitrations, and, by extension, the reasoning for their verdicts, were not public, it is known that India lost each. The detailed award of the *Cairn v. India* arbitral tribunal, constituted under the Agreement between the Government of the United Kingdom of Great Britain and Northern Ireland and the Government of the Republic of India for the Promotion and Protection of Investments ("India-U.K. BIT"),[177] may offer some insight into India's consistent lack of success in defending the retrospectively imposed capital gains tax.

Given the scope of the present Article, the focus of this analysis is on the tribunal's findings with respect to India's objection to its jurisdiction over the tax dispute, on the ground that "tax disputes are not capable of being resolved by arbitration under the BIT in light of an implied exception to the scope of application of the BIT, and of the fact that [India] and the United Kingdom [i.e., the home state] have in fact specifically agreed that tax disputes should be settled in accordance with the procedure prescribed in the contemporaneous [DTA]."[178] Notably, in the India-U.K. BIT, there was a standard-specific tax carve-out which explicitly excluded taxation measures from the most-favored nation treatment provision. Cairn Energy relied on this standard-specific tax carve-out to contest India's jurisdictional objection, stating that the specificity of the tax carve-out implied that taxation measures are "not excluded for the purposes of other substantive provisions of the BIT."[179] India argued that, although the India-U.K. BIT lacked a generic tax carve-out or any other express and general exclusion of "taxation," the exclusion of taxation measures was implied by "the existence of general limits to the scope of protection of investment treaties which exist even if they are not made explicit."[180]

While the arbitral tribunal was called to examine India's jurisdictional objection also as a matter of "international public policy, Indian law [and] Dutch law," this critique is limited to the tribunal's interpretation of the India-U.K.

175. Cairn Energy PLC and Cairn UK Holdings Ltd. (CUHL) v. India, 2016 PCA Case Repository No. 2016-7, Final Award, ¶ 124 (Dec. 21) [hereinafter Cairn].

176. *See generally* Vodafone Int'l Holdings BV v. India [I], 2016 PCA Case Repository No. 2016-35; Vodafone Grp. Plc and Vodafone Consol. Holdings Ltd. v. India [II], UNCITRAL, Order of Delhi High Court (Dec. 14, 2022), https://www.italaw.com/cases/5713 [https://perma.cc/D29A-P47N]; Vedanta Res. v. India, PCA Case Repository No. 2016-05.

177. Agreement for the Promotion and Protection of Investments, India-U.K., art. 4(3), Jan. 6, 1995, 27 U.N.T.S. 1.

178. Cairn, 2016 PCA Case Repository No. 2016-7, ¶ 764.

179. *Id.* ¶¶ 768, 780.

180. *Id.* ¶ 767.

BIT, which rested upon an untenable distinction between "tax disputes" and "tax-related investment disputes":

> [I]t merits clarifying that the present dispute is a tax-related investment dispute, not a tax dispute. More precisely, this dispute concerns alleged violations of an investment treaty resulting from certain sovereign measures taken by the Respondent in the field of taxation, also referred to as fiscal measures. This type of dispute must be distinguished from tax disputes proper, which are disputes concerning the taxability (including the tax-amount) of a specific transaction. The distinction is significant. In a tax dispute, the question is whether and how a particular transaction is taxable under the applicable (municipal) law or, possibly laws of several countries if the transaction is international. In tax-related investment disputes, on the other hand, the tribunal is tasked with determining whether the respondent state has breached substantive standards of treatment under the investment treaty through the exercise of its authority in the field of taxation, and whether liability arises as a result. The issue at stake is thus not a matter of domestic tax law; it is rather whether the fiscal measures taken by the state, valid or not under its own tax laws, violate international law.[181]

This distinction—which the arbitral tribunal provided no interpretative nor international law basis for—must be put under scrutiny because it has the potential of being misused in investor-state arbitrations. This finding, and other findings of the *Cairn* tribunal, can be critiqued in three primary ways.

First, although this is not the first exposition of a distinction between tax disputes and tax-related investment disputes,[182] it has the potential to be its most destabilizing and far-reaching enunciation. The broad terms in which the distinction is articulated by the tribunal makes it susceptible to indiscriminate misappropriation by investors who may seek to advance all kinds of claims implicating taxation measures under the guise of them being tax-related investment disputes, regardless of whether the BIT in question has a tax carve-out. Under the logic of the *Cairn* tribunal, all an investor needs to do to escape a tax carve-out is to characterize their claim as a tax-related investment dispute. This requires the tribunal to limit its focus to the substantive standards of treatment under the BIT in question, and not to determine whether the tax should have been imposed by the host state. Indeed, if the distinction between a tax dispute and tax-related investment dispute is taken to its logical extreme, it could demolish the jurisdictional dam set up by tax carve-outs, since there would be nothing prohibiting arbitral tribunals from assuming jurisdiction

181. *Id.* ¶ 793.

182. The existence of such a distinction has been advocated by certain scholars in the past. *See, e.g.*, William W. Park, *Arbitrability and Tax*, *in* Arbitrability: International & Comparative Perspectives 179, 183 (Loukas Mistelis & Stavros Brekoulakis eds., 2009); Marian, *supra* note 71, at 246.

over taxation measures—not even tax carve-outs—if the tribunals were to subscribe to the investor's characterization of their claim as only requiring a determination on the substantive standards of treatment under the BIT. After all, every claim advanced under a BIT is an investment dispute that warrants the application of these substantive standards. If that were the qualification against which jurisdictional inquiries pertaining to taxation measures were conducted, any jurisdictional hurdles could be bypassed using the standards of protection against which the measures are to be examined.

