Fair and Equitable Treatment: Why it matters and what can be done

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What Is Fair and Equitable Treatment?

Among the standards of protection owed to foreign investments under international investment agreements (IIAs) is the obligation to provide “fair and equitable treatment” (FET). FET is one of the most controversial standards of treatment included in most IIAs. Not only is it included in nearly 95% of investment treaties, but also nearly 83% of all treaty-based investor–state arbitration with data available have involved claims based on this standard of treatment, highlighting its practical relevance.

Despite its widespread inclusion, the precise meaning of the term is uncertain. FET has been considered a vague provision that lacks a definition. As a result, tribunals have tried to formulate a definition while interpreting the provision, increasingly expanding its scope and content over time.

One Standard, Many Formulations

Looking at treaty practice, there are different formulations of the standard:

1) Unqualified FET

The unqualified FET is the approach most often used in investment treaties, especially in the so-called old-generation agreements. The unqualified FET simply states that the host state shall accord fair and equitable treatment.

The inherent lack of clear definition coupled with an unqualified FET formulation gives rise to diverging interpretations. For example, the tribunal in MTD Equity Sdn. Bhd. v. Chile
examined the ordinary meaning of the words “fair” and “equitable” and found that the words stand for “just,” “evenhanded,” “unbiased,” and “legitimate,” while the tribunal in *S.D. Myers, Inc. v. Government of Canada* found that the words stand against “treatment in such an unjust or arbitrary manner that the treatment rises to the level that is unacceptable from the international perspective.”

With the growing awareness of this risk, new approaches have emerged.

### 2) FET Linked to General International Law

Other treaties link the standard to international law and state that FET shall be accorded in accordance with international law. This approach provides some additional guidance, suggesting that the provision should be interpreted by reference to international law, including customary international law (CIL). However, tribunals have sometimes interpreted this type of clause as being as demanding and protective as unqualified formulations.

### 3) FET Limited by the Minimum Standard of Treatment Under Customary International Law

In response to the above, states started to clarify that the standard goes no further than what is required by CIL. However, arbitral tribunals differ as to the content of minimum standard of treatment (MST) under CIL today, which adds further complexity to the debate on interpreting and applying the FET standard. As a result, states can no longer find a safe harbour by merely anchoring the FET standard in the MST.

### 4) FET Specifying the Situations That May Give Rise to a Violation

Another approach has been to spell out the situations that might entail an FET violation. However, the list of such situations often contains other broad and controversial concepts, such as the protection of “investor legitimate expectations” and/or providing means to expand an alleged closed list. Therefore, such lists can still maintain room for broader interpretations.

Despite various attempts by states to further clarify the measures susceptible to being challenged, the decisions rendered by arbitral tribunals still vary widely in terms of their interpretation of the standard of treatment.

### 5) FET Providing Further Guidance on the Application of the Standard

Lastly, states have attempted to ensure predictability by including provisions on how to apply the standard. For example, the European Union and Canada, parties to the Comprehensive Economic Trade Agreement, impose certain qualifiers on the gravity of government acts, such as “fundamental” breach of due process, “manifest” arbitrariness, and discrimination on “manifestly” wrongful grounds. Unfortunately, the loose concept of arbitrariness, even if

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4 While tribunals consistently accepted that CIL is evolutionary in nature, they have differed on the question as to whether the high threshold laid out in the *Neer* case is still needed for a breach.

5 See, for instance, EU–Singapore Investment Protection Agreement (2018), art. 2.4.
qualified with the adjective “manifest,” combined with the clarification that tribunals could consider the legitimate expectations of the investors, continues to leave the FET standard open-ended and unpredictable under the existing language.

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In sum, unfortunately, these state attempts that have been included in new-generation IIAs have not been effective in practice and have failed to completely safeguard states’ regulatory policy space. In fact, when examining recent awards rendered under new-generation agreements, it can be concluded that new treaties produce old outcomes since the interpretation of new agreements does not differ from that of old treaties. This can be exacerbated when the adjustments introduced in the new treaties maintain loopholes that allow tribunals to advance old-style interpretations.

**What Are the Problems Associated With FET?**

**One Standard, Divergent Interpretations**

One of the reasons behind the investor–state dispute settlement (ISDS) backlash is the inconsistent interpretation of similarly worded clauses and even disputes arising under the same treaty. The North American Free Trade Agreement is one example. Over the years, tribunals have given different interpretations of its Article 1105 (Minimum Standard of Treatment), some drastically different from others. Even where states have repeatedly insisted on their own interpretation of the standard and have made their original intent clear to the tribunal, tribunals sometimes still choose to ignore such original intent and decide to apply their own interpretations instead.

Another illustration is found in *TECO v. Guatemala* and *Iberdrola v. Guatemala,* where both claimants challenged the same conduct, namely a denial of justice by state adjudicatory bodies that breached the FET obligation. While the tribunal in *Iberdrola* applied a strict standard and found that there was no violation of the FET obligation, the arbitral tribunal...

