For global business, international trade and investment are bound at the hip. When businesses trade internationally, goods or services cross borders; when they invest, it is capital and other factors of production that do so. Companies trade to supply their foreign investments; they invest to facilitate and diversify their trade. In contrast, international law addresses trade and investment separately and regulates them in ways that are dramatically different. First, trade has been governed multilaterally since 1947 through what today is the World Trade Organization (WTO), whereas close to 2,600 separate bilateral investment treaties (BITs), which mushroomed only in the 1980s and 1990s, now regulate foreign direct investment (FDI). Second, hundreds of increasingly sophisticated WTO rules discipline trade, whereas a mere handful of principles cover investment—many of which derive from customary international law. Third, trade agreements are enforced exclusively between states, with reciprocal trade sanctions as the remedy of last resort; under investment treaties, private companies have standing to claim monetary damages from host country governments.

This article tries to explain some of these differences and, in particular, to elucidate some of the consequences for international economic law. It does so through the lens of a specific legal obligation that, today, is prominent in the fields of both trade and investment: the principle of nondiscrimination, as it is embodied in the requirement to provide national treatment.

For example, in 1995, a dispute between Venezuela and the United States arose out of the fact that Venezuelan sugar exports to the United States were subject to a bond required of all sugar imports, whereas U.S. sugar was not subject to such a bond. The WTO’s Dispute Settlement Body, in its 1999 ruling in United States – Sugar (Venezuela), confirmed for the first time that goods treated similarly in analogous circumstances may be compared to determine whether the measures in question are discriminatory. The United States did not comply with the ruling, and in 2002 the WTO authorized Venezuela to impose sanctions, and did so.

The authors wish to thank Deborah Upchurch and Doak Bishop for their assistance. The views expressed here are exclusively those of the authors.

1 At the WTO’s 1996 Singapore Ministerial Conference, the director-general stated that “[i]n today’s economy, trade and investment are not merely increasingly complementary, but also increasingly inseparable as two sides of the coin of the process of globalization.” WTO Press Release No. PRESS/96/42. Foreign Direct Investment Seen as Primary Motor of Globalization, Says WTO Director General (Feb. 13, 1996), at <http://www.wto.org/english/news_e/news_e.htm#archives>.


3 The obligation to provide national treatment essentially prohibits discriminating between foreign and domestic products, investments, or investors.

national treatment disputes are relatively new. One such dispute that reached the headlines in February 2007 involves Italian mining companies that have invested in South Africa and have an ongoing discrimination complaint against that country’s affirmative action program (“Black Economic Empowerment”). Should tribunals, as some have argued, apply national treatment in trade and investment as a singular doctrine—namely, as a discipline to facilitate competition and to protect foreigners against government abuse? Or, as others have advocated, should they apply national treatment in the two areas in separate and distinct ways—based on textual discrepancies and the different history, goals, and context of the two regimes? The potential for conflict between trade and investment obligations is far from theoretical. Disputes that cross the boundary between the two regimes are increasingly common, and new substantive overlaps in the treaties have begun to emerge. Private investors have realized that they can convert trade disputes into investment disputes, with the potential of winning multimillion dollar damage awards. An example is the softwood lumber dispute between the United States and Canada, which began as a trade dispute over the United States’ imposition of countervailing and antidumping duties on imports of Canadian lumber. This seemingly run-of-the-mill trade case sprouted an investment arbitration instituted by Canadian lumber companies, which claimed that the United States was interfering with their lumber products business. In another dispute the U.S. government challenged a Mexican tax on sweeteners


12 Notice of Arbitration, Terminal Forest Products, Ltd. v. United States (NAFTA Ch. 11 Mar. 31, 2004) (later consolidated with Canfor Corp. v. United States and Tembec v. United States (NAFTA Ch. 11 Consolidation Trib. Sept. 7, 2005)).
as a violation of national treatment and won before the WTO Appellate Body. Concurrently, however, U.S. investors in the Mexican sweeteners industry requested a total of U.S.$425 million in compensation from the Mexican government on the ground that the same tax violated their rights as investors under the North American Free Trade Agreement (NAFTA), including their right to national treatment. Given that the WTO had already found a violation of national treatment under trade law, should NAFTA tribunals automatically find a violation of national treatment under investment law? In December 2007, one of the two NAFTA tribunals involved in the dispute did find a violation of national treatment, though as of this writing its reasons have not been released.

Another feature fueling the renewed interest in the intersection of trade and investment law is the recent trend for multilateral trade agreements to address investment. The WTO Agreements on Trade-Related Investment Measures and the General Agreement on Trade in Services (GATS) are good examples. Conversely, in recent years, investment law has also aligned itself more closely with trade. The United States, for example, has increasingly included investment commitments in broader free trade agreements, such as NAFTA, and in bilateral free trade agreements, most recently with South Korea. Similarly, the United States has expanded the coverage of its model BIT from post-entry investment protection to trade law-style investment liberalization, which focuses on breaking down barriers to the entry and establishment of foreign capital.

The goal of this article is twofold. First, the article dissects and explains the major similarities and differences between the international trade and investment regimes. Second, in light of these similarities and differences, the article evaluates the role and evolving importance of the

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17 General Agreement on Trade in Services, Apr. 15, 1994, WTO Agreement, supra note 16, Annex 1B, in THE LEGAL TEXTS, supra note 16, at 325, reprinted in 33 ILM 1168 (1994) [hereinafter GATS]. Despite the obvious connection between TRIMs and international investment, it was actually the GATS that made more substantial inroads to including foreign direct investment (FDI) within the WTO’s liberalization agenda. Article 12(c) of the GATS defines trade in services to include a service supplier’s “commercial presence in the territory of any other member,” explicitly bringing FDI in the services industry into the fold. Under the Agreement, however, countries are required only to provide market access and national treatment in service sectors that they have specifically listed in the schedules annexed to the Agreement, and even in those sectors they are allowed to specify exceptions for FDI. GATS Arts. XVI, XVII. These escape hatches have severely curtailed the effectiveness of GATS in liberalizing FDI. See Eric M. Burr, Note and Comment, Developing Countries and the Framework for Negotiations on Foreign Direct Investment in the World Trade Organization, 12 Am. J. INT’L L. & POL’Y 1015, 1030-40 (1997) (discussing the limitations of GATS and TRIMS that developing-nation negotiators succeeded in obtaining).
19 See infra notes 37-42 and accompanying text.
national treatment principle in trade and investment treaties. We critically examine the related
case law in both forums and chart a new, more appropriate way for both trade and investment
tribunals to interpret national treatment.20 Our analysis illustrates how the divergent history,
goals, and incentives underlying treaty regimes should influence not only their design, but also
the evolving interpretation of their specific obligations. This insight has important implica-
tions for the general debate on fragmentation of international law and, to cite just one addi-
tional example, for the International Law Commission’s work on most-favored-nation treat-
ment, which also embodies the nondiscrimination principle.

The article proceeds as follows. Part I offers an overview of the common historical roots, but
diverging evolutions, of international trade and investment law. Part II explains the different
goals and political economies of the two regimes that produce many of the discrepancies
between their substantive rules. Part III applies the earlier analysis to the principle of national
treatment and examines the different objectives, importance, and evolving interpretations of
national treatment in trade and investment treaties. Part IV summarizes and explains the core
differences and similarities in national treatment jurisprudence and charts a way forward for
the resolution of future disputes. Part V concludes.

I. INTERNATIONAL TRADE AND INVESTMENT LAW: COMMON ROOTS,
DIVERGING EVOLUTIONS

A central objective of this article is to illustrate how the application of national treatment
ought to reflect the origins, evolution, and goals underlying the trade and investment regimes.
We therefore begin our analysis with a brief historical overview.

Trade and investment, together with such things as transit, liberty of conscience, and fish-
eries, were long addressed jointly in treaties of friendship, commerce, and navigation (FCN
treaties). The first treaty ever concluded by the United States was a 1778 FCN treaty with
France. Early efforts at regulation made little distinction between trade and FDI as we know
it. Indeed, at that time, trade in goods was often effectuated by individuals living abroad and
selling goods at trading posts in foreign nations.21 Thus, modern legal principles governing
trade, investment, and human rights all share the same origin: the protection and treatment
of aliens.22 Foreign investments were protected not only by FCN treaties, but also by customary
international laws regarding the treatment of aliens, especially rules on compensation for
expropriation.

These rules of custom developed over time, were sometimes challenged, and by their very
nature became binding on all states (other than persistent objectors) without the need for recip-
ciprocal treaties. Trade quickly transformed, however, into an activity where merely goods—not
aliens—were sent across borders. It consequently became distanced from the rules governing
the treatment of aliens and, in the process, from customary international law. Instead, specific
agreements gradually began to regulate trade. In 1947, the initial bilateral agreements began

22 For an elaboration on how modern international law on nondiscrimination originates in the economic sphere of international law disciplines on the treatment of aliens, see SANDRA FREDMAN, DISCRIMINATION LAW (2007).
to give way to multilateral agreements, where countries reciprocally agreed to open their markets to foreign goods. The reciprocity and particularized concessions in trade agreements largely prevented trade law principles from evolving into custom, which would go beyond reciprocity by bestowing rights on all countries.  

With decolonization and the resulting creation of newly independent states—beginning in Latin America in the early nineteenth century—customary rules on investment protection became hotly contested. In response to the rapid increase in the number of multinational enterprises engaged in natural resources activities, developing nations began to adopt defensive policies to regulate or even stop FDI. Former colonies were especially dismissive of the rule requiring “prompt, adequate, and effective compensation” in the event of expropriation, which they considered contrary to their sovereign right to full control over persons and property within their territory. In particular, postcolonial Latin American jurists drew upon the teachings of Carlos Calvo, an Argentine diplomat of the late nineteenth century, to reject the developed nations’ arguments for an “international minimum standard” of treatment for aliens. Instead, their position was that aliens were entitled only to the same level of treatment that domestic nationals receive under the domestic laws and legal system. The Calvo doctrine was therefore, somewhat ironically, an early argument for the application of “mere” national treatment under customary international law (pursuant to which, for example, U.S. investors in Mexico should not expect any treatment better than the treatment given to Mexican investors).

In response to this North-South debate, the UN General Assembly passed resolutions largely favoring the demands of developing countries. Concerned that these resolutions compromised existing customary rules on investment protection, developed countries started concluding BITs with developing countries that reconfirmed both the right to “prompt, adequate, and effective compensation” for expropriation and other “international minimum standards.” In other words, BITs owe their origin to the weakening of investment protection under customary international law.


Sornarajah, supra note 21, at 18–22.


Argentina, like many Latin American countries, has long subscribed to the Calvo Doctrine, which requires that aliens submit disputes arising in a country to that country’s local courts. The conclusion of this treaty, which contains an absolute right to international arbitration of investment disputes, removes U.S. investors from the restrictions of the Calvo Doctrine and should help pave the way for similar agreements with other Latin American states.
Beginning in the 1980s, a more favorable attitude towards FDI began to emerge in developing countries. Many were unable to repay their loans amidst the international debt crisis and began to consider FDI as a means of financing their development.\(^{31}\) The international economy had also begun to shift away from natural resource exploitation to less politically sensitive investments in manufacturing, services, and high technology. In reaction to these and other changes, developing countries independently began to liberalize their domestic-investment policies,\(^{32}\) and the number of BITs between developed and developing nations quickly rose to the current level of nearly 2,600.\(^{33}\) With more BITs in existence, and foreign investments in some countries going wrong (most notably in Argentina as a result of its 2001 financial crisis), an unprecedented wave of investor-arbitration claims were filed starting in the mid-1990s. This spike in investment disputes produced something of a backlash against BITs, with numerous countries softening their BIT commitments\(^{34}\) or withdrawing from BITs altogether.\(^{35}\)

In the meantime, the international trade regime steadily developed from the General Agreement on Tariffs and Trade (GATT) of 1947, which had only 23 parties and which focused on the reduction of tariffs, to what is currently a quasi-universal organization with 151 members and 27 treaties addressing both tariff and nontariff barriers to trade, services, and intellectual property rights.\(^{36}\) Although one of the centerpieces of the WTO is nondiscrimination—both in the form of most-favored-nation treatment and national treatment—a country can gain the guarantee of such treatment only by joining the WTO (not as a right under customary international law), and the negotiation and enforcement of trade rules remains firmly grounded in the principle of reciprocity (albeit with preferences for developing countries). Given the difficulties of reaching consensus in the ongoing Doha Development Round, no new round of trade negotiations has been concluded since the creation of the WTO in 1995. During that same period, however, the WTO dispute settlement mechanism—in particular, the WTO Appellate Body—garnered legitimacy and efficiency as a mechanism for the settlement of state-to-state trade disputes.

II. THE DIFFERENT GOALS AND POLITICAL ECONOMIES OF TRADE AND INVESTMENT TREATIES

Although they share a common origin (treatment of aliens), trade and investment disciplines have traditionally focused on different, but complementary, objectives: liberalization of trade flows, in the case of trade, and protection and promotion of foreign investment, in the case of...

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\(^{31}\) BREWER & YOUNG, supra note 25, at 113.


\(^{33}\) See supra note 2.

\(^{34}\) See NAFTA Free Trade Commission, Notes of Interpretation of Certain Chapter 11 Provisions (July 31, 2001), at <http://www.naftaclaims.com/files/NAFTA_Comm_1105_Transparency.pdf>, where the three NAFTA governments limited the scope of NAFTA Article 1105 ("Minimum Standard of Treatment in Accordance with International Law"). See also U.S. Model BIT, supra note 18 (limiting, for example, the meaning of indirect expropriation in Annex B); 2004 Canada Model BIT, at <http://www.naftaclaims.com/files/Canada_Model_BIT.pdf> (for example, setting out General Exceptions in Article X related to, inter alia, public health, the conservation of exhaustible natural resources, national security, and cultural industries).


investment. As indicated in the preamble to GATT 1947, the unequivocal goal of the international trade system has been to “expand[] the production and exchange of goods” by means of “the substantial reduction of tariffs and other barriers to trade and . . . the elimination of discriminatory treatment in international commerce.”\textsuperscript{37} The trade regime is about liberalizing trade flows through the reciprocal exchange of market access concessions between governments.

