

**Beiträge zum internationalen Handels-
und Wirtschaftsrecht**

Band 11

**The Right to Regulate
of Developing Countries
in International Investment Law**

A Contextual Approach to International Investment Agreements

By

Thomas Dromgool



Duncker & Humblot · Berlin

THOMAS DROMGOOL

The Right to Regulate of Developing Countries
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Beiträge zum internationalen Handels- und Wirtschaftsrecht

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The Faculty of Law of the Albert-Ludwigs-Universität Freiburg
accepted this work as a thesis in the year 2025.

Bibliographic information published by the German National Library

The German National Library registers this publication in
the German National Bibliography; specified bibliographic data
are retrievable on the internet about <http://dnb.d-nb.de>.

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© 2026 Duncker & Humblot GmbH, Berlin
Typesetting: 3w+p GmbH, Rimpf
Printing: Prime Rate Zrt., Budapest, Ungarn

ISSN 2942-3724
ISBN 978-3-428-19696-8 (Print)
ISBN 978-3-428-59696-6 (E-Book)

Printed on no aging resistant (non-acid) paper
according to ISO 9706 ☺

Publisher's address: Duncker & Humblot GmbH, Carl-Heinrich-Becker-Weg 9,
12165 Berlin, Germany | E-Mail: info@duncker-humblot.de
Internet: <https://www.duncker-humblot.de>

Table of Contents

Introduction	19
A. The Research Theme	19
B. The History of International Investment in Developing Countries	28
C. The Core Notions and Definitions	32
D. The Methodological Approach and Course of This Study	36

Part I

Developing Countries, the Meaning of Development, and the Right to Regulate in International Investment Law	38
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Chapter 1

The “Developing” Host State in International Investment Law	39
A. The Understanding of a Developing Country in International Investment Law	40
I. Self-Designated Developing Countries in the WTO System	40
II. Developing Countries Defined by Economic Factors	42
III. Developing Countries Defined by Further Criteria	43
B. Conclusions	45

Chapter 2

The Development Dimension of International Investment Law	46
A. Development in International Investment Law – a Problem of Definition in Article 25 ICSID Convention	47
I. Arbitral Awards in Favour of the “Development” Criterion	47
II. Arbitral Awards Neglecting a “Development” Criterion	49
III. Conclusions	52
B. Broader “Developmental Concepts” in International Investment Law	55
I. Differentiating from a “Right to Development”	55
II. Sustainable Development	56
1. Sustainable Development as a Concept in Public International Law	56
2. The Evolution of the Notion of Sustainable Development	57

III. The Content and Scope of Sustainable Development	58
1. The Principle of Common but Differentiated Responsibilities	58
2. The Principle of Sustainable Use of Natural Resources	61
3. The Principle of Equitable Utilization	63
IV. Conclusions	64
C. Instruments of Investment Protection in Developing Countries	65
I. Bilateral Investment Treaties	65
II. Free Trade Agreements	68
III. Investor State Contracts	68
IV. Conclusions	70

Chapter 3

The Right to Regulate in International Investment Law	72
A. The Right to Regulate and State Sovereignty in General International Law	72
B. Defining the Right to Regulate in International Investment Law	76
I. The Content and Scope of the Right to Regulate: Still Contentious in International Investment Law	76
II. Auxiliary Elements to the Right to Regulate	79
1. Deference	79
2. Standards of Investment Protection	81
3. Exceptions Provisions	82
a) General Exceptions Clauses	83
b) Security Exceptions Clauses	84
4. Non-Precluded Measures	85
5. Reservations	86
III. Conclusions	87
C. Arbitral Awards Confirming a Right to Regulate	89
I. Divergent Interpretations by Tribunals	89
II. Conclusions	92
D. Summary: Part 1	92

*Part 2***A Differential Treatment of Developing Countries
in International Investment Law?**