This is a fundamental misapplication of international law. In reality, as a matter of international law, it is incumbent upon the adjudicatory body in question, be it a court or an arbitral tribunal, to identify the measure under challenge as "precisely and narrowly as is reasonably possible having regard to the factual and legal issues."[183] This process of independent characterization is an essential precursor to determining whether a sovereign state has consented to resolving the dispute regarding the measure in question through ISDS by waiving its default sovereign immunity from such actions. The *Cairn* tribunal failed to identify the measure under challenge in a sufficiently precise manner by neglecting the conceptual distinction between the challenged measure (i.e., the capital gains tax retrospectively imposed by India) and the standards of protection under the India-U.K. BIT (i.e., the entitlement to fair and equitable treatment). The fact that the challenged measure must be assessed against this standard of protection under the BIT is irrelevant to whether the arbitral tribunal has the authority to adjudicate a dispute implicating the said measure.

Although the award rendered by the *Cairn* tribunal was ultimately annulled by the Court of Appeal in The Hague in December 2021, this annulment was based on the mutual agreement of the disputing parties, who had already agreed to settle the dispute. Therefore, the findings of the *Cairn* tribunal arguably remain available, at least as persuasive authority. In this regard, it warrants mentioning that the distinction espoused by the *Cairn* tribunal has been criticized in scholarship for being too "far reaching"[184] and has also been regulated by the *Cour d'appel* in Paris, which, in its decision in *Ryan et al v. Poland*, specifically sought to limit the application of the distinction to treaties that do not contain a tax carve-out.[185] However, this, too, does not eliminate the potential

183. Zachary Douglas, *State Immunity for the Acts of State Officials*, 2012 Brit. Y.B. Int'l Law 281, 328; James Crawford, *International Law and Foreign Sovereigns: Distinguishing Immune Transactions*, 1984 Brit. Y.B. Int'l Law 96, 97; The United Nations Convention on Jurisdictional Immunities of States and their Properties 66–67 (Roger O'Keefe & Christian J. Tams eds., 2012); Hazel Fox, The Law of State Immunity 410–18 (2013).

184. Błażej Kuźniacki & Stef van Weeghel, *Cairn Energy: When Retroactive Taxation not justified by Prevention of Tax Avoidance is Unfair and Inequitable*, 39 Arb. Int'l 125, 130 (2023).

185. Cour d'appel [CA] [regional court of appeal] Paris, May 30, 2022, 21/01497.

for misappropriation that the influential yet artificial distinction between tax disputes and tax-related investment disputes carries.

Second, the chasm between tax disputes and tax-related investment disputes espoused by the *Cairn* tribunal in order to assume jurisdiction over a quintessential taxation measure was coupled with other interpretative fallacies committed by the tribunal. When interpreting the dispute resolution clause in the BIT, the tribunal asked whether "the Contracting Parties consented to submit tax-related investment disputes to arbitration."[186] Notwithstanding that the question itself was premised on the inapposite term of art "tax-related investment disputes,"[187] the interpretative technique that the tribunal employed started, from the very outset, with a mischaracterization of India's argument.

The tribunal read India's argument "that, since tax matters are regulated by another international treaty, the [DTA between India and the United Kingdom], the BIT should be read so as to exclude such matters from its scope" as implying that India was invoking Article 30 of the VCLT to argue that the DTA between India and the United Kingdom "derogates from the BIT."[188] However, the tribunal misunderstood India's argument. India, not a party to the VCLT, had not invoked Article 30 at all. Instead, it was in essence urging the tribunal to factor in the DTA between India and the United Kingdom as an instrument of international law that already regulated issues of taxation between these two states, thereby indicating that the BIT between these states could not simultaneously confer upon an investor-state arbitral tribunal the jurisdiction to adjudicate Cairn's "wide-ranging challenge to India's fiscal sovereignty."[189] In other words, India's reliance on the DTA was intended only to support its argument that "India has never agreed to subject its general fiscal measures to international arbitration and tax disputes are not arbitrable."[190] This argument exemplifies an attempt at the 'systemic integration' of international law that VCLT Article 31(3)(c) seeks to achieve. Thus, the argument was ripe for consideration under Article 31(3)(c) as an invocation of the general principle of fiscal sovereignty represented in a rule of conventional international law (i.e., the DTA) that should be taken into account while interpreting the dispute resolution clause of the BIT.

Indeed, if the tribunal had been sua sponte open to the possibility of examining the relationship between the DTA and the BIT under Article 30 of the VCLT, there was nothing impeding the tribunal from considering India's

186. Cairn, 2016 PCA Case Repository No. 2016-7 at iii, ¶¶ 796–815.

187. Indeed, the tribunal provided no source or any other basis for this term, which is neither a term used in BITs or MITs nor, by appearance, used by other ISDS arbitral tribunals that have dealt with claims that challenge taxation measures.

188. Cairn, 2016 PCA Case Repository No. 2016-7, ¶ 801.

189. *Id.* ¶ 778.

190. *Id.*; *see also id.* ¶¶ 772–77.

argument as an invocation of the principle of fiscal sovereignty under Article 31(3)(c). However, the tribunal did not do so and thus ended up treating the BIT and the DTA as two fragmented instruments of international law.

Moreover, the tribunal, while focusing on the presence of a standard-specific tax carve-out in the India-U.K. BIT, committed another interpretative fallacy by premising its assumption of jurisdiction on the finding that "neither the BIT in general nor its dispute resolution provision in particular contains an exclusion for tax-related investment disputes."[191] This is a quintessentially *a contrario* interpretation of the BIT and its dispute resolution clause in particular, "by which the fact that the provision expressly provides for one category of situations is said to justify the inference that other comparable categories are excluded."[192]

This reliance on a negative or *a contrario* reasoning is inconsistent with the scheme of interpretation prescribed in Article 31 of the VCLT. The ICJ has warned against using this technique to interpret treaties in several cases. Indeed, such an *a contrario* interpretation has been deployed in international law in supplementary fashion only "when recourse to elements of Article 31 VCLT does not lead to a definite answer, and always in a manner that does not allow for an *a contrario* construction to prevail when it is not supported (or even goes against) the standard elements of treaty interpretation . . . ."[193] For instance, in the *Continental Shelf* case, Judge Arechega observed in his separate opinion that it is not "a convincing method of interpretation to invoke the text of one of these articles by arguments *a pari* or *a contrario* in order to reach a certain conclusion in respect of the other provision."[194] Similarly, in the *Question of Delimitation* case, the ICJ noted that an *a contrario* interpretation of a treaty "is only warranted . . . when it is appropriate in light of the text of all the provisions concerned, their context and the object and purpose of the treaty."[195] This finding was reiterated in the *Alleged Violations of Sovereign Rights and Maritime Spaces* case.[196] But perhaps most germane are the ICJ's findings in the *Certain Iranian Assets* case. In this case, Iran sought to defend the existence of an obligation of the United States under

191. *Id.* ¶ 809.