One may question why governments need international agreements to arrive at liberal trade policies that are, considered in themselves, already in the overall interest of each country.\textsuperscript{38} The common explanation is that without such agreements, nations would restrict trade, pushed as they are by well-organized domestic, import-competing industries.\textsuperscript{39} A trade agreement’s effect is to activate the export lobby by giving it market access abroad in exchange for trade-liberalizing “concessions” at home. The political support that governments thereby obtain from exporters can then outweigh the opponents of trade liberalization at home. Through such reshuffling of political interests, the trade agreement produces freer trade policies both at home and abroad in the nation’s overall interest, including, most specifically, the interest of consumers.

In sum, the trade regime is about overall welfare, efficiency, liberalization, state-to-state exchanges of market access, and trade opportunities—not individual rights.

The political economy of investment treaties is remarkably different.\textsuperscript{41} Traditionally, BITs are about the protection of foreign investments that are already present in the host countries.\textsuperscript{42} The very first BIT, entitled “Treaty for the Promotion and Protection of Investments” (1959), was between Germany and Pakistan. As stated in the BIT’s preamble, parties to BITs seek “to create favorable conditions for investments” by imposing international minimum standards respecting, for example, expropriation, fair and equitable treatment, and nondiscrimination.\textsuperscript{43}

\textsuperscript{37} General Agreement on Tariffs and Trade, Oct. 30, 1947, TIAS No. 1700, 55 UNTS 194 (hereinafter GATT). Importantly, from 1947 onward, the objective of trade liberalization was not an end in itself, but rather, as stated in the GATT preamble, a means toward the higher goal of “raising standards of living, ensuring full employment and a large and steadily growing volume of real income and effective demand.” In 1994, the preamble to the WTO Agreement, supra note 16, added to this goal the “objective of sustainable development, seeking both to protect and preserve the environment . . . consistent with . . . different levels of economic development.”


\textsuperscript{40} WITO Agreement, supra note 16, pmbl.

\textsuperscript{41} In support, see Trachtman, supra note 8, and Alan O. Sykes, Public v. Private Enforcement of International Economic Law: Standing and Remedy, 34 J. LEGAL STUD. 631, 644 (2005).

\textsuperscript{42} Only more recent U.S. and Canadian BITs, as well as NAFTA Chapter 11, go beyond investment protection and include investment liberalization. See NATIONAL TREATMENT, supra note 28, at 9.

This protection of investments is, in turn, “likely to promote investment, encourage private industrial and financial enterprise and to increase the prosperity of both States.”

As with trade agreements, one can inquire why countries sign BITs. In trade agreements the interests of both parties are reciprocally aligned because both seek market access in the other country. In BITs, however, the interests of capital-exporting or home countries, such as Germany, traditionally diverged from those of capital-importing or host countries, such as Pakistan. In essence, Germany seeks protection of its foreign investments, and Pakistan is happy to offer that protection only to attract and promote investment and to accelerate its economic development; more investment is exchanged for more investment protection.

Another question is why foreign investors are not content with the protections offered by the laws of their host countries. In other words, why is there a need for international law on investment protection? The first answer is that host states can unilaterally change any protection offered under their domestic laws. This risk is inherent in the asymmetrical relationship between a private investor and a sovereign state. The second, but related, answer is that foreign investors fear discrimination. The international investment regime centers on the microeconomic arena of private investors seeking to reduce the risk of investment abroad through investment protection—which, in return, lowers the cost of capital for capital-importing countries and accelerates their economic development through investment promotion. As Alan Sykes put it, “The most effective mechanism to achieve such risk reduction is a private right of action for compensatory damages should an importing nation engage in proscribed behavior.”

Preamble to the Germany-Pakistan BIT. Like trade agreements, investment treaties do not portray the promotion and protection of investment as ends in themselves. Rather, in the words of the preamble to the U.S. Model BIT, supra note 18, protection and promotion of FDI are means in pursuit of the higher goal of “maximizing effective utilization of economic resources and improving living standards . . . consistent with the protection of health, safety, and the environment, and the promotion of internationally recognized labor rights.”


Andrew T. Guzman, Why LDCs Sign Treaties That Hurt Them: Explaining the Popularity of Bilateral Investment Treaties, 38 VA. J. INT’L L. 639, 669-74 (1998) (discussing how the incentive to sign a BIT is different for individual developing countries compared to developing countries as a group).

As Thomas Wälde noted in his separate, dissenting opinion in Thunderbird v. Mexico:

Commercial arbitration is a suitable mechanism for resolving the disputes of equal parties on equal footing and without need for the purpose of taking into account the position of the weaker party; nor is there any policy purpose underlying commercial arbitration . . . . By contrast, international investment law is aimed at promoting foreign investment by providing effective protection to foreign investors exposed to the political and regulatory risk of a foreign country in a situation of relative weakness.


In recent times the argument could be made that when large multinationals invest in small developing countries, the asymmetry may sometimes work the other way. If so, the party needing protection is not so much the foreign investor, but rather the host country.

As noted in JAN PAULSSON, DENIAL OF JUSTICE IN INTERNATIONAL LAW 149 (2005): “Whatever the rosy rhetoric about the equality of treatment of nationals and foreigners, the very fact of being foreign creates an inequality. The foreigner’s obvious handicap—his lack of citizenship—is usually compounded by vulnerabilities with respect to many types of influence: political, social, cultural.”

Sykes, supra note 41, at 632. In support, see Konrad von Moltke & Howard Mann, Misappropriation of Institutions: Some Lessons from the Environmental Dimension of the NAFTA Investor-State Dispute Settlement Process, 1 INT’L ENVTL. AGREEMENTS 103, 110 (2001): “it is all but impossible to conceive of an international investment
This private approach to enforcement stands in contrast to the trade regime’s purely state-to-state enforcement mechanism, with no damages for past harm and with reciprocal withdrawal of trade “concessions” as the remedy of last resort. The trade regime is an interstate construct focused on the macro-issues of market access and trade opportunities to increase overall welfare; the investment regime, in contrast, is centered on the micro-issues of attracting and protecting investments made by individual investors. It is this protection of individual investor rights that is expected to increase FDI flows to nations with an otherwise higher risk premium.

The quid pro quo for thus attracting FDI is making oneself vulnerable to direct claims by individual investors. Most investment treaties soften this inroad into domestic regulatory affairs by including little more than a handful of rather vague disciplines, limiting the available remedy to money damages and excluding an obligation of specific performance. Whereas the normal remedy in trade law is compliance, in investment law it is compensation.

In sum, the traditional investment regime is about fairness grounded in customary rules on treatment of aliens, not efficiency. It is about protection, not liberalization, and about individual rights, not state-to-state exchanges of market opportunities.

Two other, related concerns bear upon the interpretation of trade and investment agreements. The first is that many politicians continue to regard imports of products as “bad,” the pill to swallow in exchange for more exports, and a debit on the country’s account that leads to job losses, company closures, and so on. In contrast, they consider imports of capital as “good” and as a credit on the country’s account that boosts domestic development, job creation, and so on. To put it bluntly, for many domestic decision makers, foreign products always remain foreign, whereas foreign investments become local. As a result, there are generally fewer political pressures to discriminate against foreign investment, which is generally seen as “good,” than there are to protect against foreign imports, which are generally seen as “bad.”

regime that does not incorporate some form of investor-initiated dispute settlement. The reason for this lies in the fact that international investment disputes will generally pit an individual interest against a public one.


The preamble to the U.S. Model BIT, supra note 18, stresses “the importance of providing effective means of asserting claims and enforcing rights with respect to investment under national law as well as through international arbitration.”

Under NAFTA Chapter 11, for example, tribunals can award only monetary damages or restitution of property. In the latter case, however, under Article 1135:1(b), the award “shall provide that the disputing party may pay monetary damages . . . . in lieu of restitution.”

Whereas market access and liberalization are at the center of trade agreements, in investment treaties they are absent or, at best, only newly emerging concerns (and limited largely to U.S. and Canadian BITs). See NATIONAL TREATMENT, supra note 28, at 9.

This view persists even though economic theory demonstrates that imports are generally “good” since they benefit consumers more than they harm import-competing producers.

In support, see Trachtman, supra note 8, at 191-92: “there seems to be less political pressure in host countries to construct barriers to investment than there is to construct barriers to imports of goods and services.” He nevertheless mentions a number of reasons for “economic nationalism” in the investment area. See also Bernard Hoekman & Carlos Primo Braga, Protection and Trade in Services: A Survey (World Bank Policy Research Working Paper No. WPS 1747), at 21 (Apr. 1997), at <http://www-wds.worldbank.org> (“[i]t is generally assumed that sector-specific factors of production employed in inefficient protected industries will oppose liberalization of market access. In the services-context [that is, FDI in the services industry] this may not be the case. To the extent that establishment is the most efficient mode of contesting a service market, sector-specific labor may be less opposed to liberalization, insofar as it is expected that net employment in the sector concerned will not change much upon liberalization due to the establishment of foreign-owned firms.”).
is true, there is also less need for an international investment regime than there is for an international trade regime.

This lack of parallelism might go some way to explain why there is a multilateral trade organization but no multilateral investment treaty. It might also explain not only why there are more trade rules than investment rules, but also why trade rules are more sophisticated than investment rules. At the same time, this lack of parallelism implies that investment treaties are a relatively inexpensive commitment device, especially for countries that are already on a path of economic reform— which, in turn, may explain the high number of BITs and developing countries’ willingness to sign them in the first place. Indeed, if investment treaties are meant to prohibit acts that countries are unlikely to want to undertake anyway, there is reason to interpret investment disciplines with a high degree of deference to the regulating country. The opposite may be warranted for trade disciplines, which prohibit acts that countries otherwise have difficulty resisting.

A second noteworthy difference between trade and investment relates to their relative degrees of risk and involvement in domestic affairs. Making a product in country A and exporting it to country B (an example of trade) generally implies less risk and less involvement. If the product can no longer be sold, one can always try to sell it elsewhere. From the perspective of the importing country, only the product comes in, not the producer or the production process. In contrast, investing capital in another country and producing products there is far more risky. The foreign investor typically has a deeper involvement in the importing country’s economy and social fabric. A foreign investor must not only find buyers, he must also calculate the risk of a hostile business climate, unpredictable taxes and labor regulations, or an untrustworthy or unstable system of governance and courts. If a trade deal fails, the company may still be able to ship the goods elsewhere. If an investment deal fails, the money invested is most likely gone.

At the same time, the importing country is also more involved. Investment may bring huge benefits in terms of growth, employment, and transfer of technology. It can also lead, however, to serious harm or social dislocation. With not only the products, but also the producer and production process, crossing the border, the importing country may suffer environmental

57 See Sykes, supra note 41 (“[F]or any developing country that does not plan to engage in significant expropriation or . . . prohibited activity, a credible promise of monetary compensation to investors imposes few if any offsetting costs. . . . A promise of monetary compensation to investors is thus a cheap commitment device for states with benign intentions toward investors . . . .”).

58 Using the idea that BITs are a low-cost commitment not to take acts that the national government is unlikely to want to undertake anyhow, Sykes, supra note 41, has argued against a “regulatory takings” doctrine under NAFTA Chapter 11.

59 The product itself can, of course, be dangerous, unhealthy, or socially unacceptable and may require restrictions by the importing country. But any harm (for example, to the local environment) caused in the production process abroad is, in principle, not the concern or risk of the importing country.

60 As quoted in Thomas Waelde & Abba Kolo, Environmental Regulation, Investment Protection and “Regulatory Taking in International Law, 50 INT. & COMP. L.Q. 811, 836 n. 112 (2001), Rex Zedalis notes how the differences in risk between trade and investment have important repercussions for the non-discrimination principle:

A foreign trader may have trouble in penetrating a market, but is not exposed to any significant risk. A foreign investor, on the other hand, is heavily exposed for the long-term to significant political and now regulatory risk, both in developing and developed countries. Discrimination is therefore a much more serious issue for an investor as compared to a trader.
harm, sudden relocations, or labor exploitation. The chemical disaster in Bopal and the departure of Volkswagen and Renault from Belgium are poignant examples. Investment leaves a bigger footprint, both positive and negative, than trade. As a result, and in contrast to trade, investment may necessitate and justify more extensive regulation by the importing country.

To recap, with respect to investment the importing country has (1) less incentive to restrict or mistreat foreign investments, as imports of capital are mostly seen as “good” anyway, yet also has (2) more rights to regulate foreign investment, as FDI generally leaves a bigger footprint than trade. These are both arguments in favor of according more deference to the regulating state in investor-state disputes than in trade disputes.

The history of convergence and divergence between international trade and investment law reveals different, but complementary, objectives and interests. The sophisticated interstate trading system embodied in the WTO has focused on liberalizing market access for foreign goods in order to improve the aggregate welfare of nations, whereas BITs have sought to protect individual investor rights in order to stimulate the flow of FDI into specific host nations eager to boost their economic development. The substantive standards, standing requirements, and remedies in the two disciplines have evolved to reflect these differences. We now turn to the implications of these different, but complementary, objectives for the role, scope, and interpretation of national treatment provisions in trade and investment disputes.

III. The Objectives, Evolution, and Current Interpretation of National Treatment in Trade and Investment Treaties

National treatment provisions take various forms, but their basic requirement is that nations treat foreign individuals, enterprises, products, or services no less favorably than they treat their domestic counterparts. Trade lawyers and scholars have been sorting through the legal implications of this obligation for decades in the context of the GATT and other legal agreements that underlie the WTO. As we explain below, application of the national treatment principle in trade law has oscillated between phases of varying severity and laxity. At the center of these
interpretive cycles lies the fundamental tension between the liberal devotion to free trade and the sovereign’s right to tax, legislate, and regulate according to domestically determined policy.

National treatment provisions have long been a pivotal component of multilateral trade agreements, whereas their importance in investment agreements is fairly recent and signals a substantive convergence between trade and investment law. As national treatment provisions are now commonly litigated under BITs and other international investment agreements, investment arbitration panels, too, have had to grapple with the tension between preventing discrimination against foreign investors and respecting a nation’s sovereign right to regulate. Some have referred to GATT/WTO jurisprudence, whereas others have been reluctant to import trade law national treatment tests and have, instead, begun to create a distinct body of national treatment jurisprudence, often adopting legal stances that are at odds with trade law precedents.

