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Investment Tribunals, the Duty of Compensation in Cases of Necessity

A Customary Law Void?

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1 Introduction

According to Article 27(b) of the Articles on the Responsibility of States for Internationally Wrongful Acts (ARSIWA), the successful invocation of a defence is 'without prejudice … to the question of compensation for any material loss caused by the act in question'.[1] The Commentary to this provision clarifies that this compensation is not part of the framework of reparation: it is not, in short, one of the obligations arising out of the wrongful act.[2] It concerns, instead, the question whether a State invoking a defence 'should nonetheless be expected to make good any material loss suffered by the State directly affected'.[3] Material loss, the Commentary continues, is a narrower concept than damage as it concerns only the adjustment of losses that may occur when a party relies on a defence.

Beyond this, the Commentary gives little guidance as to when such a duty could be owed. It states that in certain situations a duty of compensation 'is a proper condition' for allowing reliance on a defence, as otherwise a State might shift the burden of protecting its own interests onto other 'innocent' third parties.[4] By way of example, it notes that Hungary accepted this principle when relying on the plea of necessity in *Gabčíkovo-Nagymaros*.[5] But the Commentary does not say in respect of which defences, and in what circumstances, compensation will be due.

[1] ILC, 'Draft Articles on Responsibility of States for Internationally Wrongful Acts with Commentaries' (23 April–1 June and 2 July–10 August 2001) UN Doc A/56/10, reproduced in [2001/II – Part Two] YBILC 31 (ARSIWA).
[2] ibid, Commentary to Art 27(b) [4].
[3] ibid.
[4] ibid [5].
[5] ibid.

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Indeed, it does not say that compensation is due in cases of necessity; it only notes that Hungary offered compensation when invoking necessity. Indeed, the Commentary clarifies that it 'does not attempt to specify in what circumstances compensation should be payable'.[6] The most that it offers, by way of guidance, is that it will be for the parties involved to agree on any possible compensation.[7]

It is not unusual for parties who benefit from the plea of necessity to offer compensation to affected parties. Hungary, as noted by the ILC, did it in *Gabčíkovo-Nagymaros* and, more recently, Bolivia may be seen as having made a similar offer in an investment arbitration.[8] But such instances are certainly not the norm. In most instances, no offer of compensation will be forthcoming and, consequently, there will be no agreement between the parties. What happens, then, when the parties do not agree on any possible compensation for material loss? What happens when, as has most often been the case in practice, the State invoking a defence rejects that it owes compensation to the affected party? It is precisely here that the question whether compensation is owed, as a matter of obligation, arises.

For the most part, investment tribunals have had to address situations in which offers of, or agreements on, compensation for material loss caused by acts adopted in a state of necessity have not been forthcoming. At least four different States have relied on the defence of necessity to *justify*,[9] and thus, render lawful conduct incompatible with their obligations under bilateral investment treaties.[10] In all cases the claimants have appealed to ARSIWA Article 27(b) and argued that, notwithstanding the necessity defence, respondents were required to compensate them for the

[6] ibid [6].

[7] ibid.

[8] *South American Silver v Bolivia* (Award of 22 November 2018) PCA Case No 2013–15 [535].

[9] These are Argentina, in the various disputes brought against it by investors in the wake of the financial crisis of the early 2000s, many of which will be considered in this article; Bolivia in *SAS v Bolivia* (Award of 22 November 2018) PCA Case No 2013–15; Egypt in *Unión Fenosa v Egypt* (Award of 31 August 2018) ICSID Case No ARB/14/4; and Zimbabwe in *Pezold v Zimbabwe* (Award of 28 July 2015) ICSID Case No ARB/10/15; *Bernardus Henricus Funnekotter v Zimbabwe* (Award of 22 April 2009) ICSID Case No ARB/05/6.

[10] These are, at least, the awards available publicly. There is information that an additional State, Ukraine, invoked the necessity plea in an investment arbitration, but the award has not been published. For an overview, see, D Charlotin, 'Revealed: Tribunal in *JKX v Ukraine* Awarded Nearly 12 Million USD for Arbitrary Measures and Breach of Free Transfer Clause; Ukraine's Necessity Defence was Rejected' (*International Arbitration Reporter*, 29 June 2020) <www.iareporter.com/articles/revealed-tribunal-in-jkx-v-ukraine-awarded-nearly-12-million-usd-for-arbitrary-measures-and-breach-of-free-transfer-clause-ukraines-necessity-defence-was-rejected/> accessed 10 May 2021.

material loss suffered as a result of the allegedly justified measures. All States denied owing such compensation.

Are these States *required* to compensate claimants for the loss caused by their justified, and therefore lawful, conduct? Absent the parties' agreement, an obligation to make compensation in these circumstances requires a basis in positive law. This compensation, as the ILC Commentary to Article 27 clarifies,[11] is not a form of reparation; after all, there has been no wrongful act. So, it cannot be based on the obligation to make reparation that arises for States as a consequence of a wrongful act. It must have a discrete legal source. Investment tribunals, deciding in accordance with international law needed, therefore, to identify a positive law basis for the respondent's duty to compensate material loss resulting from acts justified by necessity.

A duty of compensation could be found in the relevant applicable treaty: the treaty may specifically provide for this.[12] Investment tribunals have also interpreted such a duty from the purpose of the Bilateral Investment Treaties (BITs) themselves. Thus, the Tribunal in *BG Group* found that a duty of compensation in these circumstances could be required by the UK–Argentina BIT.[13] But this is relatively rare. Most treaties do not make provision for compensation in relation to emergency measures and, when they do, they often provide for compensation in only a limited range of cases. In all other cases, therefore, a tribunal will need to look to other sources of international law: customary law or general principles of law. The focus of this chapter is the tribunals' engagement with customary international law in their assessment of the existence of an obligation to

[11] ARSIWA (n 1) Commentary to Art 27(b) [4].

[12] See, eg, Art 5, Agreement between the Federal Republic of Germany and Brunei Darussalam concerning the Encouragement and Reciprocal Protection of Foreign Investments (Brunei & Germany) (adopted 30 March 1998, entered into force 15 June 2004) Art 5, which states:

> Without prejudice to Paragraph 1 of this Article ["national crisis clause"], nationals and companies of one Contracting Party who in any of the situations referred to in that Paragraph suffer damages or losses in the territory of the other contracting Party resulting from:
>
> (a) requisitioning of their property by its forces or authorities, or
> (b) destruction of their property by its forces or authorities which was not caused in combat action or was not required by the necessity of the situation, shall be accorded restitution or fair and adequate compensation.

This provision is quoted in F Franke, 'The Custom of Necessity in Investor-State Arbitrations' in R Hofmann & CJ Tams (eds), *International Investment Law and General International Law* (Nomos 2011) 156 fn 203.

[13] *BG Group v Argentina* (Final Award of 24 December 2007) UNCITRAL [409].

make compensation for material loss caused by acts justified under the plea of necessity. As will be seen, tribunals have reached opposite conclusions on the existence of a duty of compensation. However, they all share in common one feature: an omission to engage with the method of customary law identification. Some tribunals assert the existence of the duty, others derive it from the elements of the customary defence of necessity, yet others still simply name-check precedents and general principles of law. But none of these awards provided *any* evidence of practice and *opinio juris* in relation to this duty.

In addition to this introduction, the chapter proceeds in three steps. Section 2 provides an overview of the investment case law. It will review the range of conclusions reached by different investment tribunals and, in so doing, focus on the reasoning deployed to reach those conclusions. It will show that, whether they accept or reject the existence of a duty of compensation, their reasoning does not involve any engagement with the elements of customary law. At most, tribunals offer vague references to previous precedents and case law, and never once to State practice and *opinio juris*. Section 3 will then focus on analysis: it reviews the available practice and *opinio juris*, limited as it is, and assesses the precedents invoked in support of the duty of compensation by these tribunals. As will be seen, the practice is scant and inconsistent and the precedents invoked are at best equivocal as to the existence of a duty of compensation. If States have expressed any *opinio* in this regard this is an *opinio non juris*: there is *no* customary obligation to make compensation in cases of necessity. Section 4 concludes.

