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Investor-state dispute settlement and tax matters: limitations on state's sovereign right to tax

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ABSTRACT
More and more countries are coordinating at the international level to implement taxation measures to counter the problem of tax avoidance by multinational corporations (MNCs). This has led to increasing internalization of taxation measures, which, in turn, will lead to greater normative dialogue between international taxation and other branches of public international law such as international investment law (IIL). This paper argues that MNCs and foreign investors have not shied from using the IIL framework to challenge sovereign taxation measures of States before investor-State dispute settlement (ISDS) tribunals. These challenges, part of the increasing judicialization of international tax measures, have generated a rich body of case law. While ISDS tribunals are generally deferential towards State's sovereign right to tax, they clearly recognize certain limits on this sovereign power. ISDS tribunals have not hesitated from laying down principles where abuse of taxation powers or imposition of taxes that are not reasonable or proportionate have been held to be inconsistent with the country's investment treaty obligations. Even carving-out taxation measures from the ambit of the investment treaty are no surety that an ISDS tribunal will not exercise jurisdiction over such tax measures especially when they are not exercised in a bona fide manner. As countries find ways to tax MNCs to counter the problem of tax avoidance, they should keep these important jurisprudential principles in mind.

KEYWORDS
Tax; ISDS; international investment law; bilateral investment treaties; right to regulate

1. Introduction

A *sine qua non* for the working of a modern State is its power to impose taxes.[1] Taxation has long been recognized as an intrinsic element of the State's sovereignty, which is a cornerstone of international law. It is a well-settled principle of international law that a sovereign's right to tax also extends to aliens,[2] including foreign investors. Over the years, there has been a widespread movement of capital across borders with increasing levels of foreign investment. Multinational corporations (MNCs) or foreign investors who are

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[1]P Dietsch, 'Rethinking Sovereignty in International Fiscal Policy' (2011) 37(5) *Review of International Studies*, 2107.
[2]A.R. Albrecht, 'The Taxation of Aliens under International Law' (1952) 29 *British Yearbook of International Law* 145. Chaisse and Mosquera, in this Asia Pacific Law Review special section 'The Future of International Tax Disputes'.

important drivers of foreign investment flows often exploit gaps in the tax systems of different countries to avoid paying tax.[3] This tax planning by MNCs, also known as base erosion and profit shifting (BEPS),[4] affects several countries.[5] To tackle such tax erosion, around 140 countries, within the framework of the Organisation of Economic Cooperation and Development (OECD) and the G20, are coordinating efforts to implement various measures.[6] As part of the BEPS project, countries are endeavouring to adopt several regulatory measures through national and international instruments to tackle the problem of tax avoidance. These initiatives on international taxation, as some scholars argue, are leading to the evolution of international tax law (ITL) as part of public international law.[7]

However, imposing taxes on MNCs, foreign investors, or their investment often sets in motion a process that brings sovereign taxation measures of the State face to face with the rights that foreign investors enjoy under international investment law (IIL)[8] – another branch of public international law. The most important source of IIL is bilateral investment treaties (BITs)[9] – treaties signed for the protection of foreign investment – and investment chapters in free trade agreements (FTAs). BITs and FTA investment chapters contain a provision that empowers foreign investors to directly bring claims against the host State challenging the latter's sovereign regulatory measures including taxation as potential treaty violations and claim compensation if successful. This is known as the investor-State dispute settlement (ISDS) mechanism. Indeed, over the years, MNCs and foreign investors have used the ISDS mechanism to challenge the host State's taxation measures that harmed them.[10] Using the ISDS mechanism to challenge sovereign taxation measures is a more attractive proposition for foreign investors than other mechanisms for resolving disputes, such as those found in bilateral tax treaties.[11] Over the years, foreign investors have used the ISDS mechanism to challenge a wide array of taxation measures such as windfall profits tax,[12] value-added tax,[13] income tax,[14] import taxes,[15] etc.

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[3]OECD, 'International Collaboration to End Tax Avoidance' (Base erosion and profit shifting - OECD BEPS) accessed 17 October 2021.
[4]Ibid
[5]Ibid
[6]See this Mann, in this Asia Pacific Law Review special section 'The Future of International Tax Disputes'.
[7]Chaisse and Mosquera, in this Asia Pacific Law Review special section 'The Future of International Tax Disputes'. See also J Chaisse and X Ji, 'Soft Law in International Law-Making: How Soft International Taxation Law in Reshaping International Economic Governance', (2018) 13 *Asian Journal of WTO and International Health Law and Policy* 463.
[8]J Chaisse, 'Investor-State Arbitration in International Tax Dispute Resolution: A Cut above Dedicated Tax Dispute Resolution' (2016) *Virginia Tax Review* 149.
[9]The total number of BITs (enforced and signed but not enforced) by the end of 2020 stood at 2943. See UNCTAD, Recent Developments in the IIA Regime: Accelerating IIA Reform <https://unctad.org/system/files/official-document/diaepcbinf2021d6_en.pdf> accessed 25 August 2021.
[10]V Vasudev, 'Interactions between Taxation Measures and International Investment Agreements' in J Chaisse et al. (eds.), *Handbook of International Investment Law and Policy* (2019); Mathew Davie, 'Taxation-Based Investment Treaty Claims' (2015) 6(1) *Journal of International Dispute Settlement* 202; TW Wälde and A Kolo, 'Coverage of Taxation Under Modern Investment Treaties' in P Muchlinski, F Ortino and C Schreuer (eds.), *The Oxford Handbook of International Investment Law* (2008).
[11]See J Chaisse, 'International Investment Law and Taxation: From Coexistence to Cooperation' (2016) E15 *Task Force on Investment Policy* (Think Piece).
[12]See Burlington Resources, Inc. v. Republic of Ecuador, ICSID Case No. ARB/08/5, Decision on Liability, 14 December 2012.
[13]See EnCana Corporation v. Republic of Ecuador, LCIA Case No. UN3481, Award, 3 February 2006.
[14]See Lacich v. Canada, NAFTA, 2009.
[15]See Link-Trading Joint Stock Company v. Department for Customs Control of the Republic of Moldova, Final Award, IIC 154 (2002), 18 April 2002.

The use of the ISDS mechanism to contest taxation measures showcases an important tension that the normative expansion of ITL poses for many branches of public international law such as IIL. Countries taking steps as part of the BEPS project will lead to a greater internationalization of taxation matters. On the one hand, this can be conceptualized as an expansion of State sovereignty in matters of taxation. On the other hand, this can also be understood as a normative encounter between ITL and other branches of public international law such as IIL. States exercising their sovereignty in matters of taxation to ward off tax avoidance by MNCs are playing an important role in building a new normative framework. This evolving normative framework could run into other existing frameworks such as IIL. In such a situation, foreign investors, as the evidence suggests, will not shy away from using the IIL framework to determine the legality of taxation measures under international law.