To some degree, a divergent interpretation of national treatment in trade and investment might result from their different institutional settings. Investment arbitrators have different professional backgrounds and motivations than WTO panelists, Appellate Body members, and their support staff. For example, investment arbitrators often have a private commercial background, whereas WTO adjudicators are mainly public officials. Moreover, WTO actors are part of a well-established and institutionalized community of trade diplomats and experts, who may sometimes find it difficult to embrace new ideas developed in investment law. Conversely, investor-state arbitration is a relative newcomer that began attracting wider attention only with the boom in cases starting in the mid 1990s. Its actors may therefore feel a need to establish and legitimize themselves—an exercise that can involve dissident behavior, including the rejection of established WTO precedents. Whatever their importance, we leave these considerations aside and focus on the possible impact of the history and underlying objectives and political economies of the two regimes.

**National Treatment in Trade Agreements**

National treatment provisions exist in a various trade law treaties, including the GATT and GATS. GATT Article III obligates WTO members to provide national treatment to imports originating in other WTO member countries. Article III:4, for example, states:

> The products of the territory of any contracting party imported into the territory of any other contracting party shall be accorded treatment no less favourable than that accorded to like products of national origin in respect of all laws, regulations and requirements affecting their internal sale, offering for sale, purchase, transportation, distribution or use.

**Objectives and evolving importance of GATT national treatment.** As originally included in the GATT, national treatment had two objectives. The first, and initially most important, objective was to ensure that nations could not circumvent their tariff reduction commitments at the
border by enacting discriminatory taxes or internal laws once goods had cleared customs.\textsuperscript{68} However, as the Appellate Body noted in its very first national treatment dispute,

> the statement . . . that "one of the main purposes of Article III [national treatment] is to guarantee that WTO Members will not undermine through internal measures their commitments under Article II [on tariffs]" should not be overemphasized. The sheltering scope of Article III is not limited to products that are the subject of tariff concessions under Article II.\textsuperscript{69}

Indeed, the second objective of GATT national treatment—which, over time, became the most prominent one—is broader and more fundamental. The Appellate Body described it thus:

> The broad and fundamental purpose of Article III is to avoid protectionism in the application of internal tax and regulatory measures. More specifically, the purpose of Article III "is to ensure that internal measures 'not be applied to imported or domestic products so as to afford protection to domestic production'". Toward this end, Article III obliges Members of the WTO to provide equality of competitive conditions for imported products in relation to domestic products.\textsuperscript{70}

There is a clear rationale for prohibiting domestic protectionism through origin-based internal measures. In political terms, discrimination creates animosity. Cordell Hull, U.S. secretary of state from 1933 to 1944 and one of the founders of the GATT regime, regarded "[t]rade discrimination . . . as the handmaiden of armed aggression." His undersecretary, Sumner Welles, insisted that "one of the surest safeguards against war is the opportunity of all peoples to buy and sell on equal terms."\textsuperscript{71} In economic terms, discrimination creates inefficiencies. Products are produced and sold not because they are made well or cheaply, but because of where they are made. Moreover, as compared to tariffs or taxes, discriminatory internal regulations are especially wasteful; unlike tariffs and taxes, origin-based regulations impose costs on foreign firms that generate no government revenue, and they require more resources to administer and enforce, leading to greater "deadweight losses" on the economy.\textsuperscript{72} Hence, if a WTO member

\textsuperscript{68} As one GATT panel put it: "[T]he intention of the drafters of the Agreement was clearly to treat the imported products in the same way as the like domestic products once they had been cleared through customs. Otherwise indirect protection could be given." Panel Report, Italian Discrimination Against Imported Agricultural Machinery, para. 11, BISD 75/60 (adopted Oct. 23, 1958).


\textsuperscript{70} Id. One delegate, quoted id. at 17 n.39, who was involved in the original negotiations of the GATT national treatment provision summarized the provision’s dual objective as follows:

> This Article in the Charter [now GATT Article III on national treatment] had two purposes, as I understand it. The first purpose was to protect the items in the Schedule . . . that is, to ensure that a country offering a tariff concession could not nullify that tariff concession by imposing an internal tax on the commodity, which had an equivalent effect. If that were the sole purpose and content of this Article, there could really be no objection to its inclusion in the General Agreement. But the Article in the Charter had an additional purpose. That purpose was to prevent the use of internal taxes as a system of protection.

\textsuperscript{71} Both quotes are taken from Richard Gardner, Sterling-Dollar Diplomacy: The Origins and the Prospects of Our International Economic Order 8, 19 (1957).

wants to be protectionist, the preferred policy instrument under trade law is a tariff at the border, not discriminatory internal measures. The GATT thus imposes a general prohibition on discriminatory internal measures, forcing nations to resort to imposing tariffs, which are systematically reduced through reciprocal concessions.

The importance of the national treatment principle within the trade regime can be sketched in three distinct periods. The first period (1947–87) focused on tariff reductions, and national treatment was relatively unimportant. It primarily served to reinforce tariff reductions, and to the extent that there were trade disputes based on national treatment, they involved relatively simple cases of de jure discrimination. In the second period, which started only in the late 1980s, national treatment became more prominent. Gradual tariff reductions increased the importance of internal, nontariff barriers as trade impediments. The first objective of national treatment, reinforcement of tariff reductions, was displaced by the second objective of ensuring equal competition between imports and domestic products. The rise of internal, nontariff barriers also increased the complexity of the national treatment discipline. More and more trade disputes centered on the question of discrimination, and most involved facially origin-neutral measures that nevertheless discriminated against imports in effect, or de facto.

The importance of the GATT national treatment discipline may be waning once again, however, in what could be seen as a third period (from the late 1990s onward). WTO members have concluded new trade agreements that impose additional requirements on technical barriers to trade (TBT Agreement) and sanitary and phytosanitary measures (SPS Agreement).

In particular, these agreements require that such measures, even if not discriminatory, must still be either “necessary” to achieve their nonprotectionist purpose or based on sound science. If, under the TBT and SPS Agreements, exporting nations can challenge directly the necessity or scientific basis of trade restrictions without having to prove a prior national treatment violation, there may be little reason to bother with the intricacies of proving de facto discrimination under GATT Article III. Yet the TBT and SPS Agreements apply only to trade in goods. With respect to trade in services, similar additional disciplines are under negotiation within GATS (pursuant to Article VI on domestic regulation), but for now, national treatment remains the core discipline for internal measures. Moreover, even for trade in goods, national treatment will remain an important discipline because certain domestic measures fall outside both the SPS and TBT Agreements.

GATT national treatment is about competitive opportunities, not actual trade flows. Because trade law’s goal is to increase liberalization and market access for imports in the interest of overall welfare, not to guarantee rights or trade flows to individual exporters (see part II above), national treatment in GATT is focused upon equalizing the competitive opportunities of

73 See GATT, supra note 37, Art. III.
74 See id., Art. II.
75 We use 1987 as a tentative cutoff date because it was the year in which the first dispute over de facto discrimination was brought (namely, the first Japan—Alcohol case).
76 Agreement on Technical Barriers to Trade, Apr. 15, 1994, WTO Agreement, supra note 16, Annex 1A, in THE LEGAL TEXTS, supra note 16, at 138 [hereinafter TBT Agreement].
78 A prominent example is internal taxation of alcoholic beverages, the subject of three WTO disputes centered on national treatment under GATT Article III:2.
imports as compared to domestic products. Just as lower tariffs create market access opportunities but do not guarantee actual sales of exports, GATT national treatment ensures equal competitive opportunities, not actual sales. The flip side of this approach is that in order to demonstrate a violation of national treatment, the exporting WTO member is not required to show how the internal measure at stake has actually impeded specific trade flows. It is sufficient to point to a measure as it exists on the books and to explain how this measure affects competitive opportunities in favor of domestic products. GATT Article III:4 explicitly applies to “all laws, regulations and requirements affecting [the] internal sale, offering for sale, purchase, transportation, distribution or use [of products].” In contrast to investment law, especially as interpreted in the Methanex Corp. v. United States dispute discussed below, there is no need to demonstrate how such laws or regulations specifically target or affect the rights of individual foreign traders or businesses. The Appellate Body summarized this crucial aspect of trade law as follows:

[Under GATT Article III (national treatment)] it is irrelevant that “the trade effects” of the tax differential between imported and domestic products, as reflected in the volumes of imports, are insignificant or even non-existent; Article III protects expectations not of any particular trade volume but rather of the equal competitive relationship between imported and domestic products.80

Cyclical interpretations of national treatment in GATT/WTO dispute settlement. Over the decades the national treatment tests applied by GATT/WTO dispute resolution panels and the Appellate Body have cycled through varying degrees of strictness and laxity.81 At least five distinct periods can be discerned. Across time, however, GATT/WTO panels and the Appellate Body have applied a two-part test to determine whether a law, regulation, or requirement complies with Article III:4. First, they determine which domestic products are to be considered “like products” for the purposes of comparison to the foreign product in question. Second, they determine whether the law or regulation in question accords the foreign product “less favorable treatment” than it does to the domestic like product.82 If the regulation is found to treat foreign products less favorably than domestic like products, they find a violation of the national treatment obligation and strike the measure down unless one of the exceptions contained in Article XX is successfully invoked.83

In the first period, from 1947 through 1987, the specific methodology for determining which products are “like products” and what constitutes “less favorable treatment” for the purposes of GATT Article III was quite permissive. As pointed out earlier, national treatment was considered a simple backup obligation to more important tariff and quota reductions.84 Only

79 Methanex Jurisdiction & Merits, supra note 8.
80 Japan—Alcohol, supra note 69, at 15 & n. 34 (referring to United States—Taxes on Petroleum and Certain Imported Substances, para. 5.1.9, GATT B.I.S.D. (34th Supp.) at 136 (adopted June 17, 1987)).
83 GATT, supra note 37, Art. XX.
84 See discussion supra note 68 and accompanying text.
measures that overtly discriminated between foreign and domestic products on their face, or de jure, were found to violate the obligation.

Beginning with the Japan—Alcohol dispute in 1987, however, GATT parties began to challenge, and GATT panels began to find violations by, measures that discriminated only implicitly, or de facto. In a world where domestic laws and regulations, not tariffs, began to constitute the major obstacles to trade, panels tightened their analyses of the likeness between products, largely to ensure equal competition between imports and domestic production. Panels did so by focusing on the objectively observable characteristics of the goods, such as physical similarities, tariff classifications around the world, whether consumers treat the products as substitutes, and whether they have similar end uses. In the period between 1987 and 1992, this second, more intrusive interpretation of national treatment emerged.

Decisions such as Tuna/Dolphin focused public attention on how this more intrusive approach can potentially impinge upon arguably legitimate domestic regulation. The United States banned imports of tuna caught within the jurisdiction of countries that did not, according to the United States, sufficiently protect dolphins. Because the method of catching tuna does not affect the tangible product characteristics of tuna itself, GATT Article III on national treatment was found not to be applicable; instead, the tuna ban was constrained as a quantitative restriction applying only to imports. It was therefore per se prohibited under GATT Article XI.

Partly in response to public outcry against the Tuna—Dolphin cases, the reports for which were never officially adopted, GATT jurisprudence briefly swung back to a more permissive stance, constituting the third period from 1992 to 1995. As of 1992, in decisions such as US—Malt Beverages and US—Automobile Taxes, GATT panels began to move away from a strictly objective evaluation of likeness, citing Article III:1’s statement that internal measures “should not be applied ... so as to afford protection to domestic production.” The panels interpreted this statement as calling for an evaluation of a regulation’s “aim and effect” within the like-products analysis; products would not be considered alike if a regulation drew a bonafide distinction between them that did not involve nationality-based discrimination and did not have a protective effect on the conditions of competition in the market.

The fourth period, running from 1995 through 2000, began with the creation of the WTO Appellate Body, which rejected the “aims and effects” test and instituted a new, stricter test. This shift back to a more intrusive interpretation of national treatment is largely explained by

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85 Japan—Alcohol, supra note 69.
87 On the crucial distinction in trade law between market access and domestic regulations, see Joost Pauwelyn, Rien ne Va Plus? Distinguishing Domestic Regulation from Market Access in GATT and GATS, 4 WORLD TRADE REV. 131 (2005).
91 GATT, supra note 37, Art. III:1
the Appellate Body’s textual approach to treaty interpretation, as was directed by WTO negotiators in the WTO treaty itself.92

The Appellate Body’s methodology can be summed up in a single word: competition. First, “a determination of ‘likeness’ under Article III:4 is, fundamentally, a determination about the nature and extent of a competitive relationship between and among products.”93 By examining the foreign and domestic products’ properties and end uses, consumers’ tastes and habits, and tariff classifications, panels determine the extent to which the products compete in the market.94 The greater the competitive relationship between the products, the more likely they are “like products” for the purposes of Article III:4. Second, in the context of Article III:4, whether “imported products are treated ‘less favourably’ than like domestic products should be assessed . . . by examining whether a measure modifies the conditions of competition in the relevant market to the detriment of imported products.”95 In other words, the mere fact that domestic and foreign products are treated differently is not sufficient to establish “less favorable treatment.”96 It is also not pertinent whether the measure’s aim or objective is to alter the conditions of competition.97 Rather, the central question is whether the difference in treatment has the effect of worsening the competitive opportunities of the foreign product in relation to like domestic products.

The Appellate Body’s test makes no room for the achievement of legitimate regulatory objectives that also have incidental protectionist effects. GATT Article XX enumerates a limited set of exceptions that a party may invoke to save a measure that formally violates Article III:4 but that is also aimed at fulfilling one of the listed legitimate regulatory purposes, such as protecting public morals or human health.98 Article XX somewhat offsets the rigidity of the national treatment test, but the article is fairly rigid itself, cabining the range of legitimate regulatory purposes to those enumerated and often applying only to the extent that a measure is “necessary” to achieve the professed purpose.99 Moreover, whereas under GATT Article III the burden of proof is on the complainant, the burden to invoke an exception under GATT Article XX is on the regulating country.