Two clarifications are necessary before proceeding. First, this chapter takes an orthodox approach to the identification of customary law, in line with the so-called 'two element theory' followed by the ILC in its recent work on customary law and supported by States in connection with that work.[14] In light of this, it will focus first and foremost on identifying existing practice and *opinio juris* of States in respect of the duty of compensation. The article will also take into account the case law of international tribunals. This is because while international courts and tribunals do not have a formal role in the development of international law, in practice, decisions of international tribunals can influence the development of

[14] UNGA, 'Identification of Customary International Law' (11 January 2019) UN Doc A/RES/73/203; see also ILC, 'Draft Conclusions on Identification of Customary International Law, with Commentaries' (30 April–1 June and 2 July–10 August 2018) UN Doc A/73/10, reproduced in [2018/II – Part Two] YBILC 122, 122–56.

international law, including the law of State responsibility and the law of investment protection.[15] Second, this chapter will take necessity *as a justification*, namely, as a defence which renders conduct lawful, and not as an excuse, namely, as a defence which excludes the consequences of a wrongful act.[16] The reasons for this choice are that the majority of States who support this defence at international law classify it as a justification, and that States have invoked it in international courts and tribunals as such.[17]

2 Investment Tribunals and the Duty of Compensation

Several States have invoked the plea of necessity in investment treaty arbitration. In most (if not all) of these instances, the parties have addressed the question of compensation in the event that the State's plea of necessity was successful. Likewise, in most instances, tribunals have addressed the duty of compensation in *obiter* only: respondents' plea of necessity having been unsuccessful on other, often multiple, grounds. Many tribunals have not addressed the question of compensation at all: having rejected the plea of necessity on other grounds, there was no need to consider this issue.[18]

[15] On this see, generally, H Lauterpacht, The Development of International Law by the International Court (Stevens & Sons 1958); P Daillier, 'The Development of the Law of Responsibility through the Case Law' in J Crawford, A Pellet & S Olleson (eds), The Law of International Responsibility (OUP 2010); CJ Tams & J Sloan (eds), The Development of International Law by the International Court of Justice (OUP 2012); C Schreuer, 'The Development of International Law by ICSID Tribunals' (2016) 31(3) ICSID Rev 728; CJ Tams, 'The Development of International Law by the International Court of Justice' in E Cannizzaro & ors (eds), *Decisions of the ICJ as Sources of International Law?* (International and European Papers Publishing 2018).

[16] If necessity were an excuse, the duty of compensation would be encompassed by the obligation to make reparation. After all, in this case, the State invoking the defence would have committed an internationally wrongful act. However, it would be a limited form of reparation: only for material loss. Necessity would then operate as a partial excuse: it would exclude some, but not all, consequences of the wrongful act for the invoking State. Note that this solution is not as simple as it might at first appear. As a matter of practice, it faces the difficulty that States do not support or invoke necessity as an excuse. As a matter of theory, it faces the difficulty of providing a principled basis for the distinction between total excuses and partial excuses. For a discussion of this issue, see: F Paddeu, *Justification and Excuse in International Law: Concept and Theory of General Defences* (CUP 2018) 81–6.

[17] F Paddeu, 'The Impact of Investment Arbitration in the Development of State Responsibility Defences' in R Hofmann, S Schill & CJ Tams (eds), *ICSID at 50: Investment Arbitration as a Motor of General International Law* (Edward Elgar, forthcoming) <https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2865718> accessed 10 May 2022.

[18] Eg *von Pezold* [624–68].

Tribunals' approaches to the duty of compensation have varied significantly, covering the full range of possibilities: some have accepted the existence of this duty, others have denied it, and others still have not taken a position. They have all had in common, however, minimal or no engagement with the evidence of the (potential) positive law source of this duty. In particular, none of these tribunals have applied the orthodox method (or any other method, for that matter) for the identification of customary law: tribunals have instead resorted to simple assertions, deductions, and denials. The next four sections review the different approaches taken by investment tribunals.

2.1 Assertions

Some tribunals have asserted the existence of a duty of compensation. When a tribunal asserts a rule, it provides no reasoning (inductive or deductive as it may be) in support of the stated rule.[19] To use Stefan Talmon's words, asserting customary rules is like pulling rabbits out of a hat.[20] To be sure, assertion is not a method for the identification of customary rules: it 'is a way of stating a conclusion.'[21] For the most part, investment tribunals have not simply 'pulled' the duty of compensation from out of a hat. But their reasoning in support of this duty is often unsuitable, and where available it is so thin as to provide no support at all.

The Tribunal in *CMS v Argentina* held that Article 27(b) 'establishe[d] the appropriate rule of international law on this issue' and that it was 'the meaning of international law or the principles governing most domestic legal systems' that a party invoking necessity owed compensation.[22] These seem to be references to customary law and general principles of law as the potential source of the duty of compensation. Reliance on each of these two sources is, however, insufficient. As to general principles, these are referred to in two paragraphs,[23] and in neither case are references provided. As to customary law, the tribunal provided no evidence

[19] S Talmon, 'Determining Customary International Law: The ICJ's Methodology between Induction, Deduction and Assertion' (2015) 26 *EJIL* 417, 434.

[20] ibid.

[21] O Sender & M Wood, 'The International Court of Justice and Customary International Law: A Reply to Stefan Talmon' (*EJIL:Talk!*, 30 November 2015) <www.ejiltalk.org/the-international-court-of-justice-and-customary-international-law-a-reply-to-stefan-talmon/> accessed 10 May 2022; See also Merkouris, 'Interpreting the Customary Rules on Interpretation' (2017) 19 ICLR 126, 137.

[22] *CMS v Argentina* (Award of 12 May 2005) ICSID Case ARB/01/8 [390].

[23] ibid [388, 390].

of practice or *opinio juris*, and simply mentioned the cases of *Orr and Laubenheimer,*[24] *General Company of the Orinoco River,*[25] *Bulgarian Property,*[26] and *Gabčíkovo-Nagymaros*[27] as precedents. To be sure, tribunals can (and do) contribute to the development of the law: but once these cases are considered in detail, it will become apparent that these decisions do not unequivocally support a duty of compensation. The award was indeed subsequently annulled, among others, due to a manifest error of law in relation to Article 27(b): as the Annulment Committee explained, this provision did not impose a duty of compensation; it was simply a without prejudice clause.[28]

The Tribunals in *Enron* and *Sempra* both noted that Article 27(b) was vague and, in line with the Commentary to this provision, that whether compensation was due in these circumstances was a matter that must be decided by the parties. Both Tribunals added that absent agreement between the parties 'this determination is to be made by the Tribunal to which the dispute has been submitted.'[29] The reasoning is not entirely clear, but it is plausible to read these awards as endorsing a duty of compensation in cases of necessity: compensation is either agreed between the parties or decided by the tribunal. The tribunals do not clarify, however, what is the source of their power to determine (and impose the payment of) compensation. Neither tribunal ultimately went on to make the determination since both rejected the Argentine defence.

The Tribunal in *South American Silver v Bolivia* was even briefer on this point. In a dispute concerning the payment of compensation for an expropriation, the Tribunal stated:

> It is clear that Bolivia's state-of-necessity [sic] defense was not designed to excuse the non-payment of compensation for the expropriation, nor could it, since the invocation of this defense does not preclude the payment of compensation by the State for the damage effectively resulting from acts attributable to it.[30]

[24] *Orr and Laubenheimer and the Post-Glover Electric Company* (1900) 15 RIAA 33.
[25] *Company General of the Orinoco* (1905) 10 RIAA 184.
[26] League of Nations, 'Report of the Commission of Enquiry on the Incidents on the Frontier between Bulgaria and Greece, Doc No C.727.M.270.1925.VII (Annex 815)' (1926) 7 LNOJ 196.
[27] *Case Concerning the Gabčíkovo-Nagymaros Project (Hungary/Slovakia)* (Judgment) [1997] ICJ Rep 7.
[28] *CMS v Argentina* (Annulment of 25 September 2007) ICSID Case No ARB/01/8 [146–7].
[29] *Enron v Argentina* (Award of 22 May 2007) ICSID Case No ARB/01/3 [345]; *Sempra Energy v Argentina* (Award of 28 September 2007) ICSID Case No ARB/02/16 [394].
[30] *South American Silver* [535, 620].