Against this background, the purpose of this article is to study the taxation-based ISDS claims brought against host States by foreign investors with a specific focus on some recently decided cases. This analysis is an important step towards fully comprehending the relationship between ITL and public international law. This analysis is also important to showcase the increasing judicialization of tax disputes before ISDS tribunals, which, in turn, would shed light on the limits of the sovereign right to tax.

While challenging taxation measures before ISDS tribunals, foreign investors have alleged the violations of several substantive protections in investment treaties, such as national treatment,[16] full protection and security[17] and umbrella clauses.[18] However, most ISDS claims have been brought for unlawful expropriation and the violation of the fair and equitable treatment (FET) provision. Therefore, this article focusses on claims under these two heads (in Parts 2 and 3). Given the sensitivity of the taxation measures and the possibility of foreign investors challenging taxation measures, some countries exclude, partially or completely, taxation matters from the purview of the investment treaty. Part 4 of the article emphasizes this aspect by studying the interpretation of the carve-out provision for taxation matters in tax-based ISDS claims. Part 5 concludes by drawing some essential principles that may be useful for States as they collectively mull over international taxation reforms.

2. Expropriation and taxation measures

Protection from unlawful expropriation is an important right that foreign investors enjoy under BITs. As the cases of direct expropriation have become rare, the disputes surrounding expropriation through indirect means, such as confiscatory taxation, are on the rise. For an analytical understanding of expropriation and taxation, the article divides the discussion on taxation and expropriation into three parts. First, the article discusses that the ISDS tribunals have upheld the general principle that taxation is part of the State's sovereign powers and does not amount to expropriation. Second, the article deliberates the situations when taxation measures can amount to expropriation, focusing on whether

[16]See Marvin Roy Feldman Karpa v. United Mexican States, ICSID Case No. ARB(AF)/99/1, Award, 16 December 2002.

[17]See Occidental Exploration and Production Company v. The Republic of Ecuador, LCIA Case No. UN3467, Final Award, 1 July 2004.

[18]See Enron Corporation and Ponderosa Assets, L.P v. Argentine Republic, ICSID Case No. ARB/01/3, Award, 22 May 2007.

the taxation measure has led to a substantial deprivation of the investment, i.e. the 'effect' of taxation on investment. Third, we study how certain tribunals seem to have included other factors besides examining the 'effect' of the taxation measure in determining whether taxation measure leads to expropriation. We call this an 'effect' plus approach.

2.1. Taxation is part of a State's sovereign power

ISDS tribunals have recognized the fundamental principle that taxation is an integral element of a State's sovereign power. Accordingly, a substantial degree of deference will be granted to States regarding their taxation measures. For instance, in *Eiser* v. *Spain*,[19] the tribunal held that the power to tax is a core sovereign power of the State that should not be questioned lightly.[20] Likewise in *El Paso* v. *Argentina*,[21] the tribunal held that 'the tax policy of a country is a matter relating to the sovereign power of the State and its power to impose taxes on its territory. The Tribunal agrees that the State has a sovereign right to enact the tax measures it deems appropriate at any particular time'.[22] The tribunal in *Burlington* v. *Ecuador*[23] also held that general taxation is part of the State's regulatory power and does not constitute an expropriation.[24]

A logical corollary to not questioning the power to tax lightly implies a general presumption that taxation measures adopted by a State are bona fide unless proved otherwise. The ISDS tribunals have upheld the principle of the presumption of validity of taxation measures. An ISDS tribunal in *Renta 4* v. *Russia*[25] opined that when it comes to examining taxation measures constituting compensable takings, the starting point should be that the taxation measures are a bona fide exercise of the State's public powers.[26] This principle was affirmed in *Novenergia II* v. *Spain*[27] and other cases.[28]

2.2. Taxation constitutes expropriation: the substantial deprivation test

Notwithstanding the State's sovereign right to impose taxes and the presumption about the validity of taxation measures, in certain situations, taxation may amount to the indirect expropriation of foreign investment. To understand when will taxation measures

[19]See Eiser Infrastructure Limited and Energía Solar Luxembourg S.à r.l. v. Kingdom of Spain, ICSID Case No. ARB/13/36, Award, 4 May 2017.
[20]Ibid., para 270. See also Unglaube v. Costa Rica, Award, 16 May 2012, para 246.
[21]See El Paso Energy International Company v. The Argentine Republic, ICSID Case No. ARB/03/15, Award, 31 October 2011.
[22]Ibid., para 290.
[23]See Burlington Resources Inc v. Republic of Ecuador, ICSID Case No. ARB/08/5, Decision on Liability, 14 December 2012.
[24]Ibid., para 391. Likewise, an ISDS tribunal in Ryan, Schooner Capital and Atlantic Investment v. Poland, Award, 24 November 2015, paras 468 and 469 held that bona fide exercise of taxation powers does not constitute expropriation. See also Valeri Belokon v Kyrgyzstan, UNCITRAL, Award, 24 October 2014, para 199.
[25]See Renta 4 S.V.S.A., Ahorro Corporación Emergentes F.I., Ahorro Corporación Eurofondo F.I., Rovime Inversiones SICAV S.A., Orgor de Valores SICAV S.A., GBI 9000 SICAV S.A. v. Russian Federation, SCC Case No. 24/2007, Award, 20 July 2012.
[26]Ibid., para 181. See also August Reinisch and Christoph Schreuer, *International Protection of Investments: The Substantive Standards* (CUP 2020), 91.
[27]See Novenergia II - Energy & Environment (SCA) (Grand Duchy of Luxembourg), SICAR v. The Kingdom of Spain, SCC Case No. 63/2015, Award, 15 February 2018, para 580.
[28]See RREEF Infrastructure (G.P.) Limited and RREEF Pan-European Infrastructure Two Lux S.à r.l. v. Kingdom of Spain, ICSID Case No. ARB/13/30, Award, 11 December 2019, paras 186 and 188; See El Paso v. Argentina, supra n. 22, para 290.

amount to expropriation, it is important to briefly explain the substantial deprivation test, which has been the dominant method followed by ISDS tribunals to determine an indirect expropriation. Also known as the 'sole effects' doctrine, as part of this test, the ISDS tribunals focus on the severity of the effect of the regulatory measure on foreign investment.[29] According to this test, measures that do not constitute direct expropriation may nevertheless constitute an indirect expropriation if the effect of the regulatory measure causes a substantial deprivation of foreign investment.[30] The tribunal in *Electrabel* v. *Hungary*[31] laid down the 'substantial deprivation' test to prove an expropriation in the following manner. The tribunal held that to establish indirect expropriation, 'the requirement under international law for the investor to establish a substantial, radical, severe, devastating or fundamental deprivation of its rights or the virtual annihilation, effective neutralization or factual destruction of its investment, its value or enjoyment'.[32] Another ISDS tribunal in *BayWar.e.* v. *Spain*[33] reiterated that an indirect expropriation requires substantial deprivation of the asset in question.[34]