In reaction to the Appellate Body’s early, strict interpretation of national treatment (1995–2000), which centered on “like products,” in recent years the interpretive pendulum

92 See Article 3.2 of the Understanding on Rules and Procedures Governing the Settlement of Disputes, Apr. 15, 1994, WTO Agreement, supra note 16, Annex 2, in THE LEGAL TEXTS, supra note 16, which refers to the “customary rules of interpretation of public international law.” Articles 31 and 32 of the Vienna Convention on the Law of Treaties start interpretation with the ordinary meaning of treaty terms and refer only in a last instance to preparatory works.


95 Korea—Beef, supra note 82, para. 137.

96 Id.


98 GATT, supra note 37, Part. II, Art. XX.

99 Hudec, supra note 97, at 636–38.
may have begun to swing back in the opposite direction again (fifth period: 2000— ). More specifically, there are important signs in recent case law that some form of aims-and-effects test is back. The reasons for this change are difficult to ascertain but may lie in the fear that WTO disciplines are becoming too intrusive and in the resulting public pressure on WTO adjudicators. Furthermore, the Appellate Body’s move from strictly textual to more contextual and teleological interpretation is characteristic of institutions that have gained a basic level of legitimacy.

An example of the change can be observed in the Appellate Body’s application of the second sentence of GATT Article III:2, which applies to tax discrepancies between directly competitive or substitutable products. In particular, the Appellate Body considers the effect and purpose of the tax measure because, according to Article III:1, a violation exists only if the regulation is applied “so as to afford protection to domestic production.” As the Appellate Body noted in Chile—Taxes on Alcoholic Beverages, “we consider that a measure’s purposes, objectively manifested in the design, architecture and structure of the measure, are intensely pertinent to the task of evaluating whether or not that measure is applied so as to afford protection to domestic production.”

In that same dispute, the Appellate Body was also willing to check whether domestic regulatory objectives other than protectionism (for example, public health or progressive taxation) could rebut the claim that Chile’s tax was applied “so as to afford protection to domestic production.” Crucially, such analysis was undertaken within the national treatment test itself, not under the GATT Article XX exceptions. The Appellate Body held, however, that the mere reference to legitimate domestic regulatory objectives was not sufficient: “The conclusion of protective application reached by the Panel becomes very difficult to resist, in the absence of countervailing explanations by Chile. The mere statement of the four objectives pursued by Chile does not constitute effective rebuttal on the part of Chile.”

Similarly, the Appellate Body has stressed the importance of a regulation’s effect on imports versus domestic products even under GATT Article III:4, despite the inapplicability of the “so as to afford protection” language to that provision. It has performed this “effects” analysis under the rubric not of likeness, but of whether the regulation provides less favorable treatment to imports versus domestic products. In EC—Asbestos, the Appellate Body stressed that finding less favorable treatment of imports is not simply a matter of identifying one single imported product that is banned and one like domestic product that is permitted. The overall effect of the measure must be to favor domestically produced products over imports.

For example, where a measure bans asbestos but permits alternative fibers, asbestos and alternative fibers may be considered “like products.” Even so, the asbestos ban is discriminatory only if it favors domestic products over imported products, so a fundamental question remains to be answered: which product is the “domestic” product and which is the “imported” product? Both asbestos and alternative fibers may have been produced domestically and imported prior

100 Appellate Body Report, Chile—Taxes on Alcoholic Beverages, para. 71, WT/DS87/AB/R (adopted Jan. 12, 2000) [hereinafter Chile—Alcohol].
101 Id.
102 Appellate Body Report, EC—Bananas, para. 216, WT/DS27/AB/R (adopted Sept. 25, 1997) (“[A] determination of whether there has been a violation of Article III:4 does not require a separate consideration of whether a measure ‘afford[s] protection to domestic production’.”).
103 EC—Asbestos, supra note 93.
to the ban. Therefore, to answer the question, it is essential to discern, among other things, whether the banned product (asbestos) is primarily imported, whereas the permitted product (alternative fibers) is primarily domestically produced. A challenger to the ban must prove that the entire group of imported asbestos and alternative fibers is treated less favorably than the entire group of domestically produced asbestos and alternative fibers. In the words of the Appellate Body,

even if two products are “like”, that does not mean that a measure is inconsistent with Article III:4. A complaining Member must still establish that the measure accords to the group of “like” imported products “less favourable treatment” than it accords to the group of “like” domestic products . . . . [A] Member may draw distinctions between products which have been found to be “like”, without, for this reason alone, according to the group of “like” imported products “less favourable treatment” than that accorded to the group of “like” domestic products.104

National Treatment in Investment Agreements

Most modern BITs include national treatment provisions that require signatory nations to provide foreign investors and investments with treatment no less favorable than they accord in like circumstances or situations to their own investors and investments.105 Investor-state disputes involving national treatment provisions in BITs are resolved by arbitral tribunals organized under the rules of various organizations, most often the International Centre for Settlement of Investment Disputes (ICSID).106 These tribunals are not required to follow each other’s precedents, and unlike in trade law, there is no appellate body to clarify and resolve conflicts in the tribunals’ applications of national treatment. Furthermore, textual variations in the national treatment provisions contained in BITs and other agreements affect their legal interpretation and effect. For example, whereas some treaties condition national treatment on the presence of “like circumstances,” others make no mention of likeness. Another factor is that there are few major precedents to evaluate. Consequently, it is difficult, though not impossible, to distill general principles about national treatment in the investment context from the decisions of investment tribunals.

Objectives and evolving importance of national treatment in investment treaties. Recall that in the GATT/WTO, national treatment has two functions. First, it protects tariff reductions against circumvention by way of discriminatory internal measures. Second, and over time more importantly, it assures equal competitive opportunities between imports and domestic production by eliminating origin-based internal measures, which are politically disruptive and economically inefficient. The origin of national treatment within investment law is strikingly different. It has obviously never served to protect tariff or other liberalization commitments, for BITs include no tariff reductions and rarely even include investment liberalization or entry as part of their mandates. More importantly, as originally construed, national treatment in the investment context coincided with the Calvo doctrine of “mere” national treatment under customary international law—pursuant to which, for example, U.S. investors in Mexico

104 Id., para. 100.
105 See, e.g., NAFTA, supra note 13, 32 ILM at 639.
106 Shenkin, supra note 43, at 549.
should not expect any treatment better than the treatment given to Mexican investors.\textsuperscript{107} Indeed, as noted earlier, the very creation of BITs was largely a reaction to such "mere" national treatment. The first BITs aimed at confirming certain international minimum standards that had to be respected for foreign investors even if they were not respected for domestic investors.\textsuperscript{108} Put differently, BITs were originally concluded in order to go beyond national treatment—and, contrary to the trade regime, not to make national treatment a central legal principle.

Although national treatment provisions were included in even the earliest BITs, what mattered in the first decades (1960s to 1980s) were rules on expropriation and other minimum standards. National treatment in the investment context gained prominence only in the late 1990s. Developing-country hosts of foreign investment gradually increased their domestic standards, often exceeding the original benchmark set by earlier international minimum standards. As the treatment of domestic investors thereby rose above the "mere" international minimum, the discipline of national treatment gained importance and attracted investors' renewed attention.

Political and economic developments since the 1980s have further induced most host countries to liberalize their markets to FDI on their own.\textsuperscript{109} As a result, investment disputes have shifted from focusing on overt instances of expropriation to claims that host nations are indirectly expropriating property or are violating national treatment obligations through the enactment of discriminatory domestic laws.\textsuperscript{110} This trend accelerated with the conclusion of NAFTA and can also be seen in the increased number of investor-state arbitration cases launched against developed countries\textsuperscript{111} where direct expropriation or blatant violations of minimum standards have not generally been at issue.\textsuperscript{112}

What is more, the renewed potential of national treatment as an investment discipline may actually be broader and deeper than in the trade context. First, unlike trade law, whose national treatment obligation remains limited to the treatment of products, national treatment in BITs

\begin{footnotesize}
\begin{enumerate}
\item \textsuperscript{107} SHEA, supra note 27, at 17–19.
\item \textsuperscript{108} See supra text accompanying note 30.
\item \textsuperscript{109} See supra notes 31–32 and accompanying text.
\item \textsuperscript{111} With NAFTA investment disciplines applying also to Canadian and Mexican investments in the United States, the shifting positions around the Calvo doctrine (or national treatment) have now come full circle. Whereas the United States was an early supporter of minimum standards against the Calvo doctrine or national treatment, the United States itself has now raised questions about the minimum standard. It does not want the minimum standard to support a requirement that foreigners invested in the United States receive treatment that is better than the treatment that U.S. investors receive. In other words, now that the minimum standard increasingly applies also to the United States, the country is shifting positions in favor of "mere" national treatment. See, e.g., Bipartisan Trade Promotion Authority Act of 2002, 19 U.S.C. §3802(b)(3) (Supp. V 2005) (expired July 1, 2007).
\item \textsuperscript{112} See Sornarajah, supra note 61, at 209 ("In the case of developing countries, most of the litigation has arisen from expropriation and not from violation of standards of treatment. The experience of the litigation under NAFTA between Canada and the United States, however, has largely concerned the treatment provisions.").
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covers the entire lifecycle or footprint of an investment. It goes far beyond measures that affect the products or services produced by foreign investors. It also covers the entire gamut of laws, rules, and regulations that may affect any aspect of an investor’s business.

Second, whereas GATT national treatment may be losing importance with the creation of the TBT and SPS Agreements, the future of national treatment in the investment context looks brighter. According to a study by the UN Conference on Trade and Development, for example, the “national treatment standard is perhaps the single most important standard of treatment enshrined in international investment agreements.” At the same time, national treatment in BITs may often coincide with, or blur the boundary between, itself and discrimination under another obligation commonly included in BITs: the fair and equitable treatment standard.

To some extent this standard, with its focus on fairness and reasonableness, can even be seen as a rough equivalent to the SPS and TBT Agreements in the trade context, with their focus on “necessity” and sound science. If so, the future of national treatment in both spheres may, after all, be similarly uncertain.

The presence of both “fair and equitable treatment” and “national treatment” provisions in BITs reminds us, however, that from the very beginning, protection of investors against discrimination was a real and primordial concern in investment treaties. Unlike GATT/WTO national treatment, where discrimination is found by comparing imports with like domestic products, investment treaties’ approach to discrimination was not concerned with relative standards of treatment. Indeed, BITs’ minimum standards were designed to counteract the Calvo doctrine, and their nondiscrimination obligations aimed at the alleged right of newly
independent developing countries to discriminate against foreign investors, especially investors of former colonial rulers.120

As part of the obligation to provide foreign investors "fair and equitable treatment" (as opposed to national treatment), countries were required to refrain from discriminating. But the standard did not call for a relative comparison of domestic and foreign investors, nor was it limited to origin-based discrimination. It was, and continues to be, a much broader standard—potentially including such things as racial or religious discrimination, and grounded in the customary international law on the treatment of aliens. Whereas nondiscrimination in trade law quickly focused on economy-wide efficiency and competition, nondiscrimination in investment law originated and remains embedded in the idea of individual fairness. For example, Article 3.1 of the Netherlands–South Africa BIT provides: “Each Contracting Party shall ensure fair and equitable treatment of the investments of investors of the other Contracting Party and shall not impair, by unreasonable or discriminatory measures, the operation, management, maintenance, use, enjoyment or disposal thereof by those investors.”121 Similarly, an oft quoted definition of “fair and equitable treatment” by the NAFTA tribunal in Waste Management puts it thus:

[D]espite certain differences of emphasis, a general standard for [NAFTA] Article 1105 [on fair and equitable treatment] is emerging. Taken together, the S.D. Myers, Mondev, ADF and Loewen cases suggest that the minimum standard of fair and equitable treatment is infringed by conduct attributable to the State and harmful to the claimant if the conduct is arbitrary, grossly unfair, unjust or idiosyncratic, is discriminatory and exposes the claimant to sectional or racial prejudice, or involves a lack of due process leading to an outcome which offends judicial propriety . . . .122

In sum, trade law’s focus on market access and liberalization centers national treatment in the GATT/WTO on efficiency concerns: protecting tariff commitments against circumvention and ensuring equal competitive opportunities to imported products. In contrast, investment law’s focus on protecting individual investors in order to attract more FDI, especially to developing countries, focuses national treatment on providing security and fairness to individual business operations by curtailing discriminatory abuse by local governments.123

120 As the representative of Indonesia put it at the negotiations of Article 2.3 of the 1966 International Covenant on Economic, Social and Cultural Rights (an article that reserves the right of developing countries to “determine to what extent they would guarantee the economic rights recognized in the present Covenant to non-nationals”):

The developing countries, which had to rebuild their national economies from the legacy left by colonialism, were not prepared to accept, equally with the highly developed countries, an obligation to guarantee the same economic rights to their nationals and to non-nationals. That was not discrimination; but it would be discrimination to compel countries of unequal strength to carry the same load. The developing countries held inevitably to correct the consequences of the discrimination practiced under the colonial regime by taking certain measures which might conflict with the interests of a privileged minority.

Id. at 60–61 (quoting UN GAOR 3d Comm., 17th sess., 1204th mtg. at 358, UN Doc. A/C.3/SR.1206 (1962)).


123 As one recent investment tribunal noted, “The purpose of [national treatment in the U.S.-Egypt BIT] is to promote foreign investment and to guarantee the foreign investor that his investment will not because of his foreign nationality be accorded a treatment less favourable than that accorded to others in like situations.” Champion Trading Co. v. Arab Republic of Egypt, ICSID Case No. ARB/02/9, para. 126.
National treatment in investment treaties focuses on harm to specific investments, not abstract competitive opportunities. Recall that trade law is about competitive opportunities, not actual trade flows. To win a national treatment claim, a WTO complaining country is not required to show that the challenged internal measure has actually impeded specific trade flows; it is sufficient to point to a measure as it exists on the books and to explain how that measure affects competitive opportunities in favor of domestic products. Not needing to prove actual harm in order to find a violation dovetails logically with the ultimate remedy for breach of WTO rules—namely, withdrawal or amendment of the inconsistent measure, not damages for harm caused. These features of trade law result from its focus on liberalization and market access for a country's exports as a whole.