192. Question of the Delimitation of the Cont'l Shelf between Nicar. and Colom. beyond 200 Nautical Miles from the Nicaraguan Coast (Nicar. v. Colom.), Judgment, 2016 I.C.J. Rep. 100, ¶ 35 (Mar. 17).

193. Sotirios Lekkas et al., *The Interpretative Practice of the International Court of Justice*, 2023 Max Planck Y.B. U.N. L. Online 316, 350; *see, e.g.*, Arrest Warrant of 11 April 2001 (Dem. Rep. Congo v. Belg.), Judgment, 2002 I.C.J. Rep. 68, ¶ 38 (Feb. 14) (separate opinions by Higgins, J., Kooijmans, J., Buergenthal, J.).

194. Cont'l Shelf (Libya v. Malta), Judgment, 1984 I.C.J. Rep. 55, ¶ 10 (Mar. 21) (separate opinion by de Arechaga, J.).

195. Nicar. v. Colom., 2016 I.C.J. Rep., ¶ 35.

196. Alleged Violations of Sovereign Rts. and Mar. Spaces in the Caribbean Sea (Nicar. v. Colom.), Judgment, 2016 I.C.J. Rep. 3, ¶ 37 (Mar. 17).

the Treaty of Amity to uphold the immunity of Iranian entities that engage in activities *jure imperii*. Iran drew this implication by presenting an *a contrario* interpretation of a provision in the Treaty (i.e., Article XI, paragraph 4 thereof) which expressly excluded immunity in the case of enterprises of a state party to the Treaty of Amity that were "publicly owned or controlled" and engaged in "commercial [or] industrial" activities within the territory of the other state party.[197] The ICJ rejected Iran's argument in its entirety, finding as follows:

> Iran goes further in contending that this provision imposes an implied obligation to uphold those immunities. [Iran] adopts, in this regard, an *a contrario* reading of Article XI, paragraph 4, whereby, in excluding from immunity only publicly owned enterprises engaging in commercial or industrial activities, this provision implicitly seeks to guarantee the sovereign immunity of public entities when they engage in activities *jure imperii* [. . . .]
>
> [T]he Court cannot adopt the interpretation put forward by Iran. It is one thing for Article XI, paragraph 4, to leave intact, by not barring them, the immunities enjoyed under customary law by State entities when they engage in activities *jure imperii*. It is quite another for it to have the effect, as Iran claims it does, of transforming compliance with such immunities into a treaty obligation, a view not supported by the text or context of the provision.
>
> If Article XI, paragraph 4, mentions only publicly owned enterprises which engage in 'commercial, industrial, shipping or other business activities', this is because, in keeping with the object and purpose of the Treaty, it pertains only to economic activities and seeks to preserve fair competition among economic actors operating in the same market. The question of activities *jure imperii* is simply not germane to the concerns underlying the drafting of Article XI, paragraph 4. The argument that this provision incorporates sovereign immunities into the Treaty thus cannot be upheld.[198]

The ICJ's analysis is transposable to the jurisdictional scenario facing the *Cairn* tribunal. If the *Cairn* tribunal had refrained from adopting an *a contrario* interpretation of the dispute resolution clause, based on the inferences it drew from the presence of a standard-specific tax carve-out, it could also have come to the conclusion that the presence of a standard-specific tax carve-out does not by implication create a treaty obligation upon India to arbitrate all tax disputes under the other standards of protection. This conclusion would have been bolstered by an appropriate application of the general principle of fiscal sovereignty, which would also have materially informed the interpretation of the dispute resolution clause in the India-UK BIT. However, the *Cairn* tribunal, like

197. Certain Iranian Assets (Iran v. U.S.), Judgment, 2019 I.C.J. Rep. 7, ¶ 60 (Feb. 13).
198. *Id.* ¶¶ 63–65.

other ISDS arbitral tribunals faced with similar jurisdictional inquiries, was oblivious to the consistently expressed admonitions against *a contrario* interpretations by the ICJ. Instead, the *Cairn* tribunal made its *a contrario* implications a central feature of its analysis. This practice differs sharply from the widely recognized view that *a contrario* implications should "never in and of itself [be] determinative of a particular interpretation," but rather be deployed only "when necessary."[199] The *Cairn* tribunal's reasoning also runs counter to the VCLT's scheme of interpretation, which prefers the text of a treaty to be the driving force of interpretation, as opposed to inferences from the absence of text.[200]

Third, although it might seem counter-intuitive to argue that a means exists to exclude certain kinds of tax disputes from an ISDS arbitral tribunal's jurisdiction even when the BIT in question does not contain a tax carve-out, such a solution is both available and desirable in light of the general principle of fiscal sovereignty.