One of the key cases that examined when the imposition of tax will amount to indirect expropriation is *Burlington* v. *Ecuador*.[35] The tribunal in this case held that there were certain limits on State's taxation powers embodied in customary international law (CIL).[36] First, the tax should not be discriminatory; second, the tax should not be confiscatory.[37] The tribunal located the authority for these customary norms especially confiscatory taxation in the writings of publicists and other instruments like the 1961 Harvard Draft Convention.[38] The tribunal held that the difference between permissible and confiscatory taxation is the effect of the tax. A taxation measure will amount to expropriation if it leads to substantial deprivation of foreign investment as a whole.[39]

The tribunal in *Encana* v. *Ecuador* also held that taxation will amount to expropriation only if the tax imposed is extraordinary, punitive in amount, or arbitrary in incidence.[40]

[29]See B Mostafa, 'The Sole Effects Doctrine, Police Powers and Indirect Expropriation under International Law' (2008) 15 *Australian Journal of International Law* 267.

[30]See Pope and Talbot Inc. v. The Government of Canada, Ad hoc Tribunal (UNCITRAL), Interim Award, 26 June 2000, para. 96; See PSEG v. Turkey, ICSID Case No ARB/02/5, Award, 19 January 2007, paras 278–80 [PSEG]; See *CMS Gas Transmission Company* v. *The Republic of Argentina*, ICISD Case No. ARB/01/8, Award, 12 May 2005, para. 262.

[31]See Electrabel S.A. v. The Republic of Hungary, ICSID Case No. ARB/07/19, Decision on Jurisdiction, Applicable Law and Liability, 30 November 2012.

[32]Ibid., para 6.62.

[33]See BayWa R.E. Renewable Energy GMBH and BayWa R.E. Asset Holding GMBH v. Kingdom of Spain, ICSID Case No. ARB/15/16, Decision on Jurisdiction, Liability and Directions on Quantum, 2 December 2019.

[34]Ibid., para 422; Also see Philip Morris Brands Sàrl, Philip Morris Products S.A. and Abal Hermanos S.A. v. Oriental Republic of Uruguay, ICSID Case No. ARB/10/7, Award, 8 July 2016, para 192; Tecinas Medioambientales Tecmed S.A. v. The United Mexican States, ICSID Case No. ARB(AF)/00/2, Award, 29 May 2003, para 115. See R Ginsburg, 'Investor-State Dispute Settlement in the Digital Economy: The Case for Structured Proportionality' (2019) 39 *Northwestern Journal of International Law & Business* 187.

[35]See Burlington v. Ecuador, supra n 24.

[36]Ibid., para 392.

[37]Ibid., para 393.

[38]See LB Sohn and Richard R Baxter, 'Responsibility of States for Injuries to the Economic Interests of Aliens' (1961) 55 *American Journal of International Law*. 545. See also J Kurtz, 'Building Legitimacy Through Interpretation in Investor-State Arbitration', in Zachary Douglas, Joost Pauwelyn, and Jorge E Vinuales (eds.) *The Foundations of International Investment Law: Bringing Theory into Practice* (OUP 2014) 257, at 294.

[39]See Burlington v. Ecuador, supra n. 24, paras 395 to 401.

[40]See Encana v. Ecuador, supra n. 14, para 177.

The principle that taxation measures constitute expropriation only if they lead to substantial deprivation of investment was also upheld in *Occidental* v. *Ecuador*[41] and *Perenco* v. *Ecuador*.[42] An upshot of this is that an economic disadvantage or minor economic pain caused by taxation will not amount to expropriation. The tax measure should result in substantially depriving the investor of her investment for it to amount to expropriation.[43]

2.3. Taxation constitutes expropriation: an 'effect plus' approach

While some tribunals have principally relied upon the substantial deprivation test that relies on the effect of the taxation measure, few other tribunals have mentioned other factors, besides effect, to decide whether taxation measures constitute an expropriation. For instance, the tribunal in *Link Trading* v. *Moldova*[44] held that 'as a general matter, fiscal measures only become expropriatory when they are found to be an abusive taking'. The tribunal then went on to explain when 'abuse' arises. According to the tribunal, abuse arises where it is demonstrated that the State has acted unfairly or inequitably towards the investment, where it has adopted measures that are arbitrary or discriminatory in their manner of implementation, or where the measures taken violate, an obligation undertaken by the State regarding the investment. Likewise, the tribunal in *Tza Yup Shum* v. *Peru*[45] said that there is a 'considerable consensus that the imposition and application of tax measures can acquire an expropriatory character if it is confiscatory, arbitrary, abusive, or discriminatory'.

Thus, these tribunals do not seem to limit their assessment to the 'effect' of the taxation measure, in their quest to determine indirect expropriation. They also focus on other factors such as whether the taxation measures are 'abusive', 'unfair', 'inequitable' and 'discriminatory' to determine indirect expropriation. This can be called an 'effect plus' approach to determining whether taxation measures constitute indirect expropriation.

However, this 'effect plus' approach, conceptually, is on a sticky wicket. As already pointed out, whether taxation measures amount to indirect expropriation is contingent on foreign investment being substantially deprived. It is quite possible that an arbitrary or discriminatory taxation measure may not result in a substantial deprivation of foreign investment. While abusive or discriminatory taxation measures might violate other BIT standards of protection such as FET or national treatment, it's difficult to argue that such a taxation measure, unless it leads to substantial deprivation of foreign investment, amounts to indirect expropriation. This principle was laid down in *Burlington* v. *Ecuador* where the tribunal held that a discriminatory tax *per se* does not amount to expropriation.[46] The discriminatory tax will amount to an indirect expropriation only if it meets the test of substantial deprivation.[47]

[41]See Occidental Petroleum Corporation v. Ecuador, ICSID Case No ARB/06/11, Award dated 5 October 2012, paras 453–455.

[42]See Perenco Ecuador Ltd. v. Republic of Ecuador and Empresa Estatal Petroleos del Ecuador (Petroecuador), ICSID Case No. ARB/08/6, Award, 27 September 2019, paras 672 and 673.