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7 See, e.g., the different interpretation of the article rendered by the tribunals of *Waste Management v. Mexico,* ICSID Case No. ARB(AF)/00/3, Award (Apr. 30, 2004), and that of *Apopex Holdings Inc. and Apotex Inc. v. United States of America,* ICSID Case No. ARB(AF)/12/1, Award (Aug. 25, 2014).


in TECO found the state to be in breach of its obligation. Another example of incoherent interpretations is found regarding breaches of legitimate expectations, with some tribunals holding that explicit undertakings and representations are required and other tribunals finding that general representations made by the government to the public at large could also qualify as the basis for an expectation.

The inconsistency in the interpretation of this standard of protection is not unique to FET, although it is more easily observed due to its broad scope. It has been argued that the inconsistency is exacerbated by the ad hoc nature of the ISDS system, where there are no binding precedents and no review of the decisions. To address this, states have been convening in United Nations Commission on International Trade Law Working Group III on Investor–State Dispute Settlement Reform and have been discussing ISDS reform.

Wide Array of Measures That Can Potentially Be Considered a Breach of the Obligation

As noted by the Merrill & Ring Forestry tribunal, “[i]n the end, the name assigned to the standard does not really matter. What matters is … all such acts or behavior” protected against by the standard. Based on arbitral practice, measures or conducts that can be considered as a breach of FET include:

1. Denial of justice
2. Breach of due process
3. Frustration of investors’ reasonable and legitimate expectations
4. Instability in the host state’s legal framework
5. Lack of transparency
6. Arbitrary decision making
7. Bad faith
8. Coercion and harassment

For a detailed overview of both cases, see Johnson, L. & Sachs, L. (2018). Inconsistency’s many forms in investor-state dispute settlement and implications for reform. CCSI Briefing Note.

See, for instance, the renewable energy cases against Spain: Charanne and Construction Investments v. Spain, SCC Case No. V 062/2012, Award, paras. 493, 499 (Jan. 21, 2016); Masdar Solar & Wind Cooperatief U.A. v. Kingdom of Spain, ICSID Case No. ARB/14/1, Award, paras. 520–521 (May 16, 2018); 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, Decision on Responsibility and on the Principles of Quantum, paras. 320–321 (Nov. 30, 2018); 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, para. 397 (Feb. 19, 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, paras. 587–596 (Mar. 12, 2019); 9REN Holding S.à r.l v. Kingdom of Spain, ICSID Case No. ARB/15/15, Award, paras. 292–299 (May 31, 2019); InfraRed Environmental Infrastructure G.P Limited and others v. Kingdom of Spain, ICSID Case No. ARB/14/12, Award, paras. 366–367 (Aug. 2, 2019); Watkins Holdings S.à r.l. and others v. Kingdom of Spain, ICSID Case No. ARB/15/44, Award, para. 533 (Jan. 21, 2020).


Merrill & Ring Forestry L.P. v. Canada, ICSID Case No. UNCT/07/1, Award, para. 210 (Mar. 31, 2010).
Importantly, each of these substantive obligations potentially covers a wide array of measures. For example, a breach of legitimate expectations can arise from legal rights grounded in contractual arrangements between the host state and the investor, formal or informal representations made to the investor or, more generally, from the regulatory framework in force in the host state at the time of the investment.¹⁴

Unpredictability Regarding Its Application Leading to Regulatory Chill

The divergent interpretations coupled with the wide scope of the FET provision result in unpredictability for states and constraints to their right to regulate. As a consequence, it is important for states to be aware of the high risks of the inclusion of an FET clause in the context of treaty negotiations, as well as the implications of the broad FET clauses included in most old-generation agreements. FET has turned into a catch-all provision that makes it difficult for states to exercise their regulatory power without risking an ISDS claim.

What Can Be Done?

Based on the analysis of treaty practice and jurisprudence, one thing is certain: states should pay special attention to the standard of treatment clause and the drafting of a FET obligation when negotiating or renegotiating IIAs.

There are three main policy actions governments may consider, with some of them offering different policy options.

Policy Option 1: No inclusion of FET standard

Given the unpredictable and sometimes conflicting approaches taken by the tribunals, states may consider simply excluding (either implicitly or explicitly) the general standard of treatment clause from their IIAs.

Policy Option 1 in practice:

- Brazil Model (2015)
- Australia–China FTA (2015)
- Pan African Investment Code

The omission can also be made explicitly:

- Intra–MERCOSUR Cooperation and Facilitation Investment Protocol (2017), Art. 4.3: “For greater certainty, the standards of “fair and equitable treatment” … are not covered by this Protocol.”

Policy Option 2: Inclusion of an alternative to the FET standard

If a standard of treatment provision is to be included in an investment treaty, in order to avoid misinterpretation by tribunals, states can consider refraining from referring to the term “fair and equitable” and include terms such as “treatment of investment,” “treatment of investors,” or “fair administrative treatment.”

For greater certainty, the provision can clarify that the standard provided does not equate to FET.