In investment law, it is more important to prove a measure's actual impact on, or harm to, a specific investor or investment. The ultimate remedy in most BITs, as well as NAFTA Chapter 11, is compensation for harm done to specific investors, not an obligation to bring the measure into conformity with, for example, national treatment. Without a direct injury to a specific investor, there is no remedy. Moreover, shifting our focus from the back-end phase of remedies to the front-end stage of jurisdiction, NAFTA Chapter 11's scope and coverage provision, Article 1101, accounts for actual impact by limiting its application to “measures adopted or maintained by a Party relating to . . . investors of another Party.” In the Methanex dispute, the tribunal analogized this condition to the concept of proximate cause in tort law and to the causation requirement for contract damages. It explained that although NAFTA Chapter 11 seeks to protect individual investors from being harmed by host governments, measures enacted by government agencies naturally have wide-ranging effects upon society. In the tribunal’s view, the requirement that a measure “relate to” an investment—which it interpreted to mean that there must be a “legally significant connection” between the measure and the foreign investment or investor—provides practical insurance that government agencies do not have to pay for every imaginable cost that a given measure might arguably impose upon foreign investors.
Commentators and tribunals are still struggling to define specifically the content and importance of the "relating to" requirement. For present purposes it suffices to note that requiring some form of direct impact or proximate cause is consistent with investment law’s focus on protecting the individual rights of investors, but would not be consistent with trade law’s focus on liberalization and market access more generally. Indeed, an examination of the cases actually submitted to trade, as opposed to investment, tribunals generally supports this divergence: most trade disputes are about laws or regulations of general application (such as tariff schemes, countrywide bans on asbestos or hormone-treated beef, or a WTO member’s intellectual property regime); in contrast, most investment disputes are about discrete acts or conduct directed at specific investors (such as a decree expropriating a specific business or plot of land, or the denial or withdrawal of a license to a particular company).

Interpretation of national treatment by investment tribunals. Like the WTO Appellate Body in approaching GATT Article III, investment tribunals applying national treatment provisions have addressed two central questions: (1) which domestic investments should be compared to the foreign investment, and (2) what constitutes "less favorable treatment" of a foreign investment in violation of the provision. Also like the WTO Appellate Body, investment tribunals have ultimately struggled with the importance of creating a test that can parse discriminatory measures from those with legitimate regulatory objectives.

In determining which foreign and domestic investments should be compared, investment tribunals have departed from trade law’s national treatment precedents and have formulated their own somewhat conflicting tests. Investment treaties usually require a comparison of treatment afforded to investments “in like circumstances” or “in like situations.” Investment tribunals have found this language to be significantly different than GATT Article III:4’s call for a comparison between “like products.” First, investment tribunals have overwhelmingly decided that, as opposed to WTO jurisprudence on “like products,” a competitive relationship is not the most fundamental ingredient of foreign and domestic investments “in like circumstances.” Most recently, the NAFTA tribunal in the Methanex dispute rejected the direct use of trade law “likeness” tests, including their focus on the competitive relationship between domestic and foreign companies. It emphasized that NAFTA Chapter 11’s goal of protecting individual investors from injury, along with its use of the phrase “in like circumstances,” was different from WTO Article III:4’s focus on “like products.”

130 For example, Weiler, supra note 127, at 906, argues that “technically, [the U.S.] argument was not based upon NAFTA Article 1101 ["related to"] but, rather, upon the United States’ reading of Article 1102 [national treatment].” He also notes, id.:

Whereas in other cases it would be relatively easy to establish that a measure directly affected an investor or investment, [Methanex] presented the unique circumstance of an investment whose business was only indirectly affected by a would-be ban on the substance for which its product was an ingredient rather than a ban on the ingredient itself.

131 That said, counterexamples exist in both regimes: many antidumping or subsidy disputes at the WTO focus on one or a limited number of exporters; recent investment disputes such as Methanex, Corn Products, see supra note 14, and Foresti, see infra note 187, target laws of general application (a prohibition on MTBE, tax on certain sweeteners, and affirmative action for blacks, respectively). These cases illustrate the recent convergence between trade and investment regimes.

132 See Methanex Jurisdiction & Merits, supra note 8, pt. IV, ch. B, paras. 34–37; Occidental Exploration & Prod Co v Republic of Ecuador, infra note 151, para. 176; Pope & Talbot Phase 2, supra note 7, para. 57.
circumstances,” indicated the “intent of the drafters to create distinct regimes for trade and investment.”

Second, tribunals in the major investment disputes have also decided that, pursuant to the “in like circumstances” test, only foreign and domestic investments that raise similar public policy concerns should be compared. This position differs from WTO jurisprudence, where, at least pursuant to the Appellate Body’s traditional, textual approach to treaty interpretation (fourth period identified above, from 1995 to 2000), the only public policy concerns that can be considered are the GATT Article XX exceptions. The suggestion that public policy concerns should play a greater role in investment treaty national treatment provisions was perhaps first offered by the Organisation for Economic Co-operation and Development (OECD). It stated that “the key to determining whether a discriminatory measure applied to foreign-controlled enterprises constitutes an exception to National Treatment is to ascertain whether the discrimination is motivated, at least in part, by the fact that the enterprises concerned are under foreign control.” The tribunal in the NAFTA investment dispute Pope & Talbot, Inc. v. Canada later expressed the same idea more clearly by stating that, in essence, “Article 1102 prohibits treatment that discriminates on the basis of the foreign investment’s nationality.” It does not prohibit differential treatment based on some other reason.

Every subsequent major investment decision has agreed that the national treatment test’s objective is to ferret out discrimination based upon nationality, though some tribunals have disagreed about the method of accomplishing that result. What is important for present purposes is that under the traditional trade law approach, differential treatment between products that sufficiently compete is almost automatically found to be a violation of national treatment; differential treatment of competing products is presumed to be based on nationality, and traditionally (at least under the fourth period identified above) no alternative explanations can be offered. In investment law, however, more positive evidence of nationality-based discrimination is required; competition and differential treatment do not normally suffice, as other policy justifications can be referred to in the national treatment test itself.

The most well-accepted method for discovering nationality-based discrimination was first suggested by the tribunal in the NAFTA dispute S.D. Myers, Inc. v. Canada. It followed the OECD’s position that a comparison between foreign and domestic investments is “only valid if it is made between firms operating in the same sector.” In S.D. Myers, a U.S. company complained that the Canadian government had destroyed its PCB remediation business by enacting, at the urge of the domestic industry, a ban on PCB exportation. In approving the OECD’s method of comparing S.D. Myers only to Canadian companies in the PCB remediation business, it noted a significant difference between GATT Article III and most investment treaties: the GATT includes a list of exceptions in Article XX that can be invoked to

134 Pope & Talbot Phase 2, supra note 7, para. 78 n.73. The tribunal refers here to page 22 of the 1993 OECD study National Treatment for Foreign-Controlled Enterprises. This OECD statement was given considerable importance because national treatment is part of the OECD Declaration on International Investment and Multinational Enterprises (Guideline II), at <http://www.oecd.org>, a declaration that has been ratified by all thirty OECD members and ten nonmembers.
135 Pope & Talbot Phase 2, supra note 7, para. 79 (emphasis added).
136 But see the new trend discussed supra text accompanying notes 100–04 and infra text accompanying notes 189–91.
137 S.D. Myers Partial Award, supra note 7, para. 248.
excuse a violation of national treatment. Because NAFTA does not include such a list of exceptions, the tribunal agreed with the OECD that any comparison of domestic and foreign investments must “take into account circumstances that would justify governmental regulations that treat them differently in order to protect the public interest.”

The tribunal compared S.D. Myers only to Canadian PCB remediation companies, based upon the presumption that all investments in the same business or economic sector raise similar public policy issues, regardless of their nationality. Canada tried to argue that because the fledgling domestic PCB waste remediation business was likely to fail if forced to compete with S.D. Myers, its export ban was based on its legitimate need to ensure a domestic capacity to remediate PCB wastes. The tribunal agreed that this goal was legitimate and that NAFTA did indeed include a concern for environmental protection. It concluded, however, that banning the exportation of PCBs was not a valid means of accomplishing that goal, especially because Canada could have accomplished the same result by granting subsidies or sourcing all government requirements to the domestic industries.

The tribunal in the Pope & Talbot lumber products dispute subsequently refined the analysis from S.D. Myers into a coherent “like circumstances” test. Based upon reasoning similar to that used in the “like circumstances” analysis of S.D. Myers, the tribunal initially presumed that any regulatory treatment of Pope & Talbot that was less favorable than the treatment received by Canadian softwood lumber producers was attributable to the company’s nationality. This presumption, which shifts the burden of proof from the complainant to the regulating defendant, obviously makes the NAFTA national treatment test more intrusive. The tribunal then stated, however, that the presumption could be rebutted by showing that the measure has “a reasonable nexus to rational government policies that (1) do not distinguish, on their face or de facto, between foreign-owned and domestic companies, and (2) do not otherwise . . . undermine the investment liberalizing objectives of NAFTA.” If the measure distinguished between Pope & Talbot and the Canadian investments based upon such a legitimate policy, those companies could not be said to be in “like circumstances,” and the tribunal would conclude that no nationality-based discrimination had taken place even if Pope & Talbot was competitively disadvantaged by Canada’s regulation.

The tribunal concluded that Canada was able to rebut the presumption that it was discriminating against Pope & Talbot based upon its nationality. The tribunal noted that the United States had made a final decision to impose countervailing duties only upon the four provinces covered by Canada’s quota regime and that Canada’s decision to include only those provinces was therefore “reasonably related to . . . removing the threat of [countervailing duty] actions.” The measure drew a legitimate distinction between companies in threatened versus non-threatened provinces, with the consequence that companies in nonthreatened provinces were not in “like circumstances” with Pope & Talbot. Only domestic companies residing within the threatened provinces could be compared to Pope & Talbot, and since those companies were equally disadvantaged, the measure could not “reasonably be said to be motivated by discrimination outlawed by Article 1102.”

138 Id., para. 246.
139 NAFTA Article 2101(1), supra note 13, explicitly provides that GATT Article XX is incorporated into certain chapters of the NAFTA, including those governing trade in goods (Part 2), “except to the extent that a provision of that Part applies to . . . investment.”
140 S.D. Myers Partial Award, supra note 7, para. 250.
141 Id., para. 255.
142 Pope & Talbot Phase 2, supra note 7, paras. 18–29.
143 Id., para. 78.
144 The tribunal concluded that Canada was able to rebut the presumption that it was discriminating against Pope & Talbot based upon its nationality. The tribunal noted that the United States had made a final decision to impose countervailing duties only upon the four provinces covered by Canada’s quota regime and that Canada’s decision to include only those provinces was therefore “reasonably related to . . . removing the threat of [countervailing duty] actions.” Id., para. 87. The measure drew a legitimate distinction between companies in threatened versus non-threatened provinces, with the consequence that companies in nonthreatened provinces were not in “like circumstances” with Pope & Talbot. Id., para. 88. Only domestic companies residing within the threatened provinces could be compared to Pope & Talbot, and since those companies were equally disadvantaged, the measure could not “reasonably be said to be motivated by discrimination outlawed by Article 1102.” Id., para. 87.
The tribunal in *Feldman v. Mexico* later reaffirmed that NAFTA’s national treatment provision is “designed to prevent discrimination on the basis of nationality.”\(^{145}\) It also reaffirmed that when a foreign investment receives less favorable treatment than a domestic investment in the same business or economic sector, tribunals should presume that the discrimination is based upon nationality.\(^{146}\) Echoing *Pope & Talbot*’s “like circumstances” analysis, the tribunal stated that in “the investment context, the concept of discrimination has been defined to imply unreasonable distinctions between foreign and domestic investors.”\(^{147}\) It therefore decided that the company controlled by Feldman (CEMSA) was “in like circumstances” only with cigarette reseller-exporters and could not be compared to cigarette producer-exporters, because there were “rational bases” for treating them differently, such as discouraging smuggling and protecting intellectual property rights.\(^{148}\) The tribunal employed a presumption that CEMSA was treated less favorably because of its nationality, noting that evidence of nationality-based discrimination usually lies in the hands of the allegedly offending government and would consequently constitute an “insurmountable burden” for the foreign investor to produce.\(^{149}\) It concluded that the Mexican government had violated its national treatment obligation because it had not shown a “reasonable nexus” between nondiscriminatory “rational government policies” and its discrepant tax treatment of CEMSA and the domestic cigarette exporters.\(^{150}\)

Other investment tribunals have not followed the business or economic sector approach to determining whether discrimination is based upon nationality. The tribunal in *Occidental Exploration & Production Co. v. Ecuador* rejected Ecuador’s argument that a U.S. oil exporter should be compared only to domestic investments in the same business sector.\(^{151}\) In so doing the tribunal further expanded the potential reach of national treatment in investment law. The dispute in question involved a foreign oil exporter’s right to a refund on value-added tax (VAT). Ecuadorian tax law provided for VAT refunds in the case of export-oriented “manufacturers.”\(^{152}\) The Ecuadorian tax agency had determined that domestic companies involved in the export of certain natural resources, including flowers, mining, and seafood—but not oil—were entitled to VAT refunds as “manufacturers.”\(^{153}\) Its only explanation for the discrepant treatment was that there was no right to a VAT refund under Ecuadorian law\(^{154}\) and that “the policy” allowed distinctions between flowers and oil.\(^{155}\)

In the context of Occidental’s national treatment claim, the Ecuadorian government fell back on the argument that flowers and oil are not in the same business or economic sector, and so should not be compared.\(^{156}\) The tribunal rejected this argument and decided, instead, that

\(^{145}\) *Feldman v. Mexico*, ICSID Case No. ARB(AF)/99/1, Award, para. 181 (Dec. 16, 2002).

\(^{146}\) *Id.*

\(^{147}\) *Id.*, para. 170.

\(^{148}\) *Id.*

\(^{149}\) *Id.*, para. 183.

\(^{150}\) *Id.*, para. 184.


\(^{152}\) *Id.*, para. 125.

\(^{153}\) *Id.*, para. 168.

\(^{154}\) *Id.*, para. 34.

\(^{155}\) *Id.*, para. 172.

\(^{156}\) *Id.*, para. 171.
the Ecuador-U.S. BIT’s “in like situations” language required the tribunal to compare Occidental to all domestic exporters, including exporters of flowers. It found that the Ecuadorian Supreme Court had concluded that the allocation of a VAT depends solely on the final destination of the good and therefore explicitly required a VAT refund for all exporters, without regard to the type of good produced. Since “the purpose of national treatment in this dispute... is to avoid exporters being placed at a disadvantage in foreign markets because of indirect taxes paid in the country of origin,” the tribunal held that “no exporter ought to be put at a disadvantageous position as compared to other exporters.” The tribunal rejected the business or economic sector test within the regulatory context of VAT refunds because the host country’s own domestic law precluded any policy argument that investments in different sectors should be treated differently.