The reasons behind the desirability of this solution are encapsulated in the discussions in the preceding sections of this Article. They rest chiefly on the merits of exalting the status of the principle of fiscal sovereignty to a general principle of international law, especially in the post-colonial narrative thereof. Nor is the availability of this solution in a situation where the BIT does not contain a tax carve-out hindered by the presence of tax carve-outs in other (comparator) BITs, or by the general state practice of including tax carve-outs in BITs. Indeed, leveraging the absence of a tax carve-out in a BIT to assert jurisdiction over tax policy would constitute an impermissible *a contrario* interpretation of the BIT. Moreover, giving effect to the principle of fiscal sovereignty even when there is no tax carve-out does not render tax carve-outs, when they exist, redundant, and consequently does not implicate the principle of *effect utile* or the general canon against superfluity. Indeed, the presence of tax carve-outs in BITs or MITs cannot be given consideration without fully comprehending the object and purpose that tax carve-outs seek to achieve. As already discussed in detail above, the most vital objective behind the inclusion of tax carve-outs in BITs or MITs is to preserve the fiscal sovereignty of the state parties to the treaty in question. This has been expressly acknowledged by many ISDS arbitral tribunals, as also already discussed.[201]

However, while tax carve-outs preserve fiscal sovereignty, they are not a prerequisite to its recognition. This warrants the question of why states would stipulate tax carve-outs at all, if their fiscal sovereignty is already considered to

199. Abdulqawi A. Yusuf & Daniel Peat, A Contrario *Interpretation in the Jurisprudence of the International Court of Justice*, 3 Can. J. Comp. Cont. L. 1, 15 (2017); Popa, *supra* note 78, at 257–58.

200. Lekkas et al., *supra* note 193.

201. *See generally* Murphy, 2012 PCA Case Repository No. 2012-16; Sun Reserve, 5 SSC Case No. 132/2016.

be a general principle of international law. The answer to this question lies in the second, perhaps equally important, objective behind tax carve-outs: to ensure greater clarity and breadth regarding the kinds of "taxation measures" excluded or carved out from the BIT. For instance, ECT Article 21(7)(a) defines the term "taxation measure" as follows:

> For the purposes of this Article:
>
> (a) The term 'Taxation Measure' includes:
>
> (i) any provision relating to taxes of the domestic law of the Contracting Party or of a political subdivision thereof or a local authority therein; and
>
> (i) any provision relating to taxes of any convention for the avoidance of double taxation or of any other international agreement or arrangement by which the Contracting Party is bound.

This inclusive definition demonstrates that the tax carve-out in Article 21(1) was intended to cover a wide array of measures. The *travaux préparatoires*, or official negotiation records, of the ECT also confirm that the definition of "taxation measure" was intentionally kept broad and non-exhaustive because being more precise would be "counterproductive" in light of "the wide variety of taxation measures" that the ECT state parties wished to cover.[202] Similarly, international jurisprudence also understands the term "measure" in broad terms, recognizing that it includes legislative, executive or judicial action. For instance, the ICJ, in the *Fisheries Jurisdiction* case, noted that the term "measure" in a treaty is not restricted to legislative measures, but "in its ordinary sense the word is wide enough to cover any act, step or proceeding, and imposes no particular limit on their material content or on the aim pursued thereby."[203] Similarly, ISDS arbitral tribunals have also long recognized that the term "measure" in BITs or MITs, especially when coupled with taxation, clearly means "something other than a 'law,' even something in the nature of a 'practice,' which may not even amount to a legal stricture."[204]

The example of the ECT aligns with several other BITs and MITs wherein states have chosen to define "measures" or "taxation measures" expansively, so as to specify that they include "law, regulation, procedure, requirement, or

202. Can. Energy Charter Secretariat, Letter Dated Mar. 19, 1993 from the Energy Charter Secretariat addressed to F. Mullen (Mar. 19, 1993).

203. Fisheries Jurisdiction (Spain v. Canada), 1998 I.C.J. Rep. 432, ¶ 66 (Dec. 4).

204. Ethyl Corporation, UNCITRAL; Canfor Corp, UNCITRAL; Freeport, ICSID Case No. ARB/20/8, ¶¶ 546–47; Loewen Group, Inc. and Raymond L. Loewen v. United States, ICSID ARB(AF)/98/3, Decision on Hearing of Respondent's Objection to Competence and Jurisdiction, ¶ 47 (Jan. 5, 2001) ("Such an interpretation of the word 'measures' accords with the general principle of State responsibility. The principle applies to the acts of judicial as well as legislative and administrative organs.").

practice." Recently, this exact expansive definition was included in the United States-Mexico-Canada Agreement in 2020 and the European Union-Singapore Free Trade Agreement in 2019.[205] Such definitions are plentiful in BITs and MITs around the globe.[206] Thus, state practice clearly confirms that a significant object and purpose behind the inclusion of tax carve-outs in BITs and MITs is to lend greater clarity and breadth to the general principle of fiscal sovereignty and not to undermine this general principle.

The presence of tax carve-outs in BITs and MITs benefits the contracting states by serving to expand the kinds of taxation measures included beyond the existing frontier already covered within the general principle of fiscal sovereignty. In the preceding Sections, the author has shown that the general principle of fiscal sovereignty covers matters that implicate a state's tax policy, best represented in the exercise of the state's legislative power to tax. This assertion aligns well with the UNCTAD's definition of fiscal sovereignty, which characterizes fiscal sovereignty as "the jurisdiction to tax . . . based on the domestic legislative process, which is an expression of national sovereignty."[207] Based on this, taxation measures that are based strictly on the host state's legislative process or that pertain to the exercise of the state's legislative power to impose tax should, in any event, always be covered within the purview of the general principle of the state's fiscal sovereignty. Pursuant to a good-faith application of this general principle, any claims brought by investors that directly challenge such a taxation measure, by, for instance, testing the validity of a legislative enactment against the investment protection standards (as distinct from its application or enforcement), should always be excluded from any offer to arbitrate under a BIT or an MIT, even in the absence of an explicit tax carve-out. In other words, claims brought by investors that challenge a policy choice of the state—usually

205. Agreement between United States-Mexico-Canada, U.S.-Mex-Can., art. 1.5, Jul 1, 2020, 134 Stat. 11; Free Trade Agreement, Eur. Union-Sing., art. 1.3, Nov. 21, 2019, https://policy.trade.ec.europa.eu/eu-trade-relationships-country-and-region/countries-and-regions/singapore/eu-singapore-agreements/texts-agreements_en [https://perma.cc/PS2H-4FKW].