95

Chapter 4

The Special Legal Status of Developing Countries – a “Differential” Approach 95

A. Foundations for a Differential Treatment of a “Developing Country” in International Law	96
I. The Necessity to Distinguish Between Developed and Developing Countries in International Investment Law	96
II. The Philosophical Basis for Development, Development Aid, and for a Differential Treatment of Developing Countries	98
III. The Moral Duty of a Differential Treatment of Developing Countries	100
B. Special and Differential Treatment of Developing Countries in International Law – the Status Quo	101
I. Capacity-Based Provisions in International Law	102
II. Special and Differential Treatment of Developing Countries in the WTO Framework	103
1. Special and Differential Treatment Provisions in WTO Law	105
2. The Relevance of WTO Law Special and Differential Treatment Provisions for Developing Countries	108
III. Special and Differential Treatment in International Environmental Law	111
1. Categories of Differential Treatment Norms in Environmental Law	111
2. Towards a Dynamic “Contextual” Interpretation of Developing Countries in Environmental Law	113
IV. A “Contextual” v. a “Differential” Approach Towards Special and Differential Treatment Norms	116
V. Conclusions for Special and Differential Treatment in International Law	118

Chapter 5

Developmental and Differential Considerations in IIAs 119

A. Special and Differential Treatment in International Investment Law	120
I. The Relevance of Special and Differential Treatment of Developing Countries in Investment Law – Reciprocity v. Factual Asymmetry	120
1. The Starting Point for Special and Differential Treatment in FTAs	121
2. The Starting Point for Special and Differential Treatment in BITs and Model BITs	122
II. The Theoretical Applicability of Special and Differential Treatment in International Investment Law	126

1. Arguments Against an Applicability of Special and Differential Treatment in International Investment Law	126
2. Arguments for an Applicability of Special and Differential Treatment in International Investment Law	129
3. Conclusions	130
B. Special and Differential Treatment and Developmental Provisions in IIAs – <i>de lege lata</i>	133
I. The Function of Preambles in IIAs	134
II. The Function of Substantive Provisions in IIAs	135
III. Special and Differential Treatment and Developmental Provisions in IIAs so far	136
1. Developmental and Special and Differential Treatment Provisions in Preambular Clauses of IIAs	137
a) Developmental and Special and Differential Treatment Provisions in FTA Preambles	137
b) Developmental and Special and Differential Treatment Provisions in BIT and Model BIT Preambles	140
2. Developmental and Special and Differential Treatment Provisions in Substantive Clauses of IIAs	142
a) Developmental and Special and Differential Treatment Provisions in FTAs	142
b) Developmental and Special and Differential Treatment Provisions in BITs	145
c) Developmental and Special and Differential Treatment Provisions in Model IIAs	148
3. Conclusions	150
C. Special and Differential Treatment in IIAs – <i>de lege ferenda</i>	151
I. Mechanisms to Include Special and Differential Treatment in International Investment law	151
II. Concerns	152
III. Considering the Level of Development in IIAs via the VCLT	153
D. Conclusions	160

Chapter 6

Developmental Considerations in Arbitral Awards – a “Contextual” Approach	161
A. The Standards of Investment Protection and Developing Countries	162
I. Fair and Equitable Treatment	162
1. Fair and Equitable Treatment as an Absolute Standard of Treatment	162
2. Fair and Equitable Treatment and the International Minimum Standard of Treatment of Aliens	164
a) Relationship of the International Minimum Standard with Fair and Equitable Treatment	164
b) Relevance of the International Minimum Standard of Treatment for Developing Countries	168