[43]Compare this with RosInvestCo Uk Ltd v. The Russian Federation, SCC Case No. V079/2005, Award, 12 September 2010, where the tribunal said, 'it … is also undisputed, as Respondent correctly argues, that States have a wide latitude in imposing and enforcing taxation laws even if resulting in substantial deprivation without compensation'.

[44]See Link-Trading v. Moldova, supra n. 16, 18 April 2002.

[45]See Tza Yap Shum v. PeruTza Yap Shum v. Republic of Peru, ICSID Case No. ARB/07/6, Award, 7 June 2011.

[46]See Burlington v. Ecuador, supra n. 24, para 402.

[47]Ibid.

Another manifestation of the 'effect plus' approach is that some ISDS tribunals have also emphasized the purpose or the intent behind the taxation measure, not just the effect of the measure. For instance, the tribunal in *Renta 4* v. *Russia* said that 'if the ostensible collection of taxes is determined to be part of a set of measures designed to effect a dispossession outside the normative constraints and practices of the taxing powers, those measures are expropriatory … '.[48] The tribunal here talked about the 'design' of the tax measure as an important element in determining expropriation, thus clearly hinting at the intent or the purpose behind the taxation measure. Likewise, the tribunal in *Yukos* v. *Russia*[49] while concluding that Russia's taxation measures had an effect 'equivalent to nationalisation or expropriation' focussed on the intent or the purpose behind Russia's taxation measures. The tribunal held that 'the primary objective of the Russian Federation was not to collect taxes but rather to bankrupt Yukos and appropriate its valuable assets.'[50]

The tribunals that have followed an 'effect plus' approach, do not explain how much normative weight one should attach to the intent or the purpose behind the taxation measure in the analysis of indirect expropriation. However, the tribunal in *Burlington* v. *Ecuador* was forthright on this when it held that while the intent behind the measure might be important, it plays a secondary role in determining indirect expropriation.[51] Thus, the evidence of intent may be important in confirming the outcome of the effects test, but it cannot replace it.[52]

Notwithstanding the 'effect plus' approach of some ISDS tribunals, the fact is that the host State's sovereign taxation measures might amount to the expropriation of foreign investment in certain situations. There is no automatic immunity to a State's taxation measures from the purview of expropriation claims. Confiscatory and abusive taxation that results in a substantial deprivation of foreign investment will be held as a breach of the BIT's expropriation provision. Now, let's turn our attention to those instances where taxation measures have been challenged as a violation of the FET provision.

3. FET and taxation

Over the years, foreign investors have used the FET provision as the primary mechanism to challenge sovereign regulatory measures including taxation that affect their investment negatively.[53] Thus, it is imperative to discuss the ISDS claims where taxation measures have been challenged for breaching the FET provision. We divide the discussion on FET and taxation into two important heads, First, the article focusses on the principle of certainty, predictability and stability of the legal framework as part of the FET provision. Here the focus is on the recent *Vodafone v India* and *Cairn Energy v India* cases where the issue was whether the imposition of retroactive taxes violates the principle of legal

[48]See Renta 4 S.V.S.A, Ahorro Corporacion Emergentes F.I., Ahorro Corporacion Eurofondo F.I., Rovime Inversiones SICAV S.A, Quasar de Valors SICAV S.A., Orgor de Valores SICAV S.a., GBI 9000 SICAV S.A. v. The Russian Federation, SCC No. 24/2007, Award, 20 July 2012, para 48.

[49]See Yukos Universal Limited (Isle of Man) v. The Russian Federation, UNCITRAL, PCA Case No. 2005-04/AA227.

[50]See Yukos Universal Limited (Isle of Man) v. The Russian Federation, supra n. 46, paras 756, 1579; See also J Chaisse (2016), supra n. 9; Sergei Paushok, CJSC Golden East Company and CJSC Vostokneftegaz Company v. The Government of Mongolia, UNCITRAL, Award on Jurisdiction and Liability, 28 April 2011, paras 330 to 336.

[51]See Burlington v. Ecuador, supra n. 24, para 401.

[52]Ibid.

[53]Ginsburg, supra n 35, 188. See also J Chaisse (2016), supra n. 9, 194–198.

certainty and thus the FET provision. Second, the article will focus on when can taxation measures breach the legitimate expectations of the investor, which is another important component of the FET provision.

3.1. Certainty, predictability and stability of the legal framework

Several ISDS tribunals have held that the stability and the predictability of the legal framework are important elements of the FET provision.[54] In the context of taxation measures, the tribunal in *Occidental* v. *Ecuador*, where certain refunds of the value-added tax (VAT) were denied to the claimants, held that as part of the FET provision, States are under an obligation not to modify the legal and business framework of an investment.[55] The *Occidental* tribunal followed what some scholars describe as a 'strict stability obligation' where any change in the regulatory regime means altering the legal framework for the investor and thus a violation of the FET without examining the justifications for such a change.[56]

The recent tribunals have adopted what Ortino calls conceptually a 'softer stability obligation' where merely a change in the regulatory regime does not mean that stability and predictability of the legal framework have been modified resulting in a violation of the FET provision.[57] As the tribunal in *Impregilo* v. *Argentina*[58] held, 'legitimate expectations of foreign investors cannot be that the State will never modify the legal framework, especially in times of crisis, but certainly, investors must be protected from unreasonable modifications of that legal framework'. Likewise, the tribunal in *Voltaic* v. *Czech Republic* ruled that the requirement of stability is not absolute and should not be interpreted in an overly broad fashion. The State has an inherent right to revise its laws, as part of its sovereign power, to respond to changing circumstances.[59] Such changes in the legal system will not violate the requirement of legal stability provided the regulatory measures are reasonably related to a legitimate public policy objective or are proportionate.[60] In other words, as it was laid down in *Jan Oostergetel* v. *Slovak Republic,* the stability of the legal and business environment does not mean the immutability of the legal framework.[61] Changing circumstances and new challenges often require States to bring about changes in their laws. If States are held liable for merely changing

[54]See CMS Gas Transmission Company v. The Republic of Argentina, ICSID Case No. ARB/01/8, Award, 12 May 2005, para 274; See LG&E Energy Corp., LG&E Capital Corp., and LG&E International, Inc. v Argentine Republic, ICSID Case No. ARB/02/1, Decision on Liability, 3 October 2006; Enron v. Argentina, supra n. 12, Award, 22 May 2007, paras 259–60; See PSEG Global, Inc., The North American Coal Corporation, and Konya Ingin Electrik Uretim ve Ticaret Limited Sirketi v. Republic of Turkey, ICSID Case No. ARB/02/5, Award, 19 January 2007, para 250; See Murphy Exploration and Production Company International v. Republic of Ecuador (II), PCA Case No. 2012–16 (formerly AA 434), Partial Final Award, 6 May 2016, para 207.