206. *See, e.g.*, Agreement for the Promotion and Reciprocal Protection of Investments, Can.-Phil., art. 1(h), Nov. 13, 1996, 1996 CTS 46 (defining "measure" to "include any law, rule, regulation, requirement, or established governmental procedure or practice"); Treaty Concerning the Encouragement and Reciprocal Protection of Investment, U.S.-Uru, art. 1, Nov. 1, 2006, T.I.A.S. 06-1101 (defining "measure" to include "any law, regulation, procedure, requirement, or practice"); Free Trade Agreement, U.S.-Dom. Rep.-Cent. Am., art. 2.1, Jan. 1, 2009, 119 Stat. 462 (defining "measure" to include "any law, regulation, procedure, requirement, or practice"); Free Trade Agreement, U.S.-S. Kor., art. 1.4, Mar. 15, 2012, 19 CFR 10.1004 (defining "measure" to include "any law, regulation, procedure, requirement, or practice"); Comprehensive Economic and Trade Agreement, Eur. Union-Can., art. 1.1, Sept. 21, 2017, 2021 CTS 6 (provisional application) (defining "measure" to include "a law, regulation, rule, procedure, decision, administrative action, requirement, practice or any other form of measure by a Party").

207. U.N. Conf. Trade & Dev., Taxation, *supra* note 39.

manifested in its legislative process[208]—to impose a tax should be foreclosed on the basis of the general principle of fiscal sovereignty, notwithstanding whether the BIT or MIT in question contains a tax carve-out. By contrast, claims that challenge other kinds of taxation measures, i.e., measures that do not pertain to the exercise of the state's legislative power to implement a policy choice but instead pertain to the application or enforcement of a taxation measure, may be considered to fall outside of the general principle of fiscal sovereignty. Thus, such claims may fall within the jurisdiction of arbitral tribunals—albeit only in the absence of a tax carve-out. A tax carve-out in the BIT or MIT in question would therefore serve to ensure that such claims would instead be caught in the jurisdictional dam. Accordingly, a tax carve-out is best construed as a declaratory provision that is intended to clarify the breadth of the taxation measures that fall outside the purview of the BIT or MIT in question.

This argument is not new. Indeed, other than the various authorities discussed in the preceding Sections, scholarly and jurisprudential, that have considered the principle of fiscal sovereignty from various angles, certain ISDS arbitral tribunals have expressly spoken about this distinction between policy-based taxation measures manifested in the exercise of the state's legislative power to tax, and other kinds of taxation measures.

Most recently, the arbitral tribunal in *Freeport-McMoRan v. Peru*, when assessing its jurisdiction over a claim implicating a taxation measure (in particular, concerning the failure by the Peruvian government to waive certain penalties and interest), noted that even though the measure under challenge may not qualify as a tax, it would qualify as a taxation measure for the purposes of the tax carve-out contained in the United States-Peru Trade Promotion Agreement ("TPA"). This determination was based on the following findings:

> Article 1.3 of the TPA broadly defines the term "measure" as "any law, regulation, procedure, requirement or practice." Any law, regulation, procedure, requirement or practice related to "taxation" is addressed by Article 22.3.1 of the TPA.
>
> Turning to the term "taxation", the Tribunal notes that the TPA refers to both "taxes" and "taxation measures." Those terms must accordingly refer to different concepts. Moreover, in the Tribunal's view, the word "taxation" refers to a broader notion than the term "tax" . . .
>
> *The Tribunal is of the view that "taxation measures" include measures that are part of the regime for the imposition and enforcement of a tax*. The Tribunal finds that the application of, or failure to apply a tax, as well as the enforcement or failure to enforce a tax constitute "practice(s)" related to "taxation" . . . .

208. As noted by the arbitral tribunal in *Murphy v. Ecuador,* "[a] State's domestic tax regime is the manifestation of its tax policies." *See* Muphy, 2012 PCA Case Repository No. 2012-16, ¶ 161.

> Finally, the Tribunal turns to the object and purpose of the Treaty. The object and purpose of the Treaty is *inter alia* to "promote regional economic integration" between the TPA parties, "establish clear and mutually advantageous rules governing their trade", "ensure a predictable legal and commercial framework for business and investment," as well as "preserve their ability to safeguard the public welfare." The purpose of Chapter Twenty-Two is to preserve the States' sovereign power in matters of legitimate regulatory interest to States. *With respect to Article 22.3 of the TPA in particular {i.e., the tax carve-out}, the Tribunal agrees with the Murphy v. Ecuador tribunal's finding, which considered that the purpose of the tax carve-out in the underlying treaty is to "preserve the States' sovereignty in relation to their power to impose taxes in their territory."*[209]

The above findings can serve as a template from which other ISDS arbitral tribunals can take inspiration, not least because they constitute a proper application of the principle of fiscal sovereignty when interpreting a tax carve-out. The findings also represent an accurate understanding of the other objective behind the inclusion of tax carve-outs in BITs or MITs, inasmuch as they do not, implicitly or explicitly, relegate the tax carve-out to being a necessary precondition in service of the preservation of a state's fiscal sovereignty. Instead, they treat the tax carve-out as what it is: a declaratory provision that seeks to broaden the purview of the kinds of taxation measures that may be excluded from an ISDS arbitral tribunal's jurisdictions, albeit not at the exclusion of the principle of fiscal sovereignty, which could independently serve to insulate matters of core fiscal policy from ISDS. In other words, a tax carve-out may be necessary to preserve a state's fiscal sovereignty over matters of "imposition and enforcement of a tax," but is not a prerequisite to the preservation of fiscal sovereignty that attaches itself to matters of core fiscal policy, usually represented in legislative enactments that impose taxes.