3. Further Elements of Fair and Equitable Treatment	169
a) Transparency	169
b) Due Process and Denial of Justice	171
4. General Assessments of Due Process in Developing Countries	175
II. Legitimate Expectations	176
1. Contents of Legitimate Expectations	176
a) Legitimate Expectations Based on the General Regulatory Framework	177
b) Legitimate Expectations Based on Contractual Arrangements, Specific Representations, Promises, or even Less	178
2. General Assessments of Fair and Equitable Treatment and Legitimate Expectations in Developing Countries	182
III. Full Protection and Security	183
1. Contents of Full Protection and Security	183
2. General Assessments of Full Protection and Security in Developing Countries	185
IV. National Treatment and Most Favoured Nation Treatment	188
1. Contents of National Treatment and Most Favoured Nation Treatment	188
a) National Treatment	189
aa) Identification of the Domestic Comparator	189
bb) Treatment no Less Favourable	191
cc) Justification of Differential Treatment	192
b) Most Favoured Nation Treatment	193
2. General Assessments of Non-Discrimination Standards in Developing Countries	198
V. Expropriation	200
1. Contents of the Non-Expropriation Standard	200
a) The Sole-Effects Doctrine	201
b) The Police Powers Doctrine	203
2. General Assessments of Non-Expropriation and Developing Countries	205
VI. Conclusions	207
B. The Relevance of the Host State's Level of Development for the Degree of Investment Protection	208
I. Host States in Political Transition	209
1. <i>Parkerings v. Lithuania</i>	210
2. <i>Paushok v. Mongolia</i>	211
3. <i>Mamidoil v. Albania</i>	213
4. Further Awards Considering Host States in Political Transition	215
5. Conclusions	217
II. Host States in Specific Socio-Political Circumstances	218
1. <i>Duke Energy v. Ecuador</i>	218
2. <i>Bayindir v. Pakistan</i>	220

3. Developing Host States Implementing Regulatory Changes Invoking Human Rights Arguments	222
a) <i>Foresti v. South Africa</i>	223
b) <i>Biwater Gauff v. Tanzania</i>	226
c) <i>South American Silver v. Bolivia</i>	229
d) Conclusions	231
III. Ongoing Political Disturbances in the Host State	234
1. <i>Pantechniki v. Albania</i>	234
2. <i>Strabag v. Libya</i>	236
3. Further Awards Considering Political Disturbances	237
4. Conclusions	240
IV. Host States Confronted with Economic and Financial Crises	241
1. The Argentine Cases	241
2. Further Awards Considering Economic Crises	244
3. Conclusions	247
V. Host States with Structural Shortcomings – an Overstretched Judiciary	247
1. <i>White Industries Australia Limited v. India</i>	247
2. Further Awards on “Denial of Justice”	251
3. Conclusions	252
VI. Relevance of the Level of Development to the Issue of Compensation	253
1. <i>AMT v. Zaire</i>	253
2. Further Awards Considering the Host State’s Level of Development on the Issue of Compensation	255
3. Conclusions	257
C. Tribunals Not Considering the Developing Status of the Host State	258
I. Non-Consideration of Transitory State	258
II. Non-Consideration of Specific Socio-Political Circumstances	260
III. Non-Consideration of Political Disturbances in the Host State	261
IV. Non-Consideration of an Economic Crisis and of Structural Shortcomings	263
D. Conclusions	264
E. Summary: Part 2	268

Part 3

The Level of Development as a Determinant of the Right to Regulate? 269

Chapter 7

The Right to Regulate in IIAs – the Existing Taxonomy 269

A. The Right to Regulate in IIAs 270

I. The Right to Regulate in Preambular Clauses of IIAs	270
1. Model IIA Preambles	271
2. BIT Preambles	273
3. FTA Preambles	274
II. The Right to Regulate in the Substantive Provisions of IIAs	277
1. Model IIAs	277
2. BITs	282
3. FTAs	283
III. Assessments of the Right to Regulate in IIAs with Developing Countries	287
B. The Right to Regulate and General Exceptions Clauses Incorporated into IIAs	288
I. The Taxonomy of General Exceptions Clauses in WTO Law	288
II. General Exceptions for Natural Resources in WTO Law	289
1. Article XX(g) GATT	290
2. Preliminary Conclusions	294
III. General Exceptions Clauses in International Investment Law	294
1. General Exceptions Clauses in Arbitral Awards	294
2. General Exceptions Clauses in IIAs	298
a) Assessment of the Existing General Exceptions Clauses in IIAs	299
b) Preliminary Conclusions	302
3. General Exceptions for Natural Resources	303
4. Applicability of Article XX GATT to International Investment Law	309
C. General Exceptions Clauses as a Means to Safeguard the Right to Regulate	312
I. The Pros and Cons of an Inclusion of Article XX GATT-like General Exceptions Clauses in IIAs	313
II. The Consequences of General Exceptions Clauses for the Right to Regulate in IIAs	313
III. Conclusions	316