[55]See Occidental v. Ecuador, supra n. 11, para 191; See J Chaisse (2016), supra n. 9, 198.

[56]See F Ortino, 'The Obligation of Regulatory Stability in the Fair and Equitable Treatment Standard: How Far Have We Come?' (2018) 21(4) *Journal of International Economic Law* 845–865.

[57]See Ortino (2018), supra n. 57; See also Saluka v. Czech Republic, Partial Award, 17 March 2006, paras 302–305.

[58]See Impregilo S.p.A. v. Argentine Republic, ICSID Case No. ARB/07/17, Award, 21 June 2011.

[59]See Voltaic Network v. Czech Republic, Award, 15 May 2019, para 488; See also Charanne v. Spain, Award, 21 January 2016, paras 510 and 513.

[60]For a detailed discussion of proportionality, Toni Marzal & Ricardo García Antón, in this Asia Pacific Law Review special section 'The Future of International Tax Disputes'.

[61]Para 224.

their laws in good faith it will have a chilling effect on their right to regulate in the public interest. To understand this point better, let us look at the specific instance of whether imposing taxes retroactively upends the certainty, predictability and stability of the legal framework.

3.2. Retroactive taxation and legal certainty

Two recent ISDS cases – *Vodafone v India*[62] and *Cairn Energy v India*[63] – dealt with the issue of whether retroactive taxation undermines the principle of legal certainty and thus violates the FET standard.[64] Before we look at these cases, it's useful to examine briefly the background of India's decision to impose retroactive taxes. In 2012, India amended the Income Tax (IT) Act[65] giving powers to the government to impose taxes retroactively on 'indirect transfers' i.e. on transfer by a non-resident of a share in a company incorporated abroad, if the share derived, directly or indirectly, its value substantially from assets located in India.[66] The 2012 amendment was brought in to nullify a decision of the Supreme Court of India involving India's tax department and Vodafone, on taxing 'indirect transfers' that the court ruled in favour of Vodafone.[67] Through an indirect transfer, Vodafone BV International (Vodafone's Netherland entity) acquired a 67 per cent stake in Hutchison Essar Limited ('HEL') an Indian entity, which carried out telecommunication business in India. The Indian tax department claimed that this transaction was taxable in India. But the Indian Supreme Court held that the transaction was an offshore one and thus, the Indian tax authority 'had no territorial tax jurisdiction' on the said transaction'.[68] The retroactive amendment legalized the tax demand on Vodafone that was struck down by India's apex court.

Vodafone challenged the imposition of the retroactive tax under the India-Netherlands BIT. The ISDS tribunal ruled in the favour of Vodafone pronouncing that India's retroactive taxation has violated the FET provision. The award is not publicly available, barring the operative part of the ruling. Thus, the reasoning of the tribunal is unknown. However, the tribunal, as evident from the operative part, held that India's 'conduct in respect of the imposition of the Claimant of an asserted liability to tax notwithstanding the Supreme Court Judgement is in breach of the guarantee of FET laid down in Article 4 (1) of the Agreement, as is the imposition of interest on the sums in question and the imposition of penalties for non-payment of the sums in question'.[69] In simple terms, the tribunal ruled that imposition of retroactive tax on Vodafone, despite the Supreme Court's decision, breaches the FET provision.

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[62]*Vodafone International Holdings BV v. Government of India* [I], PCA Case No. 2016–35

[63]*Cairn Energy PLC and Cairn UK Holdings Limited (CUHL) v. Government of India*, PCA Case No. 2016-7, Award, 21 December 2020.

[64]Very few ISDS tribunals have dealt with the issue of retroactive legislation. One of the few cases is ATA v. Jordan, where Jordan's law applied retroactively to extinguish those arbitration agreements that served as the basis for an arbitral award if the award was later annulled by the courts – ATA Construction, Industrial and Trading Company v. The Hashemite Kingdom of Jordan, ICSID Case No. ARB/08/2, Award, 18 May 2010, para 128.

[65]The Income Tax Act, 1961 <www.incometaxindia.gov.in/pages/acts/income-tax-act.aspx> accessed 30 October 2021 (hereinafter IT Act).

[66]The Finance Bill, 2012 <http://164.100.24.219/billstexts/lsbilltexts/AsIntroduced/Finance%20Bill,%20Eng..pdf> accessed 25 August 2021 (hereinafter 2012 Amendment).

[67]*Vodafone International Holdings B.V.* v. *Union of India & Anr*., [2012] 6 SCC 613.

[68]Ibid.

[69]See Vodafone v India, supra n. 63, para 363.

The 2012 amendment to the IT Act by India brought another 'indirect transfer' under the ambit of India's taxation laws. This pertained to the internal corporate restructuring carried out by Cairn Energy of its investments in India. Cairn Energy sued India alleging that the imposition of taxes retroactively violates the India-UK BIT.

India contested the tribunal's jurisdiction arguing that taxation measures are outside the ambit of the BIT. The tribunal rejected this argument. In the India-UK BIT, taxation measures are excluded from the ambit of the most favoured nation and national treatment principle, not from substantive provisions like the FET standard. Interestingly, the tribunal distinguished between a tax dispute and a tax-related investment dispute.[70] According to the tribunal, a tax dispute is a row related to the taxability of a specific transaction. On the other hand, in a tax-related investment dispute, the tribunal's task is to determine whether the host State has violated the substantive protection standards given in the BIT by exercising its authority in the field of taxation.[71]

Having made this ostensible distinction, the tribunal used the 'general principles of law' methodology to determine the content of the FET standard[72] by relying on select western-centric jurisdictions.[73] Hence, the tribunal held that the principle of legal certainty, which is very important in the context of retroactive taxation,[74] is a general principle of law that informs the content of the FET provision.[75] A cardinal aspect of legal certainty, typically speaking, is that laws should be amended prospectively, not retroactively. Specifically, in matters of taxation, the investor's conduct should be examined based on the law that existed when the transaction took place or the investment was made.