Another significant departure from the business or economic sector test—in the opposite direction as compared to Occidental’s test—was suggested by the tribunal in Methanex. The Canadian investor in that dispute was the largest supplier of methanol to California. Businesses, such as oil refiners, bought methanol and converted it into the gasoline additive MTBE. In 1999, the governor of California signed an executive order stating that MTBE constituted a “significant risk to the environment” due to leaking underground storage tanks and the chemical’s propensity to contaminate groundwater supplies. In response, the state enacted regulations banning the sale of gasoline containing MTBE in California. Methanex challenged the ban, claiming that it treated Methanex less favorably than domestic companies producing ethanol, which was the only fuel additive alternative to MTBE and which remained legal to sell in the state.

In considering whether Methanex was “in like circumstances” with domestic ethanol producers, the tribunal agreed that the function of NAFTA Article 1102 is to eliminate discrimination based upon nationality. However, instead of applying the business or economic sector test, it decided that the ideal comparison is with a domestic investment “that is like [the foreign investment] in all relevant respects, but for nationality of ownership.” Any differential treatment between identical investments could be presumed to be attributed only to the foreign investment’s nationality. The tribunal concluded that it would be “perverse” to ignore such identical investments where they exist, and therefore decided that the effect of the MTBE ban on Methanex was to be compared only to its effect upon domestic methanol producers.

In sum, every major interpretation of the “in like circumstances” or “in like situations” language in the national treatment provisions of investment agreements has rejected the trade law emphasis on alteration of the conditions of competition (the “competition test”) in favor of a test that focuses on whether an alleged discrimination is effectively based upon nationality.

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157 Id., para. 176.
158 Id., para. 141.
159 Id., paras. 175–76 (emphasis added).
160 Methanex Jurisdiction & Merits, supra note 8.
162 Id., para. 14.
163 Id., para. 19.
165 Id., para. 14.
rather than some other policy reason (the “regulatory context” test). The tests devised by investment tribunals have differed along several important factors. Most apparently, the tribunals have taken various positions on the breadth of the domestic investments to be compared. At one extreme, the Occidental tribunal compared all foreign and domestic exporters. At the other extreme, the Methanex tribunal compared only identical foreign and domestic exporters. The majority have fallen between these two extremes, comparing foreign and domestic investments in the same business or economic sector based upon the presumption that such investments raise similar public policy concerns (an approach we criticize below).

In addition, the decisions have highlighted the importance of a number of other factors. Tribunals have had to decide who carries the burden of proving that less favorable treatment is based upon the investment’s nationality. In most cases the burden of proof was shifted to the defendant as soon as the complainant established differential treatment in the same business or economic sector (another decision we question below). Tribunals have also had to decide whether, and what kinds of, domestic policies can be used to disprove that discrimination is based upon nationality. Generally, tribunals were open to any legitimate policy objective, in contrast to the closed list of policy exceptions in GATT Article XX. Finally, tribunals have begun to address the appropriate standard of review for these policies. The majority of tribunals have once again taken a considerably softer approach than the “necessity test” under many GATT Article XX exceptions, looking only for a “reasonable” or “rational” nexus between the measure and the policy pursued.

Investment tribunals have not discussed what constitutes “less favorable treatment” of a foreign investor as extensively as the “in like circumstances” requirement. Nevertheless, under this latter step in the analysis, too, investment tribunals have decided that trade law precedent is inapposite primarily because of investment law’s concentration on protecting the individual investor and the national treatment requirement’s goal of eliminating discrimination based upon nationality. At least two important components of this issue in the investment context can be identified from the existing decisions: (1) whether proof is needed of discriminatory intent, and (2) whether a foreign investment is entitled to the most favorable treatment afforded to comparable domestic investments.

Host countries have argued, and continue to argue, that national treatment in the investment context is violated only upon proof of discriminatory intent on the part of the regulating
government. In response, tribunals have held almost unanimously\(^{169}\) that discriminatory intent can play a role when objectively proven but that it is not a prerequisite for a finding of national treatment violation.\(^{170}\) This line of reasoning corresponds closely to that of the Appellate Body, which held that protectionism under GATT national treatment “is not an issue of intent.”\(^{171}\)

Host countries have sometimes argued that if a measure does not disadvantage a foreign investor with respect to a majority of comparable domestic investments, the measure does not afford that investor “less favorable treatment.”\(^{172}\) In other words, they have argued that even if a measure disadvantages a foreign investor vis-à-vis one comparable domestic investment, so long as it treats the balance of comparable domestic investments equally badly or worse, then the measure cannot be said to treat the foreign investment less favorably than domestic investments. In the context of NAFTA Chapter 11, tribunals have quickly rejected this argument by noting that Article 1102(3) expressly states that the foreign investment is entitled to “the most favorable treatment” afforded to like domestic investments.\(^{173}\) On the basis of this language, the Methanex tribunal concluded that a foreign investment is entitled to the best treatment “accorded to some members of the domestic class.”\(^{174}\)

\(^{169}\) The one exception is Methanex Jurisdiction & Merits, supra note 8, pt. IV, ch. B, para. 12 (emphasis added), where the tribunal did require discriminatory intent: “In order to sustain its claim under Article 1102(3), Methanex must demonstrate, cumulatively, that California intended to favour domestic investors by discriminating against foreign investors and that Methanex and the domestic investor supposedly being favored by California are in like circumstances.” Yet this standard may well be an aberration based on how the case was pleaded. Methanex itself had stipulated that California’s ban on MTBE “related to” its investment only if the ban was intentionally aimed at harming Methanex as a foreign company.

\(^{170}\) The tribunal in the recent dispute, Siemens v. Argentina, summarized the current state-of-play on discriminatory intent as follows:

> Whether intent to discriminate is necessary and only the discriminatory effect matters is a matter of dispute. In S.D. Myers, the tribunal considered intent “important” but not “decisive on its own.” On the other hand, the tribunal in Occidental Exploration and Production Company v. Republic of Ecuador found intent not essential and that what mattered was the result of the policy in question. The concern with the result of the discriminatory measure is shared in S.D. Myers: “The word ‘treatment’ suggests that practical impact is required to produce a breach of Article 1102, not merely a motive or intent.” The discriminatory results appear determinative in Marvin Roy Feldman Karpa v. United Mexican States, where the tribunal considered different treatment on a de facto basis to be contrary to the national treatment obligation under Article 1102 of NAFTA.

Siemens A.G. v. Argentine Republic, ICSID Case No. ARB/02/8, Award, para. 320 (Feb. 6, 2007) (citations omitted). Based on the precedents cited, the Siemens tribunal, id., para. 321, offered its own opinion: “The Tribunal concurs that intent is not decisive or essential for a finding of discrimination, and that the impact of the measure on the investment would be the determining factor to ascertain whether it had resulted in nondiscriminatory treatment.”

\(^{171}\) The Appellate Body has held:

> It is not necessary for a panel to sort through the many reasons legislators and regulators often have for what they do and weigh the relative significance of those reasons to establish legislative or regulatory intent. . . . It is irrelevant that protectionism was not an intended objective if the particular tax measure in question is nevertheless, to echo Article III:1, “applied to imported or domestic products so as to afford protection to domestic production.” This is an issue of how the measure in question is applied.

Japan—Alcohol, supra note 69, at 27–28. However, as pointed out above, see supra note 100 and accompanying text, the Appellate Body later specified in Chile—Alcohol, supra note 100, para. 71, that “a measure’s purposes, objectively manifested in the design, architecture and structure of the measure, are intensely pertinent to the task of evaluating whether or not that measure is applied so as to afford protection to domestic production.”

\(^{172}\) See, e.g., Pope & Talbot Phase 2, supra note 7, paras. 43–45.

\(^{173}\) NAFTA, supra note 13, 32 ILM at 639.

The tribunal in *Pope & Talbot* explained why such reasoning applies in the investment context in general, not just under NAFTA. Canada had drawn upon WTO Appellate Body decisions to argue that the foreign investor must prove that it is “disproportionately disadvantaged” by the measure.\(^\text{175}\) The tribunal dismissed the value of the WTO Appellate Body precedents, noting that in GATT Article III and GATS, “the prohibited activity is, unlike in NAFTA, a modification in the conditions of competition, a standard that may under certain circumstances require comparative analysis of how the various competitors are being treated.”\(^\text{176}\) Instead, the tribunal determined that the goal of the national treatment provision in the investment context is to protect individual foreign investors from discrimination based upon nationality. Because a government might discriminate against a foreign investor by disadvantaging it with respect to a single, favored domestic investor, the tribunal reasoned that the disproportionate disadvantage test would weaken NAFTA’s ability to protect foreign investors by “tend[ing] to excuse discrimination that is not facially directed at foreign owned investments.”\(^\text{177}\) The tribunal therefore decided that “any difference in treatment” between the foreign investment and any single domestic investment in like circumstances should satisfy the “less favorable treatment” factor.\(^\text{178}\)

These few precedents strongly indicate that the object and purpose of investment agreements greatly influence the test for determining whether a measure treats a foreign investment less favorably than comparable domestic investments. Because their goal is to protect individual investors from injury, national treatment provisions in investment agreements entitle foreign investments to the best treatment afforded to comparable domestic investments. In contrast to national treatment in the trade context, no group analysis comparing the entire “domestic pool” to the entire “imported pool” is called for in the investment context.

Although the national treatment jurisprudence of investment tribunals lacks consistency and is thinner and more recent than trade law jurisprudence, it does show the early signs of cyclical interpretation, from an originally intrusive construction\(^\text{179}\) to a more recent, hands-off interpretation in favor of regulating governments. Evidence of this trend can be found in *Methanex*,\(^\text{180}\) as well as in more recent awards in *Thunderbird v. Mexico*\(^\text{181}\) and *UPS v. Canada*.\(^\text{182}\) Todd Weiler goes as far as to ask whether *Methanex* should lead us to “turn the page on NAFTA Chapter Eleven.” That viewpoint deserves consideration in view of the *Methanex* tribunal’s

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\(^{175}\) *Pope & Talbot Phase 2*, supra note 7, paras. 43–45.

\(^{176}\) Id., para. 57.

\(^{177}\) Id., para. 79.

\(^{178}\) Id.

\(^{179}\) Examples can be found in the S.D. Myers and Feldman awards. See *supra* notes 137–41, 146–50, and accompanying text.

\(^{180}\) *supra* notes 127–33, 160–65, and accompanying text.

\(^{181}\) In *Thunderbird*, the majority did not find a national treatment violation even though the dissenting arbitrator was “able to identify ‘discriminatory elements’ in the greater energy, focus and effectiveness of the enforcement activities by [Mexican authorities] against Thunderbird” which had arranged (or at least tried to arrange) a clearance of its activities as compared to the main and most successful Mexican competitor, Mr. Guardia (who had always taken a non-cooperative approach).” *Walde Dissent*, *supra* note 47, para. 2.

\(^{182}\) In *UPS*, as in *Thunderbird*, the majority found no national treatment violation, see *UPS Award*, *supra* note 166, paras. 8/1–120, although the dissenting arbitrator in *UPS* did find “the basic elements of a violation of Article 1102” (Sep. Statement, Cass, Arb., para. 133) [hereinafter Cass Dissent].
insistence on a “legally significant connection” between the challenged measure and the investment, its narrowing of the comparators under national treatment, and its requirement of discriminatory intent. What is apparent, in any event, is that NAFTA tribunals’ early enthusiasm for the protection of investor interests has, in more recent cases, been tempered by references to the public interest of host governments. One can only speculate, but this shift seems at least partly a response to outcries by both NAFTA governments and public opinion. Even more so than in national treatment cases, this shift undoubtedly took place in disputes over alleged expropriation. In contrast to early cases such as Metalclad, where government action in pursuit of environmental concerns was found to constitute indirect expropriation, the Methanex tribunal took a more hands-off approach and explained the current position as follows: “[A] non-discriminatory regulation for a public purpose, which is enacted in accordance with due process and, which affects, inter alios, a foreign investor or investment is not deemed expropriatory and compensable unless specific commitments had been given by the regulating government to the then putative foreign investor . . . .”

IV. RECONCILING AND IMPROVING THE NATIONAL TREATMENT TESTS

The distinct origins and historical falling-out of international trade and investment law, coupled with their different objectives and political economies, have caused them to apply the national treatment concept in distinctive ways. The elements of national treatment under GATT Article III:4 and as interpreted by investment tribunals are summarized in Table 1.

**Explaining the Core Differences**

Let us now summarize the differences in national treatment detailed in Table 1, and offer our own critique of the case law. Since the first five, contextual items in the table (objectives of treaty; objectives of national treatment; standing; exceptions; and remedy) were extensively covered in earlier sections, we will not discuss them here; instead, we focus on the actual national treatment tests themselves.

First, trade and investment tribunals employ different concepts of “likeness” and “less favorable treatment.” The differences are grounded in the objectives and political economies of their respective regimes. The GATT Article III national treatment test centers the analysis of both concepts on the conditions of competition between foreign and domestic goods (a “competition test”). This approach is appropriate because Article III was inserted into the GATT as a reinforcement for reductions in tariffs and quotas, which themselves were aimed at creating more equal competitive opportunities for foreign products as part of the WTO’s liberalization mission. Calling two products “like” because their characteristics put them in competition with each other makes eminent sense in this context.

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183 See supra notes 127–33, 160–65, and accompanying text. What is perhaps most worrisome for investors is that both the Methanex and Thunderbird awards forced the complaining investors to pay most of the arbitration costs, including part of the legal fees of the defending government.