Chapter 8

The Right to Regulate of the Developing Host State – Attempts of a Taxonomy 317

A. The Natural Resource Context of Foreign Investments in Developing Countries	318
B. The Principle of Permanent Sovereignty over Natural Resources and the Right to Regulate of Developing Countries	319
I. The Legal Evolution of the Content of the Principle of Permanent Sovereignty over Natural Resources	320
II. The Legal Status of the Principle of Permanent Sovereignty over Natural Re- sources	324
1. The Principle of Permanent Sovereignty over Natural Resources as Customary Law in International Law	324

2. International Arbitral Awards on the Legal Status of the Principle of Permanent Sovereignty over Natural Resources	327
3. Conclusions on the Principle of Permanent Sovereignty over Natural Resources	329
III. The Effects of the Principle of Permanent Sovereignty over Natural Resources on International Investment Law	330
IV. Consideration of the Right to Regulate Natural Resources in IIAs	334
V. Conclusions for a Right to Regulate	335
C. A Differential v. a Contextual Approach to the Right to Regulate	337
I. Examples of a Differential Approach	337
1. The Doha Ministerial Declaration	337
2. The Southern African Development Community Model BIT Template	338
3. The Agreement on Establishing the African Continental Free Trade Area and the Investment Protocol	342
II. Conclusions	343
D. The Context of Natural Resource Investments and the Right to Regulate of Developing Host States – Case Studies	344
I. <i>Bear Creek v. Peru</i> – No Police Powers and Narrow General Exceptions	345
1. The Award	345
2. Considerations for a Context-Specific Right to Regulate	349
II. <i>Gold Reserve v. Venezuela</i> – Recovery of Natural Resources out of Political Opportunism	351
1. The Award	352
2. Considerations for a Context-Specific Right to Regulate	354
III. <i>Occidental v. Ecuador</i> – Internal Unrest Detrimental to the Host State’s Right to Regulate	355
1. The Award	356
2. Considerations for a Context-Specific Right to Regulate	359
IV. Conclusions	361
E. Summary: Part 3	362

Chapter 9

Summary of the Findings and Main Theses	364
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Bibliography	378
Index	412

Abbreviations

ACP	African, Caribbean and Pacific countries
AfCFTA	African Continental Free Trade Area
Art	Article
ASEAN	Association of Southeast Asian Nations
BIT	Bilateral Investment Treaty
CEPA	Comprehensive Economic Partnership Agreement
CERDS	Charter of Economic Rights and Duties of States
CETA	Comprehensive Economic and Trade Agreement
Cf	Confer
Ch	Chapter
COMESA	Common Market for Eastern and Southern Africa
ECT	Energy Charter Treaty
Ed(s)	Editor(s)
Edn	Edition
EPA	Economic Partnership Agreement
FET	Fair and Equitable Treatment
FPS	Full Protection and Security
FTA	Free Trade Agreement
GDP	Gross Domestic Product
GNI	Gross National Income
GNP	Gross National Product
ICJ Rep	International Court of Justice, Report of Judgements, Advisory Opinions and Orders
ICSID	International Centre for the Settlement of Investment Disputes
IIA	International Investment Agreement
IISD	International Institute for Sustainable Development
ILA	International Law Association
ILC	International Law Commission
ILM	International Legal Materials
IMF	International Monetary Fund
Inc	Incorporated
MFN	Most Favoured Nation Treatment
NAFTA	North American Free Trade Agreement
NIEO	New International Economic Order
No	Number
NT	National Treatment
OECD	Organization of Economic Cooperation and Development
Para	Paragraph
PCIJ	Permanent Court of International Justice
PSNR	Permanent Sovereignty over Natural Resources
SADC	Southern African Development Community

UN	United Nations
UNCITRAL	United Nations Commission on International Trade Law
UNCTAD	United Nations Conference on Trade and Development
UNDP	United Nations Development Programme
UNGA	United Nations General Assembly
UNGA Res	United Nations General Assembly Resolution
UNTS	United Nations Treaty Series
USMCA	Agreement between the United States of America, the United Mexican States, and Canada
VCLT	Vienna Convention on the Law of Treaties
Vol	Volume
WB	World Bank
WTO	World Trade Organization