There is some ambiguity in this statement. The passage uses the language of Article 27(b) (compensation is not precluded), seemingly going no further than this provision: the successful invocation of a defence is without prejudice to the question of compensation. But the passage can also be interpreted as going beyond Article 27(b); supporting a duty of compensation in (at least some) cases of necessity. The Tribunal first states that the plea of necessity cannot apply to deny compensation for expropriation: this is not what the plea was 'designed' to do. The plea of necessity cannot be invoked when the relevant primary rule excludes its invocation, implicitly or explicitly.[31] Arguably, the situation of necessity is already catered to by the primary rule on expropriation, as it is necessity that justifies the taking of the property. Necessity cannot do double work, as it were, it cannot justify the taking *and* justify the denial of compensation. The plea cannot thus be invoked as Bolivia has done. So far, so plausible. The tribunal then appears to go further. Even if necessity were applicable to this situation, it says, the plea could not deny compensation for expropriation. In short, a successful invocation of the plea would still involve an obligation to pay compensation for the expropriation. If this were the correct interpretation of the Tribunal's statement, it would be no more than an assertion that compensation was due even in cases of successful invocation of the plea – at least, in some of these cases (expropriation). The Tribunal provides no evidence of a positive law source, let alone of customary law, for this duty in the award.

2.2 Deductions

Other tribunals have obviated the need to provide a positive law basis to the duty of compensation, by grafting this obligation to the customary rule of necessity itself. They have done this by interpreting the rule on compensation as *including* a duty of compensation as one of its requirements. If the plea of necessity is recognised in customary law, and the duty of compensation is inherent in the plea, then it follows that the duty of compensation is also part of customary law. This is the case of the awards of the Tribunal and annulment committee in *EDF v Argentina*.

The *EDF* Tribunal stated that to succeed in its invocation, Argentina had to demonstrate:

> three key elements of ILC Articles 25 and 27: (i) that the wrongful act was the only way to safeguard Argentina's essential interest under Article 25 (1)(a);

[31] ARSIWA (n 1) Art 25(2)(a) & Commentary to Art 25 [19].

> (ii) that Respondent did not contribute to the situation of necessity; and (iii) that Respondent did not return to the pre-necessity *status quo* when possible, or compensate Claimants for damage suffered as a result of the relevant measures.[32]

It further explained that even if Argentina were successful in invoking the plea, this did not '*per se* preclude payment of compensation to the injured investor for any damage suffered as a result of the necessity measures enacted by the State.'[33] Having contributed to the situation of necessity, and having failed to re-establish the *status quo*, Argentina's defence failed.[34]

In annulment proceedings, Argentina claimed that the Tribunal had 'invented' this additional element.[35] The Annulment Committee, however, endorsed the Tribunal's finding. According to the Committee, this requirement had not been invented by the Tribunal, but was rather reflective of 'what is inherent in the very concept of necessity'.[36] By this, the Committee meant its temporary character: 'If a departure from a legal obligation can be justified by a state of necessity, it can be justified for only so long as that state of necessity exists'[37] – an argument also adduced by the Tribunal in *CMS*. In short, since the plea of necessity is only temporary, *therefore,* compensation is due.

Panos Merkouris has argued that deductive methods may be applied to the interpretation of customary rules the existence of which has already been established.[38] The Committee's approach could be viewed in this light, as proceeding either teleologically or by necessary implication to deduce the existence of a duty of compensation from the (established) rule of necessity. Leaving aside the doctrinal question whether interpretation of customary rules differs from their identification, it seems a step too far to accept that additional obligations may be inferred, by deduction, from established customary rules: especially where the practice supporting that rule does not provide evidence in respect of that specific obligation (as will be seen below). At any rate, even if this method were found to be in line with the generally accepted method for customary law identification, the

[32] *EDF v Argentina* (Award of 11 June 2012) ICSID Case No ARB/03/23 [1171].
[33] ibid [1177].
[34] ibid [1181].
[35] *EDF v Argentina* (Decision on Annulment of 5 February 2016) ICSID Case No ARB/03/23 [291, 325].
[36] ibid [330].
[37] ibid.
[38] Merkouris (n 21) 137.

conclusion the Committee reaches is a *non sequitur*. The temporariness of the plea (which is only a contingent feature)[39] concerns compliance with the obligation. In principle, defences do not strike down the rule at issue, which remains in force throughout the period that the defence subsists.[40] But the State's obligation to comply with the rule is set aside throughout the period in which the facts giving rise to the defence continue to exist. Once these facts come to an end, the obligation is 'restored', as it were, and the State must resume compliance with it.[41] If it does not, then the State will be *pro tanto* responsible for the violation of the obligation from the moment when the defence ceased.[42] Take the following example. Due to a situation of necessity which arose on 10 February 2020, State A was unable to comply with its treaty obligation to deliver 10 tonnes of rice on the first day of every month to State B. Say, then, that the situation of necessity ended on 15 July 2020. State A would be required on 1 August to deliver 10 tonnes of rice to State B. If it failed to deliver those on 1 August, then State A would be responsible *as from 1 August* for the failure to comply with its obligation to State B. The defence is temporary in that it can only justify State A's failure to comply with its obligation for the five months of March, April, May, June, and July. Indeed, throughout this time, State A's obligation to deliver is in abeyance due to the situation of necessity. But the plea's temporary character, which concerns the return to compliance *after* the defence has ended, has nothing to do with the question of compensation for material loss, which concerns the allocation of the losses generated *during* the situation of necessity (ie, during the period when the State was justified in not complying with the obligation). In the example above, a duty of compensation would relate to the loss caused to State B as a result of A's failure to deliver the required amount of rice for the five months between the start (on 10 February) and the end (15 July) of the situation of necessity.

[39] The temporary character of a defence is not 'inherent' in any defence (not even in the plea of necessity), and it is rather contingent on (i) the underlying obligation and (ii) on the characteristics of the specific situation. Indeed, as ARSIWA (n 1) Commentary to Art 27 [1] explains, 'it may be that the effect of the facts which disclose a circumstance precluding wrongfulness may also give rise to the termination of the obligation'.

[40] ARSIWA (n 1) Commentary to Art 27.

[41] See ibid, Art 27(a).

[42] Note that the Commentary to Art 27 allows for a partial resumption of compliance as the situation triggering the defence recedes. This might suggest that the State could be partially exonerated when this occurs. Leaving aside the difficult theoretical questions that partial justifications can raise, the Commentary to Article 12 ARSIWA states that 'partial compliance' is nevertheless a breach of international law.

The reasoning of the Tribunal – that compensation is due because of the inherent character of the plea – confuses, or fuses, resumption of compliance with compensation. In short, it confuses, or fuses, the provisions in ARSIWA Article 27(a) and Article 27(b). Resumption of compliance with the underlying obligation at the end of the situation of necessity and compensation for material loss during the period of necessity relate to two different obligations. The former, resumption of compliance, is just a consequence of the underlying obligation no longer being in abeyance. The latter is a different – new – obligation of the State invoking necessity. This is an obligation that arises *as a result* of the loss caused by the act of necessity: in our example above, the loss caused by the failure to deliver the rice. To say that the invoking State must resume compliance with the underlying obligation – which is the consequence of the defence's temporary character – has no bearing on whether the invoking State is now burdened by a new obligation to pay compensation for losses caused during the defence.

This conclusion does not change by saying that payment of compensation can only occur after the necessity has ended. We still need to find a basis in positive law for this obligation to pay compensation. The former is a question of the performance of the duty (when it falls due), the latter one of its existence. The underlying obligation cannot – itself – sustain this duty. In the example above, the obligation is to deliver rice: it is not 'to deliver rice *or pay compensation*'. It is also not a duty derived from responsibility – namely, one of forms of reparation – because there has been no wrongful act: the failure to deliver rice, in our example, was justified by necessity. What is, then, the positive law source of this obligation to pay compensation? After all, loss occasioned by a permitted or lawful act is not typically one that requires compensation. In other words, liability for the injurious consequences of lawful acts is *not the norm*. Such liability is exceptional, and needs to be grounded on a positive law rule.[43]

No positive law source – customary or otherwise – was identified by either the Tribunal or the Annulment Committee to ground the duty of compensation. The Tribunal noted and set aside the question of the customary character of the defence of necessity, arguing that the parties

[43] The obligation to pay compensation in these circumstances is substantive, in that it guides State conduct, but when attached to justified conduct, determining whether it is owed will require the use of the law of State responsibility. To argue over the primary or secondary character of such an obligation distracts from the main point: in either case, such an obligation requires a basis in positive law.

agreed on the application of ARSIWA Article 25.[44] Notably, the Tribunal does not mention whether the parties agreed on the application of Article 27(b) and, more importantly, whether they agreed on the question of compensation. The Committee, in turn, only referred to the correspondence in the *Caroline* incident which, indeed, supports the proposition that necessity is only temporary but, as will be seen, does not support a duty to pay compensation for material loss caused by an act adopted in circumstances of necessity.