However, the tribunal seemingly followed the 'softer stability obligation' approach,[76] and held that legal certainty is not absolute. Certain retroactive regulations could be justified provided they were proportional to the public purpose sought to be achieved.[77] Thus, investors' interest in legal certainty has to be balanced with India's power to regulate in the public interest. Since there is a reasonable presumption that laws will be applied prospectively, retroactive application of the law can be allowed if there is 'a specific and compelling public policy objective that warrants not only the regulatory change in general, but also the retroactive application of that change'.[78] This public policy objective should be such that could not be attained by applying taxes prospectively.[79] For example, India argued that the retroactive legislative change was intended to ensure that foreign corporations who use tax havens for the indirect transfers of underlying Indian assets, pay taxes. However, the tribunal held that this objective could be accomplished by amending the income tax law prospectively, not retroactively.[80] To

[70]Cairn Energy v India, supra n 64, para 793.
[71]Ibid., paras 793–794.
[72]Ibid., paras 1715–1717.
[73]See J Paine, Cairn Energy v India: Retroactive Taxation, Fair and Equitable Treatment and the General Principles Method (13 January 2021) EJIL Talk! <www.ejiltalk.org/cairn-energy-v-india-retroactive-taxation-fair-and-equitable-treatment-and-the-general-principles-method/> accessed 15 August 2021.
[74]Cairn Energy v India supra n. 64 para 1750.
[75]Ibid., para 1749.
[76]See Ortino (2018), supra n. 57.
[77]See Cairn v. India, supra n. 64, paras 1788–1789
[78]Ibid., para 1790.
[79]Ibid.,
[80]Cairn v. India, supra n. 64, paras 1809–1810.

justify retroactive taxation there should be some additional public policy objective.[81] Reasons that would rationalize a retroactive taxation measure cannot be the same as explanations offered for a prospective change. For a retroactive tax measure to pass the muster, the threshold should be higher. A retroactive tax measure will be allowed if the public interest that it seeks to accomplish outweighs the imperatives of ensuring legal certainty. Absent such a strong public interest justification, a retroactive measure will mean breaching the core principle of legal certainty and thus the FET provision.

The Cairn tribunal's ruling can have significant implications for States and foreign investors, not just in terms of tax-related regulatory measures but also in all other kinds of governmental measures. First, the tribunal recognized the value of legal certainty for foreign investors. Second, the tribunal documented that generally, changes in the regulatory regime should be prospective. Third, and most importantly, the tribunal did not rule that retroactive measures, per se, will mean a violation of the FET provision. In other words, retroactive regulatory measures are possible provided there is a strong public policy justification for the same. If there is a public objective that cannot be achieved through a change in the regulatory regime prospectively, a retroactive amendment will trump the necessity of ensuring legal certainty. This ruling is significant because it underlines the regulatory power of States to act in the public interest without breaching their BIT obligations. It will come in handy for States as they undertake several tax reforms as part of the BEPS project.

As a consequence of losing the ISDS disputes to Vodafone and Cairn, India amended its IT Act doing away with the retroactive application of tax law on 'indirect transfers' that was introduced in 2012.[82] This change has brought to an end the ISDS disputes due to imposing retroactive tax measures.

3.3. Legitimate expectations

As far as the content of the FET provision is concerned, a concept not too far from the certainty and predictability of the legal framework is that of legitimate expectations. ISDS tribunals have repeatedly held that legitimate expectations of foreign investors are an integral part of the FET provision.[83] However, the difficult issue has always been how to define legitimate expectations. On the one end of the spectrum are cases where ISDS tribunals have interpreted legitimate expectations in a very expansive fashion.[84] In these cases, the tribunals have held States accountable for breaching investors' legitimate expectations even if the State did not offer any clear and specific assurances to the investor.[85] On the other hand, several ISDS tribunals have held that an

[81] Ibid., paras 1794, 1801.

[82] The Taxation Laws (Amendment), Bill 2021 <http://164.100.47.4/BillsTexts/LSBillTexts/Asintroduced/120_2021_LS_E.pdf> accessed 25 August 2021 (hereinafter 2021 Amendment). See generally Prabhash Ranjan, 'Retroactive Taxation, Investor-State Dispute Settlement, and India: Life Comes a Full Circle' (2022) *Intertax*.

[83] See International Thunderbird Gaming Corporation v. The United Mexican States, UNCITRAL (NAFTA), Award, 26 January 2006.

[84] See Tecnicas Medioambientales Tecmed, S.A. v. The United Mexican States, ICSID Case No. ARB (AF)/00/2, Award, 25 May 2003; Ioan Micula, Viorel Micula, S.C. European Food S.A, S.C. Starmill S.R.L. and S.C. Multipack S.R.L v. Romania [I], ICSID Case No. ARB/05/20, Award, 11 December 2013; Gold Reserve Inc. v. Bolivarian Republic of Venezuela, ICSID Case No. ARB(AF)/09/1, Award, 22 September 2014.

[85] See A Davies, 'Investment Treaty Interpretation, Fair and Equitable Treatment and Legitimate Expectations' (2018) 15 *Manchester Journal of International Economic Law* 314, 319–323.

investor's legitimate expectations will stand breached only if the State goes back on unequivocal, specific, and express assurances given to the investor.[86] For example, in *Voltiac* v. *Czech Republic*, a four-prong test was laid down to establish whether an investor's legitimate expectations have been breached – '(a) whether the Respondent gave an assurance to maintain regulatory stability; (b) whether the Claimant effectively relied on such an assurance; (c) whether this reliance was reasonable, taking into account the prevailing social and economic circumstances in the energy sector and at the time; (d) whether the Respondent violated the Claimant's legitimate expectations, bearing in mind that *de minimis* violations do not meet the necessary threshold for treaty violations'.[87]

Tribunals dealing with taxation matters have also affirmed the principle that violation of legitimate expectations will require specific assurances from the State to the investor. For instance, in *Jan Oostergetel* v. *Slovak Republic,* the tribunal held that in the absence of specific assurances, it is neither reasonable nor legitimate for a taxpayer to be relieved of tax liabilities.[88] In *Toto* v. *Lebanon* as well, the tribunal held that in the absence of a stabilization clause or similar such requirement, changes in the regulatory framework in the form of increased taxes or customs duties will not breach the FET provision.[89] However, the tribunal added a caveat that the change in the regulatory framework should not be drastic or discriminatory.[90]

This kind of qualification is related to the caveat that was offered by the tribunal in *Philip Morris* v. *Uruguay* (although in the context of tobacco regulation) that 'changes to general legislation (at least in the absence of stabilization clause) are not prevented by the FET standard if they do not exceed the exercise of the host State's normal regulatory power in the pursuance of a public interest and do not modify the regulatory framework relied upon by the investor at the time of its investment 'outside of the acceptable margin of change'.[91] Thus, the tribunal recognized the State's right to regulate. At the same time, it framed the issue in a manner that gives the ISDS tribunal the discretion to decide the moot issue of what is 'outside of the acceptable margin of change'.