Similarly, in the case of *Spyridon Roussalis v. Romania*, the arbitral tribunal was faced with a claim under the BIT between Greece and Romania, which did not contain a tax carve-out, in which the investor had, inter alia, alleged that certain controls carried out and the decisions taken by the Romanian tax authorities were abusive and that the measures taken to enforce these decisions were disproportionate. The arbitral tribunal affirmed jurisdiction over this claim, but in the process specifically stated that "general measures of tax or economic policy not directly related to the investment, as opposed to measures specifically addressed to the operations of the business concerned, will normally fall outside the jurisdiction of the [tribunal]."[210] The context surrounding this general finding makes it clear that the tribunal's reasoning

209. Freeport, ICSID Case No. ARB/20/8, ¶¶ 546–50 (emphasis added).

210. Spyridon Roussalis v. Romania, ICSID Case No. ARB/06/1, Award, ¶ 489 (Dec. 7, 2011).

was agnostic to the presence of a tax carve-out. The tribunal went on to clarify that its assumption of jurisdiction over the investor's claim was contingent on the fact that this claim would not require it "to make decisions applying general tax policies," but would only require it to examine "decisions taken by tax authorities and courts, and actions taken by the State's authorities to enforce such decisions."[211]

The findings of the arbitral tribunal in the case of *Ryan et al. v. Poland* suggest a similar approach. In that case, the tribunal was called upon to interpret a tax carve-out contained in Article VI(2) of the BIT between the United States of America and the Republic of Poland ("U.S.-Poland BIT"). Notably, the stipulation of the tax carve-out started with the term "nevertheless," and it was preceded by a provision in Article VI(1), which provided that "[w]ith respect to its tax policies, each Party should strive to accord fairness and equity in the treatment of, and commercial activity conducted by, nationals and companies of the other Party."[212] Such a structured tax carve-out is not uncommon in BITs, especially those of the United States. While the arbitral tribunals in *Burlington*, *Occidental*, and *Murphy* were also faced with such tax carve-outs, they were not required to interpret the phrase "tax policies" contained in the provision preceding the actual tax carve-out in those cases. Distinctly, the *Ryan et al.* tribunal was required to interpret this phrase contained in Article VI(1) of the U.S.-Poland BIT, in contrast with the phrase "matters of taxation" contained in the tax carve-out (i.e., Article VI(1)) since the investors in this case had argued separately that Article VI(1) of the U.S.-Poland BIT created obligations of, inter alia, fair and equitable treatment that Poland had breached.[213] In this connection, the tribunal drew the following pertinent distinction between "matters of taxation" that the tax carve-out sought to regulate and "tax policies" in general:

> Taxation has three aspects. Levy of taxes, assessment of taxes and collection of taxes. In the view of this Tribunal, tax policies relate to the general framework under which taxes are levied. A claim that the State, as a matter of policy, has levied a tax in breach of its FET obligations under the BIT would arguably fall under Article VI(1) of the BIT. The claimant in such a case must not only demonstrate that the levy under challenge merely affects it adversely but also that the law levying the tax was the result of a tax policy of the Host State to treat the foreign investor in an unfair or inequitable manner or to deny it the protections of the BIT. "Matters of taxation," on the other hand, relate to assessment and collection of taxes (i.e. the implementation of the tax laws) and to claims about a substantive

211. *Id.* ¶¶ 492–93.

212. Vincent J. Ryan, Schooner Capital LLC, and Atlantic Investment Partners LLC v. Poland, ICSID Case No. ARB(AF)/11/3, Award, ¶ 209 (Nov. 24, 2015) [hereinafter Ryan].

213. *Id.* ¶ 271.

> law affecting an investor adversely. It is the view of this Tribunal that tax legislation which is not the product of a tax policy of the Host State to deny BIT protections to investors is a matter of taxation and not tax policy. Article VI(2) and not Article VI(1) of the BIT would, therefore, apply.[214]

The tribunal's findings implicitly affirm that matters of tax policy manifested in the exercise of the state's legislative power to tax (referred to by the tribunal as the "[l]evy of taxes") are distinct from other kinds of taxation measures that pertain to application or enforcement of taxation measures (referred to by the tribunal as "the assessment and collection of taxes"). This distinction has been alluded to by other tribunals, including the tribunal in *Paushok v. Mongolia,* which also expressed reluctance to find Mongolia in breach of the BIT in question "especially when it comes to dealing with fiscal legislation which on its face is not targeting Claimants in particular or foreign investors in general."[215] This finding contains within it the necessary implication that the tribunal might have found a breach of the BIT, had the claim implicated a discriminatory application or enforcement of taxation measures, as distinct from the legislative enactment thereof, which implicated general matters of fiscal policy.

Notably, however, while the (entire) *Ryan et al.* tribunal did remark that a claim challenging the host state's tax policy may "arguably" be advanced as a claim for a breach of the fair and equitable treatment obligation under Article VI(1) of the U.S.-Poland BIT, there was a difference of opinion on precisely this issue between the members of the tribunal. This difference provides insight into the qualifier used by the tribunal in its caveated finding. On the one hand, the majority of the tribunal went on to decide, taking inspiration from another tribunal that had decided the same issue,[216] that a BIT claim challenging a matter of tax policy would fall outside of its jurisdiction, since "Article VI(1) does not create a mandatory obligation for the state and, therefore, would not give rise to a BIT claim."[217] On the other hand, the dissenting arbitrator (i.e., the investor's appointee) Professor Francisco Orrego Vicuña, took issue with this point, finding as follows:

> In the opinion of this Arbitrator, tax policies were involved in this case since the transfers made by the Claimants were in accordance with the terms of the regulations governing this matter at the time that the investment was made and for several years thereafter until they were replaced

214. *Id.* ¶ 284.