2.3 Denials

Other tribunals have denied the existence of a duty of compensation in cases of necessity. This is clearly the case of the *LG&E* Tribunal. In its Liability decision, the Tribunal noted that Article 27(b) was a without prejudice clause, and that it did not 'not specifically refer to the compensation for one or all the losses incurred by an investor as a result of the measures adopted by a State during a state of necessity.'[45] Whether compensation was due, said the Tribunal, depended on the interpretation of the defence in question. The Tribunal focused on Article XI of the BIT and found that no compensation was due since this provision 'establishes the state of necessity as a ground for exclusion from wrongfulness of an act of the State, and therefore, the State is exempted from liability.'[46] The Tribunal's decision is grounded on Article XI of the BIT, but to the extent that the Tribunal equated Article XI to the customary plea of necessity its conclusion can be extended to the latter as well. In line with this reasoning, the *LG&E* Tribunal – the only one to have accepted Argentina's plea – eventually excluded compensation for the period covered by the necessity defence.[47] The reasoning is circular: the circumstance precluding wrongfulness of necessity does not attract a duty of compensation *because* it is a circumstance precluding wrongfulness. But the whole point is whether compensation should be due *even if* something is a circumstance precluding wrongfulness. In short, the Tribunal chose where to allocate the loss (the investor) but failed to provide a reasoned argument or any evidence of a source in positive law for this conclusion.

[44] *EDF* (Award) [1167–8].
[45] *LG&E Energy Corp, LG&E Capital Corp, LG&E International Inc v Argentine Republic* (Decision on Liability of 3 October 2006) ICSID Case ARB/02/1 [260].
[46] ibid [261].
[47] *LG&E v Argentina* (Award of 25 July 2007) ICSID Case No ARB/02/1 [106–8].

The award in *Urbaser* could be read as a denial of the duty of compensation, but it is a more equivocal precedent. The Tribunal found that Argentina's necessity plea was satisfied,[48] but it denied the payment of damages to the claimants. However, the *ratio* of this decision seems to have rested on the fact that the failure of the investment was primarily attributable to claimants themselves,[49] and not on the non-existence of a duty of compensation in cases of necessity. Indeed, the Tribunal made no comments on the existence of this, despite the fact that the parties presented arguments in this regard.[50]

2.4 Agnosticism

Finally, other tribunals have taken a more agnostic stance. The Annulment Committee in *CMS* simply noted that Article 27(b) is a without prejudice clause and not a stipulation, and that it did not attempt to 'specify in which circumstances compensation could be due, notwithstanding the state of necessity.'[51] The Annulment Committee in *Sempra*, in addressing the difference between state of necessity and the BIT's non-precluded-measures clause, noted that no compensation was due in the latter case but that the question of compensation 'was not precluded' in the former. The Tribunal thus acknowledges the possibility that compensation could be due, without taking sides in the debate.[52]

3 Doing the Homework: What Evidence for a Customary Duty of Compensation?

Tribunals' divided opinions on this point are not unique. Far from it. Scholars are equally divided on the existence of a duty of compensation in cases of necessity. Thus, some scholars have argued that international law recognises an obligation to provide compensation in these cases,[53]

[48] *Urbaser v Argentina* (Award of 8 December 2016) ICSID Case No ARB/07/26 [709 ff].
[49] ibid [847]
[50] ibid [697] (claimants), [708] (respondent).
[51] *CMS* (Annulment) [146–7].
[52] *Sempra Energy v Argentina* (Annulment of 29 June 2010) ICSID Case No ARB/02/16 [118].
[53] Eg, A Reinisch & C Binder, 'Debts and State of Necessity' in JP Bohoslavsky & JL Černič (eds), *Making Sovereign Financing and Human Rights Work* (Hart 2014) 125–6; G Bücheler, *Proportionality in Investor-State Arbitration* (OUP 2015) 243, 290–6; C Binder & P Janig, 'Investment Agreements and Financial Crises' in M Krajewski & RT Hoffmann (eds), *Research Handbook on Foreign Direct Investment* (Edward Elgar 2019) 677–8.

whereas others have expressed doubts as to the existence of this duty.[54] Many of these scholars, however, regardless of their views on the existence, in positive law, of this duty, agree that compensation would be fair in such circumstances.[55]

In the case law and the literature on this topic, arguments as to the existence of a customary duty of compensation usually rely, as evidence, on the ILC's drafting of, and Commentary to, Article 27(b), and the case law.[56] As will be seen in the next two sections, however, the evidence in support of this duty is far from clear. Regardless of how one interprets the ILC's work on, and the Commentary to, Article 27(b), only a handful of States commenting on the draft expressly supported a duty of compensation generally, or in cases of necessity specifically. Indeed, the evidence of practice and *opinio juris* in favour of this duty is scant and vague (Section 3.1), and the precedents relied upon by tribunals and scholars alike to evidence the existence of the duty of compensation are equivocal at best (Section 3.2).

3.1 Missing Practice

According to Article 38(1)(b) of the ICJ Statute, customary international law is evidenced by the existence of a 'general practice accepted as law'.[57] The practice must be general in the sense that it is 'sufficiently widespread and representative, as well as consistent.'[58] It is not necessary for all States in the international community to engage in the practice, nor is it needed for the practice to be absolutely uniform. The threshold required for the identification of any given rule of customary law may vary by reference to the context.[59] Thus, it is arguable that in the case of very exceptional circumstances, like those that trigger the plea of necessity, the threshold is lower as there

[54] See Franke (n 12) 156–7; A Kent & A Harrington, 'The Plea of Necessity Under Customary International Law: A Critical Review in Light of the Argentine Cases' in C Brown & K Miles (eds), *Evolution in Investment Treaty Arbitration* (CUP 2011) 261–3; M Paparinskis, 'Investment Treaty Arbitration and the (New) Law of State Responsibility' (2013) 24 EJIL 617, 633; R Díaz Inverso, 'El estado de necesidad como circunstancia que excluye la ilicitud en la responsabilidad internacional de los Estados' (2015) 47 Revista de Derecho Público 49, 54.

[55] S Ripinsky, 'State of Necessity: Effect on Compensation' (2007) 4(6) TDM 1; JE Viñuales, *Foreign Investment and the Environment in International Law* (CUP 2012) 390.

[56] Reinisch & Binder (n 53) 125–6; Bücheler (n 53) 243, 290–6; Binder & Janig (n 53) 677–8.

[57] Statute of the International Court of Justice (adopted 26 June 1945, entered into force 24 October 1945) 33 UNTS 993; see also *North Sea Continental Shelf Cases (Federal Republic of Germany/Netherlands; Federal Republic of Germany/Denmark)* (Judgment) [1969] ICJ Rep 3 [44].

[58] ILC (n 14) Conclusion 8(1), and references cited in the Commentary.

[59] ibid, Commentary to Conclusion 8 [2].

will be fewer opportunities for States to engage in the relevant practice. This practice must be accompanied by *opinio juris*, namely, evidence that States engage in the relevant practice out of a sense of legal obligation (or legal entitlement).[60] As will be seen, there is almost no support in the practice and *opinio juris* of States for the duty of compensation in cases of necessity.

It seems fair to read the ILC's work on Article 27(b) as generally supportive of a duty of compensation in cases of necessity.[61] Special Rapporteurs Ago and Crawford supported it, as well as several members of the Commission. None of them wished to take too exacting a position on this matter, however, because of the scarcity of practice and of the variety of cases in which this duty might arise.[62] In this regard, the ILC's work mirrors that of scholars – a strong sense that it would be fair for compensation to be due.

Nevertheless, States' views on this duty have been much more mixed and, often, negative. Only three of the States commenting on the ILC's drafts, Germany,[63] Russia[64] and the UK,[65] explicitly accepted the possibility of the duty arising in situations of necessity. Other States like Denmark (speaking on behalf of the Nordic countries),[66] the Netherlands[67] and

[60] ibid, Conclusion 9(1), and references cited in the Commentary.

