Tobacco companies may argue that a host state has failed to provide them with fair and equitable treatment, for example, by claiming that a measure is ‘arbitrary’, violates their ‘legitimate expectations’, or that its adoption will breach a requirement to provide investors with a ‘stable regulatory environment’.

Parties can respond to such claims as follows:

- The WHO FCTC is an evidence-based treaty designed to address a serious public health problem, and states which implement it in good faith and on a non-discriminatory basis are not acting
• The fair and equitable treatment standard is not intended to provide investors with substantive rights of appeal from domestic courts; tribunals recognise that a degree of deference to host state public policy decisions is appropriate.
• Investors cannot have legitimate expectations that a state will not introduce stricter tobacco regulation unless specific commitments or representations to that effect have been made by the host state to that investor.
• Fair and equitable treatment does not require a host state to freeze its regulatory regime in place.

Parties should also avoid making representations to or agreements with the tobacco industry, so as not to create legitimate expectations that they will refrain from adopting stricter tobacco control regulations.

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The tobacco industry has argued that tobacco control measures breach the obligation to provide fair and equitable treatment to foreign investors, found in most investment treaties. Philip Morris, for example, argued this in both its investment dispute against Australia and its dispute against Uruguay. Typically, such arguments take three forms:

• Assertions that a measure is ‘arbitrary’ or ‘unreasonable’
• Assertions that a measure violates ‘legitimate expectations’
• Assertions that a measure breaches a requirement to provide the investor with a stable regulatory environment

These arguments were rejected in Philip Morris v. Uruguay, which reinforces existing case law that non-discriminatory, good faith public health measures do not breach the fair and equitable treatment standard. Responses states can use against claims that tobacco control measures breach the fair and equitable treatment obligation include the following:

• Non-discriminatory measures undertaken to implement the WHO FCTC are not arbitrary: the WHO FCTC is a widely-ratified multilateral treaty containing evidence-based best practices for dealing with a recognised public health problem.
• Investors can only have legitimate expectations if a host state makes specific commitments or representations to them. Legitimate expectations cannot be created from general legal frameworks such as the grant of a trademark, or the host state’s regulatory regime before the measure was implemented. This is particularly so in relation to a heavily regulated product such as tobacco.
• The requirement for a stable regulatory environment does not prevent host states from
introducing new regulation.

Tobacco companies may also make arguments about procedural due process under the fair and equitable treatment standard, for example, by alleging that they were not sufficiently consulted during the policy or legislative development process. This page will focus primarily on fair and equitable treatment as applied to the substance of legislation. However, it should be noted that arguments about procedural due process are commonly made by the tobacco industry in domestic litigation, and that many of the types of responses states can use to defend against domestic challenges will likewise apply to investment law.

Box: What is FET?
[idea]

What is fair and equitable treatment?
Under most investment treaties, states agree to afford ‘fair and equitable treatment’ to foreign investors. Tribunals have held that the obligation to afford fair and equitable treatment entails a range of specific obligations including:

- Procedural due process by administrators and the judiciary, such as by acting impartially and giving investors a right to be heard before certain decisions are taken
- Non-discrimination and acting in good faith
- Freedom from harassment and coercion (whether by the state or third parties)
- Freedom from arbitrary action by the state
- Maintaining a stable and predictable regulatory environment
- Protection of legitimate expectations

There is ongoing debate about the exact scope of the fair and equitable treatment standard in international law, and in practice the kinds of conduct covered depend largely on the facts. However, tribunals generally consider the threshold for breach to be fairly high. In *Saluka v Czech Republic*, for example, it was defined as when a state ‘act[s] in a way that is manifestly inconsistent, non-transparent, unreasonable (i.e. unrelated to some rational policy), or discriminatory (i.e. based on unjustifiable distinctions)’ (para 309). In *Waste Management (No 2) v. Mexico*, it was considered to cover conduct that is ‘arbitrary, grossly unfair, unjust or idiosyncratic, is discriminatory and exposes the claimant to sectional or racial prejudice’ (para 98).

The decided cases generally indicate that non-discriminatory, evidence-based regulatory measures will not violate the fair and equitable treatment obligation, in the absence of a specific commitment or assurance made by the state.[/idea]
A common argument that tobacco companies make under the fair and equitable treatment standard is that tobacco control measures are ‘arbitrary’ or ‘unreasonable’. The tobacco industry typically accompanies these claims with assertions that the measures are not proving effective.’

Responding to these claims generally requires the state to provide information about its decision-making process and the evidence in support of its measure. However, good faith measures implementing the WHO FCTC and its guidelines are well-supported by international evidence and unlikely to breach this standard unless they are implemented in a discriminatory manner.

### Arbitrariness requires more than disagreement about evidence

Tobacco companies that claim that a WHO FCTC measure is arbitrary typically overstate the level of scrutiny that investment tribunals will apply toward a host state’s regulatory measures. Arbitrariness under the fair and equitable treatment standard is not concerned with differing interpretations of the evidence, and (at least in theory) covers only abusive conduct by the host state – for example, one common definition states that arbitrariness is ‘a wilful disregard of due process of law, an act which shocks, or at least surprises, a sense of juridical propriety’ \(\text{[tooltip hint=\text{Elettronica Sicula S.P.A. (ELSI), Judgment, 1989 I.C.J. Reports 15, para 128\text{"}}][*]\text{[/tooltip]}\]. Tribunals have emphasised that fair and equitable treatment standards are not intended to act as avenues of appeal from domestic courts, and that they must pay substantial deference to national authorities in assessing how to address a known public health problem \(\text{[tooltip hint=\text{Philip Morris v Uruguay para 418\"}}][*]\text{[/tooltip]}\).