Policy Option 2 in practice:

Ethiopia–Qatar BIT (2017), Article 4

ARTICLE 4: FAIR ADMINISTRATIVE TREATMENT

1. Each Contracting Party shall ensure that their administrative, legislative, and judicial processes do not operate in a manner that is arbitrary or that denies administrative and procedural due process to investors of the other State Party or their investments.

2. Investors or their investments, as required by circumstances, shall be notified in a timely manner of administrative or judicial proceedings directly affecting the Investment(s), unless, due to exceptional circumstances, such notice is contrary to domestic law.

3. The Investor or their investments shall have access to government-held information in timely fashion in accordance with domestic law and subject to the limitation on access to information under the applicable domestic law.

4. Each Contracting Party will progressively strive to improve the transparency, efficiency, independence and accountability of their legislative, regulatory, administrative and judicial processes in accordance with their respective domestic laws and regulations.15

Policy Option 3: Inclusion of a well-defined and limited FET standard

1) Using a closed list of measures that might breach the standard with no reference to investors’ legitimate expectations

If the standard of treatment clause is to be included in a treaty, we recommend limiting its scope by specifying, using a closed list, the types of conduct that would amount to a violation of the treatment.

The list may vary, but in general, it includes the following types of conduct:

1. Denial of justice in criminal, civil, or administrative proceedings
2. Fundamental breach of due process

15 Inspired by SADC Model BIT (2018).
3. Manifestly arbitrary conduct
4. Targeted discrimination on [manifestly] wrongful grounds such as gender, race, or religious belief
5. [Manifestly] abusive treatment, such as coercion, duress, and harassment.¹⁶

Policy Option 3.1 in practice:

Examples clarifying what constitutes a breach of FET

Hungary–United Arab Emirates BIT (2022), Article 2

3. With respect to the investments the following measures or series of measures constitute breach of the obligation of fair and equitable treatment:
   a. Denial of justice in criminal, civil, or administrative proceedings; or
   b. Fundamental breach of due process, including a fundamental breach of transparency and obstacles to effective access to justice, in judicial and administrative proceedings; or
   c. Manifest arbitrariness; or
   d. Targeted discrimination on manifestly wrongful grounds, such as gender, race, or religious belief; or
   e. Harassment, coercion, abuse of power, or similar bad faith conduct.

2) Providing clear guidance for their interpretation and application

To avoid expansive interpretation, it is recommended to clarify in the treaty itself the state parties’ intention on how the treatment shall be applied.

In this regard, governments may wish to consider the inclusion of some clear guidance in terms of standard of review and the burden of proof. For example, states may consider setting a high threshold for claimants to prove an alleged breach of the standard.

Policy action 3.2 in practice:


5.2. For greater certainty, paragraph 5.1 requires the demonstration of an act or actions by the government that are an outrage, in bad faith, a wilful neglect of duty or an insufficiency so far short of international standards that every reasonable and impartial person would readily recognize its insufficiency.

3) Clarifying what does not constitute a breach of FET

For greater certainty, and to prevent (as much as possible) broader interpretations, governments should consider specifying what situations or measures do not constitute a breach of the standard.

These should be presented as clarifications and not exceptions, so as to ensure this is what the contracting states mean in every situation falling under FET and to avoid a restrictive interpretation of said clarification.

For example, governments may consider **clarifying the relationship of the standard with regard to the investor’s legitimate expectations**. States should consider making it clear in the treaty that, when determining whether a treaty obligation has been breached, the tribunals shall not take investors’ expectations into consideration. They should also clarify that inconsistency alone with investor expectations does not breach the FET obligation.

In addition, states should consider the interaction between the standard of treatment clause and other clauses in investment treaties. This will ensure that careful drafting and negotiation of one particular clause are not undermined by the operation of another. In this light, states may **clarify the relationship between FET and the breach of another provision or agreement**, stating that these do not constitute a breach of the FET obligation.

**Policy action 3.3 in practice:**

Australia–United Kingdom FTA (2022), Article 13.7

(4) For greater certainty, the mere fact that a Party takes or fails to take an action that may be inconsistent with an investor’s expectations does not constitute a breach of this Article, even if there is loss or damage to the covered investment as a result.

Regional Comprehensive Economic Partnership (2020), Article 10.5

3. A determination that there has been a breach of another provision of this Agreement, or of a separate international agreement, does not establish that there has been a breach of this Article.

**Conclusion**

States have different options to address the FET issue. It is important to note that the option of keeping FET with limitations requires a great deal of caution and a careful combination of various safeguards. Governments should consider the most practical and efficient options to be implemented in the context of new negotiations or renegotiations. In case of any doubt, states should aim to prioritize options that avoid any reference to FET.

An analysis of treaty and arbitral practice highlights the risks of including FET provisions in new-generation agreements. To preserve the right to regulate, states should not only pay special attention when negotiating new-generation agreements but also take policy steps with respect to existing IIAs in place, which often include unqualified FET clauses.