[61] See, in particular, supportive remarks during the debates on this provision: ILC, 'Summary Record of the 1614th Meeting' (18 June 1980) UN Doc A/CN.4/SR.1614, Comments of Riphagen [6] & Comments of Schwebel [18 & 20]; ILC, 'Summary Record of the 1616th Meeting' (20 June 1980) UN Doc A/CN.4/SR.1616, Comments of Schwebel [11] & Comments of Calle y Calle [17]; ILC, 'Summary Record of the 1617th Meeting' (23 June 1980) UN Doc A/CN.4/SR.1617, Comments of Tsuruoka [36]. There were no specific endorsements of a duty of compensation in cases of necessity on second reading; on this occasion, the debate centred on the expansion of the duty of compensation to all cases in which defences were invoked, so no specific comments were made of the individual defences or circumstances in which the duty was owed.

[62] See, in particular, Crawford's comments in ILC, 'Second Report on State Responsibility, by Mr James Crawford, Special Rapporteur' (17 March, 1 and 30 April, 19 July 1999) UN Doc A/CN.4/498 and Add.1–4, 84 [348].

[63] ILC, 'State Responsibility: Comments and Observations Received by Governments' (25 March, 30 April, 4 May, 20 July 1998) UN Doc A/CN.4/488 and Add.1–3, 136.

[64] UNGA, 'Report of the International Law Commission on the Work of its 52nd Session (Continued)' (4 December 2000) UN Doc A/C.6/55/SR.18, 10 [53] (indicating that this assumed the plea of necessity operated to 'exempt responsibility' and not to 'preclude wrongfulness').

[65] ILC, 'State Responsibility: Comments and Observations Received From Governments' (25 March 1998) UN Doc A/CN.4/488, 136.

[66] ILC, 'Report of the International Law Commission on the Work of its 51st Session (Continued)' (20 December 1999) UN Doc A/C.6/54/SR.22, 2 [3].

[67] ILC, 'Report of the International Law Commission on the Work of its 51st Session (Continued)' (13 January 2000) UN Doc A/C.6/54/SR.21, 7–8 [52]; ILC, 'Comments and Observations Received From Governments' (19 March, 3 April, 1 May and 28 June 2001) UN Doc A/CN.4/515 and Add.1–3, 57 (adding that it should be limited to *force majeure*, state of necessity and distress).

Poland[68] generally endorsed Article 27 (or its predecessor). Their statements, however, fall short of endorsing the actual existence of a duty of compensation following invocations of necessity.[69] Austria did not outrightly reject the possibility that a duty of compensation may arise in situations of necessity, but it warned that the provision required a more specific formulation since 'it would otherwise lead to the danger of possibly undercutting the effect of circumstances precluding wrongfulness.'[70] Other States were more negative. France rejected altogether the idea that compensation may arise in the event of a successful invocation of a defence,[71] and Chile rejected it in respect of a state of necessity in particular.[72]

Furthermore, in the context of judicial or arbitral proceedings, Hungary[73] and Slovakia[74] have acknowledged the existence of the duty, while Argentina[75] and Zimbabwe[76] have rejected it. Bolivia also addressed this duty in arbitral proceedings against a foreign investor, though its position is not entirely clear. It offered compensation to the investor for the taking of property, which it justified under the plea of necessity and argued that in this way it respected the 'hypothetical interests' of the United Kingdom (the other party to the BIT) and of the international community as a whole.[77] However, the case involved an expropriation and the primary rules on expropriation themselves require compensation.

Overall, as this review shows, just over a dozen States (out of nearly 200) have expressed views on the existence of a duty of compensation in cases of necessity. As Fernando Bordin has noted, few (if any) customary rules 'even those long viewed as established, can survive the brutal scrutiny of

[68] ILC, '51st Session' (n 67) 8 [57].

[69] These States endorsed, in a general manner, ARSIWA (n 1) Art 27 (or its predecessor Art 35). However, given the wording of Art 27 (and its predecessor) the most that can be inferred from this general support is that these States do not deny the possibility that compensation may arise even if a defence is successfully invoked.

[70] ILC (n 65) A/CN.4/488, 135.

[71] ibid.

[72] UNGA, 'Record of Meeting Held on 12 Nov 1980' (12 November 1980) UN Doc A/C.6/35/SR.47 [8–9].

[73] See, *Gabčíkovo-Nagymaros Project (Hungary/Slovakia)* (Oral Proceedings) [1997] CR 97/3 (translation), 87, CR 97/4, 24–5 [36], CR 97/5, 64 & CR 97/6 (translation), 60, 66.

[74] ibid, CR 97/11, 56–7.

[75] See *CMS v Argentina* (Award) [389]; *CMS v Argentina* (Annulment) [139]; *Enron v Argentina* [344–5]; *Sempra Energy v Argentina* [393–4]; *BG Group* [398].

[76] *Pezold* [615].

[77] *South American Silver* [535].

the magnifying glass'.[78] The two-element approach to the identification of customary law, endorsed by the ILC Conclusions, must be applied with flexibility.[79] Even with this caveat in mind, however, it seems clear that the practice available at present is insufficient and is, moreover, is inconsistent as the broad range of views shows. This makes it difficult to draw any conclusions as to the existence of a customary duty of compensation. While there seems to be a trend towards favouring the recognition of this duty in the case law and scholarship, to date, such trend has not been followed by States in their practice: the evidence available at present falls far short of the requirement of generality necessary to identify a rule of customary law.

3.2 *Equivocal Precedents*

Whether international tribunals can make or develop international law, in addition to just applying the law to specific facts, is a persistent and thorny question in international law.[80] It is also a question which eschews simple answers.[81] One thing, however, is clear: as a matter of the formal sources of international law, judicial decisions are, as stated in Article 38(1)(d) of the ICJ Statute, subsidiary means for the determination of rules of law. International courts and tribunals do not *make law*, as recently reaffirmed by the ILC work on the Identification of Customary Law.[82] But this is not to say that courts and tribunals cannot act as agents of legal development.[83] As observed by Rosalyn Higgins, former President

[78] F Bordin, 'A Glass Half Full? The Character, Function and Value of the Two-Element Approach to Identifying Customary International Law' (2019) 21 ICLR 283, 297.

[79] ibid.

[80] CJ Tams & A Tzanakopoulos, '*Barcelona Traction* at 40: The ICJ as an Agent of Legal Development' (2010) 23 LJIL 781, 782.

[81] One of the most important texts on this question is H Lauterpacht, *The Development of International Law by the International Court* (Stevens & Sons 1958). For more recent works considering this question, see the collection of essays edited by CJ Tams & J Sloan (eds), *The Development of International Law by the International Court of Justice* (OUP 2013); and 2015 Gaetano Morelli Lectures, published in E Cannizzaro & ors (eds), *Decisions of the ICJ as Sources of International Law?* (International and European Papers Publishing 2018). Other reference works will be referred to throughout this chapter, as they become relevant.

[82] ILC, 'Draft Conclusions' (n 14), Conclusion 13, Commentary.

[83] See, eg, RY Jennings, 'The Judiciary, International and National, and the Development of International Law' (1996) 45 *ICLQ* 1, 3; A Pellet, 'Article 38' in A Zimmerman & ors (eds), *The Statute of the International Court of Justice: A Commentary* (OUP 2006) 789; J Crawford, *Brownlie's Principles of Public International Law* (OUP 2012) 39–40.

of the ICJ, 'the very determination of specific disputes, and the provision of specific advice, does develop international law'.[84] To be sure, there are 'decisions and decisions', to paraphrase Jan Paulsson.[85] Some decisions will exert an influence in legal development and, again in Paulsson's words, 'become ever brighter beacons', while others 'flicker and die near-instant deaths'.[86] Judicial development of international law relies on the interactions with the decisions by other actors in this process: whether the decision is endorsed by States in their practice,[87] or it is followed by other tribunals. In turn, these interactions depend on a variety of factors such as whether the field is receptive to judicial development;[88] and whether the decision showcases certain attributes (including the authority of the tribunal, the composition of the tribunal, the context of the decisions, the size of the majority, and the quality of the reasoning).[89]

It thus seems worth examining the case law relied upon by the investment awards discussed earlier. As will be seen, the precedents invoked are, at best, equivocal on this point. In most of these cases, the existence of compensation can be explained on other, more plausible, legal bases. As such, they cannot be relied upon as evidence of the existence of a duty of compensation. It is not surprising, then, that none of these cases has become a 'bright beacon' on this point, as evidenced by how few States have endorsed the existence of the duty of compensation. The list below is not intended to be exhaustive, but merely to assess those cases that are usually cited by investment tribunals and by scholars in their analyses of the duty of compensation.