215. Sergei Paushok, CJSC Golden East Company and CJSC Vostokneftegaz Company v. Mongolia, UNCITRAL, Award on Jurisdiction and Liability, ¶ 321 (Apr. 28, 2011), https://www.italaw.com/sites/default/files/case-documents/ita0622.pdf [https://perma.cc/3CK3-LZ7D].

216. *See generally* Nations Energy Corporation, Electric Machinery Enterprises Inc., and Jamie Jurado v. Panama, ICSID Case No. ARB/06/19, Award (Nov. 24, 2010).

217. Ryan, ICSID Case No. ARB(AF)/11/3, ¶ 288.

> by rules originating in OECD recommendations, which are by definition recommendations of policy. A government is certainly entitled to change its policies, but at the same time it must guarantee the rights that have been extended to the investor, which in the instant case would mean at the very least a process of transition from one regime to the next and the non-retroactive enforcement of such new policies.[218]

The opinion of the dissenting arbitrator is aligned with the approach that the *Cairn* tribunal took while determining India's jurisdictional objection (and defenses on the merits, for that matter) against Cairn's challenge to what was fundamentally a policy shift manifested in an amendment to India's tax legislation. This approach, now that it has been solemnized by the *Cairn* tribunal, risks perpetrating a complete jurisprudential disregard of the significant distinction between matters of tax policy and matters that go only towards the application or enforcement of that tax policy. As the majority of the tribunal in *Ryan et al.* hinted, states deserve vastly more autonomy with respect to the former kinds of matters than with respect to the latter kinds, and no objective of investment protection, however noble, can justify any encumbrances on the host state's exclusive fiscal sovereignty over such matters (unless, of course, in the unlikely event that the legislature of a state enacts a change of tax policy specifically to target an investor). This ambitious solution is best achieved by recognizing matters of tax policy as manifestations of the host state's fiscal sovereignty, which, as the author has already argued, should be afforded the status of a general principle of international law that cannot be ignored when interpreting dispute resolution clauses in BITs and MITs.

Conclusion

Based on the foregoing analysis, this Article attempts to make a concrete, albeit an unpopular, case in support of creating a jurisdictional dam to prevent ISDS arbitral tribunals from casually transgressing into the solemn territory of fiscal policy. Without requiring a complete overhaul of the system of BITs and MITs, this jurisdictional dam can most efficiently be constructed, with the help of ISDS arbitral tribunals, by recognizing a state's fiscal sovereignty as a general principle of international law under Article 31(3)(c) of the VCLT. Such a recognition of the concept of fiscal sovereignty—historically among the most fortified realms of Westphalian sovereignty—will not only bring about a much-needed systemic shift of attitudes insofar as ISDS is concerned but also serves two concrete functions.

First, insofar as cases arising under treaties that contain tax carve-outs are concerned, the recognition of the general principle of fiscal sovereignty might

218. *Id.* at Dissenting Opinion, ¶ 6.

help puncture the audacious line of jurisprudence that has emerged from the *Hulley* tribunal's restriction of tax carve-outs to so-called 'bona fide' taxation measures. While the *Hulley* tribunal, and before it the *Quasar de Valores* tribunal, had espoused this restriction to ensure that sovereign conduct that is obviously "abusive [*sic*], duplicitous [*sic*] or with similar bad faith" is not left bereft of ISDS arbitral tribunals' surveillance,[219] the line of jurisprudence that has emerged from these cases has caused an indiscriminate narrowing of the scope of tax carve-outs and an inequitable allocation of the burden of proof on states at the outset of the proceedings; so much so that any hint of an allegation of bad faith by an investor often suffices to breach the tax carve-out. This, quite clearly, could not have been how states intended tax carve-outs to be applied. Notwithstanding whether the *Quasar de Valores* and the *Hulley* tribunals were correct in their prescriptions (indeed, the fate of these awards arguably shows otherwise), the time is ripe to hit the brakes on this expeditious march of jurisprudence and reorient the interpretation and application of tax carve-outs. The recognition of fiscal sovereignty as a general principle of international law will assist in achieving this objective.

The same holds true for the unruly body of cases concerning the interpretation of the term 'taxation measures.' Indeed, this line of jurisprudence has traversed a parallel, yet independent, track to the imposition of the bona fide condition on tax carve-outs. It has resulted in a cacophony of decisions that have assessed a singular taxation measure in multiple ways, leaving stakeholders confused as to which taxation measures are actually covered within carve-outs. The well-meaning dicta of the *EnCana* tribunal, which requires examining the legal operation of the measure in question (and not its economic effect) to examine the extent of its coverage within tax carve-outs, will benefit from a supplementary layer of protection to be offered by the general principle of fiscal sovereignty. This is because the clout of this general principle will ensure that the *EnCana* tribunal's dicta is strictly applied to permit jurisdiction only over measures that obviously do not impose a mandatory payment obligation upon a class of persons; if they do, tax carve-outs should rescue such measures from the surveillance of ISDS arbitral tribunals.

Second, insofar as cases arising under treaties that do not contain tax carve-outs are concerned, the judicious recognition of the principle of fiscal sovereignty is perhaps more imperative, but also more complicated. In this connection, it is important to bear in mind that the principle of fiscal sovereignty should not be seen as an all-powerful sorcerous potion that can excuse all kinds of claims implicating taxation measures from the adjudication of ISDS arbitral tribunals. Instead, the author's proposal, which aligns with how doctrine, multilateral

219. Photovoltaic Knopf, 2014 PCA Case Repository No. 2014-21, ¶ 261; ICW, 2014 PCA Case Repository No. 2014-19, ¶ 320; WA Inv., 2014 PCA Case Repository No. 2014-19, ¶ 339.

agreements, states' constitutions, as well as case law have recognized fiscal sovereignty, is that such protection ought to be extended solely to claims that implicate fundamental tax policy or fiscal policy. These matters of policy are best represented in the exercise of the states' legislative power to tax. In other words, if an investor's claim pertains to the application or enforcement of a taxation measure, and not its very enactment on the legislative sphere, fiscal sovereignty would not preclude its adjudication an ISDS arbitral tribunal.