The principle that no investor can have a legitimate expectation that the host State's laws will not change absent a stabilization clause was reaffirmed in *JSW Solar and Wirtgen* v. *Czech Republic*.[92] In this case, the Czech Republic to attract investments in the solar energy sector gave certain incentives to the investors including exemption from income tax for five years period from the start of operations of the solar plant.[93] However, due to changing economic circumstances the Czech Republic did away with most of the incentives including the income tax exemption.[94] The tribunal relying on *Total* v. *Argentina* held that ascertaining whether the State has granted a stabilization

[86]See Philip Morris v Uruguay, supra n. 35; See Total S.A. v. The Argentine Republic, ICSID Case No. ARB/04/01, Decision on Liability, 27 Dec 2010, paras 128–131.
[87]See Voltaic Network GmbH v. Czech Republic, UNCITRAL, PCA Case No. 2014-20, Award, 15 May 2019, para 500.
[88]Ibid., para 236; See Vasudev (2020), supra n. 11, 10.
[89]See Toto Costruzioni Generali S.p.A. v. The Republic of Lebanon, ICSID Case No. ARB/07/12, Award, 07 June 2012, para 244.
[90]Ibid.
[91]See Philip Morris v. Uruguay, supra n. 35, para 403.
[92]See JSW Solar (zwei) GmbH & Co. KG, Gisela Wirtgen, Jürgen Wirtgen, and Stefan Wirtgen v. Czech Republic, PCA Case No. 2014-03, Final Award, 11 October 2017.
[93]Ibid., para 16.
[94]Ibid., 375–392.

commitment or given a specific assurance to the investor requires examining 'the form, the content and the clarity of the alleged promise'.[95] Specifically, on the issue of withdrawal of tax incentives, the tribunal held that since the Czech Republic did not offer any commitment to the investor that the tax incentives will not be modified, the investors should expect that the laws will change.[96] The Cairn Energy tribunal also held that legitimate expectations require that a State should respect its specific commitments that the investor relied upon while investing.[97] The investor argued that it had a legitimate expectation that the settled understanding of the Indian IT Act on 'indirect transfers' would not be disturbed.[98] The tribunal did not agree with the investor and held that the law in India on the meaning of 'indirect transfers' was not settled at the time the investment was made and thus the investor could not have had such a legitimate expectation.[99]

This line of cases is very important because it duly acknowledges the State's right to regulate. As part of myriad regulatory challenges, States are often required to modify, alter and tweak their regulatory regimes including their taxation laws and policies. Holding State's accountable under IIL for undertaking such changes in their regulatory regimes will have a chilling effect on their sovereign right to regulate.

In sum, while tribunals will be deferential to State's sovereign right to tax, it may give rise to claims for FET breaches if the tax measures are arbitrary or if they violate the principle of legal certainty. Having discussed the possibility of taxation measures amounting to the violation of the expropriation and the FET provision, let us now turn our attention to how ISDS tribunals have interpreted the carve-out provisions on taxation.

4. Interpretation of the carve-out provisions on taxation

As mentioned, States may like to avoid international liability for their tax-related regulatory measures by carving them out from the purview of the investment treaty. Many investment treaties contain a carve-out clause for taxation measures.[100] These carve-outs could be complete or partial.[101] An example of a complete carve-out is Article 21 (1) of the Energy Charter Treaty (ECT), which provides, 'except as otherwise provided in this Article, nothing in this Treaty shall create rights or impose obligations concerning Taxation Measures of the Contracting Parties. In the event of any inconsistency between this Article and any other provision of the Treaty, this Article shall prevail to the extent of the inconsistency'. Another example of a complete carve-out is Article 2.4 (ii) of the 2016 Indian Model BIT, which excludes the application of the treaty to any law or measure on taxation. An example of a partial carve-out clause, as pointed out earlier, is Article 3(b) of the India-UK BIT, which states that the provisions of MFN and national treatment do not apply to any international agreement or arrangement relating wholly or mainly to taxation or any domestic legislation relating wholly or mainly to taxation.

[95]Ibid., para 409.
[96]Ibid., para 437.
[97]See Cairn Energy v. India, supra n. 64, para 1761.
[98]Ibid., para 1764.
[99]Ibid., paras 1766 to 1770.
[100]See generally Uğur Erman Özgür, 'Taxation of Foreign Investments under International Law: Article 21 of the Energy Charter Treaty in Context' (2015) Taxation_of_Foreign_Investments_2015_en.pdf (energycharter.org).
[101]See Vasudev (2020), supra n. 11, 4.

In this part, we focus on how the ISDS tribunals have interpreted the complete carve-out clauses for taxation. This issue is important because for a carve-out clause to work i.e. for a taxation measure to be outside the scope of the entire treaty or some of the substantive provisions, it has to be declared so by the ISDS tribunal.

The arbitral practice dealing with the ECT cases is very rich in this regard. Several claims were brought against Spain for undertaking a series of energy reforms where it imposed taxes on the production of electricity. For example, in *9REN Holding* v. *Spain*,[102] a case under the ECT, the issue before the tribunal was whether the tribunal had jurisdiction on a Spanish law that imposed taxes on the production of electricity. The tribunal held that it had no jurisdiction since taxation measures were carved-out. In *Belengeria* v. *Italy*[103] another case under the ECT involving Italy's slew of changes in the legal regime governing investments in the photovoltaic sector, the tribunal held that a certain fiscal measure called 'imbalance costs' was a taxation measure under the ECT.[104] Thus the tribunal had no jurisdiction over the measure due to ECT's carve-out for taxation measures.[105]

However, an important clarification about the carve-out of taxation measures in the ECT was made by the tribunal in the *Yukos* case.[106] The tribunal in the *Yukos* case held that the carve-out of Article 21(1) of the ECT is available only if a host country's regulations are *bona fide* exercise of tax powers.[107] Measures not adopted in good faith cannot be carved-out of the purview of the tribunal's jurisdiction.[108] This is an important contribution because the host States should not be able to benefit from tax carve-out clauses if they are used to shelter mala fide or abusive taxation measures. The purpose behind having a carve-out clause for taxation measures is to confer due regulatory latitude to States for enacting taxation measures. However, if States abuse this regulatory power, they should not be allowed to benefit from the carve-out provision.

Another important issue in the interpretation of a complete carve-out for taxation clauses is whether the regulatory measure that the State labels as a 'taxation measure' is indeed such a measure or is the State trying to use the complete carve-out to shield its non-taxation regulatory measures. This issue arose in several cases brought by investors against the Czech Republic under the ECT and also under other BITs of the Czech Republic.[109] The Czech Republic modified its already existing incentive regime for the

[102]See 9REN Holding S.a.r.l v. Kingdom of Spain, ICSID Case No. ARB/15/15, Award, 31 May 2019, paras 207–208; Also see BayWa r.e. Renewable Energy GmbH and BayWa r.e. Asset Holding GmbH v. Spain, ICSID Case No. ARB/15/16, Decision on Jurisdiction, Liability and Directions on Quantum, 2 December 2019; See Cube Infrastructure Fund SICAV and others v. Kingdom of Spain, ICSID Case No. ARB/15/20, Decision on Jurisdiction, Liability and Partial Decision on Quantum, 19 February 2019, Award, 15 July 2019; NextEra Energy Global Holdings B.V. and NextEra Energy Spain Holdings B.V. v. Kingdom of Spain, ICSID Case No. ARB/14/11, Decision on Jurisdiction, Liability and Quantum Principles,12 March 2019, Final Award, 31 May 2019; Masdar Solar and Wind Cooperatief U.A. v. Kingdom of Spain, ICSID Case No. ARB/14/1, Award, 16 May 2018.

