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## International Economic Law

23. June 2014

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**Duration:** 120 Minutes

- Please check the number of pages at the beginning as well as at the end of the test. The test includes 3 pages (including this one) and 4 questions.

**Grading:**

Question 1	15% of the total
Question 2	35% of the total
Question 3	15% of the total
Question 4	35% of the total
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Total	100%

*For the proper allocation of your time, please note the different weight of the questions.*

**Good Luck!**

### Question 1 (15%)

Discuss how Members express their voice in the IMF and World Bank, on the one hand, and the WTO, on the other hand. Based on your findings, is the WTO in your opinion a more democratic organization compared to the IMF and World Bank? Why or why not?

### Question 2 (35%)

The government of “Bioland”, a WTO Member, implements a new law that prohibits the use of any genetic engineering for certain types of grain. The new law also prohibits the import of genetically modified grain, unless the exporting country demonstrates that it fulfills the same high control standards as the authorities of “Bioland”. The government of “Bioland” claims that the law is aimed at protecting human health and preserving the natural food source of a specific rare species of insects. It has bilaterally negotiated a system of automatic approval of grain imports from “Neighborland”, also a WTO Member.

“Techland”, another WTO Member, is one of the main grain exporting countries and has used elaborate genetic engineering for many years. It argues that “Bioland” violates several WTO obligations, because its new law discriminates against grain producers from “Techland”. Amongst others, “Techland” claims that “Bioland” has no scientific proof that genetically modified grain is harmful to humans.

What is your legal assessment of the case?

### Question 3 (15%)

Between 2006 and 2011, *Lone Pine Resources Inc.*, a *US American* mining company, and its predecessors expended millions of dollars and considerable time and resources in *Quebec/Canada* to obtain the necessary permits and approvals from the Government of Quebec to mine for oil and gas in the province of Quebec, including beneath the St. Lawrence River. Suddenly, and without any prior consultation or notice, the Government of Quebec introduced a new law into the Parliament to suspend all exploration for oil and gas in the province (except for the purposes of scientific studies onshore). If the new law is adopted by the Parliament all permits pertaining to oil and gas resources beneath the St. Lawrence River will be revoked without any compensation.

A Member of the Quebec Parliament has been approached by a *US citizen* who holds a substantial number of shares of Lone Pine Resources Inc. The Member of Parliament wants to know whether the Government’s proposal complies with a shareholder’s rights under international law.

- a) Which rights could be affected?
- b) Do you see a violation of these rights?
- c) Which procedure could a shareholder rely on to raise a complaint apart from turning to national courts?

#### Question 4 (35%)

*Aqualand* is a poor, mountainous country with abundant groundwater reserves (water located beneath the earth's surface). In order to attract foreign capital, the government of *Aqualand* decided to sell concessions to exploit the groundwater reserves to foreign companies. One of them, *Sodapump Ltd.*, a French stock corporation has resorted to increase the water prices by 150% in order to cover for its investment. Furthermore, *Sodapump Ltd.* used a new technique for extracting the water reserves, which caused erosion of the soil and serious environmental damages. All of this led to violent riots by the local population (mainly poor farmers), which were not prevented by the authorities of *Aqualand*. The riots resulted in serious damages to the facilities of *Sodapump Ltd.* As the water distribution in *Aqualand* was threatened, the facilities of *Sodapump Ltd.* were occupied by the army of *Aqualand*, the management was replaced with citizens from *Aqualand* and the bank accounts of *Sodapump Ltd.* in *Aqualand* were frozen.

*Aqualand* and France have concluded a bilateral investment treaty with, among others, the following clauses:

Art. 1 (Definitions):

“Investment” means every asset that an investor owns or controls, directly or indirectly, that has the characteristics of an investment, including concession to search for and exploit natural resources.

Art. 5 (Minimum Standard of Treatment):

Each Party shall accord to covered investments treatment in accordance with customary international law, including fair and equitable treatment and full protection and security.

Art. 6 (Expropriation and Compensation):

Neither Party may expropriate or nationalize a covered investment either directly or indirectly through measures equivalent to expropriation or nationalization, except:

- (a) for a public purpose;
- (b) in a non-discriminatory manner;
- (c) on payment of prompt, adequate, and effective compensation.

Art. 7 (Transfers):

Each Party shall permit all transfers relating to a covered investment to be made freely and without delay into and out of its territory.