The Tribunal in *Philip Morris v. Uruguay*, for example, found that as long as a measure was reasonable at the time of adoption, it would not be arbitrary. In particular, it was not necessary for a Tribunal to decide whether or not the measure actually had the effect intended by the state in hindsight, or for a state to ‘prove’ the impact of each individual measure in a suite of complementary measures whose effects might be difficult to disentangle from each other. The Tribunal considered a measure to be reasonable if, at the time it was adopted, it attempted to address a real public health concern, was ‘not disproportionate’ to that concern, and was adopted in good faith.

### Good faith WHO FCTC implementation is not arbitrary

As such, non-discriminatory and good faith regulatory measures to implement the WHO FCTC, a widely-ratified treaty whose obligations and guidelines are recognised as evidence-based best practice to address a serious public health problem, are unlikely to be considered ‘arbitrary’.

For example, in *Philip Morris v. Uruguay*, the fact that Uruguay’s tobacco packaging and labelling requirements implemented the WHO FCTC in good faith and were based on international evidence and practices was sufficient to meet this standard. In particular, the tribunal considered that Uruguay’s graphic health warnings implemented an ‘internationally accepted’ principle (in the WHO FCTC...
guidelines) of having graphic health warnings that were as large as possible. It was not necessary for the tribunal to further scrutinise Uruguay’s decisions or require Uruguay to conduct additional local studies, given the evidence base provided by the WHO FCTC. Countries, particularly those with limited technical and financial resources, were entitled to rely on ‘adhesion to the FCTC and involvement in the process of scientific and technical cooperation and reporting and of exchange of information’. A majority of the Tribunal also ruled that the single presentation requirement had an evidence-based rationale that aimed to address a genuine public health concern in line with the WHO FCTC.

It should be noted that the decentralised nature of investment treaties, the variations in the way that fair and equitable treatment obligations are phrased, and the highly fact-dependent nature of adjudication of the fair and equitable treatment standard means that it may nevertheless be prudent for a state to gather the best available evidence in support of its measure, including local studies and evaluations where available.

The tobacco industry also argues that tobacco control measures violate its legitimate expectations, either with regard to its intellectual property or in relation to the regulatory environment more generally.

**Investors can only have legitimate expectations in relation to regulation if the state has made a specific promise or undertaking**

However, most tribunals have held that for a foreign investor to successfully argue that a state has failed to protect its legitimate expectations, it must demonstrate that the state has given the investor an inducement or specific commitment, or has entered into a contract or other specific legal instrument governing the relationship between the investor and the state that gives rise to such an expectation. In Philip Morris v. Uruguay, neither the grant of a trademark nor the general regulatory environment prior to Uruguay’s new tobacco packaging and labelling measures gave rise to any kind of legitimate expectations that more stringent regulations would not be adopted.
Investors in heavily regulated or increasingly regulated areas, or who make products known to be harmful, cannot legitimately expect to be free from further regulation

Additionally, several tribunals have held that investors cannot have a legitimate expectation that the state will not regulate in a policy area that is subject to regular regulatory changes or is becoming increasingly regulated. For example:

- In *Philip Morris v Uruguay*, the Tribunal noted that ‘[m]anufacturers and distributors of harmful products such as cigarettes can have no expectation that new and more onerous regulations will not be imposed’, and that given ‘widely articulated international concern for the harmful effect of tobacco’, investors could only legitimately expect ‘progressively more stringent regulation’ of tobacco products.
- In *Grand River v United States* the tribunal noted, in relation to the tobacco industry, that ‘[a]n investor entering an area traditionally subject to extensive regulation must do so with awareness of the regulatory situation.’
- In *Methanex v United States*, the tribunal noted long-standing concerns about the health and environmental effects of a gasoline additive, and held that the investor had entered the market aware of governmental monitoring of the health risks of products, as evidenced by the investor's participation in the regulatory process.

**States should avoid making specific commitments to tobacco industry investors**

Overall, it would be difficult for a tobacco industry investor to successfully argue that it held a legitimate expectation that increasingly stringent tobacco control measures would not be enacted, unless a host state has made a specific commitment to that effect. States should therefore ensure that they do not make specific commitments to tobacco industry investors or make representations to them in order to induce foreign investment.
other cases, tribunals have affirmed that the adoption of general legislative measures will not breach any obligation to provide a stable regulatory environment.

Relevant case law line

- Philip Morris v. Uruguay, ICSID Case No. ARB/10/7, Award, 8 July 2016
- Saluka Investments BV v. Czech Republic, Partial Award, 17 March 2006
- Waste Management (No 2) v. Mexico, ICSID Case No. ARB(AF)/00/3, Award, 30 April 2004
- International Thunderbird Gaming Corporation v. Mexico, Arbitral Award, 26 January 2006
- LG&E v Argentina, Case No. ARB/02/1, Decision on Liability, 3 October 2006
- BG Group v Argentina, Final Award, 24 December 2007
- Parkerings-Compagniet AS v. Republic of Lithuania, ICSID Case No. ARB/05/8, Award, 11 September 2007
- PSEG Global v Turkey, ICSID Case No. ARB/02/5, Award, 19 January 2007
- GAMI Investments v Mexico, Final Award, 15 November 2004
- Glamis Gold v United States, Award, 8 June 2009
- Grand River Enterprises Six Nations, Ltd v United States, Award, 12 January 2011
- Methanex v United States, Final Award of the Tribunal on Jurisdiction and Merits, 3 August 2005