[103]See Belenergia S.A. v. Italian Republic, ICSID Case No. ARB/15/40, Award, 28 August 2019.

[104]Ibid., paras 370–376.

[105]Ibid., para 379.

[106]Yukos Awards [Hulley Enterprises Limited (Cyprus) v. The Russian Federation, UNCITRAL, PCA Case No. AA 226; Veteran Petroleum Limited (Cyprus) v. The Russian Federation, UNCITRAL, PCA Case No. AA 228; Yukos Universal Limited (Isle of Man) v. The Russian Federation, UNCITRAL, PCA Case No. AA 227].

[107]Yukos cases, Final Award, parsa 1430–1435.

[108]See also Belenergia S.A. v. Italian Republic, paras 377–378.

[109]See WA Investments Europa Nova Limited v. Czech Republic, PCA Case No. 2014-19, Award, 15 May 2019; See Photovoltaic Knopf Betriebs GmbH v. Czech Republic, PCA Case No. 2014-21, Award, 15 May 2019; See Antaris Solar GmbH and Dr. Michael Göde v. Czech Republic, PCA Case No. 2014-01, Award, 2 May 2018.

renewable energy sector, including by imposing a levy on electricity generated by solar power plants.[110] In one of the cases, where these regulatory measures were challenged, the issue was whether the solar levy imposed by the Czech Republic is a taxation measure and thus exempt from the tribunal's jurisdiction due to the ECT's carve-out for taxation measures. The tribunal held that under Article 21 of ECT, which carves out taxation measures, whether a measure is a 'taxation measure' has to be determined as per the domestic law of the country.[111] The tribunal, after carefully assessing Czech law and judicial decisions concluded that the solar levy was not a 'taxation measure' and thus not eligible for a carve-out from the ECT.[112] The tribunal held that since the main objective of the solar levy was to reduce the incentives granted to the solar investors and not generate revenue for the State, it was not a taxation measure.[113]

Outside of the ECT too, there have been cases where the issue of interpretation of 'taxation measures' has arisen. One such case is *Encana* v. *Ecuador*, where the Article XII (1) of the Canada-Ecuador BIT had to be interpreted. Article XII (1) provides: 'except as set out in this article, nothing in this agreement shall apply to taxation measures'. However, the term 'taxation measures' is not defined in the BIT.[114] The tribunal held that whether 'something is a tax measure is primarily a question of its legal operation, not its economic effect'.[115] In other words, a measure that imposes a liability on classes of persons to pay money to the State for public purposes would qualify as a taxation measure.[116] The tribunal in *Burlington* v. *Ecuador* reaffirmed this principle and added that an additional requirement for something to be a taxation measure is that there should be no direct benefit to the taxpayer.[117] The tribunal in *Nissan* v. *India*[118] upheld the above principles and further clarified them. The tribunal held that to determine whether a measure qualifies as a taxation measure under the domestic law of the host state, the questions of 'who', 'what' and 'why' within the domestic legal framework of the host State would have to be answered.[119] The issue of 'who' means which entities under the host State's laws are empowered to collect or administer taxes; the question of 'what' deals with the qualitative nature of the measure, and the question of 'why' implies the purpose of the measure i.e. whether it is inspired principally by tax objectives.[120]

5. Conclusion

The important takeaways from the discussion in this Special section article are as follows. First, foreign investors are increasingly using the IIL framework to challenge sovereign taxation measures of countries. Second, ISDS tribunals recognize the State's sovereign

[110]See I.C.W. Europe Investments Limited v. Czech Republic, PCA Case No. 2014-22, Award, 15 May 2019.
[111]See I.C.W. Europe Investments Limited v. Czech Republic, supra n. 115, paras 290–293.
[112]Ibid., paras 294–307.
[113]Ibid., para 317.
[114]See Vasudev (2020), supra n. 11, 13.
[115]See Encana v Ecuador, supra n. 14, para 142.
[116]Ibid.
[117]See Burlington v. Ecuador, supra n. 24, para 159.
[118]See Nissan Motor Company Ltd. v. Republic of India, UNCITRAL, PCA Case No. 2017/37, Decision on Jurisdiction, 29 April 2019.
[119]Ibid., para 386.
[120]Ibid.

right to impose a tax as an important component of the State's public power. Third, nonetheless, the tribunals recognize certain limits on State's sovereign power to tax. Thus, abusive or confiscatory taxation would fall foul of the substantive standards given in the investment treaties. Likewise, a discussion of the FET cases demonstrates that while countries have a right to change their tax-related legal regimes, these changes should be reasonably related to a legitimate public welfare objective and should be proportional to the public purpose they seek to achieve. Any drastic or unproportionate modification in the tax-related legal regime could violate the principle of legal certainty, and thus the FET provision. As the Cairn Energy tribunal shows, bringing the retroactive application of tax laws would require additional justification. Fourth, inserting carve-out provisions for taxation measures in investment treaties could be an important method to preserve tax-related sovereignty. However, such carve-outs cannot be used to shield taxation measures that are mala fide or abusive.

These takeaways are critical for States as they plan to coordinate and implement new international taxation measures as part of the BEPS project. Given the increasing judicialization of tax measures under the IIL framework, MNCs or other claimants might challenge the new taxation measures. Thus, as the discipline of ITL grows organically, it would face increasing encounters and interactions with other international law frameworks such as IIL. States should be alert to this possibility. As States develop their policy arsenal to ensure that MNCs and other foreign investors do not indulge in practises such as tax avoidance, they should simultaneously do the following to minimize the use of IIL by foreign investors to challenge taxation measures. First, recraft the existing BITs to carve-out taxation measures from the jurisdictional purview of ISDS tribunals. Second, adopt taxation measures that are bona fide, reasonable and proportionate to the public objective they seek to achieve, and not taxation measures that are excessive or disproportionate. Even if foreign investors challenge such bona fide and reasonable taxation measures, it is highly unlikely that the ISDS tribunals would declare such measures illegal. Thus, the States will be able to exercise their sovereign right to regulate without worrying about breaching investment treaty obligations.