Introduction

A. The Research Theme

The subject of this study is the “right to regulate” in international investment agreements and broader international investment law concerning developing countries. On the investor’s side, there is generally a strong interest in the long-term stability of the investment and thus of the host State and its regulations. On the host State’s side, there is the interest in attracting foreign investment, but also the trend towards regulation protecting strategic industries, in particular those pertaining to natural resources, such as oil, gas or water is significant.¹ This lets the basic concern of balancing private investor and public interests in international investment law and arbitration remain pertinent.² Changing circumstances in the host State will exacerbate these often-opposing interests. In the eyes of the investor, especially in developing countries the degree of predictability and stability of the investment environment may be lower compared to industrialised host States: political systems may change, social unrest may escalate, financial crises could aggravate, and structural shortcomings can hamper legal security. Then again, the host State is usually more dependent on foreign investment, the lower its level of development and, due to its weaker bargaining power, it may even refrain from enacting regulations in order to avoid an investor-state dispute.³ Regardless of whether this may actually be the case, statistics show that developing countries are almost traditionally respondents to investor-State disputes and often high awards are rendered

¹ On how the growing demand for natural resources embedded in current changes of the international order will pressure States to secure them, see Heike Krieger/Jonas Püschmann, *Securing of Resources as a Valid Reason for Using Force? A Pre-Emptive Defence of the Prohibition on the Use of Force*, in: Michael Lysander Fremuth/Jörn Griebel/Robert Heinsch (eds), *Natural Resources and International Law – Developments and Challenges: A Liber Amicorum in Honour of Stephan Hobe* (Nomos 2021).

² See already Anna Joubin-Bret/Marie-Estelle Rey/Jörg Weber, *International Investment Law and Development*, in: Marie-Claire Cordonier Segger/Markus W Gehring/Andrew Paul Newcombe (eds), *Sustainable development in world investment law* (Kluwer Law International 2011) Chapter 2, 5.2; cf Surya P Subedi, *International investment law: reconciling policy and principle* (Bloomsbury Publishing 2024) 8 et seq.

³ Some in the literature cite the risk of “regulatory chill” here, meaning that the conclusion of international investment agreements will already impose constraints on the ability of host State governments to adopt the policies needed to promote development. However, the actual influence on legislative enactment must remain an empirical question and will not be part of this study; for an overview see Kyla Tienhaara, *Regulatory Chill and the Threat of Investment Arbitration*, in: Chester Brown/Kate Miles (eds), *Evolution in Investment Treaty Law and Arbitration* (Cambridge University Press 2011) 606.

against them.⁴ This field of tension and uncertainty intensifies in changing geopolitical contexts. At the time of writing, geopolitical upheavals are taking place. Established norms and the traditional order of general international law and international economic law are being called into question and in some cases undermined. One geopolitical marker would be the Russian war against Ukraine since February 2022 has continuous impact on international investment law and arbitration as a whole.⁵ Furthermore, political transitions in entire regions, such as in the Arab Spring, which found its late continuation in Syria in December 2024 with the fall of the Assad regime, have brought back to mind old concerns about the security of foreign investment in developing countries.⁶ All these events vividly illustrate how much the environment to a foreign investment can change and how much the protection of investments but also the regulatory scope of a host State will depend on the specific local circumstances.⁷

At the same time, the global economic landscape built out of multilateral trade as well as international investment agreements which is surrounding the sovereign States is being reshaped almost dramatically. The first Trump administration from 2016 onwards already had a massive impact on the United States' investment protection policy and the landscape of investment protection agreements – especially multilateral free trade agreements – as a whole. The former North American Free

⁴ Some of the largest awards so far were rendered against developing countries: *ConocoPhillips Petrozuata BV, ConocoPhillips Hamaca BV and ConocoPhillips Gulf of Paria BV v Bolivarian Republic of Venezuela*, ICSID Case No ARB/07/30, Award of 8 March 2019 – approximately USD 8.3 billion; *Tethyan Copper Company Pty Limited v Islamic Republic of Pakistan*, ICSID Case No ARB/12/1, Award of 12 July 2019 – approximately USD 5.7 billion; *Occidental Petroleum Corporation and Occidental Exploration and Production Company v The Republic of Ecuador*, ICSID Case No ARB/06/11, Award of 5 October 2012 – approximately USD 1.77 billion.