However, if an investor seeks, in effect, to challenge a new tax policy or a change in the tax policy of a state (as was arguably the case in *Cairn*), an ISDS arbitral tribunal must more carefully scrutinize its jurisdiction under a dispute resolution clause, by giving due weight to the general principle of fiscal sovereignty under VCLT Article 31(3)(c). It can be envisaged, on the basis of such an application of fiscal sovereignty, that a dispute that implicates a ubiquitously applicable (i.e., non-discriminatory) tax policy is not a dispute "related to" an investment, since the measure in question relates to larger sovereign interests of fiscal policy. The most efficient way to deal with such disputes is for arbitral tribunals to decline jurisdiction over them, since that is the only route through which matters of fiscal policy can be insulated from adjudication in ISDS. Indeed, several states have already started to take steps to offset the jurisprudence of ISDS arbitral tribunals using interpretative techniques to assume jurisdiction over taxation measures. A typical example of such steps is the stipulation of much more far-reaching tax carve-outs that are increasingly being seen in modern BITs[220] and Model BITs.[221] However, pending a comprehensive

220. *See, e.g.*, Bilateral Investment Treaty, India-U.A.E., Feb. 13, 2024, *available at* https://investmentpolicy.unctad.org/international-investment-agreements/treaties/bilateral-investment-treaties/5119/india---united-arab-emirates-bit-2024- [https://perma.cc/U7BB-MY9P]. The treaty contains the following tax carve-out addressing jurisdiction:

> This Treaty shall not apply to . . . any measure regarding taxation, including measures taken to enforce taxation obligations. For greater certainty, it is clarified that where the Party in which Investment is made decides that conduct alleged to be a breach of its obligations under this Treaty is a subject matter of taxation, such decision of that Party, whether before or after the commencement of arbitral proceedings, shall be non-justiciable and it shall not be open to any arbitration tribunal to review such decision.

Id. cl. 2.4(ii).

221. *See, e.g.*, 2021 Model FIPA, Canada at art. 11, *available at* https://investmentpolicy.unctad.org/international-investment-agreements/treaty-files/6341/download [https://perma.cc/JM57-3AKX] (last accessed Apr. 15, 2025) (containing a detailed tax carve-out). This carve-out, of course, excludes from the purview of some of the BIT's substantive obligations "a new taxation measure that is aimed at ensuring the equitable and effective imposition or collection of taxes (including, for greater certainty, a measure that is taken by a Party to ensure compliance with the Party's taxation system or to prevent the avoidance or evasion of taxes) and that does not arbitrarily discriminate between persons, goods or services of the Parties." *Id.* art. 11(3)(d). Further, it also contains a six-month exhaustion of remedies requirement for expropriation claims concerning taxation measures, whereby such claims must first be submitted for joint

reform of states' treaty practice, the Article proposes to use the general principle of fiscal sovereignty to construct a jurisdictional dam between matters that fall squarely within a state's exclusive prerogative to orient its fiscal policy and matters that constitute an ostensibly discriminatory or inequitable application or enforcement of such policy vis-à-vis investors. If applied systemically, ISDS arbitral tribunals would assume jurisdiction only over the latter kinds of disputes.

It is true that this proposal may give rise to uncertainties as to which matters actually qualify as attacks on a state's tax or fiscal policy, as opposed to genuine complaints about the incorrect application or enforcement of such policy. Despite this uncertainty, the proposed framework nonetheless represents a substantial improvement for ISDS over the current framework, which focuses almost exclusively on assessing the legal operation of a state's taxation measure or questioning its bona fide nature. This framing promotes ambiguities that disproportionately advantage investors and worsens the quality of discourse by incentivizing investors to raise allegations of bad faith. This, in turn, eliminates the possibility of giving effect to the legitimate distinction between matters of fiscal policy and matters that pertain squarely to the application or enforcement of such policy.

As Professor Jennifer Bird-Pollan remarks, the fundamental fallacy in making it easier for investors to breach the jurisdictional dam concerning tax disputes is that there is an inherent "misalignment of the parties involved in a BIT arbitration . . . because investors, both corporations themselves and the individual investors in those corporations, are driven by profit maximization, the calculation those investors will make in choosing whether or not to go forward with arbitration will be determined by the likelihood of creating profit" and not "by thoughts of the well-being of the BIT signatory country's citizens, or by the nation's sovereign authority to determine its own tax laws."[222] This misalignment between the objectives of profit maximization on the one hand and the preservation of sovereign control over tax policy on the other is exacerbated when one considers that investors traditionally come from capital-exporting, developed nations, and the fiscal sovereignty under attack is usually that of capital-importing, developing nations of the Global South, which may already have implicitly agreed to waive some of their fiscal sovereignty to benefit from foreign investments. Adding further limitations to such states' fiscal sovereignty, without their explicit consent, destroys even the façade of

determination by "the taxation authorities of each Party." *Id.* art. 11(5)(b). In addition, the provision also interestingly stipulates that "[i]n the event of any inconsistency between the provisions of this Agreement and any [DTA], the provisions of [the DTA] shall prevail to the extent of the inconsistency." *Id.* art. 11(2).

222. Bird-Pollan, *supra* note 6, at 125–26.

sovereign egalitarianism in international law. International legal scholarship has demanded a "postcolonial problematization of state sovereignty rather than a postcolonial alternative to it" in order to reorient mainstream discourses, which will help achieve the noble dream of sovereign egalitarianism.[223] This dream is far from being a reality in today's post-colonial world. In these circumstances, it is incumbent upon legal scholarship to ask the right questions, because oftentimes asking the right questions takes one halfway towards reaching the right answers. This Article is an attempt to do just that.

223. Pourmoukhtari, *supra* note 16, at 1768.