- a) You are the legal counsel of *Sodapump Ltd.*, what are your arguments with regard to damages caused by rioters to the water plant, to the occupation of the water plant by *Aqualand's* army and to the freezing of the bank accounts of *Sodapump Ltd.*?
- b) Given its experience in *Aqualand*, *Sodapump Ltd.* considers withdrawing from investments in developing countries completely because of the associated risks. How would you argue in favour of future investments? Are there any measures that you would suggest to *Sodapump Ltd.* to reduce the risks associated with investing in politically unstable countries?

## IEL written exam – Part I – Key

### Question 1 (15%)

Discuss how Members express their voice in the IMF and World Bank, on the one hand, and the WTO, on the other hand. Based on your findings, is the WTO in your opinion a more democratic organization compared to the IMF and World Bank? Why or why not?

- IMF/WB: Voting power depends on share in the institution's capital ("quota"), which is assigned to a Member dependent on the Member's relative position in the world economy.
- IMF/WB: Not all countries have their "own" Executive Director. Membership is organized in constituencies (e.g., "Helvetistan" for Switzerland), i.e. countries coordinate/bundle their voting power and are represented by a common Executive Director.
- WTO decision-making bodies take decisions by consensus (as a rule) or by majority vote (as an exception). I.e., each Member has a veto power (consensus) or at least one vote (majority voting).
- WTO: Voice does not depend on relative position of the Member in international trade.
- WTO: All Members can participate in all decision-making bodies.
- Dispute Settlement process also counts as a feature of a democratic organization.

Both conclusions regarding the democratic governance structure are legitimate:

- One could argue that it is fair to give economically more developed countries more say in the IMF's/WB's policies, as they are the ones bearing the bigger risks related to lending activity. Veto power by each member can make policies ineffective, which is not necessarily more democratic. Developing countries will have a hard time to effectively participate in the increasingly technical policy-making of the WTO. De facto, it is mostly the advanced economies determining the policy of the WTO.
- One could also argue that IMF/WB are money-driven and that the distribution of votes within the IMF/World Bank is not appropriate anymore, as developing and emerging economies are underrepresented.

## Question 2 (35%)

The government of “Bioland”, a WTO Member, implements a new law that prohibits the use of any genetic engineering for certain types of grain. The new law also prohibits the import of genetically modified grain, unless the exporting country demonstrates that it fulfills the same high control standards as the authorities of “Bioland”. The government of “Bioland” claims that the law is aimed at protecting human health and preserving the natural food source of a specific rare species of insects. It has bilaterally negotiated a system of automatic approval of grain imports from “Neighborland”, also a WTO Member.

“Techland”, another WTO Member, is one of the main grain exporting countries and has used elaborate genetic engineering for many years. It argues that “Bioland” violates several WTO obligations, because its new law discriminates against grain producers from “Techland”. Amongst others, “Techland” claims that “Bioland” has no proof that genetically modified grain is harmful to humans.

What is your legal assessment of the case?

- Potential violation of Art. III:4 GATT (national treatment): De facto discriminatory application of internal regulation? Several lines of argumentation are possible:
  - a)** New law does not affect grain as a product (genetic engineering = non-product-related process and production method); i.e. it does not fall within the scope of Art. III:4 GATT (argumentation used in Tuna/Dolphin II).
  - b)** If Art. III:4 GATT applies, one has to discuss whether genetically modified grain is “like” grain that is not genetically modified. Either: “Bioland” must not treat grain from “Techland” as a product less favorable than grain from “Bioland” as a product, independent of the way it was produced (genetic engineering = non-product-related process and production method). Grain is grain, i.e. its properties, nature and quality; the end-uses; and consumers’ tastes and habits speak in favor of “like product”. Or: genetic modification is more than a non-product-related process and production method, i.e. it changes the properties of grain or consumers distinguish between genetically modified and non-modified grain. Genetically modified and non-modified grain is therefore not in an immediately competitive relationship, i.e. not “like products”.
  - c)** Application of the “aims and effects test”: “Bioland” does not pursue a protectionist but an environmental purpose.
- The bilaterally negotiated automatic imports approval for “Neighborland” violates the MFN-obligation of Art. I:1 GATT: grain from “Techland” should not receive treatment less favorable than grain from “Neighborland” if they are “like products”. Here it is an origin-

based, i.e. de jure, discrimination. No hint in the case that “Techland” and “Neighborland” form a customs union or free trade area according to Art. XXIV:5 GATT.