⁵ Since Russia's full-scale invasion of Ukraine in February 2022, a number of disputes have arisen not only in connection with the impairment of the interests of foreign investors in Ukraine and Russia, but also in connection with the sanctions – including the freezing of assets – imposed by Western and allied States. Already since the annexation of Crimea, in violation of international law in 2014, there have been a number of investment arbitrations against Russia (eg, *PJSC CB PrivatBank and Finance Company Finilon LLC v Russian Federation*, PCA Case No 2015-21; *Stabil LLC and others v Russian Federation*, UNCITRAL, PCA Case No 2015-35; *NJSC Naftogaz of Ukraine and others v Russian Federation*, PCA Case No 2017-16). Some investors will also be able to invoke the Energy Charter Treaty (ECT), which Russia cancelled in 2009, as there is a survival clause in Article 45(3)(b) ECT, see Dai Tamada, *War in Ukraine and Implications for International Investment Law* International Community Law Review 26 (2024) 1–2, 187–207, available at <https://doi.org/10.1163/18719732-12341499> accessed 18 July 2025.

⁶ After the established rulers in four other Arab countries, Egypt, Libya, Tunisia and Yemen, were toppled between 2011 and 2014.

⁷ Eg foreign direct investment in countries in the region of the Arab Spring has already deteriorated considerably during the uprisings and regime changes between 2011 and 2014, see Nayef AlShammari/John Willoughby/Mariam Behbehani, *Political unrest, the Arab Spring, and FDI flows: A quantitative investigation* (2023) 11(2) Cogent Economics & Finance.

Trade Agreement (NAFTA)⁸ was terminated and replaced with the United States–Mexico–Canada Agreement (USMCA).⁹ Then the United States also withdrew from the Trans-Pacific Partnership (TPP), which was effectively the largest investment agreement ever negotiated and the Trans-Atlantic Trade and Investment Partnership (TTIP),¹⁰ which would be almost as large, was not negotiated any further.¹¹ Besides, in the last decade protectionist trade policies have increased worldwide, particularly visible in the “US-China trade war” since 2018 that has effectively paralysed the World Trade Organization (WTO) to date.¹² The trend finds its continuance in the tariff war declared under the Trump II administration.¹³ These shifts take place before the backdrop of a number of developing countries and emerging economies, above all the BRICS¹⁴ countries India, South Africa and Brazil renegotiating new bilateral investment treaties and terminating all current ones, in order to pursue a new investment protection policy based on their own

⁸ The North American Free Trade Agreement (NAFTA), (signed 17 December 1992, terminated 1 July 2020), 32 ILM 296.

⁹ Agreement between the United States of America, the United Mexican States and Canada (USMCA), (signed 30 November 2018, effective 1 July 2020).

¹⁰ See the draft for the EU–USA Free Trade Agreement, Transatlantic Trade and Investment Partnership (TTIP), EU draft proposal on trade in services, investment and e-commerce for the TTIP negotiations, (2 July 2013).

¹¹ See Lauren Mandell, *The Trump Administration’s Impact on US Investment Policy*, ICSID Review-Foreign Investment Law Journal 35 (2020) 345–68.

¹² Already the Trump I administration accused China of unfair trade practices and found that the WTO would not be able to find satisfactory solutions here. Thus, the US began setting tariffs in particular on steel and aluminum as well as other trade barriers on China in 2018. Since then, the US and China have been in a trade conflict, which, by its scope, is unprecedented in the history of international trade. The United States has also blocked all judicial appointments to the WTO’s Appellate Body. With no judges to hear appeals, this body has been inoperable since 2019. Also, the Biden administration from 2021 maintained most of the measures, including the blocking of the Appellate Body and bypassing the WTO dispute settlement process, which arguably impairs the WTO (see 2017 US Trade Representative’s Report to Congress on China’s WTO Compliance, available at <https://ustr.gov/sites/default/files/files/Press/Reports/China%202017%20WTO%20Report.pdf> last accessed 18 July 2025); Kristen Hopewell, *The World is abandoning the WTO and America and China are leading the way*, Foreign Affairs, 7 October 2024, available at <https://www.foreignaffairs.com/united-states/world-abandoning-wto-china-leading-way-kristen-hopewell> accessed 18 July 2025.