3.2.1 The Neptune (1797)

During the Napoleonic wars, *The Neptune*,[90] an American vessel on voyage from Charleston to Bordeaux, carrying rice among other things, was stopped and seized by the British navy in April 1795.[91] The Admiralty

[84] R Higgins, *Problems and Process: International Law and How We Use It* (OUP 1995) 302.
[85] J Paulsson, 'International Arbitration and the Generation of Legal Norms: Treaty Arbitration and International Law' (2006) 3(5) TDM 11.
[86] ibid.
[87] A Boyle & C Chinkin, *The Making of International Law* (OUP 2007) 301; Tams, 'Development by ICJ' (n 15) 97–8.
[88] Tams, 'Development by ICJ' (n 15) 95.
[89] ILC, 'Report of the International Law Commission on the Work of its 68th Session' (2 May–10 June and 4 July–12 August 2016) UN Doc A/71/10, Ch 5, Commentary to Conclusion 13, 109 [3]; see also Schreuer (n 15) 738–9; Boyle & Chinkin (n 87) 300–10.
[90] *The Neptune* (1797) 4 Moore Arbitrations 3843.
[91] For a historical-legal background to this dispute, see SC Neff, *The Rights and Duties of Neutrals* (Manchester University Press 2000) 63 ff.

Court of London ordered the sale of the *Neptune*'s cargo to the British Government at the invoice price plus 10% profit. The owner claimed that it was owed the commercial price at which the articles would have sold in Bordeaux.[92] Before the Commission established under the Jay Treaty,[93] the British rejected the claim arguing that the seizure was lawful as the merchandise constituted contraband and, in the alternative, the seizure was a lawful preemptive purchase to provide for a threatened famine.[94] On this latter claim, agents for the British Crown asserted that the 'capture was made under such circumstances of distress as rendered the act lawful against the neutral'.[95]

The British claim of pre-emptive purchase was understood by the Commissioners as a plea of necessity.[96] Deciding by majority, the Commissioners rejected the British argument[97] as the conditions of the plea were not met in fact.[98] Nevertheless, in his consideration of this plea, Commissioner Pinkney endorsed a duty of compensation in the following cases: 'Great Britain might be able to say to neutrals "You shall sell to us", but it does not follow that she could also say "You shall sell to us upon worse terms than you would have procured elsewhere in the lawful prosecution of your commerce"'.[99]

While the *Neptune* is often cited as evidence of the existence of a duty of compensation,[100] three important factors detract from the weight and precedential value of this case. First, the applicable law by the Commission included 'justice, equity and the law of nations',[101] such that very little can be inferred from this case as to the positive law between

[92] *Neptune* 3844.
[93] Treaty of Amity, Commerce and Navigation between his Britannic Majesty and the United States of America (Jay Treaty) (Great Britain & US) (adopted 19 November 1794, entered into force 29 February 1796) 52 CTS 249.
[94] *Neptune* 3844.
[95] As quoted by Commissioner Gore, ibid, Opinion of Mr Gore, 3846.
[96] *Neptune* 3873.
[97] ibid, Opinion of Mr Gore, 3853; ibid, Opinion of Mr Pinkney, 3874–5; ibid, Opinion of Mr Trumbull, 3885. Only these three (out of five) Commissioners in the majority issued written opinions.
[98] ibid, Opinion of Mr Gore, 3853; ibid, Opinion of Mr Pinkney, 3874–5.
[99] ibid 3875.
[100] See, eg, Bücheler (n 53) 290; R Manton, 'Necessity in International Law' (PhD thesis, University of Oxford, 2016) 211–12 <https://ora.ox.ac.uk/objects/uuid:0ee2dd8e-6eac-4364-b538-21ae5eb932a2/download_file?file_format=pdf&safe_filename=Ryan%2BManton%252C%2BNecessity%2Bin%2BInternational%2BLaw.pdf&type_of_work=Thesis> accessed 10 May 2022.
[101] Jay Treaty, art VII.

https://doi.org/10.1017/9781009255462.010 Published online by Cambridge University Press

States at the time.[102] Second, only one of the five Commissioners upheld the existence of this duty. Lastly, the Commission rejected the plea of necessity so Pinkney's statement was only *obiter*.

3.2.2 The Caroline Incident (1837)

In 1837, Canadian rebels were attempting to declare, and establish, an independent Republic of Canada in the British colony of Upper Canada (now Ontario). The US steamer the *Caroline* supplied Canadian rebels and their US recruits on Navy island, within Ontario, from the US shore of the Niagara river. On 29 December 1837, British forces entered US territory and apprehended and destroyed the *Caroline*, which was moored off Fort Schlosser in the American bank of the river.[103] The incident led to a protracted diplomatic correspondence between the two States, in which the notions of self-preservation, self-defence, and necessity were invoked. And it is indeed in relation to self-defence that the incident is renowned: the so-called 'Webster formula' of self-defence, still invoked today,[104] was articulated by the US Secretary of State, Daniel Webster, in a letter to his British counterpart.[105]

The US demanded redress for Britain's wrong, including compensation for the value of the destroyed property, which it estimated at $5000 US dollars.[106] Britain disputed the illegality of its actions claiming to have acted in self-preservation and self-defence,[107] thus rejecting the claim for

[102] See S Heathcote, 'State of Necessity and International Law' (PhD Thesis No 772, Graduate Institute of International and Development Studies, 2005) 137.

[103] For a detailed exposition of the facts see H Jones, 'The *Caroline* Affair' (1976) 28 Historian 485.

[104] For example, see M Wood, 'The Caroline Incident – 1837' in T Ruys, O Corten & A Hofer (eds), *The Use of Force in International Law: A Case-Based Approach* (OUP 2018) 10–4.

[105] D Webster, 'Letter from Daniel Webster, US Secretary of State, to Henry Fox, British Minister in Washington, Dated 24 April 1841' in WR Manning (ed), *Diplomatic Correspondence of the United States: Canadian Relations*, Vol 3 (Carnegie Endowment 1943) 145.

[106] A Stevenson, 'Letter from Andrew Stevenson, United States Minister to Great Britain, to Lord Palmerston, British Foreign Secretary, Dated 22 May 1838' in WR Manning (ed), *Diplomatic Correspondence of the United States: Canadian Relations*, Vol 3 (Carnegie Endowment 1943) 449, doc 1445 & 451. The value of the destroyed property was estimated at US $5000.

[107] See, eg, H Fox, 'Letter from Henry Fox to John Forsyth, US Secretary of State, dated 6 February 1838' in WR Manning (ed), *Diplomatic Correspondence of the United States: Canadian Relations*, Vol 3 (Carnegie Endowment 1943) 422; L Palmerston, 'Letter from Lord Palmerston, British Foreign Secretary, to Andrew Stevenson, American Minister in London, Dated 27 August 1841' in WR Manning (ed), *Diplomatic Correspondence of the United States: Canadian Relations*, Vol 3 (Carnegie Endowment 1943) 644–5.

reparation. The parties eventually settled the dispute with a (feeble) apology from the UK, which nevertheless insisted on the permissibility of its actions. The issue of compensation did not ultimately play a role in the settlement of the dispute. But there is here an interesting twist. The letter sent by Lord Ashburton, on behalf of the UK, to Webster included the following paragraph:

> If the Boat which was destroyed could by any fair construction of the case have been considered as the private property of a citizen bona fide and innocently employed by him as a passage vessel, compensation for its loss might perhaps have been admitted, but it is notorious that it was part and parcel of the armament of the insurgent force, and I have reason to know, that the property in part, if not wholly, was in British subjects. Under such circumstances no question of compensation could be entertained or expected.[108]

A copy of this letter, with these words crossed over but still legible, was kept in the Public Record Office, at the Foreign Office in London.[109] This original letter was subsequently withdrawn at the request of Lord Ashburton and replaced with another letter, amended by agreement of the parties. This second letter did not include the paragraph just quoted on compensation. As Lord Ashburton explained to Lord Aberdeen in this connection, on subsequent consideration he had thought it 'expedient to suppress' this paragraph from his original note.[110]

The *Caroline* incident was referred to by the Annulment Committee in *EDF*, in considering the duty of compensation. But it is doubtful that this case actually supports a duty of compensation. First, Britain did not accept the principle that compensation was payable to the owner of *The Caroline*: even if the latter had been innocent, Ashburton only says that compensation 'might perhaps have been admitted'. Second, such a statement was

[108] WR Manning (ed), *Diplomatic Correspondence of the United States: Canadian Relations*, Vol 3 (Carnegie Endowment 1943) 770, note 1.