184 Methanex Jurisdiction & Merits, supra note 8, Pt. IV, ch. D, para. 7. Similarly, the U.S. Model BIT, supra note 18, Annex B, Art. 4(b), specifies: “Except in rare circumstances, non-discriminatory regulatory actions by a Party that are designed and applied to protect legitimate public welfare objectives, such as public health, safety, and the environment, do not constitute indirect expropriations.”
<table>
<thead>
<tr>
<th>TABLE 1. NATIONAL TREATMENT IN TRADE AND INVESTMENT</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>National treatment in trade</strong></td>
</tr>
<tr>
<td>(GATT Article III:4)</td>
</tr>
</tbody>
</table>

**BACKGROUND**

<table>
<thead>
<tr>
<th>Objectives of treaty</th>
<th>Liberalization and market access for goods</th>
<th>Protection of investors and promotion of investment</th>
</tr>
</thead>
<tbody>
<tr>
<td>Objectives of national treatment</td>
<td>Avoid internal circumvention of tariff reductions; equal competitive opportunities for imports and domestic products</td>
<td>Protect individual investors against discriminatory abuse by host governments</td>
</tr>
<tr>
<td>Standing</td>
<td>State-to-state dispute settlement only</td>
<td>Private investors have standing</td>
</tr>
<tr>
<td>Exceptions</td>
<td>GATT Articles XX-XXI</td>
<td>No GATT Article XX-like exceptions</td>
</tr>
<tr>
<td>Remedy</td>
<td>Obligation to end the discrimination; no damages for past harm</td>
<td>Compensation of individual harm; no obligation to change law</td>
</tr>
</tbody>
</table>

**ACTUAL TEST**

<table>
<thead>
<tr>
<th>Scope of application</th>
<th>As soon as measure “affects” products</th>
<th>Measure must be “related to” (have “significant legal connection” with) the investment (Methanex)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Comparator/ “likeness”</td>
<td>“Competition test”: Imports and domestic products must be “like products” defined as products in a competitive relationship based on objective criteria (physical characteristics, tariff classification, end uses, consumer preferences)</td>
<td>“Regulatory context test”: foreign and domestic investment must be in “like circumstances”—namely, investments that are:</td>
</tr>
<tr>
<td></td>
<td></td>
<td>1. in the same business or economic sector (majority of NAFTA cases)</td>
</tr>
<tr>
<td></td>
<td></td>
<td>2. exporters (Occidental)</td>
</tr>
<tr>
<td></td>
<td></td>
<td>3. identical (Methanex)</td>
</tr>
<tr>
<td>“Less favorable treatment”</td>
<td>No requirement of discriminatory intent; measure must affect conditions of competition against group of foreign imports as opposed to group of like domestic products (EC—Adhesin)</td>
<td>No requirement of discriminatory intent; foreign investors are entitled to the most favorable treatment received by any single domestic investor in like circumstances (Pope &amp; Talbot)</td>
</tr>
<tr>
<td>Public policy justifications</td>
<td>Appear as limited exceptions in GATT Articles XX-XI</td>
<td>Appear as rebuttal to “like circumstances”: any reasonable domestic policy not based, directly or indirectly, upon nationality discrimination</td>
</tr>
<tr>
<td>Burden</td>
<td>Under the exceptions, on the defendant</td>
<td>If investor shows less favorable treatment than a single domestic investor in same sector, burden of proving that discrimination was not based upon nationality shifts to defendant</td>
</tr>
<tr>
<td>Review</td>
<td>Link between measure and public policy is “necessity” (e.g., human health) or “related to” (e.g., conservation of exhaustible natural resources)</td>
<td>Link between measure and public policy is one of “reasonable” or “rational” relationship</td>
</tr>
</tbody>
</table>
Trade law's competition test is further supported by the regime's historical focus on market access opportunities and overall welfare, rather than individual trading rights. Using competition as the crucial test may make it easier to find a violation of national treatment under the GATT than under investment treaties—since in trade, differential treatment between competing products is largely presumed to be based on nationality. As explained earlier, this easier path may well be appropriate given that (1) because imports are generally considered “bad” and capital inflows “good,” there are more incentives for domestic politicians to cheat on trade agreements than on investment treaties; (2) unlike investment disputes, legal standing in trade disputes is limited to states and serves as a political filter against too many complaints; (3) any national treatment violation in trade can be justified by explicit exceptions in GATT Article XX, whereas investment treaties usually lack explicit exceptions; and (4) unlike the monetary damages available under investment treaties, the ultimate remedy for WTO violations is limited to prospective compliance.

Investment tribunals, in contrast, have properly declined to import trade law's focus on competition into their national treatment tests. Although the objective and purpose of each investment treaty must be evaluated independently, the overall history of investment treaties demonstrates that national treatment provisions were inserted into most BITs to protect individual foreign investors from targeted attacks by their host governments. BITs traditionally focus on the security and fairness for individual investors rather than on economy-wide efficiency or competition. The objective of protecting individual investors from discrimination has appropriately led investment tribunals to focus upon the circumstances giving rise to governmental choices concerning the regulation of investments.

The language of NAFTA Article 1102 warrants this approach. It states that a party shall accord “treatment no less favorable than that it accords, in like circumstances, to investments of its own investors.”\(^{185}\) Under this formulation it is not the investment or the investor that must be “like”; the provision calls, instead, for a comparison of the circumstances in which a government regulates foreign and domestic investments.\(^{186}\) What matters is not the positioning of those investments in relation to each other within the market (“competition test”), but rather the factual support for the government’s distinction between the two when taking regulatory action (“regulatory context test”). Within investment law there are conceivably circumstances that would warrant discrepant regulation of two companies even if they are competitors, just as there are circumstances that would warrant equal regulation of two companies that do not even compete.

This focus on regulatory context is appropriate in that investments, in comparison to trade, have a much broader impact on society and operate in the context of an equally broad array of regulations. International investment causes the producer and the production process to cross the border, so investments leave a larger footprint, both positive and negative, than trade. By the same token, investments may necessitate and justify more extensive regulation by the importing country. Investment tribunals therefore need to pay closer attention to regulatory context and alternative policy justifications before finding any national treatment violation.

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\(^{185}\) NAFTA, supra note 13, 32 ILM at 639.

\(^{186}\) As Todd Weiler, supra note 127, at 915 (footnote omitted), has pointed out: “Simply put, to understand whether a domestic and a foreign investor are suitable comparators requires one to understand the circumstances of the measure as imposed upon them. In some cases, it will matter what kind of products the investors make; in others it will not.”
The second difference between the national treatment tests is in their method for assessing less favorable treatment. In cases of de facto discrimination, the WTO's analysis of less favorable treatment from *EC—Asbestos* properly reflects trade law's focus upon liberalization, countrywide efficiency, and market access for a country's exporters. It evaluates a measure's anti-competitive effect upon the *entire group* of like foreign products, not upon a single producer. In contrast, investment tribunals (in particular, the *Pope & Talbot* tribunal) have correctly decided that it is enough for a foreign investor to prove that it was treated less favorably than a single domestic investor in like circumstances. The objective of BITs is, after all, the protection of individual investors. If a government's decision to favor a domestic investor over a foreign investor is based upon the foreign investor's nationality, it is no less discriminatory just because other domestic investors are denied the same advantage. This second difference may make it easier to find a violation of national treatment under investment treaties than under the GATT, since under investment treaties there is no need for a group-based analysis.

The third and related difference is that where individual investors are seeking to prove that they have been injured by a discriminatory measure, it is sensible to require complainants under a BIT to prove a legally significant connection between the measure and the injury sustained. This requirement dovetails with private standing for investors and the remedy of damages before investment tribunals. It is inspired, moreover, by the core goal of BITs to protect individual investor rights—which dictates that before one can claim such protection, one must show a significant legal or other connection with the challenged measure. In a case like *Foresti v. South Africa*—the ongoing complaint by Italian mining companies invested in South Africa against that country’s affirmative action program under the Black Empowerment Act (BEA)—this requirement poses an additional hurdle for the complainant, which will have to demonstrate how the BEA specifically targets or affects its investment. This third difference (like the first, but unlike the second) makes it easier to find a violation of national treatment under the GATT than under investment treaties, because the GATT allows laws or regulations of general application to be challenged without a particularized showing of harm.

**Proposing a Common Core**

Despite the differing emphasis of trade law on liberalization and investment law on protection, and despite the different applications of “likeness” and “less favorable treatment” that occur as a result, let us not lose sight of the features that unite their tests for national treatment.

First, for investors as much as traders, the promise of national treatment is a level economic playing field between foreign and domestic market participants. As noted at the outset of this article, trade and investment are bound at the hip from a business perspective. In both fields, national treatment protects weaker-placed foreigners from government abuse abroad.

Second, national treatment provisions in both trade and investment agreements fundamentally imply an obligation not to discriminate, either directly or indirectly, on the basis of nationality. No other form of discrimination (for example, on the basis of race or sex) is covered by either type of national treatment. Tribunals in both contexts provide defending nations an opportunity to bring forth objective evidence that a given measure’s deleterious effects upon foreigners do not stem from nationality. In the investment context, the broad reference to

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187 *See Foresti v. South Africa, ICSID Case No. ARB(AF)/07/1 (registered Jan. 8, 2007).*
investors “in like circumstances” has consistently enabled tribunals to balance investor interests with an unlimited list of legitimate government concerns—a list far broader than the exceptions in GATT Article XX.

In trade disputes, domestic policy considerations are traditionally confined to the limited, exhaustive list of exceptions of GATT Article XX. In our view, however, there is no reason for this limitation, at least not for claims of de facto discrimination. Even before regulating countries find themselves with no defense but to invoke GATT Article XX exceptions (because a national treatment violation has been found), they ought to have the opportunity to explain why differential treatment is based not on nationality, but on other legitimate policy concerns.188

Recent WTO cases (referred to earlier as a fifth period in GATT/WTO national treatment interpretation, from 2000 on) have revived the possibility of evaluating the policy basis of a measure within the very definition of national treatment itself, and we applaud these developments. Recall, for example, Chile—Taxes on Alcoholic Beverages, which noted that “a measure’s purposes . . . are intensely pertinent”;189 Dominican Republic—Cigarettes, where the Appellate Body accepted evidence that discrepant tax burdens resulted not from nationality, but from differing shares of the domestic market;190 and EC—Biotech, where the panel remained unconvinced that discrepant treatment was based upon nationality rather than perceived safety concerns.191 These cases demonstrate that the extent of consideration given to legitimate domestic policy concerns in trade and investment law is converging: in investment law, the test is already one of “regulatory context”; in trade law, the “competition test” is gradually being—and, in our view, should be—supplemented by an examination of the policy justifications for the regulation in question. Such an examination may demonstrate that the differential treatment between imported and like domestic products is based on a legitimate objective, and not nationality.

Third, in both trade and investment cases, the burden of proving nationality-based discrimination, including less favorable treatment of foreign products or investors, rests on the complaining party. In our view, whether this burden is discharged must be decided on a case-by-case basis, taking into account elements such as discriminatory effect, objective evidence of a protectionist purpose (not subjective intent), and evidence of alternative nonprotectionist purposes or other causes for discrepant treatment that have nothing to do with the origin of the product or investment. In most cases, to rebut the complainant’s claim of discrimination, the defendant will introduce evidence on the absence of a discriminatory effect or the presence of nonprotectionist purposes, like public health, the environment, or consumer protection. In the end, the adjudicator must weigh all of the evidence together and decide whether the complainant has met his burden of proving that the regulation treats imports or foreign investors less favorably than domestic products or investors.

188 As Joel Trachtman pointed out, supra note 8, at 196, “simply examining whether any two competing products are treated differently, anti-discrimination rules would inappropriately invalidate much valid regulation.”
189 Chile—Alcohol, supra note 100, para. 71.
In trade law, proof that a measure treats the group of foreign “like products” less favorably than the group of domestic “like products” may raise a presumption that the discrepant treatment is indeed based upon nationality. As noted earlier, however, in our view defendants must be allowed to rebut such a presumption by proving that the discrepant treatment is merely a by-product of a legitimate government goal not based on national origin. Even products that compete in the market—and that are therefore included in the group of “like products” can and do have characteristics with different regulatory implications. Though no WTO report has yet held as much, a defendant should be able to rebut the presumption by proving that the discrepant treatment resulted from a factual difference related to the products that has important regulatory consequences.

Assume, for example, that the United States imposes a higher carbon tax on steel made with coal (“high-carbon steel”) than on steel made with natural gas (“low-carbon steel”). Assume further that China challenges this tax differential and argues that the United States violates national treatment by treating imported Chinese high-carbon steel less favorably than domestic U.S. low-carbon steel. In other words, it argues that the United States subjects Chinese high-carbon steel to a higher tax than domestic low-carbon steel. In these circumstances, a finding of differential treatment between these two types of steel, which compete in economic terms and are therefore probably “like products,” be enough to conclude that the U.S. carbon tax constitutes nationality-based discrimination? The answer, in our view, is no. Before a violation of national treatment can be found, China ought to explain how the tax differential relates to national origin—for example, by demonstrating that prior to the creation of the tax, the group of Chinese imports was predominantly high carbon, whereas the group of U.S. products was predominantly low carbon. Conversely, the United States must at least have the opportunity to rebut any presumption of nationality-based discrimination based on the “likeliness” of the steel—for example, by explaining how the differential treatment relates solely to concerns over global climate change, and not to the nationality of the steel.

In contrast, investment tribunals should be far more reticent than trade tribunals to accord a presumption of nationality-based discrimination based upon a comparison of foreign and domestic investor groups. As noted earlier, investment treaties focus on protecting individual investors, and investments generally operate within a broader regulatory context than trade. Furthermore, the limited incentives for countries to cheat on BITs and the generous standing rules and remedies available in investment treaties offer additional reasons to give more deference to regulating governments in investment, as opposed to WTO, disputes.

Investment tribunals have had some difficulty identifying the types of circumstances that should be considered “like.” At the one extreme, the Methanex tribunal held that only identical foreign and domestic investments should be compared, because if two such investments received discrepant treatment, it would have to be attributable to nationality discrimination. While we agree that discrepant treatment of two investments identical in every respect but nationality can safely be attributed to nationality discrimination, it does not follow that equal treatment of two otherwise identical foreign and domestic investments demonstrates that a

192 This is not to say that no presumptions at all should be used in national treatment examinations under investment law. Presumptions are needed since de facto discrimination can, by definition, never be proven 100 per cent. If national treatment means anything different from the nondiscrimination component of fair and equitable treatment, presumptions must be made. Adjudicators should not make presumptions as quickly or as easily, however, as they do under trade law.
measure has not discriminated against the foreign investment. It may still be the case that the foreign investment has been discriminated against with respect to some other, not completely identical, domestic investment.