¹³ The Trump II administration imposed a series of tariffs on almost all imports, particularly steel, aluminum, and Chinese goods, with the goal of protecting American Industries and reducing trade deficits. These tariffs were part of a broader “America First” trade policy, aimed at encouraging domestic manufacturing and addressing what was perceived as unfair trade practices by other countries, especially China. However, they sparked trade tensions, retaliatory tariffs, concerns over their impact on consumers and global supply chains as well as foreign investments, see Cédric Dupont/Thomas Schultz, *Trump’s tariffs: from a trade problem into an investment problem?* (2025) *Journal of International Dispute Settlement* 16(3).

¹⁴ The BRICS describe themselves as an informal group of states comprising its original members Brazil, Russia, India, China, South Africa, and (as of 2024) Saudi Arabia, Egypt, United Arab Emirates, and Iran, see BRICS portal, available at <https://infobrics.org> accessed 18 July 2025.

Model Bilateral Investment Treaties (Model BITs).¹⁵ Africa as a whole has also taken a new path by creating with the African Continental Free Trade Area (AfCFTA) – the largest by the number of countries participating – and thereby is also setting its own new standards for investment protection.¹⁶ In this sense, the “right to regulate” of developing countries in international investment agreements (IIAs) takes on a new relevance.

The right to regulate is a term which enjoys increasing prevalence in international investment law. IIAs more frequently include such a right for the host State, particularly when they are of the new generation.¹⁷ In 2024 there were more than 2,500 IIAs in force.¹⁸ Roughly 130 of them included an explicit reference to a right to regulate.¹⁹ However, it remains unclear what exactly the right to regulate entails and where its boundaries lie vis-à-vis foreign investment. It could for example be equated with policy space already inherent to a State. Yet, it could also be understood as a legal right giving States the freedom to derogate from standards of investment protection in the pursuit of public policy objectives such as environmental protection, public health or security without having to compensate the investor. A notable example of the right to regulate being successfully invoked can be found in *Philip Morris v. Uruguay*, a landmark case involving investor-state dispute settlement under international investment law. Philip Morris International argued that

¹⁵ Eg India has unilaterally terminated most of its former BITs (75 out of 83) by 2024 and introduced its own Indian Model BIT (2015); for an updated overview see Krystal Lee, Investment Treaty Arbitration: India, Global Arbitration Review <https://globalarbitrationreview.com/insight/know-how/investment-treaty-arbitration/report/india> accessed 18 July 2025; for the decision of India to terminate most of its existing BITs see Prime Minister of India, www.pmindia.gov.in/en/news_updates/cabinet-approves-bilateral-investment-treaty-between-india-and-cambodia-to-boost-investment/?comment=disable accessed 18 July 2025; see below Chapter 7, A. II. 2.

¹⁶ 55 African States have agreed on the AfCFTA; cf African Union, List of Signatories as of October 2024 [https://africa-eu-partnership.org/en/afcfat#:~:text=The%20AfCFTA%20agreement%20has%20been,%2C%20Rwanda%2C%20Saharawi%20Republic%2C%20Sao and Trade Law Centre \(Tralac\), https://www.tralac.org/documents/resources/cfta/4241-afcfat-agreement-signature-and-ratification-list-05-12-2020/file.html](https://africa-eu-partnership.org/en/afcfat#:~:text=The%20AfCFTA%20agreement%20has%20been,%2C%20Rwanda%2C%20Saharawi%20Republic%2C%20Sao and Trade Law Centre (Tralac), https://www.tralac.org/documents/resources/cfta/4241-afcfat-agreement-signature-and-ratification-list-05-12-2020/file.html) accessed 18 July 2025. Intra-African investment will be subject to the so-called AfCFTA Investment Protocol (2023); see below in detail Chapter 5, B. III. 1. a).