[109] ibid.

[110] As quoted in Ld Ashburton, 'Lord Ashburton's letter to Lord Aberdeen, Dated 13 August 1842' (*Avalon Project*, Yale University, 2021) <https://avalon.law.yale.edu/19th_century/br-1842d.asp#ash1> accessed 10 May 2022, which stated that: 'By my despatch No 14 of the 28th ult, I had the honour of sending your Lordship copy of my note to Mr Webster on the subject of the Caroline. It was on consideration thought expedient to suppress a paragraph of that note, which related to the question of compensation to the owner of the vessel. I have therefore to ask your Lordship's permission to substitute the accompanying corrected copy of that note, and to request that the former may be cancelled. There is no other difference between these copies but the omission of the paragraph above referred to'.

not communicated to the US and compensation was not actually paid to the owner of the steamer. Third, the legal principle at issue in this dispute remains contested: while some argue that the parties relied on the plea of necessity,[111] others have argued that the legal principle at issue was that of self-defence.[112]

3.2.3 Orr and Laubenheimer (1900)

Orr and Laubenheimer, two US citizens, were engaged in the banana trade, importing bananas to the United States from the Nicaraguan port of Bluefields, on the mouth of the Rama River.[113] Bananas grew in plantations along the banks of the river and its tributaries, and were transported to the port by tugboats. In 1894, in the course of suppressing an insurrection in Bluefield, a Nicaraguan general seized two of Orr and Laubenheimer's tugboats to transport troops down the Rama river to Bluefields. Orr and Laubenheimer subsequently claimed indemnity for damages sustained as a result of Nicaragua's alleged seizure and detention of the tugboats, and the matter was submitted to arbitration by agreement of the governments of the US and Nicaragua. In its decision, the Arbitrator stated that the 'rights incident to a state of war … justify the use by any Government, in an emergency, of any private property found available.'[114] It went on: 'Full compensation, however, for all damage suffered by private parties must afterwards be made. But the obligation rests upon every party damaged to do all in his power to reduce his losses to a minimum. That is the law the world over…'[115]

This award was referred to by the Tribunal in *CMS* in support of the proposition that acts of necessity generate a duty of compensation for material loss. But that is reading too much into this short decision, for three reasons. First, as per the parties' agreement, Nicaragua 'waive[d] its denial of liability … and agree[d] that said arbitrator may award such sum as he believe[d] said Orr and Laubenheimer … to be justly entitled to'.[116]

[111] *The Caroline* is, for example, included in ARSIWA (n 1) Commentary to Art 25 [5]. It was also relied upon by the Annulment Committee in *EDF v Argentina*, when discussing the latter's plea of necessity, as discussed in Section 3.2.

[112] See Paddeu (n 16) 351–7, and references cited therein.

[113] *Orr and Laubenheimer*.

[114] ibid 40.

[115] ibid 40.

[116] Protocol of an Agreement Between the United States and Nicaragua for the Arbitration of the Amount of Damages to be Awarded Orr and Laubenheimer and the Post-Glover Electric Company (Nicaragua & US) (adopted 22 March 1900, entered into force 22 March 1900, terminated 16 June 1900) 15 RIAA 35, Art III.

Second, as a result of the waiver on the question of liability, the arbitrator did not need to, and did not, apply international law to the dispute: its task was to decide the amount of *just* compensation due. Finally, if there is a legal basis for Nicaragua's obligation to compensate, this is the right of angary. Pursuant to this right, as explained by Oppenheim, States engaged in hostilities are entitled to use the property of neutrals 'provided the articles concerned are serviceable to military ends and wants', and so long as, in every case, 'the neutral owner [is] fully indemnified.'[117]

3.2.4 Company General of the Orinoco (1905)

The case involved the rescission of concession contracts between Venezuela and a French Company, signed in the late 1880s. The contract was for the exploitation of vegetable and mineral resources on territory that Venezuela believed to be under its sovereignty.[118] Following protests by Colombia,[119] Venezuela rescinded the contract with the French company. Venezuela subsequently found that most of the territory in the concession was under the sovereignty of Colombia.[120] The company claimed compensation from Venezuela, and the matter came before the Franco-Venezuelan Mixed Commission. Umpire Plumley upheld the rescission but ordered the payment of compensation to the company. In his reasoning, he framed the question as one of necessity.[121] In his view:

> As the Government of Venezuela, whose duty of self-preservation rose superior to any question of contract, it had the power to abrogate the contract in whole or in part. It exercised that power and canceled [sic] the provision of unrestricted assignment. It considered the peril superior to the obligation and substituted therefor [sic] the duty of compensation.[122]

The peril, as the Umpire explained, came from multiple sources. It came from the Colombian government, which claimed sovereignty over much of the area under concession, and which threatened force to recover the territory, but also from the local population and businessmen who were

[117] L Oppenheim, *International Law – Vol 2: War and Neutrality* (Longmans 1906) 395 [365].
[118] *Company General of the Orinoco* 260.
[119] ibid 257–8.
[120] ibid 269.
[121] More specifically, the Umpire framed the question as one about 'self-preservation'. On the relation between a discrete (and general) rule of necessity and the right of self-preservation and why claims of self-preservation need not (and should not) be equated with invocations of such a discrete rule of necessity, see Paddeu (n 16) 346–63.
[122] *Company General of the Orinoco* 280.

dissatisfied by the monopoly granted to the company and who, with the support of the local government, revolted sometimes violently.[123]

As with the *Neptune*, there are a number of factors which may diminish the weight and precedential value of this decision in respect of the duty of compensation.[124] First, there is uncertainty as to the law actually applied by the Umpire to decide the case.[125] The Umpire was competent to take into account, in reaching his decision as to the need for compensation, 'the ethical precepts of international law, equity and good conscience'.[126] On the specifics of the case, the Umpire held that 'if there were aught of wrong towards the Company General of the Orinoco done or permitted by the respondent Government', then he may award 'damages if justice and equity so permit and so require.'[127] Ultimately, in his view, there was 'no inequity' in apportioning some of the loss caused to the company by the rescission on the Government.[128] The decision was thus apparently based on equitable considerations.

Second, even if by application of international law, the award of compensation can be explained on other legal bases. It could be explained as a case of compensation for wrongful conduct: the compensation paid was not for the damage caused by the rescission of the contract itself, but rather for the breach of the contract before its termination.[129] Or it can be explained as involving the application 'of the rule that compensation must be paid when foreign-owned property is expropriated in the public interest.'[130] This explanation is more convincing than the former, as it can account for the necessity-like reasoning of the Umpire.[131] Being able to account for this reasoning of the Umpire is particularly important for two reasons: first, because it is this aspect of the reasoning that scholars seize upon to provide support for the existence of a duty of

[123] ibid 281–2.
[124] eg Bücheler (n 53) 290–1.
[125] On which see Heathcote (n 102) 226–8.
[126] *Company General of the Orinoco* 277. As established by the terms of the Protocol Relating to the Settlement of Indemnities Between France and Venezuela (France & Venezuela) (adopted 19 February 1902) published in J Ralston & WT Sherman Doyle (eds), *Report of French-Venezuelan Mixed Claims Commission of 1902* (US GPO 1906) 1.
[127] *Company General of the Orinoco* 278.
[128] ibid 284.
[129] M Forteau, 'Reparation in the Event of a Circumstance Precluding Wrongfulness' in J Crawford, A Pellet & S Olleson (eds), *The Law of International Responsibility* (OUP 2010) 889.
[130] M Akehurst, 'International Liability for Injurious Consequences Arising Out of Acts Not Prohibited by International Law' (1985) 16 NYIL 3, 12, fn 45.
[131] Bücheler (n 53) 290.

compensation; and, second, because there are considerable doubts as to the recognition of a defence of necessity in the positive law of the time.[132] As Sarah Heathcote explains, there exist in international law primary rules 'in the image of necessity': these are substantive rules of international law that cater to a specific (factual) situation of necessity. A State's right to expropriate property is precisely one of these rules, as it can only be exercised in situations of public necessity. As the Umpire noted in the award, a situation of public necessity existed in Venezuela at the time, as a result of the external (from Colombia) and internal (local population) threats that the country was facing.[133] In such circumstances, the rescission of the concession was an expropriation of foreign-owned property due to necessity. The payment of compensation in this case was, therefore, a matter of the primary rule in question (expropriation) rather than one of the applications of the plea of necessity under the law of State responsibility.