- Violation of Art. XI GATT (quantitative restrictions) by imposing an import ban.

In a next step, it has to be analyzed if there are justifications for the violations mentioned above. Art. XX GATT lists possible national public interest aspects for a possible justification:

- Applicability of Art. XX(g) GATT? Rare species of insects as an “exhaustible natural resource”, law is related to their preservation and applies to domestic production and consumption in an even-handed manner. I.e. measure is provisionally justified. Does it constitute an arbitrary or unjustifiable discrimination between Members (chapeau of Art. XX GATT)? “Bioland” is essentially forcing other governments to adopt the same policies and standards (extraterritorial effect of the measure). Although no viable less invasive measures to achieve the same environmental purpose are available, negotiation efforts were uneven, i.e. “Neighborland’s” exception from the strict controls endangers the achievement of the environmental goal and goes against the very objective of the new law. This seems “arbitrary and unjustifiable” (Retreaded Tyres Case).
- Applicability of Art. XX(b) GATT and SPS? Under this exception, the ban must contribute to the reduction of risks to human health and there must be no less trade-restrictive measure available. The SPS concretizes the exception of Art. XX(b) GATT. The ban constitutes a food safety measure under the SPS. The main question is whether the available scientific evidence is sufficient to preclude risks to human health. Measures that conform to international standards are perceived as consistent with the GATT. Measures that go beyond international standards must be subjected to a risk assessment. If there is incomplete scientific evidence, “Bioland” can take the measures on a precautionary basis.

### Question 3 (15%)

Between 2006 and 2011, Lone Pine Resources Inc., a US American mining company, and its predecessors expended millions of dollars and considerable time and resources in Quebec/Canada to obtain the necessary permits and approvals from the Government of Quebec to mine for oil and gas in the province of Quebec, including beneath the St. Lawrence River. Suddenly, and without any prior consultation or notice, the Government of Quebec introduced a new law into the Parliament to suspend all exploration for oil and gas in the province (except for the purposes of scientific studies onshore). If the new law is adopted by the Parliament all permits pertaining to oil and gas resources beneath the St. Lawrence River will be revoked without any compensation.

A Member of the Quebec Parliament has been approached by a US citizen who holds a substantial number of shares of Lone Pine Resources Inc. The Member of Parliament wants to know whether the Government's proposal complies with a shareholder's rights under international law.

- a) Which rights could be affected?
- First of all, the source for rights of the investors is the **NAFTA** (because of the US-Canada context of the case) **and customary international law as well as general principles of international law**.
  - Property Rights could be affected (**unlawful expropriation**/Art. 1110 NAFTA), as the suspension of mining permits could amount to an expropriation.
  - **Fair and equitable treatment** (Art. 1105 NAFTA), as the investors were not informed about the possible new law.
  - **National Treatment** (Art. 1102 NAFTA), as the new law could be discriminative towards foreign investors.
- b) Do you see a violation of these rights?
- Expropriation: According to art. 1110 NAFTA, an expropriation has to be **a)** for a public purpose, **b)** on a non-discriminatory basis, **c)** in accordance with due process of law and art. 1105 NAFTA and **d)** must be compensated without delay and in full. The suspension of a mining permit can amount to an indirect expropriation (covered by art. 1110 NAFTA), as the investor cannot operate anymore without the permit and it renders its investment worthless. With regard to non-discrimination, there is no apparent discrimination of LonePine Ressources at hand. With regard to the criterion of due process of law, Canada did not notify the investor in a timely fashion and LonePine Ressources had not to expect a change of law and with regard to compensation, it is not apparent, that LonePine Ressources was compensated for the expropriation.
  - Fair and Equitable Treatment: The treatment of LonePine Resources by Canada cannot be considered as fair and equitable, as the change of law and the possible revocation of mining permits has not been communicated to LonePine Resources.

- National Treatment: There is no indication that Canadian investors are favored over foreign investors.
- c) Which procedure could a shareholder rely on to raise a complaint apart from turning to national courts?
- The problem is whether a shareholder is violated in his rights. The relevant case law here is Barcelona Traction: Shareholders cannot invoke expropriation of the company in court because they do not have the legal position to represent the company's interest.
  - The shareholder needs to approach the company which could then initiate proceedings under NAFTA art. 1118 NAFTA, if this process fails, the company could initiate arbitral proceedings according to art. 1120 NAFTA.