Imagine, for example, that Methanex had been able to prove that ethanol produced by domestic companies raised the same health and environmental concerns as Canadian-produced MTBE, but that California had decided only to regulate MTBE while leaving ethanol unregulated. In this situation, the foreign investment would have been treated less favorably than the domestic product despite factual support for equal treatment in the specific circumstances of California’s decision to regulate MTBE, leading to a strong inference of nationality-based discrimination. In other words, if ethanol and MTBE actually had raised the same regulatory concerns, the Methanex tribunal’s identical comparator test would not have caught the discrimination. Its error was to focus solely on the characteristics of the investments themselves, rather than on the factual support for the government’s decision to regulate.

The Occidental tribunal’s decision, at first blush, seems to make a similar mistake in the opposite direction by comparing all exporters without regard to their business or economic sector, leading to the seemingly absurd result that exporters of flowers were lumped into the same category as exporters of oil. In reality, however, the test applied by the Occidental tribunal was truer to the objectives of national treatment in the investment context than was the test of the Methanex tribunal. The Occidental tribunal essentially held that the Ecuadorian government could provide no sound basis for distinguishing between flowers and oil within the specific regulatory circumstance of a VAT refund. One can question the correctness of the outcome of this case; there may actually have been sound reasons for making such a distinction. Nevertheless, the tribunal’s test was the correct one because it focused not on indicia of the investments’ likeness, but rather on the absence of any legitimate reason to distinguish between the foreign and domestic investments in the specific circumstances surrounding VAT refunds.

The Occidental tribunal’s decision to reject the “same business or economic sector” test was also defensible. That test is merely a peg upon which a complainant can hang an argument that there is no sound basis for distinguishing between its own investment and a domestic investment in the circumstances of a particular regulation. There is nothing to preclude a complainant from presenting a fact-based argument that, in particular regulatory circumstances, its investment should be treated the same as an investment in a completely separate sector. If one investor is a toy manufacturer, and another a maker of dies for fabric, but each uses the same potentially harmful chemical in their production processes, one would not necessarily expect them to be treated differently by a chemical regulation simply because they are in different sectors of the economy.

The majority in UPS v. Canada did not use the “same business or economic sector” test either. Instead, it used a broader comparison of the regulatory differences between mail and postal traffic, on the one hand, and courier shipments, on the other, to find that UPS and Canada Post were not in “like circumstances.” According to the tribunal, such regulatory differences are accepted both in other countries and in relevant international agreements. By

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193 Substantive Ecuadorian tax law prevented the tribunal from exploring this issue. See supra note 158 and accompanying text.

194 UPS Award, supra note 166, paras. 87–120. The same tribunal, id., paras. 173–81, also referred to the universal service requirement imposed on Canada Post as an element that put it in different circumstances than private operators such as UPS or, for that matter, Canadian courier companies competing with UPS. Although the tribunal
allowing broader comparisons that go beyond competing investors, national treatment in investment treaties may cast a larger web than national treatment in trade agreements, where comparators must be competitors. This broader range of comparisons may, in some cases, make it easier to find a violation of national treatment under investment treaties than under trade agreements.

Since comparisons between investment treaties can go beyond considerations of competition, the Pope & Talbot and Feldman tribunals, in our view, wrongly imposed a presumption of “like circumstances” for investments in the same business and economic sector. In particular, they were wrong to shift the burden of proof from complainant to defendant. More often than not, investments in the same business or economic sector will be treated equally by a non-discriminatory regulation since they will raise similar regulatory issues. It therefore makes sense for tribunals to see discrepant treatment between foreign and domestic investments in the same sector as counting in favor of the complainant; but it is an entirely different proposition to relieve the complainant of its burden to prove that a given regulation is discriminatory solely on the basis of that one discrepancy. That is, government defendants should not be deemed guilty until proven innocent merely because a regulation has a discrepant effect upon two members of the same business sector. To preserve the regulatory autonomy of states and to place the overall burden of proof on complainants, they should bear the burden of proving—in both trade and investment cases—that a regulation discriminates based on origin.

This conclusion has implications for cases such as Foresti v. South Africa. Although the details of this complaint are not known, the mere fact that Foresti is in the same mining business as a South African mining company controlled by blacks should not suffice to create a presumption of nationality-based discrimination. National treatment covers only discrimination based on nationality, not discrimination based on race. To be successful Foresti must demonstrate how South Africa’s affirmative action program disfavors foreign investors based on their nationality. At the same time, South Africa must be given the opportunity to explain why its program has nothing to do with disfavoring foreigners (for example, Italians) but, instead, is aimed at promoting a traditionally disadvantaged segment within its own society over other segments of that society.

A fourth similarity between the trade and investment law national-treatment tests concerns the kind of nexus that is required between the challenged measure and a public policy invoked to justify differential treatment. In trade law, it seems that the Appellate Body believes that this link or nexus should be something less than “necessity.” Indeed, in Chile—Taxes on Alcoholic Beverages, Chile argued that GATT Article III did not require that it demonstrate that its tax was right to refer to these broader regulatory concerns, it is unfortunate, even troubling, that it did not even allude to economic competition. See Cass Dissent, supra note 182, paras. 18–26.

195 But see supra note 192.
196 As noted by the majority in UPS v. Canada, supra note 166, para. 84, the “legal burden” of proving a national treatment violation under NAFTA Article 1102 is one “that rests squarely with the Claimant. That burden never shifts to the Party, here Canada.” Ronald Cass, see Cass Dissent, supra note 182, para. 17, however, would have shifted the burden of proof once UPS had established a competitive relationship, similar to what traditionally happens in WTO jurisprudence. Not surprisingly, many host countries have argued along similar lines. See, e.g., Government of Canada Rejoinder, para. 48, UPS Award, supra note 166; Methanex v. United States, Rejoinder of Respondent United States of America, para. 179 (Apr. 23, 2004), Methanex Jurisdiction & Merits, supra note 8.
197 See supra note 187 and accompanying text.
was “necessary” to achieve the nonprotectionist objectives of health protection and progressive taxation. The Appellate Body responded as follows:

[W]e agree with Chile that it would be inappropriate, under Article 111:2, second sentence, of the GATT 1994, to examine whether the tax measure is necessary for achieving its stated objectives or purposes . . . . It appears to us that the Panel did no more than try to relate the observable structural features of the measure with its declared purposes, a task that is unavoidable in appraising the application of the measure as protective or not of domestic production.198

Indeed, to require strict “necessity” as part of the GATT national treatment test itself could lead to odd results. Under the explicit exceptions to national treatment in GATT Article XX, some justifications are acceptable under a weaker “related to” test;199 consequently, to require “necessity” within the national treatment test itself would somehow mean that the rule (“necessity”) is sometimes stricter than the exception (“related to”). If so, the exception would lose its effect. Furthermore, cases of de jure discrimination are subject to the “related to” test under the GATT Article XX(g) exception. Therefore, counterintuitively, requiring “necessity” within GATT Article III would make it easier to justify de jure discrimination (under Article XX(g)) than de facto discrimination (under Article III).200 Yet it makes sense to require a lesser degree of connection to defend against a claim of de facto discrimination, where nationality-based discrimination cannot be proven with absolute certainty, than against a claim of de jure discrimination, where nationality-based discrimination is readily apparent. Adopting a nexus requirement less than “necessity” within the national treatment test itself therefore seems appropriate in most circumstances.

It is debatable whether a measure should merely “relate to” a legitimate government purpose (a “rational relationship” requirement) or whether it should be “substantially related to” that purpose. We agree with the approach described by the Appellate Body in applying the “necessity test” under GATT Article XX: the required degree of nexus should vary with “the relative importance of the interests or values furthered by the challenged measure.”201 That is, the nexus required within the national treatment test itself should vary depending on the “relative importance” of the nonprotectionist objective proffered by the defendant. The required nexus could be “related to,” “substantially related to,” or, in certain circumstances, “necessary to achieve” the nonprotectionist objective. In this regard, it is important to remember that within the national treatment analysis as a whole, evidence of a nonprotectionist objective should be only one of several factors to determine whether discrimination is nationality based.

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198 Chile – Alcohol, supra note 100, para. 72 (emphasis added).
199 An example is the GATT exception for conservation of exhaustible natural resources. GATT, supra note 37, Art. XX(g).
200 Surprising consequences may also follow if the nexus required within national treatment itself is something less than “necessity.” If a panel finds that a measure is not, for example, "related to" a legitimate government objective and therefore constitutes de facto discrimination under GATT Article III, then, a fortiori, a necessity requirement for an exception under GATT Article XX cannot possibly be met. The exceptions in GATT Article XX are not therefore inconsequential. They remain fully operational in cases of de jure discrimination, for which less favorable treatment based upon nationality is a foregone conclusion, and as potential justifications under any GATT provisions other than Article III (of special note in this context is Article XI, which imposes a general prohibition on quantitative border restrictions).
Investment tribunals have, at least so far, consistently referred to a nexus of "reasonable" or "rational" relationship between the measure and the objective pursued. They have thereby wisely avoided the stricter "necessity" test, which would intrude much further into the regulatory autonomy of host states. In NAFTA Chapter 11 and most BITs, there is no explicit list of exceptions like that found in GATT Article XX, so the trade law arguments presented above on the interaction between the GATT's national treatment rule and its built-in exceptions do not apply. Nevertheless, the heart of national treatment in the investment context is the same as it is in the trade context: elimination of nationality-based discrimination—and of nationality-based discrimination alone. Therefore, in the investment context, it is also appropriate to vary the nexus requirement depending on specific circumstances of each case and "the 'relative importance' of the interests or values furthered by the challenged measure."202

V. CONCLUSION

Historically, international trade and investment treaties have focused on different, but complementary, objectives. International trade agreements, such as the GATT and GATS, sought to liberalize market access for foreign goods and services in order to boost overall welfare through a more efficient allocation of the world's resources. International investment agreements, primarily BITs, provide stable legal standards and an autonomous enforcement system to reduce the risk premium for individual investors, thereby promoting greater flows of capital across borders and the economic development of host countries. In a historical context defined by the convergence and divergence of the trade and investment fields, this article has explored how differences in origin, objectives, and political economy have affected the development and application of national treatment within trade and investment disputes.

One conclusion is that trade and investment tribunals apply significantly different national treatment tests that are tailored to the objectives and political economies of their respective disciplines. As a consequence, investors cannot assume that they will prevail on a national treatment claim before an investment tribunal even if their country has earlier prevailed on the same claim at the WTO, and vice versa. In essence, national treatment in trade focuses on whether domestic and imported products compete in the market place, which requires a broad comparison between the two countries' groups of like products or services. Once a tribunal has found sufficient competition, it can presume that any differential treatment is based on nationality unless the regulating government can show otherwise.

202 Along these lines, albeit in the context of discrimination under the MFN clause, see Parkerrings-Compagniet AS v. Republic of Lithuania, ICSID Case No. ARB/05/8, Award, para. 368 (Sept. 11, 2007) ("[D]iscrimination must be unreasonable or lacking proportionality, for instance, it must be inapposite or excessive to achieve an otherwise legitimate objective of the State. An objective justification may justify differentiated treatments of similar cases. It would be necessary, in each case, to evaluate the exact circumstances and the context" (para. 368). "[A] less favourable treatment is acceptable if a State's legitimate objective justifies such different treatment in relation to the specificity of the investment" (para. 371)). In that BIT dispute, the City of Vilnius's rejection of the claimant's project to build two car parks—in favor of the tender-proposal of another foreign company—was found not to violate MFN treatment, because the two proposals were significantly different. For example, the car parks proposed by the claimant extended more significantly into Vilnius's Old Town, which is a UNESCO-protected site, and there were also differences in terms of size, historical and archaeological preservation, and environmental protection. See id., paras. 392, 396. According to the tribunal, these differences between the two proposals put the investors in "unlike circumstances"; hence, no discrimination could be found.
In contrast, national treatment in investment must center on the individual foreign investor. Although establishing a violation of national treatment may require a significant legal connection between the challenged measure and the investment, this focus on individual investors dispenses of a group-based evaluation between the broader classes of foreign versus domestic investors. Moreover, in the investment context, competition between differently treated investors should not be sufficient to presume nationality-based discrimination. Instead, the entire regulatory context in which the foreign and domestic investors find themselves must be considered. Since competition is not the core test, assessments of national treatment in investment treaties may also lead to comparisons between investors that are not even competitors, so long as the regulatory circumstances in which they find themselves are sufficiently alike.

Some of the differences in establishing violations of national treatment make a claimed violation of national treatment easier under trade law than under investment law. Examples include trade tribunals’ imposition of a presumption of violation based on differential treatment and competition alone, and the absence of a requirement to show a significant legal connection between a measure and specific traders. Other differences have the opposite effect and facilitate findings of national treatment violations in the investment context. For example, investment tribunals need not perform a group-based evaluation and may compare broader classes of investors, and investors themselves have standing to bring claims.

A second conclusion of this study is that, notwithstanding these differences and what we described as cyclical patterns of interpretation that oscillate between phases of severity and laxity, a common core of national treatment in both the trade and investment disciplines is emerging. Both regimes are grappling with the same core issue: the design of a national treatment test that eliminates discrimination against foreigners without encroaching too far upon domestic regulatory sovereignty. To find this equilibrium, we propose that national treatment should prevent not just any form of differential treatment between products, services, or investors, but only discrimination that can be demonstrated to be based on nationality. As banal as this statement might seem, when examining claims of de facto discrimination, trade tribunals too quickly find nationality-based discrimination based on mere discrepant treatment of two competing products. In contrast, investment tribunals too quickly conclude that no such discrimination exists, sometimes because they are willing to compare only identical investors.

Robert Hudec, the greatest scholar of national treatment jurisprudence in the GATT/WTO, once aptly observed that “there has always been some concern that the [national treatment] test would fail to prohibit some . . . distinctions that should be prohibited, and prohibit some . . . distinctions that should not be prohibited.” The ongoing struggle of both trade and investment tribunals is to refine their national treatment tests to prohibit only that discrepant treatment that is based upon nationality, while recognizing the legitimacy of factual distinctions between products, investors, and investments that have genuine public policy and regulatory implications.

203 Hudec, supra note 97, at 626.