3.2.5 Properties of Bulgarian Minorities in Greece (1926)

Following the exchange of minorities provisions in the post-World War I settlements, foreign refugees of Greek origin were transferred from Turkey to Greece. In order to house them, the Greek Government forced Bulgarian minorities to move out of their homes in Greece. The matter was considered by a League of Nations' Commission of Enquiry.[134] By the time the Commission issued its report, the Bulgarian minorities had left Greece and the Greek refugees were already settled in the homes. The Commission allowed that the take-over of Bulgarian property by Greece had been the result of a situation of what it termed '*force majeure*'. Indeed, according to the report, to remove the Greek refugees to allow the return of the owners would have been impossible in these circumstances, as well as undesirable.[135] Nevertheless, the Commission argued that it could not be expected that the Bulgarian minorities would simply renounce their right to the homes, so it was just that they receive compensation for the value of their property.[136]

[132] See IV Hull, *A Scrap of Paper: Breaking and Making International Law During the Great War* (Cornell University Press 2014) 44–5; Paddeu (n 16) 382–6.
[133] Heathcote (n 102) 228–9.
[134] League of Nations, 'Report of the Commission of Enquiry on the Incidents on the Frontier between Bulgaria and Greece, Doc No C.727.M.270.1925.VII (Annex 815)' (1926) 7 LNOJ 196, 209.
[135] ibid 209.
[136] ibid.

The argument for a duty of compensation is more plausible in this instance, but it is not clear cut. The situation certainly seems to be one that could fit within the plea of necessity (as currently formulated): in order to protect one interest (housing Greek refugees), Greece infringed the rights of others (Bulgarian minorities). But here too there are a number of factors which may weaken this argument. To begin with, the Commission spoke of *force majeure* and not of necessity. Much of contemporary doctrine has tended to assume that *force majeure* and 'necessity' were used interchangeably at the time, but this view requires some nuance. The concepts are (and were) indeed different, and I have argued elsewhere that reference was made to '*force majeure*' during this period to address situations of necessity because international law did not recognise a rule of necessity at the time.[137] At any rate, even if this had been a case decided on a plea of necessity (at least in substance, if not expressly), it does not seem that the requirements of the plea were met. As Heathcote has argued, this was not a case of protecting a superior interest as against an inferior one: in this case, the interests were equal for 'why should Bulgarian minorities, who … had only been in Greece for a decade or so … be moved out of their homes to house refugees of Greek origins – the Smirna "Greeks" [who] had been in Turkey for centuries?'[138]

Once more, the Commission's decision is better explained on other legal bases: either as a situation of reparation for wrongful conduct or, as in the *Orinoco Company* case, as a case of expropriation for public necessity.[139] In any event, there are doubts as to whether the basis of the Commission's recommendation was premised on law at all. While its mandate was to 'establish the facts enabling the responsibility to be fixed, and supply the necessary material for the determination of any indemnities or reparation which may be considered appropriate', the Council did not specify the basis (legal or otherwise) upon which such 'responsibility' and 'indemnities' ought to be decided. Perhaps for this reason, Michael Akehurst has interpreted the Commission's finding as a political compromise.[140]

3.2.6 Gabčíkovo-Nagymaros (1997)

The dispute between Slovakia and Hungary concerned the unilateral termination of the Treaty of 1977, which envisaged a joint project between

[137] Paddeu (n 16) 382–6.
[138] Heathcote (n 102) 224.
[139] ibid 223–4.
[140] Akehurst (n 130) 12, fn 45.

the two States for the construction of a system of locks in the Danube, by Hungary. Among other things, Hungary invoked the plea of necessity to justify its unilateral termination of the Treaty. At the time of unilateral termination, both parties had commenced the works already. Slovakia had completed a section of works in one of the sectors, so the question as to whether any compensation was due to Slovakia as a result of the unilateral termination emerged. The ICJ rejected Hungary's plea of necessity, but it noted that 'Hungary [had] pointed out' that a duty to compensate Slovakia for the works undertaken existed.[141] The Court's statement was *obiter* and is not a direct endorsement by the Court of the duty: it is merely a description of Hungary's position. As such, not much weight can be given to the judgment itself.

More pertinent are, at any rate, the statements made by Hungary during the proceedings. Hungary raised the point multiple times during the oral phase of the proceedings.[142] In very clear terms, Hungary stated that

> Hungary recognizes that in modern international law the plea of necessity can only be admitted on a limited and strictly defined basis. 'Necessity' allows the sovereign State to commit what would otherwise be an unlawful act while avoiding international responsibility – though not the requirement to make appropriate compensation.

Slovakia's own views on the matter were less assertive. It recognised that the duty of compensation was required as a matter of fairness[143] and common sense, but it warned of the risk of States 'buying' their 'way out of [their] breaches of its international obligations'.[144]

4 Assessment

Investment tribunals have tackled the question of compensation in cases of necessity in numerous cases. Their conclusions on the point (almost always in *obiter*) are as varied as the reasoning behind them. A common thread among them is that they have, for the most part, failed to assess the positive law basis for the existence (or non-existence) of the duty of compensation. Only a handful of decisions name-check some precedents and cases, but none of them in any way refer to State practice or *opinio juris*.

[141] *Gabčíkovo-Nagymaros* (Oral Proceedings) [48].
[142] See, eg, ibid [48].
[143] This is the English translation of the statement found in the *Gabčíkovo-Nagymaros* (Oral Proceedings): CR 97/11, 54. Note that the original French version uses the term 'equité'.
[144] ibid 55.

To be sure, the question of compensation in cases of necessity is a philosophically and theoretically difficult one, having troubled legal scholars and theorists for many centuries.[145] It is a question that elicits intuitive and often strongly held opinions: it would be unfair for the affected party to bear the burden of the protection of others' interests. In short, it would be unfair to let the loss lie where it falls. And yet, the action that causes the loss is a permitted one, it is lawful behaviour, and under normal circumstances, we would not expect those acting lawfully to compensate losses caused by their actions. In the absence of a wrong, losses do lie where they fall: herein lies the dilemma at the heart of the duty of compensation. And yet, necessitated acts seem different from other lawful acts that cause loss. Indeed, necessitated acts have a baggage that other lawful acts do not: they evoke moral hazard and, in the history of international law, they evoke abusive behaviour by powerful States.

This baggage explains the intuitive perceptions of unfairness at the allocation of loss onto the affected party, and the support for a re-distribution of the loss onto the agent. It may also explain, at least partly, why investment tribunals have been sympathetic to the idea that States invoking necessity owe a duty of compensation to the affected parties. But this is no justification for these tribunals' omission to engage with the methods of law ascertainment: aside from the fairness and justness of the duty of compensation, is there evidence that this is required by positive law; is there evidence, in particular, of practice and *opinio juris* about the existence of this duty? As shown, there is not only limited practice and *opinio juris* on this duty, but the few precedents cited in investment decisions do not support, nor do they provide evidence of, the existence of a duty of compensation. The nobility of the sentiment is no substitute for the absence of positive law on the existence of this duty. Indeed, in asserting or deducing the duty of compensation in this manner, investment tribunals are closer to deciding the matter *ex aequo et bono*, for which they would need specific consent by the parties, than by application of the rules of international law, as they are mandated to do.

[145] For an overview of scholars' approach to this question, both historical and contemporary, see J Salter, 'Hugo Grotius: Property and Consent' (2001) 29 Political Theory 537; J Salter, 'Grotius and Pufendorf on the Right of Necessity' (2005) 26 HPT 285; SD Sugarman, 'The "Necessity" Defense and the Failure of Tort Theory: The Case Against Strict Liability for Damages Caused While Exercising Self-Help in an Emergency' (2005) 5(2) Issues in Legal Scholarship 1.