#### Question 4 (35%)

Aqualand is a poor, mountainous country with abundant groundwater reserves (water located beneath the earth's surface). In order to attract foreign capital, the government of Aqualand decided to sell concessions to exploit the groundwater reserves to foreign companies. One of them, Sodapump Ltd., a French stock corporation has resorted to increase the water prices by 150% in order to cover for its investment. Furthermore, Sodapump Ltd. used a new technique for extracting the water reserves, which caused erosion of the soil and serious environmental damages. All of this led to violent riots by the local population (mainly poor farmers), which were not prevented by the authorities of Aqualand. The riots resulted in serious damages to the facilities of Sodapump Ltd. As the water distribution in Aqualand was threatened, the facilities of Sodapump Ltd. were occupied by the army of Aqualand, the management was replaced with citizens from Aqualand and the bank accounts of Sodapump Ltd. in Aqualand were frozen.

Aqualand and France have concluded a bilateral investment treaty with, among others, the following clauses:

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##### Art. 7 (Transfers):

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a) You are the legal counsel of Sodapump Ltd., what are your arguments with regard to damages caused by rioters to the water plant, to the occupation of the water plant by Aqualand's army and to the freezing of the bank accounts of Sodapump Ltd?

- With regard to the damages caused by the rioters: According to art. 5 of the BIT, Aqualand has to ensure a minimum standard of protection from third parties and especially offer full protection and security to investors. This includes stopping rioters from damaging an investment (e.g. the plant in question). This responsibility goes very far, as a host state is required to take appropriate measures to ensure such an attack does not occur on the investment. As a conclusion, Aqualand has violated art. 5 of the BIT.
  - With regard to the occupation of the water plant by the army: The question arises, if the occupation by the army is tantamount to an expropriation under art. 6 of the BIT. In the Metalclad case, the arbitrators found, that any deprivation of rights of operation of an investment is tantamount to an expropriation. One can conclude that the occupation by the army and the replacement of the management is such a deprivation of rights. However, such an expropriation can be justified, if certain criteria are matched: **a)** for a public purpose, meaning that the objective of the expropriation must be for a public purpose. In the case at hand, the water price was increased by the investor, as he had to cover for its investment. It can be argued, that the host state has interest in keeping low water prices in order for its population to have access to fresh water. It has to be considered however, that the acting host state (i.c. Aqualand) is defining what it considers a public purpose. **b)** in a non-discriminatory manner, meaning that the investor in question is discriminated in comparison to other market participants. In our case this is not apparent. **c)** an obligation to pay prompt, adequate and effective compensation, meaning that the host state has to pay a compensation promptly after the expropriation took place (prompt), the compensation has to place the investor in the same financial position as that in which the expropriation had not happened (adequate) and the compensation must be in a form usable by the investor (effective; convertible currency, but also marketable bonds. In our case, it is not apparent that Aqualand offered any compensation to Sodapump Ltd, thus one can conclude that Aqualand violated art. 6 BIT.
  - With regard to the freezing of assets by Aqualand: According to art. 7 of the BIT, an investor has the right to move his financial assets in and out of the host state freely. In our case, the assets of Sodapump Ltd. Were frozen by the government and as such art. 7 of the BIT was violated by Aqualand.
- b) Given its experience in Aqualand, Sodapump Ltd. considers withdrawing from investments in developing countries completely because of the associated risks. How would you argue in favour of future investments? Are there any measures that you would suggest to Sodapump Ltd. to reduce the risks associated with investing in politically unstable countries?
- Sodapump should carefully analyse the situation and the associated risks in each country it is doing business in and not jump to conclusions from its experience in Aqualand. Withdrawing

may have serious consequences on the local population (jobs, infrastructure etc.) which may result in reputational risks for Sodapump.

- The first option in mitigating risk is to turn to France: Sodapump may want to discuss the situation with the French government and ask for assistance. France has a legal obligation to protect Sodapump (diplomatic protection) against violations of the BIT or take preventive measures by asking for export and investment insurance.
- In order to insure itself against non-commercial risks, the investor can seek insurance by the MIGA (a World Bank group institution). In the context of the case, MIGA can insure the following (art. 11 MIGA): Transfer of currency, expropriation and civil disturbance. MIGA offers these insurances in order to promote investments and development in host countries. Also, private actors are offering investment guarantees to investors.