¹⁷ “New generation IIAs” mean such IIAs concluded after 2010, whereas “old generation IIAs” were concluded before 2010, see UNCTAD, Phase 2 of IIA Reform: Modernizing the Existing Stock of Old-Generation Treaties, 2 IIA Issues Note, June 2017; see eg on the right to regulate in new generation IIAs: Catharine Titi, The right to regulate in international investment law (Nomos 2014).

¹⁸ UNCTAD, Investment Policy Hub <https://investmentpolicy.unctad.org> accessed 18 July 2025; IIA Navigator update: new treaties, in force and dates terminations of 13 Apr 2023, available at <https://investmentpolicy.unctad.org/news/hub/1716/20230413-ii-a-navigator-up-date-new-treaties-in-force-dates-and-terminations> accessed 18 July 2025.

¹⁹ See the searchable database for different contents of all IIAs: Electronic Database of Investment Treaties (EDIT), available at <https://edit.wti.org/document/investment-treaty/search> accessed 18 July 2025.

Uruguay's tobacco control regulations, as part of its public health strategy to reduce smoking, expropriated their intellectual property (trademarks) and violated the fair and equitable treatment standard under the bilateral investment treaty between Switzerland and Uruguay. However, the investment law Tribunal upheld Uruguay's right to regulate and found that the country's measures were within its sovereign right to protect the public health, even if they negatively affected foreign investments.²⁰ Furthermore, the Tribunal took into account that Uruguay was – at the time of the investment – a “country with limited technical and economic resources.”²¹ The award can be seen as a success for Uruguay,²² but above all for the right to regulate in the public interest in general. The Tribunal emphasised this right and – in contrast to most other tribunals – took into account the circumstances of the host State in the context of its level of development.

Still, the question of the content and scope of the right to regulate of the host State is particularly pertinent in view of the ever-present and opposing interests of developing countries and foreign investors. Notably, IIAs and international investment tribunals rarely relate the right to regulate to the special circumstances often present in a developing country. However, in *Mamidoil v. Albania* the Tribunal took the host State's circumstances into account, when the Greek company Mamidoil sued Albania under the Greece–Albania Bilateral Investment Treaty²³ for not renewing its lease to operate an oil storage facility in the port of Durrës. Albania defended its actions, amongst others by arguing that the company did not meet environmental and regulatory standards, and the country's need to develop the port for public purposes.²⁴ The Tribunal ultimately found that the Albanian modernisation measures did not breach Mamidoil's legitimate expectations.²⁵ It considered Albania was undergoing significant reforms to modernise its legal and economic system, particularly regarding environmental regulations and land use considering “Albania had just emerged from a long period of communist stagnation, isolation

²⁰ *Philip Morris Brand Sàrl (Switzerland), Philip Morris Products SA (Switzerland) and Abal Hermanos SA (Uruguay) v Oriental Republic of Uruguay*, ICSID Case No ARB/10/7, Award of 8 July 2016, para 422, finding that the investor's expectations “do not affect the State's rights to exercise its sovereign authority to legislate and to adapt its legal system to changing circumstances.”

²¹ *Philip Morris Brand Sàrl (Switzerland), Philip Morris Products SA (Switzerland) and Abal Hermanos SA (Uruguay) v Oriental Republic of Uruguay*, ICSID Case No ARB/10/7, Award of 8 July 2016, para 393.

²² The Tribunal ordered Philip Morris to bear all the costs of the arbitration proceedings and to pay Uruguay USD 7 million as partial reimbursement of the country's legal costs.

²³ *Mamidoil Jetoil Greek Petroleum Products Société SA v Republic of Albania*, ICSID Case No ARB/11/24, Award of 30 March 2015. Claims were brought under the Greece–Albania BIT of 1991 and the Energy Charter Treaty; in detail see below Chapter 6, B. I. 3.

²⁴ *Mamidoil Jetoil Greek Petroleum Products Société SA v Republic of Albania*, ICSID Case No ARB/11/24, Award of 30 March 2015, para 60.

²⁵ *Mamidoil Jetoil Greek Petroleum Products Société SA v Republic of Albania*, ICSID Case No ARB/11/24, Award of 30 March 2015, paras 625–6, 723.